

Full-Length Practice Test 8

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

Part 1: Individuals

1. The standard deduction for a dependent is limited to the greater of \$1,300 or:
 - A. Earned income plus \$450
 - B. \$500
 - C. Unearned income
 - D. \$2,000

2. To claim head of household status, an unmarried taxpayer must pay more than half the cost of:
 - A. All household expenses
 - B. Dependents' support
 - C. Maintaining the home
 - D. Medical care

3. A couple divorced on December 30 must file for that year as:
 - A. Married filing jointly
 - B. Single or head of household
 - C. Qualifying surviving spouse
 - D. Married filing separately

4. The tax benefit rule requires income inclusion when:
 - A. Previously deducted amounts are recovered
 - B. Expenses are paid
 - C. Refunds are received
 - D. Deductions are claimed

5. Prizes and awards are excludable from income when:
 - A. Under \$100
 - B. For achievements
 - C. From employers
 - D. Transferred to charity without acceptance

6. Cancellation of debt income is excludable if the taxpayer is:
 - A. Employed

- B. Insolvent
 - C. Married
 - D. Self-employed
7. Life insurance proceeds paid by reason of death of the insured are generally:
- A. Partially taxable
 - B. Fully taxable
 - C. Excluded from income
 - D. Deferred
8. The qualified tuition reduction for employees of educational institutions applies to:
- A. All education
 - B. Undergraduate only
 - C. Graduate business courses
 - D. Undergraduate and graduate courses
9. Foster care payments from a state agency are:
- A. Excluded from income
 - B. Partially taxable
 - C. Fully taxable
 - D. Deferred
10. Clergy housing allowances are excluded from income tax but subject to:
- A. FICA
 - B. State tax only
 - C. AMT
 - D. Self-employment tax
11. Alaska Native Corporation dividends are:
- A. Fully excluded
 - B. Partially excluded
 - C. Fully taxable
 - D. Tax-deferred
12. Qualified disaster relief payments are:
- A. Partially taxable
 - B. Fully taxable
 - C. Excluded from income
 - D. Subject to AMT

13. The educator expense deduction allows teachers to deduct up to:
- A. \$100
 - B. \$200
 - C. \$500
 - D. \$300
14. Health savings account contributions by employers are:
- A. Excluded from employee income
 - B. Taxable wages
 - C. Subject to FICA only
 - D. Partially taxable
15. The penalty for early withdrawal of savings is deducted as:
- A. Itemized deduction
 - B. Business expense
 - C. Adjustment to income
 - D. Tax credit
16. IRA contributions for the prior year can be made until:
- A. December 31
 - B. Tax return due date excluding extensions
 - C. April 30
 - D. October 15
17. Traditional IRA deduction phase-out begins for active participants at approximately for single filers:
- A. \$77,000
 - B. \$100,000
 - C. \$50,000
 - D. \$125,000
18. Roth IRA contribution phase-out begins at approximately for single filers:
- A. \$100,000
 - B. \$146,000
 - C. \$125,000
 - D. \$200,000
19. The deduction for self-employed health insurance is taken as:
- A. Itemized deduction
 - B. Business expense on Schedule C
 - C. Adjustment to income

D. Tax credit

20. Jury duty pay turned over to employer is:

- A. Deductible as adjustment to income
- B. Not deductible
- C. Itemized deduction
- D. Business expense

21. Qualified performing artists can deduct business expenses if AGI before deduction doesn't exceed:

- A. \$10,000
- B. \$25,000
- C. \$12,000
- D. \$16,000

22. Armed Forces reservist travel expenses exceeding 100 miles are deductible as:

- A. Itemized deduction
- B. Business expense
- C. Adjustment to income
- D. Not deductible

23. The deduction for self-employment tax equals:

- A. Full amount
- B. One-half of SE tax
- C. One-third of SE tax
- D. Not deductible

24. Archer MSA contributions by self-employed individuals are:

- A. Not deductible
- B. Itemized deduction
- C. Business expense
- D. Adjustment to income

25. Penalties on early withdrawal of time deposits are:

- A. Deductible as adjustment to income
- B. Not deductible
- C. Itemized deduction
- D. Business expense

26. Attorney fees for unlawful discrimination claims are deductible up to:

- A. \$5,000

- B. \$10,000
- C. \$25,000
- D. Amount included in income

27. Medical expenses must exceed what percentage of AGI to be deductible:

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

28. Cosmetic surgery is deductible if:

- A. Elective
- B. For appearance
- C. Medically necessary
- D. Always deductible

29. Long-term care insurance premiums are deductible based on:

- A. Policy cost
- B. Age of insured
- C. Health status
- D. Not deductible

30. Capital expenses for medical care improvements are deductible to the extent they exceed:

- A. Increase in home value
- B. Insurance reimbursement
- C. 7.5% of AGI
- D. \$10,000

31. Medical mileage for 2024 is approximately:

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

32. State and local income tax or sales tax deduction is elected:

- A. Automatically
- B. By filing form
- C. By taxpayer choice
- D. By IRS determination

33. Real property taxes are deductible when:
- A. Assessed
 - B. Paid
 - C. Due
 - D. Liened
34. Personal property taxes are deductible if based on:
- A. Purchase price
 - B. Age of property
 - C. Weight
 - D. Value of property
35. Mortgage insurance premiums are:
- A. Deductible subject to income limits
 - B. Not deductible
 - C. Fully deductible
 - D. Tax credit eligible
36. Points paid on home purchase are:
- A. Deductible in year paid
 - B. Amortized over loan term
 - C. Not deductible
 - D. Tax credit
37. Points paid on refinancing are:
- A. Not deductible
 - B. Partially deductible
 - C. Amortized over loan term
 - D. Fully deductible in year paid
38. Investment interest includes interest on debt to purchase:
- A. Personal residence
 - B. Municipal bonds
 - C. Business property
 - D. Taxable investments
39. Cash charitable contributions require written acknowledgment for amounts of:
- A. \$100 or more
 - B. \$250 or more
 - C. \$500 or more

D. \$1,000 or more

40. Clothing donated to charity is valued at:

- A. Original cost
- B. Replacement cost
- C. Current market value
- D. Fair market value

41. Charitable mileage rate is:

- A. 14 cents per mile
- B. 21 cents per mile
- C. 67 cents per mile
- D. 58 cents per mile

42. Donations of appreciated property held short-term are deductible at:

- A. Fair market value
- B. Original cost
- C. Lesser of basis or FMV
- D. Greater of basis or FMV

43. Casualty loss deduction requires loss in federally declared disaster exceeding:

- A. \$100 per event
- B. \$100 per event plus 10% of AGI
- C. 10% of AGI
- D. \$500 per event

44. Theft losses are deductible in the year:

- A. Discovered
- B. Reported
- C. Prosecuted
- D. Reimbursed

45. Gambling losses are deductible up to:

- A. \$3,000
- B. 50% of winnings
- C. 10% of AGI
- D. Gambling winnings

46. Tax preparation fees for 2018–2025 are:

- A. Fully deductible

- B. Partially deductible
- C. Not deductible
- D. Tax credit eligible

47. The child tax credit is available for qualifying children under age:

- A. 18
- B. 17
- C. 19
- D. 21

48. The child tax credit begins phasing out at approximately for single filers:

- A. \$200,000
- B. \$400,000
- C. \$125,000
- D. \$75,000

49. Credit for other dependents who don't qualify for child tax credit is:

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

50. The dependent care credit maximum expenses for two or more children:

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

51. The dependent care credit percentage for higher income taxpayers is:

- A. 35%
- B. 20%
- C. 25%
- D. 15%

52. Adoption credit maximum for 2024 is approximately:

- A. \$10,000
- B. \$12,000
- C. \$15,000
- D. \$16,810

53. The adoption credit phases out beginning at approximately:
- A. \$100,000
 - B. \$200,000
 - C. \$252,150
 - D. \$300,000
54. Child and dependent care expenses are reportable on Form:
- A. 8863
 - B. 8862
 - C. 2441
 - D. 8332
55. Earned income credit requires qualifying children to have valid:
- A. Birth certificate
 - B. Social Security number
 - C. Passport
 - D. School records
56. EITC without qualifying children is available to taxpayers at least age:
- A. 25
 - B. 21
 - C. 19
 - D. 18
57. American opportunity credit maximum per student is:
- A. \$2,000
 - B. \$4,000
 - C. \$1,000
 - D. \$2,500
58. American opportunity credit covers the first:
- A. 2 years
 - B. 5 years
 - C. 4 years
 - D. 6 years
59. Lifetime learning credit percentage is:
- A. 25%
 - B. 20%
 - C. 30%

D. 100%

60. Lifetime learning credit maximum per return is:

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

61. Energy efficient home improvement credit for 2024 is:

- A. 10%
- B. 30%
- C. 26%
- D. 22%

62. Residential energy credit for solar panels has:

- A. Annual limit
- B. No dollar limit
- C. \$2,000 limit
- D. Lifetime limit

63. Electric vehicle credit requires final assembly in:

- A. North America
- B. United States
- C. NAFTA country
- D. Any country

64. Used electric vehicle credit maximum is:

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

65. Premium tax credit is reconciled on Form:

- A. 8962
- B. 1095-A
- C. 8962
- D. 8965

66. Excess advance premium tax credit repayment is capped for taxpayers with income below:

- A. 200% of poverty line

- B. 400% of poverty line
- C. 300% of poverty line
- D. 500% of poverty line

67. Retirement savings contributions credit maximum rate is:

- A. 20%
- B. 30%
- C. 10%
- D. 50%

68. Retirement savings credit applies to contributions up to:

- A. \$2,000
- B. \$4,000
- C. \$6,000
- D. \$10,000

69. Foreign tax credit carryback is:

- A. 2 years
- B. 3 years
- C. 1 year
- D. Not allowed

70. Foreign tax credit carryforward is:

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

71. General business credit carryback is:

- A. 1 year
- B. 2 years
- C. 3 years
- D. Not allowed

72. General business credit carryforward is:

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

73. First-time homebuyer credit from 2008 required repayment over:
- A. 10 years
 - B. 20 years
 - C. 15 years
 - D. 5 years
74. Making work pay credit was available in:
- A. 2010–2012
 - B. 2009–2010
 - C. 2008–2009
 - D. 2011–2012
75. Estimated tax safe harbor for higher income taxpayers requires payment of:
- A. 100% of prior year tax
 - B. 90% of current year tax
 - C. 80% of current year tax
 - D. 110% of prior year tax
76. Estimated tax payments are due quarterly on the 15th of April, June, September, and:
- A. January
 - B. December
 - C. October
 - D. November
77. Underpayment penalty can be avoided by owing less than:
- A. \$500
 - B. \$100
 - C. \$1,000
 - D. \$2,000
78. Farmers and fishermen estimated tax safe harbor is:
- A. 90%
 - B. 66.67%
 - C. 100%
 - D. 50%
79. Excess Social Security withholding by multiple employers is claimed as:
- A. Credit on return
 - B. Refund request
 - C. Itemized deduction

D. Adjustment to income

80. Federal income tax withheld is claimed as:

- A. Itemized deduction
- B. Adjustment to income
- C. Business expense
- D. Payment/credit

81. Net investment income tax rate is:

- A. 0.9%
- B. 3.8%
- C. 2.9%
- D. 1.45%

82. Net investment income tax threshold for single filers is approximately:

- A. \$125,000
- B. \$250,000
- C. \$200,000
- D. \$400,000

83. Additional Medicare tax applies to wages exceeding for single filers:

- A. \$125,000
- B. \$250,000
- C. \$400,000
- D. \$200,000

84. Additional Medicare tax rate is:

- A. 0.9%
- B. 3.8%
- C. 1.45%
- D. 2.9%

85. Self-employment tax applies to net self-employment income of at least:

- A. \$1,000
- B. \$400
- C. \$600
- D. \$100

86. Optional methods for computing self-employment tax are available when net earnings are less than:

- A. \$400

- B. \$6,540
- C. \$6,107
- D. \$5,000

87. Nonfarm optional method can be used for up to:

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

88. Farm optional method requires gross farm income of no more than:

- A. \$5,000
- B. \$6,540
- C. \$10,000
- D. \$9,060

89. Household employment taxes are reported on Schedule:

- A. C
- B. H
- C. SE
- D. EIC

90. Household employees must receive W-2 if cash wages exceed:

- A. \$1,000
- B. \$2,000
- C. \$2,700
- D. \$600

91. Nanny tax threshold for 2024 is approximately:

- A. \$2,700
- B. \$2,500
- C. \$3,000
- D. \$2,000

92. Form 8919 reports uncollected Social Security and Medicare tax on:

- A. Self-employment income
- B. Investment income
- C. Rental income
- D. Wages from employers who didn't withhold

93. Repayment of supplemental unemployment benefits is treated as:
- A. Adjustment to income
 - B. Itemized deduction
 - C. Adjustment to income in year repaid
 - D. Not deductible
94. Disability income exclusion requires permanent and total disability beginning before age:
- A. 50
 - B. 65
 - C. 62
 - D. 55
95. Interest on educational savings bonds is excludable if used for qualified expenses and modified AGI doesn't exceed approximately for single filers:
- A. \$50,000
 - B. \$75,000
 - C. \$100,000
 - D. \$96,800
96. Qualified tuition programs (529 plans) allow tax-free distributions for K-12 tuition up to:
- A. \$10,000 per year
 - B. \$5,000 per year
 - C. Unlimited
 - D. Not allowed
97. Coverdell ESA contributions are limited to:
- A. \$500
 - B. \$1,000
 - C. \$2,000
 - D. \$5,000
98. Coverdell ESA beneficiary must be under age:
- A. 21
 - B. 18
 - C. 24
 - D. 30
99. Section 1031 like-kind exchanges apply to:
- A. Personal property
 - B. Securities

- C. Partnership interests
- D. Real property

100. Boot received in like-kind exchange is recognized up to:
- A. Realized gain
 - B. Fair market value
 - C. Basis
 - D. Depreciation

Part 2: Businesses

1. Constructive receipt occurs when income is:
 - A. Invoiced
 - B. Earned
 - C. Deposited
 - D. Credited to account

2. Prepaid income for services is generally included in income when:
 - A. Received
 - B. Invoiced
 - C. Earned
 - D. Contracted

3. Long-term contract income recognition uses percentage of completion or:
 - A. Cash method
 - B. Accrual method
 - C. Completed contract method
 - D. Installment method

4. Installment method is not available for:
 - A. Real estate sales
 - B. Dealer sales
 - C. Casual sales
 - D. Investment property

5. Gross profit percentage in installment sales equals:
 - A. Gross profit divided by contract price
 - B. Sales price minus basis
 - C. Total payments received
 - D. Down payment percentage

6. Recapture income in installment sales is recognized:
 - A. Over payment period
 - B. Ratably
 - C. When received
 - D. In year of sale

7. Imputed interest rules apply to seller financing when stated rate is below:
 - A. Prime rate
 - B. 10%
 - C. Applicable federal rate
 - D. 5%

8. Related party installment sale requires holding property for:
 - A. 2 years
 - B. 1 year
 - C. 6 months
 - D. 3 years

9. Inventory must be written down to market when market is less than cost and write-down is:
 - A. Optional
 - B. Required
 - C. Not allowed
 - D. Deferred

10. Lower of cost or market valuation applies to:
 - A. Services
 - B. Real estate
 - C. Securities
 - D. Inventory

11. LIFO liquidation occurs when:
 - A. Inventory sold
 - B. Method changed
 - C. Ending inventory less than beginning
 - D. Business closed

12. UNICAP applies to retailers with average gross receipts exceeding:
 - A. \$10 million
 - B. \$29 million

- C. \$25 million
- D. \$50 million

13. Small business taxpayers can avoid UNICAP if average receipts don't exceed:

- A. \$29 million
- B. \$25 million
- C. \$50 million
- D. \$10 million

14. Section 263A uniform capitalization rules apply to:

- A. Service businesses
- B. Retailers under threshold
- C. Producers
- D. All businesses

15. Mixed service costs under UNICAP are allocated using:

- A. Square footage
- B. Hours worked
- C. Sales revenue
- D. Reasonable method

16. Interest capitalization applies to property with production period exceeding:

- A. 1 year
- B. 6 months
- C. 2 years
- D. 90 days

17. Avoided cost method for interest capitalization uses:

- A. Prime rate
- B. Weighted average rate
- C. AFR
- D. Stated rate

18. Real property production period for interest capitalization is:

- A. 6 months
- B. 1 year
- C. 2 years
- D. 90 days

19. Personal property production period for interest capitalization is:

- A. 6 months
- B. 1 year
- C. 90 days
- D. 2 years

20. Business startup costs exceeding \$50,000 reduce the \$5,000 first-year deduction:

- A. Proportionally
- B. To zero
- C. By half
- D. Dollar-for-dollar

21. Organizational costs first-year deduction is reduced when total costs exceed:

- A. \$50,000
- B. \$55,000
- C. \$25,000
- D. \$10,000

22. Section 195 startup costs are amortized over:

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

23. Syndication costs for partnerships are:

- A. Deductible
- B. Not deductible or amortizable
- C. Amortized
- D. Capitalized

24. Research and experimentation costs for 2024 must be:

- A. Amortized over 5 years
- B. Expensed
- C. Capitalized
- D. Deferred

25. Section 174 research costs include:

- A. Land
- B. Marketing
- C. Administrative overhead
- D. Experimental/laboratory costs

26. Software development costs can be amortized over:
- A. 15 years
 - B. 5 years
 - C. 36 months
 - D. 60 months
27. Goodwill amortization period is:
- A. 15 years
 - B. 10 years
 - C. 5 years
 - D. 20 years
28. Covenant not to compete is amortized over:
- A. Actual term
 - B. 15 years
 - C. Contract period
 - D. 5 years
29. Customer lists acquired in business purchase are amortized over:
- A. 5 years
 - B. 10 years
 - C. 3 years
 - D. 15 years
30. Self-created goodwill is:
- A. Amortizable
 - B. Expensed
 - C. Capitalized
 - D. Not amortizable
31. Section 197 intangibles must be acquired in connection with:
- A. Any purchase
 - B. Stock purchase
 - C. Trade or business acquisition
 - D. Asset purchase
32. Patent costs are amortized over:
- A. 17 years
 - B. Remaining legal life

- C. 15 years
- D. 20 years

33. Trademark acquired separately from business is amortized over:

- A. 10 years
- B. 5 years
- C. 15 years
- D. Remaining legal life

34. Going concern value is amortized over:

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

35. Franchise fees are:

- A. Amortized over 15 years
- B. Expensed
- C. Capitalized
- D. Not deductible

36. Lease acquisition costs are amortized over:

- A. 15 years
- B. 5 years
- C. Actual lease term
- D. Remaining lease term

37. Section 179 property must be used more than 50% for:

- A. Investment
- B. Business
- C. Personal use
- D. Rental

38. Section 179 deduction is limited to:

- A. Net income
- B. Gross income
- C. Taxable income from business
- D. Wages

39. Bonus depreciation for 2024 applies at:

- A. 60%
- B. 80%
- C. 100%
- D. 50%

40. Qualified improvement property is depreciated over:

- A. 27.5 years
- B. 39 years
- C. 15 years
- D. 20 years if bonus depreciation not elected

41. Nonresidential real property recovery period is:

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

42. Office equipment is depreciated over:

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

43. Computers are depreciated over:

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

44. Land improvements are depreciated over:

- A. 7 years
- B. 10 years
- C. 20 years
- D. 15 years

45. Mid-quarter convention applies when over 40% of property is placed in service in:

- A. First quarter
- B. Fourth quarter
- C. Second quarter
- D. Third quarter

46. Luxury automobile depreciation limits apply to vehicles with gross weight under:
- A. 8,000 pounds
 - B. 10,000 pounds
 - C. 6,000 pounds
 - D. 14,000 pounds
47. SUVs over 6,000 pounds have Section 179 limit of approximately:
- A. \$29,200
 - B. \$20,200
 - C. \$12,200
 - D. Full amount
48. Listed property includes passenger automobiles used 50% or less for:
- A. Personal use
 - B. Investment
 - C. Rental
 - D. Business
49. Partnership income is taxed to partners when:
- A. Distributed
 - B. Earned
 - C. Received
 - D. Allocated
50. Partnership basis is increased by partner's share of:
- A. Liabilities
 - B. Distributions
 - C. Losses
 - D. Cash
51. Recourse debt is allocated to partners who bear:
- A. Profits
 - B. Control
 - C. Economic risk of loss
 - D. Management
52. Nonrecourse debt in partnerships is generally allocated based on:
- A. Capital accounts
 - B. Ownership percentage

- C. Services
- D. Profit-sharing ratio

53. Partner's basis in distributed property is generally:

- A. Fair market value
- B. Carryover basis
- C. Zero
- D. Partner's basis in interest

54. Partnership liquidating distribution of property only creates loss if property is:

- A. Appreciated
- B. Depreciable
- C. Cash, receivables, or inventory only
- D. Any property

55. Section 751 property includes unrealized receivables and substantially appreciated:

- A. Inventory
- B. Capital assets
- C. Equipment
- D. Real estate

56. Inventory is substantially appreciated when FMV exceeds adjusted basis by more than:

- A. 10%
- B. 20%
- C. 25%
- D. 50%

57. Partnership tax year must conform to majority partners or principal partners or use least aggregate deferral unless:

- A. Business purpose shown
- B. IRS approves
- C. Section 444 election made
- D. All partners agree

58. Section 444 election allows deferral of maximum:

- A. 3 months
- B. 6 months
- C. 4 months
- D. 2 months

59. Section 7519 required payments compensate for tax deferral from:
- A. Fiscal year
 - B. Estimated taxes
 - C. Section 444 election
 - D. Installment sales
60. Partnership self-employment income includes guaranteed payments and distributive share for:
- A. Limited partners
 - B. All partners
 - C. Managing partners
 - D. General partners
61. Family partnership income must be allocated based on capital if capital is material income-producing factor and family member provides substantial services unless:
- A. Services compensated first
 - B. Partnership agreement allocates differently
 - C. IRS approves
 - D. All agree
62. Partnership minimum gain prevents distributions that would create or increase negative capital account attributable to:
- A. Nonrecourse debt
 - B. Recourse debt
 - C. Partner loans
 - D. Contributed property
63. Qualified nonrecourse financing for real estate increases at-risk basis if from qualified person and not from:
- A. Bank
 - B. Seller
 - C. Related party
 - D. Lender
64. S corporation election requires filing Form 2553 by:
- A. December 31
 - B. Tax year-end
 - C. Return due date
 - D. 15th day of 3rd month of year

65. S corporation inadvertent termination can be waived if corrected and corporation agrees to make adjustments requested by:
- A. Shareholders
 - B. IRS
 - C. State
 - D. Board
66. S corporation passive investment income termination requires excess passive income for:
- A. 1 year
 - B. 2 years
 - C. 3 consecutive years
 - D. 5 years
67. S corporation new election after termination requires waiting:
- A. 5 years
 - B. 3 years
 - C. 2 years
 - D. 1 year
68. S corporation AAA is decreased by:
- A. Income
 - B. Contributions
 - C. Tax-exempt income
 - D. Distributions and losses
69. S corporation distributions from AAA are tax-free to extent of:
- A. E&P
 - B. Stock basis
 - C. Debt basis
 - D. Capital
70. S corporation loss limitation is based on stock basis plus:
- A. Debt basis
 - B. AAA
 - C. E&P
 - D. Liabilities
71. C corporation accumulated earnings credit is at least:
- A. \$150,000
 - B. \$100,000

- C. \$250,000
- D. \$500,000

72. Personal service corporations accumulated earnings credit is:

- A. \$250,000
- B. \$100,000
- C. \$500,000
- D. \$150,000

73. PHC tax applies when more than 50% owned by 5 or fewer individuals and 60% or more of income is:

- A. Passive
- B. PHC income
- C. Investment
- D. Foreign

74. Personal holding company tax is imposed on undistributed personal holding company income at:

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

75. Dividends paid deduction for PHC purposes includes dividends paid within:

- A. Tax year
- B. 2½ months after year-end
- C. Extended due date
- D. 3½ months after year-end

76. Consent dividends are treated as paid on last day of tax year and immediately contributed back as:

- A. Loan
- B. Distribution
- C. Gift
- D. Capital contribution

77. Schedule M-2 reconciles unappropriated retained earnings from beginning to end of year showing distributions and:

- A. Income
- B. Accumulated adjustments
- C. Earnings and profits
- D. Capital changes

78. Schedule M-3 is required for corporations with assets of:
- A. \$10 million or more
 - B. \$5 million or more
 - C. \$50 million or more
 - D. \$25 million or more
79. Controlled group limitations apply to accumulated earnings credit, Section 179, and AMT exemption when applicable which must be divided among members unless:
- A. Equal allocation elected
 - B. All consent
 - C. Unequal allocation elected
 - D. IRS approves
80. Parent-subsidary controlled group requires parent to own 80% of voting power or value with stock ownership determined by value unless election made to use:
- A. Voting power only
 - B. Fair market value
 - C. Book value
 - D. Voting power for all
81. Section 1202 gain exclusion for qualified small business stock requires holding for more than:
- A. 1 year
 - B. 5 years
 - C. 3 years
 - D. 10 years
82. Section 1202 exclusion percentage for stock acquired after September 27, 2010 is:
- A. 50%
 - B. 75%
 - C. 100%
 - D. 60%
83. Section 1244 stock ordinary loss treatment applies to stock issued for money or property up to:
- A. \$1 million
 - B. \$500,000
 - C. \$10 million
 - D. \$5 million
84. Section 1244 ordinary loss limit is \$50,000 for single filers and:

- A. \$50,000 for MFJ
- B. \$75,000 for MFJ
- C. \$25,000 for MFJ
- D. \$100,000 for MFJ

85. Built-in gains tax for S corporations applies at rate of:

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

86. LIFO recapture tax for C to S conversion is paid in:

- A. 4 installments
- B. Lump sum
- C. 2 installments
- D. 10 installments

87. Corporate formation under Section 351 requires property transfer for stock and transferors own 80% immediately after exchange based on voting power and:

- A. Value
- B. Number of shares
- C. Control
- D. Ownership percentage

88. Section 351 boot includes assumption of liabilities exceeding:

- A. Basis
- B. Fair market value
- C. Adjusted basis of property transferred
- D. Stock value

89. Section 358 basis in stock received in Section 351 exchange equals basis of property transferred minus boot received plus gain recognized less:

- A. Liabilities assumed
- B. Cash received
- C. Fair market value
- D. Stock value

90. Section 362 basis to corporation of property received in Section 351 exchange equals transferor's basis plus gain recognized by:

- A. Corporation

- B. Shareholders
- C. Transferor
- D. Transferors

91. Section 1245 recapture applies to gain from disposition of depreciable personal property and is treated as ordinary income to extent of:
- A. Depreciation
 - B. Gain
 - C. Lesser of gain or depreciation
 - D. Basis
92. Section 1250 recapture for real property sold after 1986 applies to additional depreciation which is depreciation exceeding:
- A. Basis
 - B. Straight-line
 - C. Gain
 - D. Fair market value
93. Unrecaptured Section 1250 gain is taxed at maximum rate of:
- A. 20%
 - B. 15%
 - C. 28%
 - D. 25%
94. Section 291 corporate recapture requires corporations to recapture as ordinary income 20% of the lesser of gain or depreciation on:
- A. Real property
 - B. Personal property
 - C. Section 1245 property
 - D. All property
95. Corporate liquidation under Section 331 results in shareholders recognizing gain or loss equal to distribution received less:
- A. Basis
 - B. Stock basis
 - C. E&P
 - D. Fair market value
96. Section 332 liquidation of 80% subsidiary by parent results in nonrecognition of gain or loss to parent and carryover basis in assets unless election made under Section:

- A. 351
- B. 336
- C. 338
- D. 334

97. Section 338(h)(10) election treats qualified stock purchase of S corporation or target subsidiary as asset sale and requires joint election by:

- A. Buyer
- B. Buyer and seller
- C. Seller
- D. Target

98. Employment tax deposits must be made by electronic funds transfer if total taxes in lookback period exceeded:

- A. \$50,000
- B. \$100,000
- C. \$2,500
- D. \$1,000

99. Form 940 for FUTA is filed:

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

100. Form 941 deposits are due next business day if accumulated undeposited taxes exceed \$100,000 or following deposit schedule which is semi-weekly or:

- A. Daily
- B. Monthly
- C. Quarterly
- D. Annually

Part 3: Representation, Practices, and Procedures

1. Circular 230 regulations governing practice before the IRS are issued by:

- A. IRS Commissioner
- B. Congress
- C. Treasury Secretary
- D. Department of Treasury

2. Former IRS employees can enroll without examination after:
 - A. 3 years service
 - B. 5 years service
 - C. 10 years service
 - D. 7 years service

3. Enrolled retirement plan agents practice is limited to:
 - A. All tax matters
 - B. Income tax
 - C. Employee plans under ERISA
 - D. Retirement income

4. AFSP participants complete continuing education of:
 - A. 18 hours annually
 - B. 72 hours per cycle
 - C. 16 hours annually
 - D. 24 hours annually

5. The registered tax return preparer program was discontinued in:
 - A. 2011
 - B. 2012
 - C. 2015
 - D. 2013

6. Unenrolled preparers can represent before revenue agents and:
 - A. Appeals
 - B. Counsel
 - C. Customer service representatives
 - D. Tax Court

7. Limited practice requires preparer to have prepared and:
 - A. Filed return
 - B. Signed return
 - C. Reviewed return
 - D. Supervised preparation

8. Practitioners must promptly advise clients of noncompliance and:
 - A. Consequences
 - B. Report to IRS
 - C. File corrections

D. Withdraw

9. Client records must be returned upon request regardless of:

- A. Payment
- B. Engagement status
- C. Completion
- D. Fees owed

10. Contingent fees are permitted for examinations, claims, and:

- A. Original returns
- B. Routine advice
- C. Judicial proceedings
- D. All services

11. Positions lacking substantial authority must be disclosed unless having at least:

- A. More likely than not
- B. Reasonable basis
- C. Should level
- D. Any support

12. Covered opinions require Section 10.35 compliance and conclusions at:

- A. Reasonable basis
- B. Substantial authority
- C. Should level
- D. More likely than not

13. Written tax advice standards are found in Circular 230 Section:

- A. 10.37
- B. 10.35
- C. 10.34
- D. 10.33

14. Best practices under Section 10.33 are:

- A. Mandatory
- B. Enforceable
- C. Aspirational
- D. Required

15. Unconscionable fees are determined by time, difficulty, and:

- A. Results

- B. Customary charges
- C. Client income
- D. Complexity

16. Prohibited solicitation includes false statements, coercion, and:

- A. Overreaching
- B. Advertising
- C. Direct mail
- D. Networking

17. Conflicts of interest require informed consent that must be:

- A. Verbal
- B. Implied
- C. Documented
- D. Written

18. Federally authorized practitioner privilege applies to tax advice in noncriminal matters before IRS or:

- A. State agencies
- B. Appeals
- C. Federal courts
- D. All courts

19. Practitioner privilege does NOT apply to communications regarding tax shelters or:

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

20. Former government employee restrictions on matters personally participated in are:

- A. Temporary
- B. 5 years
- C. 2 years
- D. Permanent

21. Circular 230 sanctions include censure, suspension, disbarment, and:

- A. Monetary penalties
- B. Criminal charges
- C. License revocation
- D. Imprisonment

22. OPR cases are heard by:
- A. Tax Court
 - B. Appeals
 - C. Administrative Law Judges
 - D. IRS Commissioner
23. Enrolled agent CE requires minimum per year of:
- A. 20 hours
 - B. 16 hours
 - C. 24 hours
 - D. 30 hours
24. Ethics CE for enrolled agents is 2 hours annually totaling per cycle:
- A. 3 hours
 - B. 4 hours
 - C. 8 hours
 - D. 6 hours
25. Enrolled agent enrollment cycle is:
- A. 2 years
 - B. Annually
 - C. 3 years
 - D. 5 years
26. Form 2848 must be signed by:
- A. Taxpayer only
 - B. Representative only
 - C. Both taxpayer and representative
 - D. IRS
27. Form 8821 authorizes receiving information but NOT:
- A. Receiving copies
 - B. Representing taxpayer
 - C. Contacting IRS
 - D. Reviewing account
28. Power of attorney can be limited to specific matters and:
- A. Years
 - B. Forms

- C. Issues
- D. Tax years

29. CAF number links to practitioner record and is used to:

- A. Identify cases
- B. Track authorizations
- C. Link Forms 2848
- D. Create account

30. CAF retention period for Form 2848 is 3 years unless retention box is:

- A. Checked
- B. Initialed
- C. Signed
- D. Dated

31. PTINs must be renewed:

- A. Every 3 years
- B. Every 2 years
- C. Never
- D. Annually

32. Signing preparers must include on returns their PTIN and:

- A. License number
- B. Signature
- C. SSN
- D. EIN

33. Substantial portion threshold is lesser of \$10,000 or:

- A. 5% of gross income
- B. 10% of gross income
- C. 20% of gross income
- D. 25% of gross income

34. Due diligence penalty per failure for covered credits is:

- A. \$100
- B. \$500
- C. \$1,000
- D. \$590

35. Form 8867 retention period is:

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

36. Willful conduct penalty is greater of \$5,000 or:

- A. 50% of income
- B. 75% of income
- C. 100% of income
- D. \$10,000

37. Disclosure penalty maximum per calendar year is:

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

38. Aiding and abetting penalty for corporations is:

- A. \$10,000
- B. \$5,000
- C. \$25,000
- D. \$50,000

39. Six-year assessment statute applies when gross income omitted exceeds 25% or basis overstated by:

- A. Any amount
- B. \$5,000
- C. 25% of basis
- D. 25% or \$5,000

40. Fraud statute burden of proof by clear and convincing evidence is on:

- A. Taxpayer
- B. IRS
- C. Court
- D. Preparer

41. Refund statute limit is tax paid within 3 years plus extension period before claim or:

- A. All tax paid
- B. 6 years
- C. 2 years
- D. 5 years

42. Collection statute suspension adds suspension period plus:
- A. 30 days
 - B. 90 days
 - C. 60 days
 - D. 30-90 days
43. Statute extension Form 872 requires signature by taxpayer and:
- A. IRS
 - B. Revenue agent
 - C. Manager
 - D. Commissioner
44. Mitigation provisions prevent double taxation or:
- A. Double benefit
 - B. Hardship
 - C. Double deduction
 - D. Unfairness
45. Correspondence examinations represent approximately what percentage of exams:
- A. 50%
 - B. 70%
 - C. 25%
 - D. 80%
46. Office examinations typically last:
- A. 1-2 hours
 - B. 1 day
 - C. 3-4 hours
 - D. Half day
47. Field examinations typically last:
- A. Hours
 - B. Months
 - C. 1-2 days
 - D. Days to weeks
48. Audit reconsideration requests are submitted to:
- A. Examination
 - B. Appeals

- C. Campus that conducted audit
- D. Local office

49. Disagreeing with examination without requesting Appeals results in:

- A. Assessment
- B. Statutory notice of deficiency
- C. Collection
- D. Litigation

50. Appeals settlements occur in approximately what percentage of cases:

- A. 90%
- B. 50%
- C. 75%
- D. 60%

51. Statutory notice of deficiency allows 90 days or 150 days if addressed outside U.S. to petition Tax Court or taxpayer must pay and file:

- A. Prepayment review
- B. Deficiency procedure
- C. Appeals review
- D. Refund suit

52. Fast Track Settlement goal is resolution within:

- A. 30 days
- B. 90 days
- C. 60 days
- D. 120 days

53. Fast Track Mediation participation is:

- A. Mandatory
- B. Voluntary
- C. Required
- D. Automatic

54. Arbitration applies to factual issues not law or:

- A. Mixed questions
- B. Interpretation
- C. Application
- D. Policy

55. Small case procedures apply to disputes of \$50,000 or less and decisions are not:
- A. Appealable
 - B. Published
 - C. Binding
 - D. Precedential
56. Small case decisions are designated as:
- A. Regular
 - B. Memorandum
 - C. Summary opinions
 - D. Final
57. Summary opinions are small cases and not appealable or:
- A. Precedential
 - B. Published
 - C. Binding
 - D. Final
58. District Court appeals go to:
- A. Circuit Court
 - B. Tax Court
 - C. Court of Federal Claims
 - D. Supreme Court
59. Court of Federal Claims offers advantage of judges with:
- A. Jury trials
 - B. Specialized expertise
 - C. Quick resolution
 - D. Nationwide jurisdiction
60. Golsen rule creates different results based on taxpayer's residence making choice of residence relevant to litigation strategy to select most favorable:
- A. Precedent
 - B. Judge
 - C. Procedure
 - D. Circuit
61. Supreme Court grants certiorari in approximately what percentage of petitions:
- A. 1%
 - B. 5%

- C. 10%
- D. 25%

62. Principal residence levy requires approval from:

- A. Tax Court
- B. Appeals
- C. Federal court
- D. Magistrate

63. Federal tax lien priority is generally determined by:

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

64. Offer in compromise requires compliance with terms including filing and payment for specified period requiring:

- A. Tax liability
- B. Filing compliance
- C. Payment history
- D. All of these

65. Streamlined installment agreements apply to liabilities of \$50,000 or less requiring payment within:

- A. 24 months
- B. 36 months
- C. 72 months
- D. 60 months

66. Currently not collectible determination is based on:

- A. Payment plan
- B. Hardship
- C. Asset liquidation
- D. Offer amount

67. Collection due process hearing request suspends collection and provides right to contest liability if no prior opportunity plus propose alternatives and decisions are appealable to:

- A. Appeals
- B. Court of Federal Claims
- C. District Court
- D. Tax Court

68. Innocent spouse relief types include traditional innocent spouse, separation of liability, and:
- A. Equitable relief
 - B. Injured spouse
 - C. Partial relief
 - D. Full relief
69. Injured spouse allocation is based on each spouse's:
- A. Income only
 - B. Equal split
 - C. Contribution to refund
 - D. IRS determination
70. Taxpayer Advocate Service assists with economic harm, hardship, and:
- A. All cases
 - B. Systemic problems
 - C. Collections only
 - D. Audits only
71. LITCs provide representation, education, advocacy, and are funded by:
- A. State grants
 - B. Private donations
 - C. Court fees
 - D. IRS grants
72. Whistleblower mandatory awards for qualifying cases range from:
- A. 15-30%
 - B. 10-20%
 - C. 5-15%
 - D. 20-40%
73. Identity theft victims receive Identity Protection PIN and assistance from:
- A. Local office
 - B. Appeals
 - C. Specialized unit
 - D. TAS
74. Taxpayer Bill of Rights includes how many rights:
- A. 5 rights
 - B. 8 rights

- C. 10 rights
- D. 12 rights

75. Publication 1 explains taxpayer rights which total:

- A. 10 rights
- B. 5 rights
- C. 8 rights
- D. 12 rights

76. Examination scope can be specific items or comprehensive based on:

- A. Specific items
- B. IRS discretion
- C. Multiple years
- D. Taxpayer request

77. Protective claims preserve refund rights when circumstances prevent timely filing of complete claim by filing:

- A. Protective claim
- B. Extension
- C. Incomplete claim
- D. Amended return

78. Penalty abatement requires showing ordinary care and prudence but failure due to:

- A. Willful neglect
- B. Lack of funds
- C. Reasonable cause
- D. First time

79. First time abate requires clean history for prior:

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

80. Accuracy-related penalty rate is:

- A. 10%
- B. 20%
- C. 30%
- D. 40%

81. Civil fraud penalty rate is:

- A. 75%
- B. 50%
- C. 100%
- D. 60%

82. Failure to file penalty is per month:

- A. 10%
- B. 1%
- C. 5%
- D. 2%

83. Failure to pay penalty rate per month is:

- A. 0.5%
- B. 0.25%
- C. 1%
- D. 2%

84. Combined failure to file and pay penalty maximum per month is:

- A. 10%
- B. 5%
- C. 7.5%
- D. 4.5%

85. Estimated tax penalty is calculated on:

- A. Quarterly basis
- B. Annual basis
- C. Monthly basis
- D. Semi-annual basis

86. Trust fund recovery penalty for responsible persons equals:

- A. 100%
- B. 50%
- C. 75%
- D. 25%

87. Information return penalty if corrected within 30 days is:

- A. \$60
- B. \$120
- C. \$50

D. \$580

88. Erroneous refund claim penalty rate is:

- A. 10%
- B. 20%
- C. 25%
- D. 30%

89. Frivolous return penalty amount is:

- A. \$1,000
- B. \$10,000
- C. \$5,000
- D. \$2,500

90. Multiple penalties for same conduct result in:

- A. All applicable penalties
- B. Highest penalty
- C. One penalty maximum
- D. Average of penalties

91. Penalty disputes can be appealed to:

- A. Tax Court only
- B. District Court only
- C. No appeal
- D. Appeals Office

92. Penalty abatement can be requested:

- A. Before assessment only
- B. Within 30 days
- C. Any time
- D. Within 2 years

93. Payment designation when multiple liabilities allows:

- A. IRS designation only
- B. Taxpayer designation
- C. Statutory order
- D. Oldest first

94. Partial payment installment agreements are based on:

- A. Full payment required

- B. 50% minimum
- C. Not available
- D. Ability to pay

95. Doubt as to liability offers involve:

- A. Same as collectibility
- B. No offers allowed
- C. Appeals only
- D. Genuine dispute

96. Effective tax administration offers require:

- A. Collectibility based
- B. Not available
- C. Exceptional circumstances
- D. Same criteria

97. Offer processable requirements include filing and:

- A. Payment only
- B. Current compliance
- C. No requirements
- D. Financial disclosure

98. Offer investigation includes financial review, verification, and:

- A. No investigation
- B. Asset verification
- C. Filing review
- D. Third-party contacts

99. Offer acceptance requires compliance with terms for specified period including filing and payment making agreement:

- A. Binding
- B. Unconditional
- C. Temporary
- D. Discretionary

100. Offer default results in:

- A. Renegotiate
- B. Partial reinstatement
- C. Full reinstatement
- D. No consequence

Answer Explanations - Practice Test 8

Part 1: Individuals

1. Correct Answer: A (Earned income plus \$450)

The standard deduction for a dependent is limited to the greater of \$1,300 (for 2024) or the dependent's earned income plus \$450, not to exceed the standard deduction for a non-dependent taxpayer. This formula ensures dependents can offset their earned income with a standard deduction while also providing a minimum deduction for those with little or no earned income. The \$450 addition helps offset investment income up to that amount.

2. Correct Answer: C (Maintaining the home)

To qualify for head of household status, an unmarried taxpayer must pay more than half the cost of maintaining the home for the year. This includes expenses such as rent, mortgage interest, property taxes, insurance, utilities, repairs, and food consumed in the home. The home must be the main home for the taxpayer and a qualifying person (such as a dependent child or parent) for more than half the year, though parents don't need to live with the taxpayer.

3. Correct Answer: B (Single or head of household)

Taxpayers who are divorced or legally separated under a decree of divorce or separate maintenance on the last day of the year are considered unmarried for the entire year. They must file as single, or if they qualify, as head of household. They cannot file as married filing jointly or married filing separately because they are not married on December 31. The last day of the year determines filing status.

4. Correct Answer: A (Previously deducted amounts are recovered)

The tax benefit rule requires taxpayers to include in income amounts recovered in the current year that were deducted in a prior year, but only to the extent the prior deduction provided a tax benefit. For example, if state income taxes were deducted as an itemized deduction in a prior year and a refund is received in the current year, the refund must be included in income to the extent the prior deduction reduced tax liability. If the taxpayer used the standard deduction in the prior year, the refund is not taxable because no tax benefit was received.

5. Correct Answer: D (Transferred to charity without acceptance)

Prizes and awards are generally taxable as ordinary income. However, certain prizes and awards for religious, charitable, scientific, educational, artistic, literary, or civic achievement (like the Nobel Prize) can be excluded from income if the recipient was selected without any action on their part, is not required to render substantial future services, and the prize is transferred directly to a governmental unit or charity designated by the recipient without the recipient ever receiving the funds.

6. Correct Answer: B (Insolvent)

Cancellation of debt (COD) income is generally taxable, but several exclusions exist. The insolvency exclusion allows taxpayers to exclude COD income to the extent they were insolvent (liabilities exceeded assets) immediately before the debt cancellation. Other exclusions include bankruptcy, qualified farm debt, qualified real property business debt, qualified principal residence debt (expired after 2020 but extended periodically), and student loan discharge for certain public service. The exclusion prevents taxing taxpayers who cannot pay.

7. Correct Answer: C (Excluded from income)

Life insurance proceeds paid by reason of the death of the insured are excluded from income under Section 101(a). This is one of the most significant income exclusions in the tax code. The exclusion applies to death benefits paid to beneficiaries in lump sum or installments. Interest earned on proceeds held by the insurance company is taxable. Accelerated death benefits paid to terminally or chronically ill individuals are also excluded.

8. Correct Answer: D (Undergraduate and graduate courses)

Qualified tuition reduction programs allow employees of educational institutions to exclude from income the value of tuition reductions for education at their institution or another institution with a reciprocal agreement. The exclusion covers undergraduate education for the employee, spouse, and dependents. Graduate education is also covered for teaching or research assistants. Graduate education for employees is covered if the education is for teaching or research, but not for other employees unless the tuition reduction was offered before 1996.

9. Correct Answer: A (Excluded from income)

Foster care payments received from a state, political subdivision, or qualified foster care placement agency for caring for qualified foster individuals in the taxpayer's home are excluded from income. The exclusion covers payments for regular foster care, difficulty-of-care payments for individuals with disabilities, and qualified Medicaid waiver payments. The exclusion ensures foster parents aren't taxed on reimbursements for caring for foster children, recognizing the charitable nature of foster care.

10. Correct Answer: D (Self-employment tax)

Ministers' housing allowances (whether cash allowances or the rental value of a home provided) are excluded from income tax to the extent used for housing expenses, but are subject to self-employment tax. Ministers pay self-employment tax on their ministerial earnings including housing allowances, unless they've elected exemption from self-employment tax under Section 1402(e) based on religious opposition to public insurance. This creates a split treatment where housing is tax-exempt for income tax but taxable for SE tax.

11. Correct Answer: B (Partially excluded)

Alaska Native Corporation dividends paid to Alaska Natives or descendants as shareholders are partially excluded from income. The first \$2,000 per year of such dividends (as of 2024) is excluded from gross income under Section 7871(b). This exclusion recognizes the unique status of Alaska Native Corporations established under the Alaska Native Claims Settlement Act to manage land and resources for Alaska Natives. Amounts over \$2,000 are taxable.

12. Correct Answer: C (Excluded from income)

Qualified disaster relief payments are excluded from income under Section 139. This includes payments from government agencies or charitable organizations to individuals affected by federally declared disasters to reimburse or pay for reasonable and necessary personal, family, living, or funeral expenses incurred as a result of the disaster. The exclusion also covers payments for repair or rehabilitation of personal residences or repair/replacement of personal property. This exclusion provides tax relief to disaster victims.

13. Correct Answer: D (\$300)

The educator expense deduction allows eligible educators (teachers, instructors, counselors, principals, or aides who work at least 900 hours during the school year in K-12) to deduct up to \$300 (for 2024, adjusted for inflation) of unreimbursed expenses for books, supplies, equipment, and professional development. If both spouses are educators, they can deduct up to \$300 each (\$600 total) if filing jointly. The deduction is taken as an adjustment to income on Schedule 1.

14. Correct Answer: A (Excluded from employee income)

Employer contributions to employees' Health Savings Accounts are excluded from the employee's gross income and are not subject to income tax withholding or FICA taxes. The contributions are reported on Form W-2 in Box 12 with code W but are not included in wages. This favorable treatment encourages HSA participation. Combined employer and employee contributions cannot exceed the annual HSA contribution limit (\$4,150 for self-only coverage in 2024).

15. Correct Answer: C (Adjustment to income)

The penalty for early withdrawal of savings from time deposits (certificates of deposit) is deducted as an adjustment to income on Schedule 1, not as an itemized deduction. Banks and other financial institutions report the penalty on Form 1099-INT in Box 2. This above-the-line deduction is available even if the taxpayer doesn't itemize deductions. The penalty represents forfeited interest, and the deduction ensures taxpayers aren't taxed on interest they never received.

16. Correct Answer: B (Tax return due date excluding extensions)

IRA contributions for a tax year can be made at any time during the year or by the due date of the tax return for that year (not including extensions). For most taxpayers, this means contributions for 2024 can be made through April 15, 2025. The contribution is designated for the prior year when made between

January 1 and the filing deadline. Extensions don't extend the contribution deadline. This timing allows taxpayers to assess their tax situation before making IRA contributions.

17. Correct Answer: A (\$77,000)

For 2024, the traditional IRA deduction phase-out for single filers covered by a workplace retirement plan begins at approximately \$77,000 of modified adjusted gross income and is completely phased out at \$87,000. For married filing jointly where the IRA contributor is covered by a workplace plan, the phase-out range is approximately \$123,000-\$143,000. These limits are adjusted annually for inflation. Taxpayers not covered by workplace plans can deduct IRA contributions regardless of income.

18. Correct Answer: B (\$146,000)

Roth IRA contribution eligibility begins phasing out at approximately \$146,000 for single filers (complete phase-out at \$161,000) for 2024. For married filing jointly, the phase-out range is approximately \$230,000-\$240,000. These limits are adjusted annually for inflation. Unlike traditional IRAs, there's no age limit for Roth contributions, and contributions aren't deductible but qualified distributions are tax-free. The income limits make Roth IRAs unavailable to high-income taxpayers.

19. Correct Answer: C (Adjustment to income)

Self-employed individuals can deduct health insurance premiums for themselves, their spouses, and dependents as an adjustment to income on Schedule 1, not as an itemized deduction or business expense on Schedule C. The deduction is limited to net self-employment income and isn't available for months when eligible for employer-sponsored coverage. This above-the-line deduction provides parity with employees who receive employer-paid health insurance as a tax-free fringe benefit.

20. Correct Answer: A (Deductible as adjustment to income)

When employees are required to turn over jury duty pay to their employer (because the employer continues paying their salary during jury duty), they can deduct the amount turned over as an adjustment to income on Schedule 1. The jury duty pay is included in income (typically reported on Form 1099-MISC), and the deduction prevents double taxation of the same funds. This adjustment ensures employees aren't taxed on jury pay that went to their employer.

21. Correct Answer: D (\$16,000)

Qualified performing artists can deduct employee business expenses as an adjustment to income (rather than as itemized deductions subject to the 2% floor, which are suspended for 2018-2025) if they meet three tests: (1) performed services as an employee for at least two employers with at least \$200 from each, (2) employee business expenses attributable to performing arts exceed 10% of gross income from performing arts, and (3) adjusted gross income before this deduction doesn't exceed \$16,000. This special deduction recognizes the unique expenses of performing artists.

22. Correct Answer: C (Adjustment to income)

Armed Forces reservists can deduct unreimbursed travel expenses (transportation, meals, and lodging) for traveling more than 100 miles from home to perform reserve duties as an adjustment to income on Schedule 1. The deduction is limited to the regular federal per diem rate (for lodging, meals, and incidental expenses) and the standard mileage rate (for vehicle expenses). This deduction recognizes the unique obligations of reservists who must travel for training and service.

23. Correct Answer: B (One-half of SE tax)

Self-employed individuals can deduct one-half (50%) of their self-employment tax as an adjustment to income on Schedule 1. This deduction provides parity with employees, whose employers pay half of FICA taxes (and deduct that portion as a business expense). The deduction equals one-half of the self-employment tax calculated on Schedule SE. This adjustment ensures self-employed individuals aren't taxed on the "employer" portion of their SE tax.

24. Correct Answer: D (Adjustment to income)

Self-employed individuals who maintain Archer Medical Savings Accounts can deduct contributions to these accounts as an adjustment to income on Schedule 1. Archer MSAs are similar to Health Savings Accounts but were available earlier and are limited to self-employed individuals and employees of small employers. No new Archer MSAs can be established after 2007, but existing accounts can continue. The deduction provides tax benefits similar to HSAs for qualifying individuals.

25. Correct Answer: A (Deductible as adjustment to income)

Penalties imposed by financial institutions for early withdrawal of funds from time deposit savings accounts (certificates of deposit) are deductible as an adjustment to income on Schedule 1. These penalties represent forfeited interest that the taxpayer doesn't actually receive. Financial institutions report the penalty in Box 2 of Form 1099-INT. The adjustment ensures taxpayers aren't taxed on interest they had to forfeit as a penalty, providing accurate income measurement.

26. Correct Answer: D (Amount included in income)

Attorney fees and court costs paid for claims involving unlawful discrimination (employment discrimination, civil rights violations), whistleblower claims, and certain other unlawful practices are deductible as an adjustment to income on Schedule 1. The deduction is limited to the amount of the judgment or settlement included in gross income. This above-the-line deduction ensures plaintiffs aren't taxed on the gross recovery when a portion goes to attorneys, preventing the injustice of taxation on funds never received.

27. Correct Answer: A (7.5%)

Medical expense deductions are allowed only to the extent total qualified medical expenses exceed 7.5% of adjusted gross income. The 7.5% floor was made permanent (previously scheduled to increase to 10%). Qualified medical expenses include payments for diagnosis, cure, mitigation, treatment, or prevention of disease; payments for treatments affecting body structure or function; prescription drugs; insulin; and

medical insurance premiums (if not paid pre-tax). The high floor limits the deduction to those with substantial medical costs.

28. Correct Answer: C (Medically necessary)

Cosmetic surgery or other procedures are deductible as medical expenses only if medically necessary—meaning necessary to ameliorate a deformity arising from congenital abnormality, personal injury from accident or trauma, or disfiguring disease. Elective cosmetic procedures performed solely to improve appearance are not deductible. Examples of deductible procedures include reconstructive surgery after mastectomy or surgery to correct congenital defects. The distinction focuses on medical necessity versus vanity.

29. Correct Answer: B (Age of insured)

Long-term care insurance premium deductions are limited based on the age of the insured at the end of the tax year. For 2024, the limits range from approximately \$470 for individuals age 40 or younger to \$5,880 for those 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. The age-based limits recognize that premiums increase with age.

30. Correct Answer: A (Increase in home value)

Capital expenses for permanent improvements to a home for medical reasons (such as adding ramps, widening doorways, or installing lifts for disabled individuals) are deductible as medical expenses to the extent the cost exceeds the increase in the home's value. If the improvement doesn't increase home value (or increases it less than the cost), the excess is a current medical deduction. If the improvement increases value by the full cost, no current deduction is allowed but the increased basis may benefit the taxpayer on sale.

31. Correct Answer: D (21 cents)

The standard mileage rate for medical purposes (and moving purposes for active duty military) for 2024 is 21 cents per mile. This rate is set annually by the IRS and is lower than the business mileage rate because it's intended to cover only actual costs, not including profit. Taxpayers can deduct medical mileage for transportation to receive medical care for themselves, their spouses, or dependents. Parking fees and tolls are separately deductible in addition to mileage.

32. Correct Answer: C (By taxpayer choice)

Taxpayers can elect to deduct either state and local income taxes OR state and local general sales taxes as an itemized deduction, but not both. Most taxpayers choose income taxes, but those in states with no income tax benefit from deducting sales taxes. The IRS provides optional sales tax tables based on income and family size, or taxpayers can deduct actual sales taxes paid if they maintain records. The election is made annually on Schedule A.

33. Correct Answer: B (Paid)

Real property taxes are deductible as itemized deductions in the year paid, not when assessed or due. Cash-basis taxpayers deduct taxes when actually paid. Property taxes paid through escrow accounts are deductible when the lender pays them from the escrow account, not when the homeowner pays into escrow. Only the portion of the tax that represents tax on real property is deductible; special assessments for improvements (streets, sewers) aren't deductible as taxes.

34. Correct Answer: D (Value of property)

Personal property taxes are deductible only if based on the value of the property and imposed on an annual basis. Many states impose annual taxes on automobiles, boats, or other personal property based on value. Registration fees, license fees, or taxes based on weight, model year, or other criteria aren't deductible. The tax must be ad valorem (based on value) to qualify. Combined with income/sales taxes and real property taxes, total SALT deduction is limited to \$10,000.

35. Correct Answer: A (Deductible subject to income limits)

Mortgage insurance premiums (PMI) are deductible as home mortgage interest, subject to income phase-outs. The deduction phases out ratably between AGI of \$100,000 and \$109,000 (completely phased out above \$109,000) and isn't available for married filing separately. This deduction has expired and been extended multiple times; it must be currently in effect to claim. Qualified mortgage insurance must be in connection with acquisition debt on a qualified residence. The deduction helps homebuyers who can't make 20% down payments.

36. Correct Answer: A (Deductible in year paid)

Points paid on the purchase of a principal residence are fully deductible in the year paid if certain requirements are met: (1) the loan is for the purchase or improvement of the principal residence, (2) paying points is established business practice in the area, (3) points don't exceed amounts generally charged, (4) the taxpayer uses the cash method, (5) points aren't for items usually separately stated (appraisal, title fees), and (6) funds provided by the taxpayer at or before closing equal or exceed points charged. Points meeting these tests are immediately deductible.

37. Correct Answer: C (Amortized over loan term)

Points paid on refinancing a home mortgage must be amortized (deducted ratably) over the life of the loan. For example, \$3,000 in points on a 30-year refinance creates annual deductions of \$100. If the loan is paid off early (through sale or refinancing), remaining unamortized points can be deducted in that year. Points on refinancing used to improve the principal residence may be immediately deductible for the portion allocable to improvements, with the remainder amortized.

38. Correct Answer: D (Taxable investments)

Investment interest expense includes interest paid on money borrowed to purchase property held for investment, such as stocks, bonds, or other taxable investments. It doesn't include interest on loans to purchase tax-exempt securities (which is not deductible), passive activities (subject to passive loss rules),

or principal residences (deductible as home mortgage interest). Investment interest is deductible only to the extent of net investment income, with excess carrying forward indefinitely to future years.

39. Correct Answer: B (\$250 or more)

Cash charitable contributions of \$250 or more require contemporaneous written acknowledgment from the charity to be deductible. The acknowledgment must state the contribution amount, describe any goods or services provided in return, and provide a good faith estimate of the value of such benefits. "Contemporaneous" means obtained by the earlier of the date the return is filed or the due date (including extensions). Canceled checks are sufficient for contributions under \$250 but not for \$250 or more.

40. Correct Answer: D (Fair market value)

Clothing and household items donated to charity are valued at fair market value—the price a willing buyer would pay a willing seller. For used items, this typically means the thrift store value. Items must be in good used condition or better to be deductible (items in poor condition require appraisal if over \$500). Taxpayers can use valuation guides (like those from Salvation Army or Goodwill) to determine reasonable values. Original cost is irrelevant for used property donations.

41. Correct Answer: A (14 cents per mile)

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 taxpayers use their vehicles for charitable volunteer work, such as driving for charitable organizations, attending charitable events, or traveling to provide charitable services. Parking fees and tolls are separately deductible in addition to the mileage rate. The low rate reflects that charitable activity shouldn't generate profit from mileage.

42. Correct Answer: C (Lesser of basis or FMV)

Donations of appreciated property held short-term (one year or less) must be reduced to the lesser of cost basis or fair market value for deduction purposes. This prevents taxpayers from deducting appreciation that would have been ordinary income if the property were sold. For long-term property, taxpayers generally can deduct fair market value (subject to percentage limitations). The rule ensures only long-term appreciation receives favorable treatment, encouraging long-term holding for charitable purposes.

43. Correct Answer: B (\$100 per event plus 10% of AGI)

Personal casualty and theft losses are deductible only if occurring in a federally declared disaster area (for 2018-2025 under TCJA). Each loss event must exceed \$100, and total losses for the year must exceed 10% of adjusted gross income. The \$100 floor applies per casualty event, so multiple events create multiple \$100 reductions. After applying both floors, the excess is an itemized deduction. These high thresholds limit casualty loss deductions to truly catastrophic losses.

44. Correct Answer: A (Discovered)

Theft losses are deductible in the year discovered, not necessarily when the theft occurred or when reported to police. This recognizes that thefts often aren't known immediately when they occur. For federally declared disasters (the only deductible thefts for 2018-2025), discovery is typically when the taxpayer becomes aware of the loss. Expected reimbursements from insurance must reduce the loss; if reimbursement is later determined not to be received, the taxpayer can claim the unreimbursed amount in that later year.

45. Correct Answer: D (Gambling winnings)

Gambling losses are deductible as itemized deductions only to the extent of gambling winnings reported as income for the year. Losses cannot exceed winnings—taxpayers cannot create an overall loss from gambling activities. Professional gamblers report on Schedule C and can deduct losses without this limitation. The restriction prevents casual gamblers from using losses to offset other income while ensuring they pay tax only on net gambling income if they itemize.

46. Correct Answer: C (Not deductible)

Tax preparation fees are not deductible for 2018 through 2025 due to the Tax Cuts and Jobs Act's suspension of miscellaneous itemized deductions subject to the 2% of AGI floor. Before 2018, tax preparation fees were deductible as miscellaneous itemized deductions. After 2025, unless extended, the deduction would return for taxpayers who itemize. Fees for tax advice related to business income can still be deducted as business expenses on the appropriate schedule.

47. Correct Answer: B (17)

The child tax credit is available for qualifying children who are under age 17 at the end of the tax year. The child must be the taxpayer's son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, or descendant of any of them (grandchild, niece, nephew). The child must have a valid Social Security number, be claimed as a dependent, live with the taxpayer for more than half the year (with exceptions), not provide more than half their own support, and be a U.S. citizen, national, or resident alien.

48. Correct Answer: A (\$200,000)

The child tax credit begins phasing out at \$200,000 of modified adjusted gross income for single filers (and \$400,000 for married filing jointly). The credit is reduced by \$50 for each \$1,000 (or fraction thereof) of MAGI exceeding the threshold. This phase-out can completely eliminate the credit for high-income taxpayers. The threshold was significantly increased by the Tax Cuts and Jobs Act, making the credit available to many more middle- and upper-middle-income families than previously.

49. Correct Answer: D (\$500)

The credit for other dependents is \$500 per qualifying dependent who doesn't qualify for the \$2,000 child tax credit. This includes dependents age 17 or older, dependents who don't have Social Security numbers (who have ITINs instead), 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, beginning at \$200,000 for single filers.

50. Correct Answer: C (\$6,000)

The dependent care credit is calculated on qualifying expenses up to \$3,000 for one qualifying individual or \$6,000 for two or more qualifying individuals. Qualifying individuals are children under age 13 or disabled dependents or spouses. The expenses must be for care that allows the taxpayer to work or look for work. The credit percentage ranges from 20% to 35% of qualifying expenses depending on AGI, making the maximum credit \$2,100 ($\$6,000 \times 35\%$) for taxpayers with low AGI.

51. Correct Answer: B (20%)

The dependent care credit percentage is 35% for taxpayers with AGI of \$15,000 or less, decreasing by 1% for each \$2,000 of AGI above \$15,000 until it reaches the minimum of 20% at AGI of \$43,000 or more. This sliding scale targets benefits to lower-income taxpayers. For example, at AGI of \$25,000, the percentage is 30% ($\$10,000$ over $\$15,000 = 5$ increments $\times 1\% = 5\%$ reduction from 35%). The American Rescue Plan temporarily increased these percentages for 2021 only.

52. Correct Answer: D (\$16,810)

The adoption credit for 2024 is approximately \$16,810 per child (adjusted annually for inflation). The credit covers qualified adoption expenses including adoption fees, court costs, attorney fees, traveling expenses, and other directly related expenses. The credit is available for adopting any child under age 18 or a person physically or mentally incapable of self-care. Special needs adoptions qualify for the full credit even if actual expenses are less. The credit significantly offsets adoption costs.

53. Correct Answer: C (\$252,150)

The adoption credit begins phasing out at approximately \$252,150 of modified adjusted gross income for 2024 (adjusted annually for inflation) and is completely phased out at approximately \$292,150. The credit is reduced proportionally within this \$40,000 range. The phase-out is calculated by multiplying the credit by the ratio of excess MAGI over the threshold to the \$40,000 phase-out range. The phase-out limits the credit to low- and middle-income families, though the threshold is relatively high.

54. Correct Answer: C (2441)

Child and dependent care expenses are reported on Form 2441, Child and Dependent Care Expenses. The form calculates the credit by listing qualifying persons, care providers, expenses paid, and applying the appropriate percentage based on AGI. The form also enforces the dollar limits (\$3,000 or \$6,000) and earned income limitations. Information from Form 2441 flows to Schedule 3 and Form 1040. Care providers must be identified with name, address, and taxpayer identification number.

55. Correct Answer: B (Social Security number)

To claim the Earned Income Tax Credit for qualifying children, each child must have a valid Social Security number (SSN) issued before the due date of the return (including extensions). Individual Taxpayer Identification Numbers (ITINs) or other forms of identification don't qualify for EITC purposes. The SSN requirement helps prevent fraudulent EITC claims and ensures qualifying children are authorized to work in the U.S. Adoption Taxpayer Identification Numbers (ATINs) also don't qualify.

56. Correct Answer: A (25)

Taxpayers without qualifying children can claim the Earned Income Tax Credit if they're at least age 25 but under age 65 at the end of the tax year, lived in the U.S. for more than half the year, and meet income requirements. For 2024, the maximum EITC without children is approximately \$632 (much less than with children). The age requirement ensures the credit targets low-income workers of working age, not students or early retirees.

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

The American Opportunity Tax Credit maximum is \$2,500 per eligible student per year, calculated as 100% of the first \$2,000 of qualified education expenses plus 25% of the next \$2,000. Up to \$1,000 (40%) of the credit is refundable. The credit is available for the first four years of post-secondary education for students pursuing a degree or credential and enrolled at least half-time. Income phase-outs apply, limiting the credit to middle-income taxpayers.

58. Correct Answer: C (4 years)

The American Opportunity Tax Credit covers the first four years of post-secondary education. The credit is claimed for expenses paid for academic periods beginning in the tax year for students who haven't completed four years of post-secondary education before the tax year. Students must be enrolled at least half-time for at least one academic period during the year. The four-year limit generally covers a bachelor's degree program, encouraging completion of undergraduate education.

59. Correct Answer: B (20%)

The Lifetime Learning Credit equals 20% of up to \$10,000 in qualified education expenses, for a maximum credit of \$2,000 per tax return (not per student). Unlike the American Opportunity Credit, there's no limit on the number of years the credit can be claimed, it's available for graduate and professional degree courses, and part-time students qualify. The credit is completely nonrefundable. The LLC provides continuing education support throughout a taxpayer's lifetime.

60. Correct Answer: C (\$2,000)

The Lifetime Learning Credit maximum is \$2,000 per tax return (20% of \$10,000 in qualifying expenses), regardless of how many students are in the family. This contrasts with the American Opportunity Credit, which is per student. The LLC can be claimed for one or more students in the same family, but total expenses used for the credit cannot exceed \$10,000, resulting in a \$2,000 maximum credit per return. The per-return limit encourages the AOTC for eligible students.

61. Correct Answer: B (30%)

The energy efficient home improvement credit for 2024 is 30% of qualifying expenditures for improvements to existing homes, including high-efficiency heating and cooling systems, water heaters, biomass stoves, and energy-efficient windows, doors, and insulation. The credit was enhanced and extended by the Inflation Reduction Act. Annual limits apply for certain items. The 30% rate applies through 2032, then decreases to 26% (2033) and 22% (2034).

62. Correct Answer: B (No dollar limit)

The residential energy credit for solar electric property, solar water heating, geothermal heat pumps, fuel cells, small wind energy property, and battery storage technology has no annual or lifetime dollar limit (except for fuel cells, which are limited). The credit is 30% of costs for property placed in service through 2032, then 26% (2033), 22% (2034), and expires after 2034. The unlimited credit strongly incentivizes renewable energy adoption without artificial caps.

63. Correct Answer: A (North America)

The electric vehicle credit requires that the vehicle's final assembly occur in North America (United States, Canada, or Mexico). Additionally, starting in 2023, battery component and critical mineral sourcing requirements phase in, with increasing percentages required to be from North America or free trade agreement countries. MSRP limits apply (\$80,000 for vans, SUVs, and trucks; \$55,000 for other vehicles), as do buyer income limits. The North American assembly requirement encourages domestic manufacturing.

64. Correct Answer: D (\$4,000)

The used electric vehicle credit, available starting in 2023, is the lesser of \$4,000 or 30% of the sale price. To qualify, the vehicle must be at least two years old, sold by a dealer, cost \$25,000 or less, and not have been previously claimed for the used EV credit. The buyer's modified AGI cannot exceed \$75,000 (single), \$112,500 (head of household), or \$150,000 (married filing jointly). The credit encourages used EV purchases for moderate-income buyers.

65. Correct Answer: C (8962)

The premium tax credit is reconciled on Form 8962, Premium Tax Credit (PTC). The form compares advance premium tax credits received during the year (reported on Form 1095-A from the Marketplace) with the actual premium tax credit calculated based on final household income and family size. If advance credits exceeded the actual credit, the excess must be repaid (subject to caps for lower-income taxpayers). If actual credit exceeds advance credits, the difference is refunded. Reconciliation is required for anyone receiving advance credits.

66. Correct Answer: B (400% of poverty line)

Excess advance premium tax credit repayment is capped for taxpayers with household income below 400% of the federal poverty line. The caps range from \$325 for single filers with income under 200% of

poverty to \$2,800 for married filing jointly with income between 300% and 400% of poverty (2024 amounts). Above 400% of poverty, full repayment is required. The caps protect lower-income taxpayers from large repayment obligations when income increases or circumstances change during the year.

67. Correct Answer: D (50%)

The retirement savings contributions credit (Saver's Credit) maximum rate is 50% of qualified contributions (up to \$2,000), resulting in a maximum credit of \$1,000. The rate decreases to 20% or 10% as AGI increases, and the credit is unavailable above certain income thresholds (approximately \$76,500 for married filing jointly in 2024). The credit is nonrefundable. It applies to contributions to IRAs, 401(k)s, 403(b)s, and similar plans, encouraging retirement savings by low- and moderate-income workers.

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

The retirement savings contributions credit applies to qualified contributions up to \$2,000 per individual (\$4,000 for married couples if both qualify). Qualified contributions include traditional and Roth IRA contributions, 401(k) salary deferrals, 403(b) contributions, SIMPLE IRA contributions, and contributions to other qualified plans. The credit is 50%, 20%, or 10% of contributions depending on AGI, providing a maximum credit of \$1,000 per person. The credit incentivizes retirement saving for lower-income workers.

69. Correct Answer: C (1 year)

The foreign tax credit has a 1-year carryback and 10-year carryforward. Unused foreign tax credits arise when the foreign taxes paid or accrued exceed the foreign tax credit limitation (U.S. tax on foreign-source income). The carryback and carryforward rules allow taxpayers to use excess credits in years when they have capacity under the limitation. Credits are carried back one year first, then carried forward up to 10 years. This smooths out year-to-year variations in foreign income and taxes.

70. Correct Answer: B (10 years)

Foreign tax credit carryforwards are allowed for 10 years. Excess foreign tax credits not usable in the current year or carryback year can be carried forward and used in any of the next 10 years, subject to the foreign tax credit limitation in those years. The credits must be used in chronological order (oldest first). After 10 years, unused credits expire and are lost. The lengthy carryforward period provides substantial time to utilize foreign tax credits.

71. Correct Answer: A (1 year)

The general business credit has a 1-year carryback and 20-year carryforward under current law. Previously some general business credits didn't have carrybacks, but the Tax Cuts and Jobs Act established a uniform 1-year carryback for credits arising in 2018 and later. The general business credit includes many component credits like the research credit, work opportunity credit, and disabled access credit. Carrybacks and carryforwards are used in order: carrybacks first, then current year, then carryforwards.

72. Correct Answer: D (20 years)

General business credit carryforwards are allowed for 20 years. This lengthy carryforward period gives businesses substantial time to use credits that can't be used currently due to insufficient tax liability or limitations. Credits are carried forward in chronological order (oldest first). After 20 years, unused credits expire and cannot be used. The 20-year period balances allowing businesses to benefit from earned credits while preventing indefinite carryforwards.

73. Correct Answer: C (15 years)

The first-time homebuyer credit available in 2008 functioned as an interest-free loan that generally had to be repaid over 15 years (1/15 per year for 15 years, starting with the second year after the credit was claimed). The credit was up to \$7,500 (\$8,000 for homes purchased in 2009-2010 under enhanced provisions that didn't require repayment except upon sale within three years). The 2008 credit's repayment requirement was unusual for tax credits.

74. Correct Answer: B (2009-2010)

The Making Work Pay Credit was available for tax years 2009 and 2010 under the American Recovery and Reinvestment Act. The credit was up to \$400 for single filers or \$800 for married filing jointly, calculated as 6.2% of earned income. Most workers received the credit through reduced payroll tax withholding. The credit was designed to provide immediate economic stimulus during the Great Recession by increasing take-home pay. It expired after 2010.

75. Correct Answer: D (110% of prior year tax)

High-income taxpayers (AGI exceeding \$150,000, or \$75,000 for married filing separately) must pay estimated taxes equal to 110% of the prior year's tax liability to meet the safe harbor and avoid underpayment penalties. Regular taxpayers need to pay only 100% of prior year tax or 90% of current year tax. The 110% requirement recognizes that high earners have more resources and capacity for tax planning. This safe harbor provides certainty for estimated tax planning.

76. Correct Answer: A (January)

Individual estimated tax payments are due quarterly on April 15, June 15, September 15, and January 15 of the following year. If the due date falls on a weekend or holiday, the payment is due the next business day. The January payment covers the final quarter (September-December) of the prior year. Taxpayers can avoid making the January payment if they file their tax return and pay all tax owed by January 31.

77. Correct Answer: C (\$1,000)

The underpayment penalty can be avoided if the total tax owed (after subtracting withholding and credits) is less than \$1,000. This de minimis rule recognizes that small underpayments shouldn't trigger penalties. Other ways to avoid the penalty include paying at least 90% of current year tax, at least 100% (or 110% if high income) of prior year tax, or qualifying for a waiver based on reasonable cause. The \$1,000 threshold provides a cushion for minor underpayments.

78. Correct Answer: B (66.67%)

Farmers and fishermen (those with at least two-thirds of gross income from farming or fishing) have a special estimated tax safe harbor: they're exempt from underpayment penalties if they file their tax return and pay all tax owed by March 1 (instead of April 15), or make one estimated tax payment by January 15 for at least 66.67% (two-thirds) of current year tax or 100% of prior year tax. This recognizes seasonal income patterns in farming and fishing.

79. Correct Answer: A (Credit on return)

When an employee works for multiple employers in one year and total wages exceed the Social Security wage base (\$168,600 for 2024), excess Social Security tax is withheld because each employer withholds separately without knowledge of wages from other employers. The employee claims credit for the excess Social Security tax withheld on Schedule 3, which flows to Form 1040. This credit doesn't apply to self-employment tax or when a single employer overwithholds (which the employer must correct).

80. Correct Answer: D (Payment/credit)

Federal income tax withheld from wages is claimed as a payment and credit against tax liability on Form 1040. The withheld amount is reported on Form W-2 and reduces tax owed or increases refund due. Withholding is credited as if paid ratably throughout the year, even though actual withholding may vary by pay period. This "constructive payment" rule affects underpayment penalty calculations, treating withholding as evenly spread throughout the year.

81. Correct Answer: B (3.8%)

The net investment income tax (NIIT) rate is 3.8% of the lesser of net investment income or modified adjusted gross income exceeding threshold amounts (\$200,000 for single filers, \$250,000 for married filing jointly, \$125,000 for married filing separately). Net investment income includes interest, dividends, capital gains, rents, royalties, and passive activity income, minus related expenses. The tax was enacted as part of the Affordable Care Act to help fund Medicare and applies in addition to regular income tax.

82. Correct Answer: C (\$200,000)

The net investment income tax threshold for single filers is \$200,000 of modified adjusted gross income (for 2024 and subsequent years; not indexed for inflation). For married filing jointly, the threshold is \$250,000; for married filing separately, \$125,000. The 3.8% tax applies to net investment income to the extent MAGI exceeds these thresholds. For example, a single filer with \$220,000 MAGI pays NIIT on net investment income up to \$20,000 (the excess over \$200,000).

83. Correct Answer: D (\$200,000)

Additional Medicare tax applies to wages, railroad retirement compensation, and self-employment income exceeding \$200,000 for single filers (and head of household), \$250,000 for married filing jointly, or \$125,000 for married filing separately. The 0.9% additional tax is on amounts exceeding these thresholds. Employers must withhold additional Medicare tax when individual wages exceed \$200,000, regardless of filing status. This can create underwithholding or overwithholding for married couples.

84. Correct Answer: A (0.9%)

The additional Medicare tax rate is 0.9% on wages and self-employment income exceeding threshold amounts (\$200,000 for single filers). This tax is in addition to the regular 1.45% Medicare tax on all wages (2.9% for self-employed). The additional tax has no employer match—it applies only to employees. Combined with regular Medicare tax, high earners pay 2.35% Medicare tax on wages above thresholds (3.8% for self-employed, including the employer-equivalent portion).

85. Correct Answer: B (\$400)

Self-employment tax applies when net earnings from self-employment equal or exceed \$400. This low threshold captures virtually all self-employment income. Below \$400, no self-employment tax is owed and Schedule SE isn't required. The \$400 threshold has remained unchanged for decades. Self-employment tax equals 15.3% (12.4% Social Security + 2.9% Medicare) of 92.35% of net self-employment earnings, with Social Security portion capping at the wage base.

86. Correct Answer: C (\$6,107)

The optional methods for computing self-employment earnings are available when actual net earnings from self-employment are less than \$6,107 (for 2024, adjusted annually for inflation) and less than 72.189% of gross income from self-employment. These methods allow self-employed individuals to pay self-employment tax even when net earnings are low or negative, preserving Social Security coverage and credits. The nonfarm optional method uses two-thirds of gross nonfarm income (up to \$6,107). The farm optional method uses the lesser of two-thirds of gross farm income or \$5,880.

87. Correct Answer: A (5 years)

The nonfarm optional method for computing self-employment earnings can be used in no more than five years (not necessarily consecutive). This limitation prevents indefinite use of the method to artificially increase earnings and Social Security credits. The farm optional method has no such limitation and can be used in any number of years. Both methods allow payment of self-employment tax when net earnings are low, preserving Social Security coverage without requiring profitable operations.

88. Correct Answer: D (\$9,060)

The farm optional method requires gross farm income to be no more than \$9,060 (for 2024, adjusted annually) or actual net farm earnings to be less than \$6,560. Under this method, the taxpayer reports two-thirds of gross farm income (up to \$6,107) as net earnings from farm self-employment. Unlike the nonfarm optional method, the farm method can be used in any number of years without limitation, recognizing the volatility of farm income.

89. Correct Answer: B (H)

Household employment taxes (the "nanny tax") are reported on Schedule H, Household Employment Taxes, which is filed with Form 1040. Schedule H calculates Social Security, Medicare, and federal unemployment (FUTA) taxes for household employees. These taxes apply when household employees

(babysitters, housekeepers, gardeners, etc.) are paid cash wages exceeding threshold amounts (\$2,700 for 2024 for Social Security/Medicare; \$1,000 for FUTA). Schedule H allows household employers to pay these taxes with their income tax rather than making quarterly deposits.

90. Correct Answer: C (\$2,700)

Household employers must provide Form W-2 to household employees who were paid cash wages of \$2,700 or more in 2024 (adjusted annually for inflation) for Social Security and Medicare tax purposes. The threshold for federal unemployment tax is lower (\$1,000 per calendar quarter). Even if wages don't exceed \$2,700, the employer must withhold and pay income tax if the employee requests it and the employer agrees. The W-2 must be provided by January 31.

91. Correct Answer: A (\$2,700)

The household employment tax threshold for 2024 is approximately \$2,700. Household employers must pay Social Security and Medicare taxes (FICA) when they pay cash wages of \$2,700 or more to any household employee during the calendar year. Federal unemployment tax (FUTA) applies if household wages total \$1,000 or more in any calendar quarter. These thresholds are adjusted annually for inflation. The nanny tax ensures household workers have Social Security coverage.

92. Correct Answer: D (Wages from employers who didn't withhold)

Form 8919, Uncollected Social Security and Medicare Tax on Wages, is used by employees whose employers didn't withhold Social Security and Medicare taxes from wages. Common situations include worker misclassification (treated as independent contractor but actually employee) or employer failure to withhold. The form calculates the employee's share (7.65%) of FICA taxes on unreported wages. This ensures employees receive Social Security credits even when employers fail to properly withhold and remit taxes.

93. Correct Answer: C (Adjustment to income in year repaid)

Repayment of supplemental unemployment benefits (SUB pay) previously included in income creates a deduction in the year of repayment. If repayment is \$3,000 or less, it's claimed as an adjustment to income on Schedule 1. If over \$3,000, the taxpayer can choose between an itemized deduction or a credit for tax paid on the repaid amount in prior years (claim of right). The repayment deduction prevents double taxation when benefits must be returned.

94. Correct Answer: B (65)

The disability income exclusion under Section 105(d) applies to individuals who retired on disability before reaching minimum retirement age and who are permanently and totally disabled. The exclusion (limited to \$5,200 or less depending on filing status and AGI) phases out at higher income levels. Permanent and total disability means unable to engage in any substantial gainful activity due to physical or mental condition that has lasted or can be expected to last at least 12 months or result in death. The exclusion recognizes the special needs of disabled individuals.

95. Correct Answer: D (\$96,800)

The interest exclusion for Series EE or I U.S. savings bonds used for qualified higher education expenses begins phasing out at approximately \$96,800 modified AGI for single filers in 2024 (adjusted annually), with complete phase-out at approximately \$111,800. For married filing jointly, the range is approximately \$145,200 to \$175,200. The bonds must be issued after 1989 to taxpayers age 24 or older, and proceeds must be used for tuition and fees (not room and board) at eligible institutions.

96. Correct Answer: A (\$10,000 per year)

Qualified tuition programs (529 plans) can distribute up to \$10,000 per year per beneficiary for K-12 tuition at elementary or secondary public, private, or religious schools. This provision was added by the Tax Cuts and Jobs Act. The \$10,000 is per beneficiary, so multiple children allow multiple \$10,000 distributions. Distributions for K-12 expenses other than tuition (books, computers, room and board) don't qualify for tax-free treatment. The provision expands 529 plan utility beyond college savings.

97. Correct Answer: C (\$2,000)

Coverdell Education Savings Account contributions are limited to \$2,000 per year per beneficiary, regardless of the number of contributors. The contribution limit phases out for high-income taxpayers (\$95,000-\$110,000 for single filers, \$190,000-\$220,000 for married filing jointly). Contributions aren't deductible, but earnings grow tax-free and distributions are tax-free if used for qualified education expenses. Coverdell ESAs can be used for K-12 and college expenses, providing more flexibility than 529 plans for K-12 use.

98. Correct Answer: B (18)

Coverdell ESA beneficiaries must be under age 18 when contributions are made (except for special needs beneficiaries, who have no age limit). Account funds must be distributed by age 30 or transferred to another family member's Coverdell ESA to avoid taxation and penalties. If not used by age 30, the earnings portion is subject to income tax and 10% penalty, and the distribution is deemed to occur on the 30th birthday unless rolled to another beneficiary.

99. Correct Answer: D (Real property)

Section 1031 like-kind exchanges apply only to real property (real estate) held for investment or use in a trade or business, effective for exchanges after December 31, 2017. The Tax Cuts and Jobs Act eliminated personal property from Section 1031 treatment. Both properties exchanged must be like-kind (all real estate is considered like-kind to other real estate) and held for investment or business use, not personal use or dealer inventory. The exchange allows deferral of gain recognition.

100. Correct Answer: A (Realized gain)

Boot (cash or other property that doesn't qualify for like-kind treatment) received in a Section 1031 exchange is recognized (taxable) up to the amount of realized gain. If boot 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 replacement property is adjusted for boot received and gain recognized, preserving deferred gain for future recognition.

Part 2: Businesses

1. Correct Answer: D (Credited to account)

Under the constructive receipt doctrine, cash-method taxpayers must include income in gross income when it is credited to their account, set apart for them, or otherwise made available so they can draw upon it at any time. The taxpayer need not have actual physical possession. Constructive receipt prevents cash-method taxpayers from deferring income by simply not collecting it. Income is constructively received in the tax year when the right to receive it becomes unrestricted, regardless of when actually collected.

2. Correct Answer: A (Received)

Prepaid income for services is generally included in income when received, even for accrual-method taxpayers. This is the "all events test" for income recognition, which is modified for advance payments. However, accrual-method taxpayers can elect to defer certain advance payments for services to the next tax year under Revenue Procedure 2004-34 if the services will be performed by the end of that next year. Cash-method taxpayers include prepaid income when received. This treatment prevents indefinite deferral of advance payments.

3. Correct Answer: C (Completed contract method)

Long-term contracts (generally contracts not completed within the same tax year) must use the percentage of completion method under Section 460, recognizing income and expenses based on the percentage of the contract completed during the year. The completed contract method (recognizing all income and costs upon completion) is generally not allowed except for certain small construction contracts and home construction contracts. The exception for small contractors requires meeting the small business taxpayer exception (\$29 million average gross receipts).

4. Correct Answer: B (Dealer sales)

The installment method of reporting gain is not available for dealer dispositions (sales of inventory or property held for sale to customers in the ordinary course of business) or sales of publicly traded securities. The installment method allows taxpayers to recognize gain as payments are received rather than all at once at the time of sale. It's available for casual sales of personal or real property and sales of property used in a trade or business. Dealers must recognize all gain in the year of sale.

5. Correct Answer: A (Gross profit divided by contract price)

The gross profit percentage in installment sales equals gross profit (sales price minus adjusted basis) divided by contract price (sales price minus liabilities assumed by buyer). This percentage is applied to each payment received to determine the gain recognized in that year. The formula: Gain recognized =

Payment received \times (Gross profit \div Contract price). This method spreads gain recognition over the payment period, matching taxation with cash receipt.

6. Correct Answer: D (In year of sale)

Depreciation recapture (Section 1245 and 1250 recapture) on installment sales must be recognized in full in the year of sale, not spread over the installment payment period. Only the gain exceeding recapture income can be reported on the installment method. This prevents taxpayers from converting ordinary income (recapture) into capital gain through installment reporting. The recapture amount is treated as payment received in the year of sale for purposes of calculating the installment sale gain.

7. Correct Answer: C (Applicable federal rate)

Imputed interest rules under Section 1274 require imputing interest income on seller-financed sales when the stated interest rate is below the applicable federal rate (AFR). The IRS publishes AFRs monthly based on federal borrowing rates. When stated interest is insufficient, interest is imputed, increasing interest income to the seller and interest expense (possibly deductible) to the buyer, while reducing the amount treated as purchase price. This prevents conversion of interest income into capital gain.

8. Correct Answer: A (2 years)

Related party installment sales require both parties to hold the property for at least 2 years to avoid acceleration of the deferred gain. If either party disposes of the property within 2 years (except due to death or involuntary conversion), the original seller must recognize the remaining deferred gain. Related parties include family members and controlled entities. This rule prevents related parties from using installment sales to shift basis without economic substance.

9. Correct Answer: B (Required)

When the market value of inventory falls below cost, the inventory must be written down to the lower market value. This write-down is required under the lower of cost or market valuation method, which applies to most inventory accounting methods (except LIFO). The write-down creates a current deduction, reducing taxable income. The write-down must be based on actual market conditions, not mere estimates. This requirement ensures inventory is not overstated on the balance sheet.

10. Correct Answer: D (Inventory)

The lower of cost or market valuation method applies to inventory held by businesses for sale to customers. Market value is generally replacement cost (but not exceeding net realizable value or below net realizable value minus normal profit margin). Securities held for investment are marked to market if the taxpayer is a dealer or makes a mark-to-market election. Real estate and services don't use lower of cost or market valuation. The method ensures inventory is valued conservatively.

11. Correct Answer: C (Ending inventory less than beginning)

LIFO liquidation occurs when ending inventory quantities are less than beginning inventory, causing older, lower-cost LIFO layers to be matched against current revenues. This creates higher gross profit and taxable income because the older, cheaper inventory is expensed. LIFO liquidations can result from intentional inventory reductions or unintentional shortages. The tax consequences of liquidating LIFO layers can be significant, creating incentives to maintain inventory levels.

12. Correct Answer: B (\$29 million)

UNICAP (uniform capitalization rules) under Section 263A applies to retailers with average annual gross receipts exceeding \$29 million (for the three preceding tax years, adjusted for inflation). Retailers below this threshold are exempt from UNICAP and can expense costs that would otherwise be capitalized. This small business exemption reduces compliance burdens for smaller retailers. Producers remain subject to UNICAP regardless of size, but the threshold exempts small retailers.

13. Correct Answer: A (\$29 million)

Small business taxpayers with average annual gross receipts of \$29 million or less (for the three preceding tax years, adjusted for inflation in 2024) are exempt from several complex accounting rules including UNICAP, percentage of completion method for long-term contracts, and inventory accounting requirements. These taxpayers can use the cash method, treat inventory as non-incidentals and supplies, and avoid capitalization requirements. This significant simplification reduces compliance costs for small businesses.

14. Correct Answer: C (Producers)

Section 263A uniform capitalization rules require producers of real or tangible personal property to capitalize direct costs and allocable indirect costs into inventory or self-constructed assets. Producers include manufacturers, growers, and contractors. Service businesses are generally exempt because they don't produce tangible property. Retailers under the \$29 million threshold are also exempt. UNICAP ensures proper matching of production costs with revenue when inventory is sold or assets are placed in service.

15. Correct Answer: D (Reasonable method)

Mixed service costs (costs that benefit both production and non-production activities, such as human resources, accounting, or general management) must be allocated under UNICAP using any reasonable allocation method. Acceptable methods include ratio of direct labor costs, ratio of gross receipts, square footage, or other methods that reflect the activities' actual benefit from the mixed service costs. The method must be consistently applied and reasonably reflect cost causation.

16. Correct Answer: A (1 year)

Interest capitalization applies to production expenditures for property with a production period exceeding one year and an estimated cost exceeding \$1 million (for real property) or exceeding two years (for certain personal property). The capitalized interest becomes part of the asset's basis and is recovered through

depreciation rather than currently deducted. This requirement matches the cost of financing with the production of the asset, preventing current deduction of costs that benefit future periods.

17. Correct Answer: B (Weighted average rate)

The avoided cost method for capitalizing interest uses the weighted average interest rate on the taxpayer's outstanding debt (other than debt specifically traceable to the production expenditure). Interest on debt specifically incurred to finance production is capitalized at the actual rate on that debt. The avoided cost represents interest the taxpayer would have avoided by not undertaking the production expenditure. This method measures the true financing cost of production.

18. Correct Answer: C (2 years)

Real property has an interest capitalization production period of more than 2 years for certain long-production-period property. Generally, real property requires more than one year production period and estimated cost exceeding \$1 million for interest capitalization to apply. The 2-year period applies to specific long-production-period property definitions. Personal property requires more than two years or one year with cost over threshold amounts.

19. Correct Answer: D (2 years)

Personal property with a production period exceeding 2 years is subject to interest capitalization if it also has an estimated cost exceeding \$1 million. For property with production periods of more than one year but not exceeding two years, interest capitalization applies only if cost exceeds \$1 million. The 2-year threshold identifies truly long-production-period property where interest capitalization is appropriate to match costs with economic benefit periods.

20. Correct Answer: D (Dollar-for-dollar)

The \$5,000 first-year deduction for startup costs is reduced dollar-for-dollar when total startup costs exceed \$50,000. When startup costs reach \$55,000, the entire \$5,000 deduction is eliminated, and all costs must be amortized over 180 months. This phase-out targets the immediate deduction benefit to smaller startups with modest costs. Larger startups must amortize costs from the beginning, reflecting the longer-term benefit of significant startup expenditures.

21. Correct Answer: A (\$50,000)

Organizational costs (costs of creating a corporation or partnership) have a first-year deduction of up to \$5,000, reduced dollar-for-dollar when total organizational costs exceed \$50,000. When costs reach \$55,000, no first-year deduction is available and all costs are amortized over 180 months. This mirrors the startup cost treatment. Organizational costs include legal fees, state incorporation fees, and costs of organizational meetings but not syndication costs or costs of issuing stock.

22. Correct Answer: C (180 months)

Section 195 startup costs exceeding the first-year deduction (\$5,000 reduced by excess over \$50,000) are amortized over 180 months (15 years), beginning with the month business begins. Startup costs include investigating creating or acquiring a business, creating an active business, and pre-opening activities. The 180-month period balances recognizing that startup costs benefit the entire business life against the administrative difficulty of determining actual benefit periods.

23. Correct Answer: B (Not deductible or amortizable)

Syndication costs for partnerships (costs of promoting and marketing partnership interests to investors, such as commissions, professional fees for issuing and marketing interests, and printing costs for offering materials) are neither deductible nor amortizable. They're capitalized but not recovered unless the partnership terminates. This treatment differs from organizational costs (which are amortizable) because syndication costs relate to acquiring capital rather than organizing the partnership entity. The distinction prevents deduction of capital-raising costs.

24. Correct Answer: A (Amortized over 5 years)

Research and experimentation costs under Section 174 must be capitalized and amortized over 5 years (for U.S. research) or 15 years (for foreign research) for amounts paid or incurred in tax years beginning after December 31, 2021. Previously, R&E costs could be currently expensed. The amortization begins at the midpoint of the tax year. This change, part of the Tax Cuts and Jobs Act, generates significant revenue but is controversial for reducing innovation incentives.

25. Correct Answer: D (Experimental/laboratory costs)

Section 174 research and experimentation costs include experimental and laboratory costs, costs of obtaining a patent, and costs of developing prototypes or pilot models. Excluded are ordinary testing or inspection for quality control, efficiency surveys, management studies, consumer surveys, advertising, and research in connection with literary, historical, or similar projects. Land acquisition and depreciable property costs are also excluded. The definition focuses on scientific or technological uncertainty resolution.

26. Correct Answer: C (36 months)

Software development costs can be amortized over 36 months (3 years), beginning with the month the software is placed in service, under Section 167(f). This applies to purchased software or developed software that's not otherwise depreciable or amortizable. Off-the-shelf software costing less than \$100,000 can be expensed currently under de minimis rules. The 36-month period recognizes software's relatively short useful life compared to other intangibles.

27. Correct Answer: A (15 years)

Goodwill acquired in a business acquisition is amortized over 15 years under Section 197, regardless of actual useful life. The amortization is straight-line, beginning with the month of acquisition. Self-created goodwill is not amortizable. The 15-year period was chosen as a compromise between taxpayer desires

for shorter periods and government concerns about overvaluation and premature deductions. The mandatory 15-year period eliminates disputes over goodwill useful life.

28. Correct Answer: B (15 years)

Covenants not to compete acquired in a business acquisition are amortized over 15 years under Section 197, regardless of the actual term of the covenant. Before Section 197, covenants were amortized over their actual terms, creating incentives to negotiate long covenant terms. The 15-year mandatory period eliminates this planning opportunity and prevents disputes about covenant valuation and useful life. The treatment is the same as goodwill because both are Section 197 intangibles.

29. Correct Answer: D (15 years)

Customer lists acquired in connection with a trade or business acquisition are Section 197 intangibles amortized over 15 years. Self-created customer lists are not amortizable. The 15-year period applies regardless of actual expected life or customer turnover. This treatment prevents disputes about customer list valuation and useful life. The requirement to acquire the list in a business acquisition prevents current deduction of costs that create self-created customer relationships.

30. Correct Answer: D (Not amortizable)

Self-created goodwill (value built up through operations, reputation, customer relationships developed internally) is not amortizable because it wasn't acquired in a transaction. Only purchased goodwill acquired in a business acquisition can be amortized over 15 years under Section 197. This distinction prevents businesses from currently deducting costs of building reputation and customer relationships, while allowing recovery of amounts actually paid for these intangibles in acquisitions.

31. Correct Answer: C (Trade or business acquisition)

Section 197 intangibles must be acquired in connection with acquiring a trade or business to qualify for 15-year amortization. Separately acquired intangibles (purchased individually, not as part of a business) don't qualify for Section 197 treatment and are amortized over actual useful life (if determinable) or not at all. The business acquisition requirement ensures Section 197 applies to true business combinations where individual asset values are hard to determine.

32. Correct Answer: B (Remaining legal life)

Patents are amortized over their remaining legal life (or actual useful life if shorter) when purchased separately from a business. Patents acquired in a business acquisition are Section 197 intangibles amortized over 15 years. Self-created patent costs (research costs, legal fees to obtain patent) are generally expensed currently or capitalized and amortized under other rules. The remaining legal life approach for separately purchased patents recognizes the defined statutory protection period.

33. Correct Answer: D (Remaining legal life)

Trademarks acquired separately from a business acquisition are amortized over remaining legal life or actual useful life if determinable. However, if a trademark has indefinite useful life (which is common), it's not amortizable when purchased separately. Trademarks acquired in a business acquisition are Section 197 intangibles amortized over 15 years regardless of actual life. The distinction between purchased separately and acquired in business affects amortization treatment significantly.

34. Correct Answer: C (15 years)

Going concern value (the value of a business as an operating entity above the value of individual assets) is a Section 197 intangible when acquired in a business acquisition, amortized over 15 years. Going concern value is similar to goodwill—it represents the ability of the business to generate income without interruption when transferred. The 15-year mandatory period prevents disputes about whether value should be classified as going concern or goodwill and what the useful life should be.

35. Correct Answer: A (Amortized over 15 years)

Franchise fees paid to acquire a franchise are Section 197 intangibles when acquired in connection with a trade or business, amortized over 15 years. Contingent franchise fees (such as royalties based on revenue) are deductible as paid. The 15-year period applies regardless of the actual franchise term. Renewal fees are similarly amortized over 15 years from the renewal date. This treatment standardizes amortization of franchise costs.

36. Correct Answer: D (Remaining lease term)

Lease acquisition costs (amounts paid to acquire a lease, such as key money or acquisition bonuses) are amortized over the remaining term of the lease at the time the costs are incurred. If the lease has renewal options, the amortization period includes renewal periods if renewal is reasonably certain. This treatment matches the deduction with the lease's economic benefit period. The costs become part of the lease's basis for amortization purposes.

37. Correct Answer: B (Business)

Section 179 property must be used more than 50% for business in the year placed in service to qualify for expensing. If business use is 50% or less, Section 179 is not available and regular depreciation must be used (with business-use limitation for listed property). If property that qualified for Section 179 drops to 50% or less business use in a later year, recapture of the Section 179 deduction occurs. The more-than-50% test ensures the property is predominantly business-use.

38. Correct Answer: C (Taxable income from business)

The Section 179 deduction is limited to taxable income from the active conduct of all trades or businesses. Losses from one business offset income from others, and if the result is zero or negative, no Section 179 deduction is allowed for that year. The limitation prevents Section 179 from creating or increasing net operating losses. Disallowed amounts carry forward indefinitely to future years when business income is available. W-2 wages and investment income don't count toward the limitation.

39. Correct Answer: A (60%)

Bonus depreciation for 2024 is 60% of the cost of qualified property placed in service during the year. The Tax Cuts and Jobs Act provided 100% bonus depreciation for property placed in service from September 27, 2017 through 2022, then phases down: 80% (2023), 60% (2024), 40% (2025), 20% (2026), and 0% (2027 and later). Bonus depreciation applies to new and used qualified property with recovery periods of 20 years or less.

40. Correct Answer: C (15 years)

Qualified improvement property (QIP) placed in service after December 31, 2017, has a recovery period of 15 years using straight-line depreciation. QIP includes improvements to the interior of nonresidential real property placed in service after the building was first placed in service, such as interior walls, ceilings, floors, HVAC, electrical, plumbing, and security systems. A technical error in the Tax Cuts and Jobs Act initially gave QIP a 39-year recovery period, but the CARES Act retroactively corrected this to 15 years effective for property placed in service after 2017. The 15-year period makes QIP eligible for bonus depreciation (since bonus applies to property with recovery periods of 20 years or less), providing significant tax benefits for interior improvements to commercial buildings.

41. Correct Answer: B (39 years)

Nonresidential real property (commercial buildings, office buildings, stores, warehouses) has a Modified Accelerated Cost Recovery System (MACRS) recovery period of 39 years using the straight-line method and mid-month convention. This long recovery period reflects real estate's extended useful life. Residential rental property uses 27.5 years. The 39-year period for nonresidential property recognizes longer economic life and slower obsolescence compared to residential property.

42. Correct Answer: A (7 years)

Office equipment (desks, chairs, file cabinets, office furniture) is 7-year property under MACRS. The recovery period is based on Asset Class 00.11 (Office Furniture, Fixtures, and Equipment). Seven-year property uses 200% declining balance depreciation with half-year or mid-quarter convention. Computers are 5-year property. The 7-year classification for office equipment reflects expected useful life and replacement cycles for office furnishings.

43. Correct Answer: C (5 years)

Computers and peripheral equipment are 5-year property under MACRS, classified in Asset Class 00.12 (Information Systems). This includes hardware, integrated systems, and peripheral equipment. Software is separately amortized over 36 months. The 5-year recovery period reflects computers' relatively short useful life and rapid technological obsolescence. Five-year property uses 200% declining balance depreciation with half-year or mid-quarter convention.

44. Correct Answer: D (15 years)

Land improvements (parking lots, sidewalks, fences, outdoor lighting) are 15-year property under MACRS, classified in Asset Class 00.3. The recovery period uses 150% declining balance with half-year or mid-quarter convention. Land itself is not depreciable. The 15-year period for land improvements reflects their longer useful life compared to personal property but shorter life than buildings. Landscaping costs are sometimes currently deductible as repairs rather than capital improvements.

45. Correct Answer: B (Fourth quarter)

The mid-quarter convention applies when more than 40% of total depreciable property (by basis, not number of items) placed in service during the year is placed in service in the fourth quarter (October-December). When triggered, all property placed in service during the year uses the mid-quarter convention instead of half-year convention. This anti-abuse rule prevents taxpayers from loading up depreciation deductions by purchasing property late in the year. Real property always uses mid-month convention regardless.

46. Correct Answer: C (6,000 pounds)

Luxury automobile depreciation limits apply to passenger automobiles with gross vehicle weight under 6,000 pounds. Vehicles over 6,000 pounds (most SUVs, trucks, vans) are exempt from luxury auto limits but face Section 179 limitations (approximately \$29,200 for 2024 if over 6,000 pounds). The 6,000-pound threshold creates a planning opportunity for businesses to purchase heavier vehicles to avoid the restrictive luxury auto depreciation caps while getting larger first-year deductions.

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

Heavy SUVs and trucks over 6,000 pounds gross vehicle weight are exempt from luxury automobile depreciation limits but Section 179 expensing is capped at approximately \$29,200 (2024, adjusted for inflation). Amounts exceeding this can be depreciated or claimed as bonus depreciation (if available and elected). This limitation prevents businesses from immediately expensing very expensive heavy vehicles, while still allowing more generous deductions than luxury auto limits permit for lighter passenger vehicles.

48. Correct Answer: D (Business)

Listed property (passenger automobiles, computers not used at regular business establishment, and certain other property) must be used more than 50% for qualified business use to avoid restrictive depreciation rules. Business use doesn't include investment use or use as an employee (unless for employer's convenience and required as condition of employment). If business use is 50% or less, straight-line depreciation over ADS life is required, and Section 179 and bonus depreciation are not available.

49. Correct Answer: B (Earned)

Partnership income is taxed to partners when earned by the partnership, regardless of when distributed. This is the "pass-through" nature of partnerships—income, gains, losses, and deductions flow through to partners annually based on their distributive shares. Partners report their shares on their individual returns

whether or not cash is distributed. This prevents deferral through retaining earnings in the partnership and ensures single-level taxation.

50. Correct Answer: A (Liabilities)

Partner basis is increased by the partner's share of partnership liabilities. When partnership liabilities increase (new borrowing), partners' bases increase. When liabilities decrease (debt repayment), bases decrease. This treatment reflects that partners are at risk for partnership debt (for recourse debt) or share in leveraging the partnership (for nonrecourse debt). Basis is also increased by capital contributions and income shares, and decreased by distributions and loss shares.

51. Correct Answer: C (Economic risk of loss)

Recourse debt in partnerships is allocated to the partners who bear the economic risk of loss—those who would be obligated to pay the debt if the partnership couldn't. This is determined through "constructive liquidation" analysis: assuming the partnership's assets become worthless, the partnership is liquidated, and determining who would be required to contribute to satisfy the debt. This allocation ensures basis is given to partners actually at risk for the debt.

52. Correct Answer: D (Profit-sharing ratio)

Nonrecourse debt in partnerships (debt for which no partner bears economic risk of loss) is generally allocated based on the partners' shares of partnership profits. This allocation method reflects that partners share in the benefits of leverage through profit participation. Nonrecourse debt can also be allocated using the "partner's share of minimum gain" or other methods that reflect economic arrangements. The allocation must have substantial economic effect or meet the alternate test.

53. Correct Answer: B (Carryover basis)

A partner's basis in property distributed from a partnership is generally the partnership's basis in the property (carryover basis), subject to limitations. The partner's basis cannot exceed their basis in the partnership interest (reduced by cash received). If multiple properties are distributed, basis is allocated first to unrealized receivables and inventory at partnership basis, then to other properties proportionally. This carryover basis preserves built-in gain or loss for recognition when the partner sells the property.

54. Correct Answer: C (Cash, receivables, or inventory only)

A partner recognizes loss on a liquidating distribution only if the distribution consists solely of cash, unrealized receivables, and inventory, and the total basis of these items is less than the partner's basis in the partnership interest. The loss equals the excess of basis over the sum of cash plus the partnership's basis in the receivables and inventory distributed. Property distributions other than cash, receivables, and inventory prevent loss recognition, preventing artificial loss creation through distributions.

55. Correct Answer: A (Inventory)

Section 751 property (hot assets) includes unrealized receivables (for cash-method taxpayers or certain recapture income) and inventory items substantially appreciated in value. Substantially appreciated means inventory's fair market value exceeds 120% of its adjusted basis to the partnership. When Section 751 property is present, portions of partnership distributions or sales of partnership interests create ordinary income rather than capital gain, preventing conversion of ordinary income into capital gain through distributions or sales.

56. Correct Answer: B (20%)

Inventory is substantially appreciated when its fair market value exceeds adjusted basis by more than 20% (FMV > 120% of basis). This 120% test determines whether inventory is "substantially appreciated" Section 751 property, triggering ordinary income treatment on certain distributions or sales of partnership interests. The 20% threshold identifies significant appreciation that Congress wanted to prevent from being converted to capital gain through partnership transactions designed to change character.

57. Correct Answer: C (Section 444 election made)

Partnership tax years must generally conform to the tax year of majority partners (over 50% interest), or if no majority, to principal partners' year (5%+ partners with same year), or if no principal partners share a year, use the least aggregate deferral year. However, partnerships can use a different tax year by either (1) establishing a business purpose for the different year (obtaining IRS approval through business purpose showing) or (2) making a Section 444 election allowing certain fiscal years (typically resulting in no more than 3 months deferral) with required payments to prevent deferral benefits. The Section 444 election is a specific statutory mechanism allowing deviation from the general conformity rules without proving business purpose, though it requires making required payments under Section 7519.

58. Correct Answer: A (3 months)

A Section 444 election allows partnerships, S corporations, and personal service corporations to elect a fiscal year providing a deferral of not more than 3 months from the required year. For example, a partnership with a required calendar year can elect a year ending September 30, October 31, or November 30. The election requires making "required payments" under Section 7519 to compensate the government for tax deferral. The 3-month limit balances taxpayer convenience against preventing excessive deferral.

59. Correct Answer: C (Section 444 election)

Section 7519 required payments compensate the government for tax deferral created by Section 444 fiscal year elections. The required payment approximates the tax deferral value to partners or S corporation shareholders from having income deferred due to the fiscal year. The payment is calculated based on deferred net income and the highest individual tax rate. The payment is refundable when the fiscal year is terminated or excess payments have been made.

60. Correct Answer: D (General partners)

Partnership self-employment income includes distributive shares and guaranteed payments for general partners. Limited partners' distributive shares are generally not subject to self-employment tax (except guaranteed payments for services, which are self-employment income for all partners). This distinction reflects general partners' active role in management versus limited partners' passive investor role. The classification affects a significant amount of income for professionals using partnerships (law firms, accounting firms).

61. Correct Answer: A (Services compensated first)

In family partnerships where capital is a material income-producing factor, income must be allocated based on capital contributed by each partner. However, when a family member provides substantial or material services to the partnership, those services must be reasonably compensated FIRST before allocating remaining income based on capital. This prevents shifting service income to family members in lower tax brackets through capital allocations. After reasonable compensation for services is paid, the remaining income is allocated based on capital interests. The reasonable compensation requirement under Section 704(e) ensures that family members who work in the partnership receive appropriate compensation for their services rather than having all income allocated as capital income.

62. Correct Answer: A (Nonrecourse debt)

Partnership minimum gain represents the amount of gain that would be recognized if the partnership disposed of property subject to nonrecourse debt for no consideration other than relief from the debt. Partners' shares of minimum gain prevent distributions that would create or increase negative capital accounts attributable to nonrecourse debt. The minimum gain chargeback rules require allocating gain to partners when minimum gain decreases, ensuring partners who received distributions bear the ultimate tax burden.

63. Correct Answer: C (Related party)

Qualified nonrecourse financing for real estate increases a partner's at-risk basis if the debt is from a qualified person (commercial lender or government), secured only by the real property, and represents arm's-length terms. The financing cannot be from sellers or related parties, and the partner cannot be the lender or related to the lender. This exception recognizes that nonrecourse financing is standard and economically sound for real estate, allowing partners to be "at risk" for such debt.

64. Correct Answer: D (15th day of 3rd month of year)

S corporation elections must be filed on Form 2553 by the 15th day of the third month of the tax year for which the election is to take effect. For calendar-year corporations, this is March 15. Late elections are effective for the following year unless the IRS grants relief for reasonable cause. All shareholders must consent to the election. Elections made after the 2½-month deadline but before the return due date may be accepted if reasonable cause is shown.

65. Correct Answer: B (IRS)

S corporation inadvertent terminations (such as exceeding 100 shareholders or issuing prohibited second class of stock) can be waived if the termination was inadvertent, steps are taken within a reasonable time to correct the situation, and the corporation and shareholders agree to make adjustments required by the IRS. The IRS has authority to waive terminations and allow S status to continue or be reinstated, preventing harsh results from technical violations.

66. Correct Answer: C (3 consecutive years)

S corporation elections terminate if the corporation has accumulated earnings and profits from C corporation years AND passive investment income exceeds 25% of gross receipts for three consecutive years. The termination is effective on the first day of the tax year following the third consecutive year. The rule prevents S corporations from being used as personal holding companies. Corporations can avoid termination by distributing E&P or reducing passive income.

67. Correct Answer: A (5 years)

After S corporation election termination (voluntarily or involuntarily), the corporation generally must wait 5 years before re-electing S status without IRS consent. This waiting period discourages casual elections and terminations. The IRS can grant permission to re-elect before 5 years if there was a change in ownership exceeding 50% or the termination was inadvertent. The 5-year rule prevents gaming the system through alternating between C and S status.

68. Correct Answer: D (Distributions and losses)

The Accumulated Adjustments Account (AAA) is decreased by distributions (to the extent of AAA), losses, and deductions (including nondeductible, non-capital expenses that aren't chargeable to basis). AAA is increased by income (other than tax-exempt income). The account can have a negative balance from losses but distributions cannot reduce it below zero. AAA tracks post-S-election earnings that have been taxed but not distributed, determining whether distributions are taxable.

69. Correct Answer: B (Stock basis)

S corporation distributions from AAA are tax-free to the extent of the shareholder's stock basis. Distributions first come from AAA (tax-free to extent of basis), then from accumulated E&P if any (taxable as dividends), then as return of remaining stock basis (tax-free), and finally as capital gain if basis is zero. The ordering ensures earnings already taxed aren't taxed again on distribution, while preserving dividend treatment for C corporation earnings.

70. Correct Answer: A (Debt basis)

S corporation loss limitations are based on stock basis plus debt basis from direct loans from shareholder to corporation. Unlike partnerships, S corporation entity liabilities don't create basis—only direct shareholder loans. Losses first reduce stock basis to zero, then debt basis. When debt basis is reduced by losses, subsequent income must first restore debt basis before being taxable to the shareholder. This creates more restrictive loss limitations than partnerships.

71. Correct Answer: C (\$250,000)

The accumulated earnings tax (penalty tax on unreasonable accumulation of earnings to avoid shareholder dividend tax) provides an accumulated earnings credit of at least \$250,000 for most corporations. Personal service corporations (health, law, accounting, etc.) have a credit of only \$150,000. This credit represents the amount deemed reasonable to accumulate without specific business need justification. Accumulations exceeding the credit require showing reasonable business needs to avoid the 20% penalty tax.

72. Correct Answer: D (\$150,000)

Personal service corporations (corporations substantially all of whose activities involve performing services in health, law, accounting, engineering, architecture, actuarial science, performing arts, or consulting, and substantially all stock owned by employees) have an accumulated earnings credit of \$150,000 (compared to \$250,000 for other corporations). The lower credit reflects that service corporations have less need for large capital accumulations than manufacturing or other capital-intensive businesses.

73. Correct Answer: B (PHC income)

Personal holding company (PHC) tax applies when more than 50% of stock value is owned by five or fewer individuals (ownership test) AND 60% or more of adjusted ordinary gross income is personal holding company income (income test). PHC income includes dividends, interest, rents (unless significant services provided), royalties, and certain other passive income. The tax is 20% on undistributed PHC income, in addition to regular corporate tax.

74. Correct Answer: C (20%)

The personal holding company tax is imposed at 20% on undistributed personal holding company income. This is in addition to the regular 21% corporate income tax rate, creating a combined 41% tax rate (though not technically additive because the PHC tax is on undistributed income after regular tax). The high combined rate encourages distribution of passive income to shareholders rather than accumulation in closely held corporations. Dividends paid deduction can reduce or eliminate PHC tax.

75. Correct Answer: B (2½ months after year-end)

For personal holding company (PHC) purposes, the dividends paid deduction includes dividends paid during the tax year PLUS dividends paid within 2½ months after the close of the tax year (if the corporation elects to treat them as paid on the last day of the tax year). This is called a "consent dividend" or dividends paid after year-end but treated as paid in the prior year. The 2½-month rule allows corporations to reduce PHC tax by making distributions shortly after year-end when they determine their PHC liability. The extended due date is too late—the dividends must be actually paid (or consented to) within 2½ months. This timing rule provides some flexibility while preventing indefinite deferral of distributions.

76. Correct Answer: D (Capital contribution)

Consent dividends are hypothetical dividends that shareholders agree to treat as having been distributed and immediately recontributed as capital. The corporation gets a dividends paid deduction (reducing or eliminating PHC tax or accumulated earnings tax) without actually paying cash. Shareholders report the consent dividend as income and increase stock basis. This mechanism allows corporate tax reduction without cash distribution, useful when corporations want to retain cash for business purposes.

77. Correct Answer: A (Income)

Schedule M-2 for C corporations reconciles unappropriated retained earnings per books from the beginning to the end of the year. It shows the beginning balance, additions (primarily net income per books and other increases), and deductions (primarily distributions to shareholders and other decreases), arriving at the ending balance. The schedule tracks book retained earnings, not tax earnings and profits (E&P), which is tracked separately. Schedule M-2 shows how book income increases retained earnings and how distributions reduce them, providing a complete picture of changes in the corporation's accumulated book earnings during the year.

78. Correct Answer: A (\$10 million or more)

Schedule M-3 (Net Income/Loss Reconciliation for Corporations) is required for corporations with total assets of \$10 million or more (reporting corporations). Schedule M-3 provides much more detailed reconciliation of net income per books with taxable income than Schedule M-1, separating temporary and permanent differences and providing greater transparency. The threshold captures larger corporations where detailed reconciliation provides meaningful information for IRS examination planning.

79. Correct Answer: C (Unequal allocation elected)

Controlled group members must share certain tax benefits including Section 179 expensing limits (\$1,220,000 for 2024 with \$3,050,000 phase-out), accumulated earnings credit (\$250,000 for most corporations, \$150,000 for personal service corporations), and AMT exemption (when applicable). The limits can be allocated among members either equally (each member gets an equal share) or unequally (members agree on different allocations). The default is equal allocation, but members can elect unequal allocation by agreement filed with their returns. All members don't need to consent to unequal allocation—the allocation is made by the group and filed with returns. IRS approval is not required. The allocation flexibility allows groups to direct tax benefits where most beneficial.

80. Correct Answer: A (Voting power only)

Parent-subsidiary controlled groups require the parent to own at least 80% of voting power AND 80% of value of another corporation's stock. Stock ownership is generally determined by both voting power and value. However, Section 1563(f)(5) allows controlled groups to make an election to use voting power only instead of both voting power and value. This election simplifies the determination by eliminating the need to value stock—the test becomes just 80% of voting power. The election must be made by all component members and applies consistently. This voting-power-only election makes controlled group determination more straightforward when stock valuation is difficult or uncertain.

81. Correct Answer: B (5 years)

Section 1202 gain exclusion for qualified small business stock requires holding the stock for more than 5 years. The exclusion percentage depends on acquisition date: 50% for stock acquired before February 18, 2009; 75% for stock acquired February 18, 2009 through September 27, 2010; 100% for stock acquired after September 27, 2010. The C corporation issuing the stock must meet requirements including aggregate gross assets under \$50 million and being engaged in an active trade or business.

82. Correct Answer: C (100%)

Section 1202 provides 100% exclusion of gain from qualified small business stock acquired after September 27, 2010, and held more than 5 years. The excluded gain is limited to the greater of \$10 million or 10 times the stock's adjusted basis. For stock acquired February 18, 2009 through September 27, 2010, the exclusion is 75%. For earlier acquisitions, 50%. The 100% exclusion strongly incentivizes investment in qualifying small businesses.

83. Correct Answer: A (\$1 million)

Section 1244 stock (allowing ordinary loss treatment rather than capital loss) requires the corporation to have received money or property totaling \$1 million or less for stock as a contribution to capital and as paid-in surplus. If the corporation receives more than \$1 million, stock issued for the excess doesn't qualify for Section 1244 treatment. The limitation targets the benefit to truly small business startups. Stock must be issued to individuals for money or property (not services or securities).

84. Correct Answer: D (\$100,000 for MFJ)

Section 1244 ordinary loss treatment is limited to \$50,000 per year for single filers and \$100,000 for married filing jointly. Losses exceeding these limits are treated as capital losses subject to the \$3,000 annual limitation. The ordinary loss treatment allows small business investors to offset failed business investments against ordinary income rather than being limited to capital loss treatment. This significantly benefits investors in small businesses that fail.

85. Correct Answer: B (21%)

The built-in gains tax for S corporations applies at the 21% corporate rate (the C corporation rate). The tax is imposed on recognized built-in gains (appreciation at the time of S election) recognized during the recognition period (5 years after converting from C to S). This prevents C corporations from converting to S status solely to avoid corporate tax on appreciated assets. The tax applies in addition to flow-through of gain to shareholders.

86. Correct Answer: A (4 installments)

LIFO recapture tax arising when a C corporation using LIFO converts to S status is paid in four equal installments. The first installment is due by the due date of the last C corporation return, with subsequent

installments due by the due dates of returns for the following three years. LIFO recapture income equals the excess of FIFO inventory value over LIFO value at the conversion date. The installment payment eases the cash flow burden of paying tax on phantom LIFO reserve income.

87. Correct Answer: A (Value)

Section 351 corporate formation requires transferors of property to control the corporation immediately after the exchange, measured by ownership of at least 80% of voting power AND 80% of the total number of shares of all other classes of stock (by value). The control test has two components: voting power (for voting stock) and value (for all stock including nonvoting). All transferors as a group must meet the 80% test—individual transferors can own less. The "immediately after" requirement uses step transaction doctrine to prevent pre-arranged sales from breaking control. Both voting power and value tests must be satisfied for Section 351 nonrecognition treatment.

88. Correct Answer: C (Adjusted basis of property transferred)

Section 351 boot includes cash and other property (property other than stock of the transferee corporation) received by transferors. Liabilities assumed by the corporation are generally not treated as boot, with an important exception: if the total liabilities assumed exceed the total adjusted basis of all property transferred by a transferor, the excess is treated as boot (gain) to that transferor. This prevents taxpayers from extracting basis tax-free through assumption of liabilities.

89. Correct Answer: A (Liabilities assumed)

The shareholder's basis in stock received in a Section 351 exchange equals the basis of property transferred, minus boot (cash and other property) received, minus liabilities assumed by the corporation, plus gain recognized (including gain from excess liabilities). This formula preserves unrecognized gain or loss in the stock basis for future recognition. The basis mechanics ensure that built-in gain or loss is deferred, not eliminated, by the Section 351 exchange.

90. Correct Answer: D (Transferors)

The corporation's basis in property received in a Section 351 exchange equals the transferor's basis in the property plus gain recognized by the transferor on the exchange (including gain from excess liabilities treated as boot). This carryover basis plus gain recognized preserves built-in gain or loss in the property for the corporation. The corporation steps into the transferor's shoes regarding basis, ensuring built-in gain is recognized eventually when the corporation disposes of the property.

91. Correct Answer: C (Lesser of gain or depreciation)

Section 1245 recapture applies to gain from disposition of depreciable personal property (and certain other property), requiring ordinary income recognition equal to the lesser of (1) gain realized or (2) total depreciation (including Section 179 and bonus depreciation) taken. Any gain exceeding recapture is Section 1231 gain (potentially long-term capital gain). Recapture ensures depreciation deductions that

offset ordinary income are recaptured as ordinary income on disposition, preventing conversion to capital gain.

92. Correct Answer: B (Straight-line)

Section 1250 recapture for real property applies only to additional depreciation—depreciation exceeding what would have been allowed under the straight-line method. For property placed in service after 1986 (when straight-line became mandatory for real property), there is no additional depreciation, so Section 1250 recapture is zero. However, unrecaptured Section 1250 gain (total depreciation, not just excess) is taxed at a maximum 25% rate rather than capital gains rates.

93. Correct Answer: D (25%)

Unrecaptured Section 1250 gain (the portion of gain attributable to straight-line depreciation on real property) is taxed at a maximum rate of 25%, higher than the 0%, 15%, or 20% long-term capital gains rates but lower than ordinary income rates. This intermediate rate applies to all depreciation on real property sold at a gain, even though Section 1250 recapture itself is zero for post-1986 property. The 25% rate applies to individual taxpayers, not corporations.

94. Correct Answer: A (Real property)

Section 291 corporate recapture requires C corporations (not S corporations or individuals) to recapture as ordinary income 20% of the lesser of (1) gain realized or (2) total depreciation taken on Section 1250 property (real property). This "corporate recapture" converts 20% of what would otherwise be capital gain into ordinary income. The recapture is in addition to regular Section 1250 recapture (which is typically zero for post-1986 property). This rule ensures corporations pay some ordinary income tax on real property gains.

95. Correct Answer: B (Stock basis)

Under Section 331 (liquidation of a corporation), shareholders recognize gain or loss equal to the liquidating distribution received minus their stock basis. The gain or loss is generally capital (long-term if stock held over one year). The distribution is treated as payment in exchange for stock, creating a sale or exchange transaction. The liquidation creates two levels of tax: corporate level (gain or loss on distributing appreciated or depreciated property) and shareholder level (on liquidating distribution).

96. Correct Answer: C (338)

Section 332 liquidation of an 80%-or-more owned subsidiary results in nonrecognition of gain or loss to the parent corporation and carryover basis in the subsidiary's assets. However, if a Section 338 election is made (specifically a Section 338(h)(10) election for subsidiaries in consolidated groups or S corporations), the stock acquisition can be treated as an asset acquisition, allowing a step-up in basis to fair market value. The Section 338 election must be made jointly by the parent and subsidiary. This election allows the acquiring corporation to get fair market value basis in subsidiary assets rather than carryover basis, though it triggers immediate tax on the deemed asset sale.

97. Correct Answer: B (Buyer and seller)

A Section 338(h)(10) election for a qualified stock purchase of an S corporation or a target subsidiary in a consolidated group treats the transaction as an asset sale for tax purposes rather than a stock sale. The election requires joint consent of the buyer and the seller (or selling consolidated group). The election allows basis step-up without actual asset sale, but requires the seller to pay tax on the deemed asset sale. This election is common in corporate acquisitions.

98. Correct Answer: A (\$50,000)

Employment tax deposit schedules are determined by the lookback period (the 12-month period ending June 30 of the prior year). If total employment taxes in the lookback period were \$50,000 or less, the employer is a monthly depositor. If total taxes exceeded \$50,000, the employer is a semi-weekly depositor. Regardless of schedule, all employment tax deposits must be made by electronic funds transfer (EFTPS)—there is no paper deposit option. The \$50,000 threshold determines deposit frequency, not whether electronic deposit is required. Additionally, if taxes reach \$100,000 or more on any day, next-day deposit is required regardless of normal schedule.

99. Correct Answer: D (Annually)

Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return, is filed annually for the calendar year. The return is due by January 31 of the following year (or February 10 if all FUTA tax was deposited timely). FUTA tax is 6% on the first \$7,000 of each employee's wages, reduced by credit for state unemployment taxes (typically 5.4%), resulting in a net 0.6% federal rate. Employers must make quarterly deposits if FUTA tax exceeds \$500 per quarter.

100. Correct Answer: B (Monthly)

Form 941 deposit schedules are either monthly or semi-weekly, based on the total tax liability reported in the lookback period (the 12-month period ending June 30 of the prior year). Monthly depositors deposit by the 15th of the following month. Semi-weekly depositors deposit by Wednesday for payments made Saturday through Tuesday, and by Friday for payments made Wednesday through Friday. If accumulated taxes reach \$100,000 or more, next-day deposit is required regardless of schedule.

Part 3: Representation, Practices, And Procedures

1. Correct Answer: D (Department of Treasury)

Circular 230, Regulations Governing Practice Before the Internal Revenue Service, is issued by the Department of Treasury under Title 31 of the Code of Federal Regulations (31 CFR Part 10). While the IRS administers Circular 230 through the Office of Professional Responsibility, the Treasury Department has the authority to issue and amend these regulations. Congress grants this authority through statute, but doesn't issue the regulations itself.

2. Correct Answer: B (5 years service)

Former IRS employees can enroll without examination if they had continuous service for at least 5 years in positions regularly requiring application and interpretation of the tax code and regulations, and they apply within 3 years after separation from IRS employment. This recognizes the expertise gained through substantial IRS experience. The enrollment is conditioned on the IRS employee not having been involved in misconduct and being in good standing at separation.

3. Correct Answer: C (Employee plans under ERISA)

Enrolled retirement plan agents (ERPAs) can practice before the IRS only on matters related to employee plans under ERISA (Employee Retirement Income Security Act). Their practice is limited to Form 5500 series examinations and related retirement plan matters. They cannot represent clients on income tax, estate tax, or other tax matters. This limited enrollment recognizes specialized expertise in retirement plan administration and compliance.

4. Correct Answer: A (18 hours annually)

Annual Filing Season Program (AFSP) participants must complete 18 hours of continuing education annually, including 6 hours of federal tax law updates, 2 hours of ethics, and 10 hours of other federal tax topics. AFSP is a voluntary program providing limited practice rights (similar to unenrolled preparers) to participants who complete the CE. Participants receive a Record of Completion and can represent taxpayers before revenue agents on returns they prepared and signed.

5. Correct Answer: D (2013)

The Registered Tax Return Preparer (RTRP) program was discontinued in 2013 after federal courts ruled the IRS lacked statutory authority to regulate tax return preparers beyond those specifically authorized by Congress (enrolled agents, attorneys, CPAs, enrolled actuaries, enrolled retirement plan agents). The program had required testing and continuing education for all paid preparers. Currently, the IRS can only regulate specific categories of practitioners.

6. Correct Answer: C (Customer service representatives)

Unenrolled return preparers have limited practice authority allowing them to represent taxpayers before customer service representatives, revenue agents, and similar IRS employees during examinations, but only regarding returns or claims for refund they personally prepared and signed. They cannot represent clients before Appeals, Collection, Counsel, or Tax Court. This limited authority recognizes preparers' familiarity with returns they prepared without granting full practice rights.

7. Correct Answer: B (Signed return)

Limited practice authority requires the preparer to have prepared and signed the return or claim for refund. Merely filing, reviewing, or supervising preparation isn't sufficient. The preparer must be the signing preparer (or nonsigning preparer who prepared a substantial portion) and must have actually signed the return. This requirement ensures the preparer has direct knowledge of the return's contents and positions.

8. Correct Answer: A (Consequences)

When practitioners discover client noncompliance or errors, Circular 230 requires them to promptly advise the client of the noncompliance and the consequences of the noncompliance. Practitioners don't report to the IRS, file corrections without authorization, or automatically withdraw. The duty runs to the client. The practitioner should also advise on corrective measures, but the client decides whether to correct the noncompliance.

9. Correct Answer: D (Fees owed)

Practitioners must return client records upon request, regardless of fees owed for work performed. "Client records" include records originally provided by the client and records necessary for the client to comply with federal tax obligations. Practitioners can retain copies and working papers, but cannot hold client records hostage for unpaid fees. This rule ensures clients can meet tax obligations and obtain representation from other practitioners.

10. Correct Answer: C (Judicial proceedings)

Contingent fees are generally prohibited but are permitted for services in connection with (1) IRS examinations or audits of original returns, (2) claims for refund or credit (except for preparing original returns), and (3) judicial proceedings. These exceptions recognize that contingency arrangements are appropriate for dispute resolution where the outcome is uncertain. Preparing original returns for contingent fees remains prohibited.

11. Correct Answer: B (Disclosed)

Tax return positions must have at least reasonable basis (approximately 20% likelihood of success). Positions lacking substantial authority (approximately 40% likelihood) must be disclosed to avoid accuracy-related penalties. Practitioners can take positions with reasonable basis if disclosed, but cannot take positions lacking even reasonable basis. The disclosure requirement (typically using Form 8275) alerts the IRS to the position and protects against penalties.

12. Correct Answer: D (More likely than not)

Covered opinions (opinions on listed transactions, significant purpose transactions, and certain other tax-motivated transactions) require compliance with Section 10.35 of Circular 230 and must reach conclusions at the more likely than not confidence level (over 50%) or higher, or clearly state the practitioner cannot reach that level. These heightened standards for covered opinions reflect their potential for abuse and ensure comprehensive analysis of all significant tax issues.

13. Correct Answer: A (10.37)

Written tax advice standards are found in Circular 230 Section 10.37. These standards require practitioners to base advice on reasonable factual and legal assumptions, reasonably consider all relevant facts, not rely on unreasonable representations, relate applicable law to facts, and not take into account possibility that

returns won't be audited. Section 10.35 covers covered opinions, Section 10.34 covers standards for tax returns, and Section 10.33 covers best practices.

14. Correct Answer: C (Aspirational)

Best practices under Circular 230 Section 10.33 are aspirational guidelines, not mandatory enforceable standards. They recommend practices such as clearly communicating terms of engagement, establishing facts through reasonable inquiry, advising clients of engagement limitations, and identifying and resolving issues. Violations of best practices don't result in discipline. Following best practices helps practitioners avoid problems and provides quality service.

15. Correct Answer: B (Customary charges)

Unconscionable fees are determined based on factors including time required, difficulty of issues, novelty of issues, skill required, and customary charges for similar services. A fee is unconscionable if clearly excessive under these factors. All fee arrangements (hourly, flat, value-based, contingent where permitted) are acceptable if reasonable. Practitioners should communicate fee arrangements clearly and provide fee information in writing upon request.

16. Correct Answer: A (Overreaching)

Solicitation is prohibited if it involves false or misleading communications, coercion, overreaching, or harassing conduct. Truthful advertising, marketing, networking, and targeted outreach are permitted. Overreaching includes excessive pressure or taking advantage of vulnerable persons. Professional solicitation must maintain dignity and accuracy. The prohibition prevents unprofessional conduct while allowing legitimate marketing to attract clients.

17. Correct Answer: D (Written)

Conflicts of interest require informed written consent from all affected clients. The consent must be in writing (not just verbal or implied), and clients must be informed of the conflict and its implications. If the conflict is too severe to cure with consent (direct adversity in same proceeding), the practitioner must decline or withdraw. The written consent requirement ensures clients knowingly agree to representation despite conflicts.

18. Correct Answer: C (Federal courts)

The federally authorized tax practitioner privilege applies to confidential communications between taxpayers and federally authorized tax practitioners (attorneys, CPAs, enrolled agents) regarding tax advice in noncriminal tax matters before the IRS or in federal court proceedings. The privilege doesn't apply to state courts, state agencies, or criminal matters. It's narrower than attorney-client privilege, applying only to tax advice (not return preparation).

19. Correct Answer: B (Criminal matters)

The federally authorized practitioner privilege does NOT apply to written communications regarding tax shelters or criminal tax matters. The privilege also doesn't apply to return preparation, state proceedings, or communications not related to tax advice. These limitations significantly narrow the privilege's scope compared to attorney-client privilege. The exclusion for criminal matters recognizes the government's strong interest in prosecuting tax crimes.

20. Correct Answer: D (Permanent)

Former government employees cannot represent clients on matters in which they personally and substantially participated while government employees. This restriction is permanent for those specific matters. The "revolving door" restriction prevents conflicts of interest and protects government integrity. Former employees can represent clients on other matters not involving their personal substantial participation. The restriction applies regardless of time elapsed since government service.

21. Correct Answer: A (Monetary penalties)

Circular 230 sanctions include censure (public or private reprimand), suspension (prohibition from practice for specified period), disbarment (indefinite prohibition), and monetary penalties. Criminal charges and license revocation are separate matters outside Circular 230. Monetary penalties can be assessed per violation (\$1,000 for practitioners, up to \$50,000 for firms). The sanctions protect taxpayers and tax system integrity by enforcing professional standards.

22. Correct Answer: C (Administrative Law Judges)

Office of Professional Responsibility (OPR) disciplinary cases are heard by Administrative Law Judges (ALJs) in formal proceedings. OPR investigates complaints and prosecutes cases. Practitioners can contest charges before ALJs, who issue decisions. Decisions can be appealed to the Treasury Secretary. This administrative process provides due process while keeping discipline within the executive branch rather than involving Tax Court or other courts.

23. 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 16-hour annual minimum prevents clustering all CE in one year. At least 2 hours annually (6 per cycle) must cover ethics. The CE requirement ensures EAs maintain current knowledge. Failure to meet requirements results in ineligibility for renewal.

24. Correct Answer: D (6 hours)

Ethics continuing education for enrolled agents totals 6 hours per 3-year enrollment cycle, consisting of 2 hours annually. Ethics CE must cover Circular 230 and professional responsibilities. The annual requirement ensures regular updating on professional standards. Ethics courses must be specifically designated as ethics CE by providers. The requirement emphasizes the importance of professional conduct and obligations.

25. Correct Answer: C (3 years)

The enrolled agent enrollment cycle is 3 years. Enrollment is renewed every 3 years upon filing Form 8554 and certifying completion of continuing education requirements (72 hours including 6 hours ethics). The cycle begins when enrollment is granted or renewed. EAs must complete renewal by the enrollment cycle expiration date to avoid lapse of enrollment and practice rights.

26. Correct Answer: C (Both taxpayer and representative)

Form 2848, Power of Attorney and Declaration of Representative, must be signed by both the taxpayer AND the representative. The taxpayer signs Part I granting authority to the representative for specified tax matters and years. The representative signs Part II (Declaration of Representative) certifying they are authorized to represent the taxpayer and are eligible to practice before the IRS (as an attorney, CPA, enrolled agent, or other qualifying practitioner). For joint returns, both spouses must sign if both are granting authority. The dual signature requirement ensures both parties acknowledge the representation relationship and the representative's authority. The IRS does not sign Form 2848—it's an agreement between taxpayer and representative that is filed with the IRS.

27. Correct Answer: B (Representing taxpayer)

Form 8821 authorizes designated persons to inspect and receive confidential tax information but does NOT authorize representing the taxpayer, advocating positions, signing agreements, or binding the taxpayer. It's purely informational access. Form 8821 is useful for allowing accountants, family members, or others to obtain tax information without granting representation authority. For representation, Form 2848 is required.

28. Correct Answer: D (Tax years)

Powers of attorney can be general (all matters, all years) or limited to specific matters, specific tax forms, specific issues, or specific tax years. The scope should match the representation needs. Limiting the POA to specific matters or years protects taxpayer interests by preventing representatives from accessing unrelated information or acting beyond the intended scope. The authorization must clearly state what authority is granted.

29. Correct Answer: C (Link Forms 2848)

The CAF (Centralized Authorization File) number is assigned to practitioners and used to link all Forms 2848 to the practitioner's record. When practitioners file Forms 2848, they provide their CAF number, allowing the IRS to centrally manage all authorizations for that practitioner. The CAF number helps track representation relationships and ensures current authorizations are accessible to IRS personnel working with the taxpayer.

30. Correct Answer: A (Checked)

Forms 2848 remain in the CAF for 3 years from the date recorded, unless earlier revoked or superseded. However, if the retention box is checked on a new Form 2848, prior authorizations are retained rather than

automatically revoked. This allows taxpayers to add representatives without removing existing ones. Without checking the retention box, new Forms 2848 for the same matters revoke prior authorizations.

31. Correct Answer: D (Annually)

Preparer Tax Identification Numbers (PTINs) must be renewed annually. The renewal period opens in mid-October, and PTINs expire December 31. Preparers renew online at IRS.gov and pay a renewal fee. Without a current PTIN, preparers cannot prepare returns for compensation. Annual renewal ensures current contact information and allows the IRS to suspend or revoke PTINs for practitioners ineligible due to conduct issues.

32. Correct Answer: B (PTIN)

Signing preparers (those with primary responsibility for overall substantive accuracy) must sign returns manually or electronically and include their PTIN. The PTIN identifies the preparer for IRS compliance and enforcement. Returns without preparer PTIN signatures can be rejected or subject to processing delays. The PTIN also creates accountability—the signing preparer is subject to preparer penalties for return positions.

33. Correct Answer: C (20% of gross income)

A substantial portion for nonsigning preparers is a schedule or entry affecting tax liability (or refund or credit claimed) of at least the lesser of \$10,000 or 20% of gross income shown on the return (for individual and certain other returns). For business returns, the threshold is \$400,000 or 20% of gross income. The substantial portion test determines when someone assisting with a return is subject to preparer responsibilities and penalties.

34. Correct Answer: D (\$590)

The due diligence penalty for EITC, CTC, ACTC, AOTC, or HOH is \$590 per failure (2024, adjusted for inflation). If a return claims multiple covered items, the penalty is \$590 for each, potentially totaling several thousand dollars for one return. The penalty applies when preparers fail to meet due diligence requirements: completing Form 8867, making reasonable inquiries when information appears incorrect, and maintaining records. The significant penalty encourages careful compliance.

35. Correct Answer: A (3 years)

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

36. Correct Answer: B (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 penalty applies for willful attempts to understate tax or reckless or intentional disregard of rules. The 75% rate (compared to 50% for unreasonable positions) reflects greater culpability. The penalty can accumulate quickly for preparers with systematic violations across multiple returns.

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

The penalty for unauthorized disclosure or use of tax return information is \$250 per disclosure, with a maximum of \$10,000 per calendar year. Criminal penalties (up to \$1,000 fine and 1 year imprisonment) can also apply. The annual cap limits civil penalties while the per-violation amount creates deterrence. These penalties protect taxpayer privacy by discouraging preparers from misusing confidential client information for marketing or other unauthorized purposes.

38. Correct Answer: A (\$10,000)

The aiding and abetting understatement penalty is \$1,000 for individual returns and \$10,000 for corporate returns, per taxpayer per document. This penalty applies to those who aid, assist, procure, advise, or counsel with understatements of tax liability, with knowledge the document will be used for understatement. The higher corporate penalty reflects larger tax amounts typically involved. The penalty deters participation in tax evasion by non-preparers.

39. Correct Answer: D (25% or \$5,000)

The 6-year assessment statute applies when gross income omitted exceeds 25% of gross income shown on the return, or when there's an overstatement of basis in property by more than 25% (\$5,000 threshold also applies in certain cases). The extended statute gives the IRS more time to discover substantial omissions. For basis overstatements, the 25% threshold and \$5,000 amount help identify significant misstatements warranting extended examination period.

40. Correct Answer: B (IRS)

In fraud cases, the burden of proof is on the IRS to establish fraud by clear and convincing evidence (higher than the usual preponderance of evidence standard). The IRS must prove the taxpayer intended to evade tax through intentional wrongdoing. This high standard protects taxpayers from frivolous fraud allegations. Once fraud is proven, there's no statute of limitations on assessment—the IRS can assess tax at any time.

41. Correct Answer: C (2 years)

The refund statute limitation is the later of 3 years from filing or 2 years from payment of tax. Returns filed before the due date are deemed filed on the due date. The refund amount is limited to tax paid within the period used for the claim (3 years before filing or 2 years before payment). This dual limitation ensures adequate time whether taxpayers filed early or paid late.

42. Correct Answer: D (30-90 days)

The collection statute is suspended during various events (offers in compromise, collection due process hearings, bankruptcy, innocent spouse requests, installment agreement requests) and adds the suspension period plus an additional 30 to 90 days. Each suspension extends the 10-year collection period, potentially allowing collection beyond 10 years after assessment. The additional days after suspension ends allow the IRS time to resume collection activities.

43. Correct Answer: A (IRS)

Statute of limitations extensions are made on Form 872 (or similar forms) and must be signed by the taxpayer (or authorized representative with specific authority to extend) and by the IRS. The consent requires mutual agreement—taxpayers aren't required to agree, but refusing may result in immediate assessment. Extensions can be for fixed periods or indefinite, and can cover all issues or specific items.

44. Correct Answer: C (Double deduction)

Mitigation provisions allow adjustments outside the normal statute of limitations to prevent double taxation or double deductions. If an item is adjusted in an open year but the related item is in a closed year, the mitigation rules may allow adjustment in the closed year to achieve equitable results. This prevents taxpayers or the government from benefiting from inconsistent treatment across years when statutes prevent normal correction.

45. Correct Answer: B (70%)

Correspondence examinations conducted entirely by mail represent approximately 70% of all IRS examinations. These exams typically involve straightforward issues like substantiation of deductions, credits, or income items. Taxpayers respond by mail with explanations and supporting documents. No in-person meeting occurs. This high percentage reflects the IRS's limited resources and focus on efficiently examining many returns for common issues.

46. Correct Answer: A (1-2 hours)

Office examinations conducted at IRS offices typically last 1-2 hours, though complex cases may require longer or multiple appointments. Taxpayers or representatives bring records and documentation to the IRS office for review. These exams involve more issues or complexity than correspondence exams but less than field audits. The limited duration reflects the scope of issues examined and the efficiency of in-office review.

47. Correct Answer: D (Days to weeks)

Field examinations conducted at the taxpayer's place of business or representative's office typically last days to weeks, depending on complexity. Revenue agents conduct field audits for complex returns, businesses, or high-income individuals. The examination may span multiple days over several weeks or months. The extended duration reflects comprehensive review of books, records, and business operations requiring substantial time and examination resources.

48. Correct Answer: C (Campus that conducted audit)

Audit reconsideration requests are submitted to the IRS campus that conducted the original audit. Taxpayers request reconsideration when they have additional information not considered originally or when the audit was conducted without their participation (default assessment). The request should include documentation supporting a different result. Reconsideration provides opportunity to present facts and challenge assessments based on new information.

49. Correct Answer: B (Statutory notice of deficiency)

If taxpayers disagree with examination results and don't request an Appeals conference (or can't reach agreement in Appeals), the IRS issues a statutory notice of deficiency (90-day letter). This formal notice gives taxpayers 90 days (150 if addressed outside U.S.) to petition Tax Court. If no petition is filed, the IRS can assess the deficiency and begin collection. The notice provides the last opportunity for prepayment judicial review.

50. Correct Answer: A (90%)

Approximately 90% of cases settle in Appeals without going to litigation. The high settlement rate reflects Appeals' independence from examination, authority to consider hazards of litigation, and skill in facilitating settlements. Most taxpayers and the IRS prefer settling to the time, cost, and uncertainty of litigation. Appeals provides an effective forum for resolving disputes through negotiation and compromise on reasonable terms.

51. Correct Answer: D (Refund suit)

The statutory notice of deficiency provides 90 days to petition Tax Court for prepayment review. If taxpayers don't petition 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. This "pay first" requirement distinguishes refund suits from Tax Court deficiency procedures. The choice between prepayment (Tax Court) and pay-and-sue (refund courts) is strategic.

52. Correct Answer: C (60 days)

Fast Track Settlement aims to resolve cases within 60 days using an Appeals mediator while the case remains in examination. Both the examination team and taxpayer must agree to participate. FTS provides expedited dispute resolution without waiting for formal Appeals referral. The 60-day goal keeps cases moving while providing independent Appeals input. Actual resolution time varies based on case complexity.

53. Correct Answer: B (Voluntary)

Fast Track Mediation participation is voluntary—both the taxpayer and the IRS must agree to participate. FTM is available after the case is referred to Appeals and uses an Appeals mediator to facilitate settlement. The voluntary nature ensures both parties are willing to engage in mediation. The program provides structured facilitation to help parties reach settlement in 40-120 days, faster than traditional Appeals.

54. Correct Answer: D (Policy)

Arbitration in Appeals applies to factual issues, not legal issues or policy issues. When Appeals cannot resolve disputes and both parties agree, an arbitrator (typically a neutral expert) makes a binding determination on factual issues. Legal questions, policy determinations, and mixed questions of law and fact don't qualify for arbitration. The limitation to factual issues recognizes arbitrators' expertise in fact-finding but preserves government authority over legal interpretations and policy.

55. Correct Answer: A (Appealable)

Small case procedures in Tax Court apply to disputes of \$50,000 or less per tax year. Decisions are final and not appealable by either party. This trade-off provides simplified procedures, relaxed evidence rules, informal hearings, and faster resolution in exchange for finality. The decisions have no precedential value and cannot be cited. The \$50,000 limit and non-appealable nature distinguish small cases from regular Tax Court procedures.

56. Correct Answer: C (Summary opinions)

Small case Tax Court decisions are designated as "Summary Opinions" and are final, not appealable, and not precedential. They can't be cited as authority. Summary opinions are issued more quickly than regular decisions. The summary designation alerts readers that the decision has no precedential value and settled a small case under simplified procedures. Regular decisions and memorandum decisions address different types of cases.

57. Correct Answer: A (Precedential)

Summary opinions (small cases) are not appealable, not precedential, and can't be cited as authority. This distinguishes them from Regular decisions (published, precedential, addressing novel issues) and Memorandum decisions (applying established law, not published in official reports but citable). The non-precedential nature of summary opinions reflects the simplified procedures and limited review in small cases.

58. Correct Answer: A (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 Court reviews both legal and factual issues, though it gives deference to factual findings (clear error standard). Legal conclusions are reviewed de novo. The circuit courts create the appeals pathway from District Court toward potential Supreme Court review if certiorari is granted.

59. Correct Answer: B (Specialized expertise)

The Court of Federal Claims offers the advantage of judges with specialized expertise in tax, government contracts, and takings cases. All CFC judges handle these specialized matters, developing expertise beyond what's typical in District Court (where judges handle all types of cases). For complex tax issues, this specialization can be valuable. The CFC sits in Washington DC but hears cases nationwide through judges traveling on circuit.

60. Correct Answer: D (Circuit)

The Golsen rule requires Tax Court to follow the precedent of the Circuit Court where the taxpayer resides (and where appeal would lie), even if Tax Court disagrees. This creates different results for identical facts depending on residence, reflecting circuit splits in tax law. The rule makes circuit choice relevant to Tax Court litigation strategy. Taxpayers in circuits favorable to their position benefit from Golsen, while those in unfavorable circuits may prefer District Court if in a different circuit.

61. Correct Answer: A (1%)

The Supreme Court grants certiorari in approximately 1% of petitions, making Supreme Court review rare and highly selective. The Court grants review for cases involving important legal issues, circuit splits, or conflicts with prior Supreme Court decisions. Most tax cases don't reach the Supreme Court. The low grant rate means most tax law is finally determined by Circuit Courts, creating the importance of circuit precedent.

62. Correct Answer: D (Magistrate)

Principal residence levy requires written approval from a U.S. District Court judge or magistrate. This judicial oversight protects homes from seizure without court approval. The requirement recognizes homes' special status and importance. Other property can generally be levied without court approval after proper notice. The judicial approval requirement ensures IRS collection doesn't improperly deprive taxpayers of their homes.

63. 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 on assessment and demand, but isn't effective against certain creditors and purchasers until Notice of Federal Tax Lien is filed. Priority disputes are complex and consider perfection dates of competing interests. The first-in-time rule creates certainty in determining which creditor has priority.

64. Correct Answer: D (All of these)

Offer in compromise acceptance creates a binding agreement requiring compliance with terms including filing all required returns, paying all taxes for the offer tax year and specified future years (typically 5 years), and making all required estimated tax payments or deposits. Non-compliance with any of these conditions defaults the offer, reinstating the full original liability plus interest. The comprehensive compliance requirements ensure future tax obligations are met.

65. Correct Answer: C (72 months)

Streamlined installment agreements apply to individual liabilities of \$50,000 or less and require full payment within 72 months (6 years). Taxpayers must be current on filing obligations and can't have had installment agreements or offers in compromise in the past 5 years. No financial statement is required. The streamlined process provides quick approval without detailed financial analysis, encouraging voluntary compliance through accessible payment arrangements.

66. Correct Answer: B (Hardship)

Currently not collectible (CNC) status is based on financial hardship—the IRS determines the taxpayer cannot pay any amount because payment would prevent meeting basic necessary living expenses. CNC temporarily suspends collection but doesn't forgive the liability. Interest and penalties continue accruing, and the collection statute continues running. The IRS periodically reviews CNC accounts to determine if circumstances improved allowing collection resumption.

67. Correct Answer: D (Tax Court)

Collection Due Process hearing requests suspend collection and provide rights to challenge the collection action, raise defenses, propose collection alternatives, and contest underlying liability if no prior opportunity. CDP hearing determinations are appealable to Tax Court, providing judicial review of collection decisions. This distinguishes CDP from equivalent hearings (which don't provide Tax Court review). The Tax Court review provides important protection ensuring proper collection procedures.

68. Correct Answer: A (Equitable relief)

Innocent spouse relief types include (1) traditional innocent spouse relief under Section 6015(b), (2) separation of liability relief under Section 6015(c), and (3) equitable relief under Section 6015(f). Equitable relief is available when traditional or separation relief don't apply but considering all facts and circumstances it would be inequitable to hold the requesting spouse liable. The three types provide comprehensive relief framework for different situations.

69. Correct Answer: C (Contribution to refund)

Injured spouse allocation is based on each spouse's contribution to the joint refund, including income earned, withholding, estimated payments, and credits. Form 8379 calculates allocation between spouses. The injured spouse receives their allocated share of the refund, protecting it from offset for the other spouse's separate debt. The contribution-based allocation ensures each spouse receives their fair share of the refund they helped create.

70. Correct Answer: B (Systemic problems)

Taxpayer Advocate Service (TAS) assists taxpayers experiencing economic harm (suffering or about to suffer significant hardship as a result of IRS action or inaction), significant hardship, OR when the IRS hasn't responded through normal channels. Additionally, TAS identifies and addresses systemic problems—issues affecting multiple taxpayers or creating widespread problems in tax administration. The National Taxpayer Advocate reports these systemic issues to Congress annually in the "Purple Book" and "Objectives Report." TAS's dual mission helps individual taxpayers while also identifying and fixing systemic problems that harm many taxpayers, improving overall IRS operations and taxpayer service.

71. Correct Answer: D (IRS grants)

Low Income Taxpayer Clinics provide free or low-cost representation, education, and advocacy, funded by IRS grants but operated independently by law schools, legal aid organizations, and nonprofits. The

grant funding comes from the IRS (authorized by Congress) but clinics maintain independence. This structure ensures access to representation for low-income taxpayers while maintaining clinic autonomy from the IRS they sometimes oppose in representation.

72. Correct Answer: A (15-30%)

Whistleblower mandatory awards for qualifying cases (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 the significance and value of information provided. For smaller cases, discretionary awards up to 15% may be available. The substantial award percentage incentivizes reporting of significant tax noncompliance, benefiting government revenue.

73. Correct Answer: C (Specialized unit)

Identity theft victims receive Identity Protection PINs and assistance from the IRS Identity Theft specialized unit. The unit helps resolve account issues, prevents future fraudulent returns, and provides identity verification procedures. IP PINs allow legitimate taxpayers to e-file while preventing fraudulent returns using stolen identities. The specialized unit provides expertise in handling the complex account issues identity theft creates.

74. Correct Answer: C (10 rights)

The Taxpayer Bill of Rights includes 10 rights: right to be informed, right to quality service, right to pay no more than the correct amount, right to challenge IRS position, right to appeal, right to finality, right to privacy, right to confidentiality, right to representation, and right to a fair and just tax system. These rights codify taxpayer protections and set expectations for IRS conduct. The 10 rights framework ensures comprehensive protection.

75. Correct Answer: A (10 rights)

Publication 1, Your Rights as a Taxpayer, explains the 10 taxpayer rights included in the Taxpayer Bill of Rights. The publication is an important educational resource helping taxpayers understand their rights and IRS obligations. It covers examination, appeals, and collection rights. Publication 1 must be provided at initial contact in examination and collection cases, ensuring taxpayers are informed of their protections.

76. Correct Answer: B (IRS discretion)

Examination scope can be specific items (correspondence exam for particular deductions) or comprehensive (field audit reviewing all aspects of the return), based on IRS discretion and case selection criteria. The IRS determines scope based on examination issues, resources, and compliance objectives. While taxpayers can propose limiting scope, the IRS has broad authority to examine returns to verify accuracy. Exam scope affects burden and duration.

77. Correct Answer: A (Protective claim)

Protective claims preserve refund rights when circumstances prevent timely filing of a complete claim. The protective claim states the refund basis but doesn't quantify the amount (which may be determinable later). This preserves rights while awaiting information or resolution of related matters. Once information is available, the taxpayer files a complete claim. Protective claims prevent loss of refund rights when timing constraints make complete claims impossible.

78. Correct Answer: C (Reasonable cause)

Penalty abatement based on reasonable cause requires showing the taxpayer exercised ordinary business care and prudence but nevertheless failed to comply due to circumstances beyond their control. Reasonable cause is a facts-and-circumstances determination. Examples include serious illness, death, unavoidable absence, destruction of records by casualty, or reliance on competent professional advice. The reasonable cause defense provides fairness when failures aren't due to willful neglect.

79. Correct Answer: D (3 years)

First-time abate penalty relief requires a clean compliance history for the prior 3 years—no penalties assessed in the prior 3 years and current filing and payment compliance. FTA is available for failure-to-file, failure-to-pay, and failure-to-deposit penalties. It's an administrative relief granted without showing reasonable cause. The 3-year clean history requirement rewards prior compliance while providing relief for isolated failures.

80. Correct Answer: B (20%)

The accuracy-related penalty is 20% of the portion of underpayment attributable to negligence, substantial understatement, substantial valuation misstatement, or substantial overstatement of pension liabilities. The 20% rate creates a meaningful deterrent to careless or aggressive positions. The penalty can be avoided by showing reasonable cause and good faith, or through adequate disclosure of positions. The penalty addresses various types of inaccurate reporting.

81. Correct Answer: A (75%)

The civil fraud penalty is 75% of the portion of underpayment attributable to fraud. Fraud requires proving intent to evade tax through intentional wrongdoing, using clear and convincing evidence (higher standard than usual preponderance). The 75% rate (compared to 20% for accuracy-related penalties) reflects the serious nature of intentional fraud. The fraud penalty also opens the assessment statute indefinitely.

82. Correct Answer: C (5%)

The failure-to-file penalty is 5% of unpaid tax per month (or partial month), up to 25% maximum. The penalty encourages filing even when unable to pay. When both failure-to-file and failure-to-pay penalties apply, the failure-to-file penalty is reduced by the failure-to-pay penalty for the same month. The 5% monthly rate creates significant penalty exposure for extended filing delays.

83. Correct Answer: A (0.5%)

The failure-to-pay penalty is 0.5% of unpaid tax per month (or partial month), up to 25% maximum. The rate is reduced to 0.25% per month while an installment agreement is in effect and current. The lower rate (compared to 5% for failure-to-file) recognizes that failure to pay is less serious than failure to file. The penalty continues accruing until the tax is paid or the 25% cap is reached.

84. Correct Answer: B (5%)

When both failure-to-file and failure-to-pay penalties apply, the combined penalty is limited to 5% per month. The failure-to-file penalty (5%) is reduced by the failure-to-pay penalty (0.5%) for the same month, preventing double penalty. This coordination prevents the penalties from compounding to 5.5% monthly. After the failure-to-file penalty reaches its 25% maximum, the failure-to-pay penalty continues at 0.5% monthly until it also reaches 25%.

85. Correct Answer: A (Quarterly basis)

The estimated tax penalty under Section 6654 is calculated on a quarterly basis—separately for each quarterly payment due date (April 15, June 15, September 15, and January 15 of the following year). The penalty is computed for each quarter based on whether the required quarterly payment was made timely and in the correct amount. Underpayment for one quarter can't be offset by overpayment in another quarter. The quarterly calculation means taxpayers with uneven income throughout the year can use the annualized income installment method to reduce penalties by adjusting required payments to match when income was actually received.

86. Correct Answer: A (100%)

The trust fund recovery penalty equals 100% of the unpaid trust fund taxes (income tax withholding, employee Social Security and Medicare). Responsible persons who willfully fail to pay over collected taxes are personally liable. "Responsible" means having authority over financial affairs; "willfully" means knowing of the duty and intentionally failing to perform it or recklessly disregarding it. The 100% penalty ensures collection even when the business can't pay.

87. Correct Answer: A (\$60)

The information return penalty for failure to file correct information returns (Forms W-2, 1099, 1098, etc.) is \$60 per return if the failure is corrected within 30 days of the required filing date (for 2024, adjusted annually for inflation). If corrected after 30 days but by August 1, the penalty is \$120 per return. If corrected after August 1 or not corrected, the penalty is \$310 per return. Intentional disregard results in a minimum penalty of \$630 per return with no maximum. The tiered penalty structure encourages prompt correction—the sooner errors are fixed, the lower the penalty. Annual maximum penalties also apply unless intentional disregard is involved.

88. Correct Answer: B (20%)

The penalty for erroneous claims for refund or credit is 20% of the excessive claim amount. This penalty applies to excessive amounts claimed on refund or credit claims. It deters frivolous or inflated refund

claims while allowing legitimate claims. The 20% rate creates meaningful deterrence. The penalty ensures taxpayers don't claim excessive refunds hoping the IRS won't detect the error.

89. Correct Answer: C (\$5,000)

The frivolous return penalty is \$5,000 for returns based on frivolous positions (tax protester arguments) or designed to delay or impede tax administration. The penalty is in addition to other penalties and can be assessed immediately. Frivolous positions include arguments that taxes are unconstitutional, wages aren't income, or similar discredited claims. The \$5,000 penalty deters tax protester filings that waste IRS resources.

90. Correct Answer: B (Highest penalty)

When multiple penalties could apply to the same conduct or portion of an underpayment, generally only the highest penalty applies—penalties don't stack on the same underpayment. For example, the accuracy-related penalty (20%) and the civil fraud penalty (75%) cannot both apply to the same portion of an underpayment—the fraud penalty (being higher) would apply. However, different penalties CAN apply to different portions of the same return, and procedural penalties (like failure-to-file and failure-to-pay) can apply alongside accuracy penalties because they address different conduct. The general principle prevents duplicative penalties on the same underpayment while allowing penalties for distinct violations.

91. Correct Answer: D (Appeals Office)

Penalty disputes can be appealed to the IRS Appeals Office for independent review. Appeals can consider penalty abatement based on reasonable cause, statutory exceptions, or administrative relief like first-time abate. If Appeals doesn't resolve the dispute, taxpayers can litigate penalties in Tax Court (for deficiency cases) or District Court/Court of Federal Claims (for refund suits after payment). The Appeals process provides opportunity to resolve penalty disputes administratively.

92. Correct Answer: C (Any time)

Penalty abatement can be requested at any time, even after assessment. Taxpayers can request abatement based on reasonable cause, first-time abate, or other grounds. The IRS can abate penalties administratively or through Appeals. There's no time limit for requesting abatement (though refund statute limits may apply to seeking refunds). The ability to request abatement after assessment provides flexibility in penalty relief.

93. Correct Answer: B (Taxpayer designation)

When taxpayers have multiple liabilities and make payments, they can designate how payments are applied to specific tax periods or types. Without designation, the IRS applies payments according to its own procedures (generally oldest liability first). Taxpayer designation allows strategic payment application to minimize interest and penalties. The designation must be made at the time of payment. This control over payment application helps taxpayers manage multiple liabilities.

94. Correct Answer: D (Ability to pay)

Partial payment installment agreements (PPIAs) are based on the taxpayer's ability to pay as determined through financial analysis using Form 433-A (individuals) or Form 433-F (Collection Information Statement). The monthly payment equals the taxpayer's disposable income (income minus necessary living expenses). PPIAs are available when taxpayers cannot pay the full liability within the remaining collection statute. Payments continue until the collection statute expires, potentially resulting in partial forgiveness of remaining balance. There's no 50% minimum or other fixed percentage—the payment is based entirely on financial ability to pay.

95. Correct Answer: D (Genuine dispute)

Doubt as to liability offers in compromise involve genuine disputes about whether the tax is legally owed. This differs from doubt as to collectibility (can't pay full amount). Doubt as to liability applies when there's legitimate disagreement about the existence or amount of the liability. The offer provides an alternative to litigation for resolving liability disputes. Evidence must support the dispute—mere disagreement without substantiation isn't sufficient.

96. Correct Answer: C (Exceptional circumstances)

Effective tax administration (ETA) offers apply when collection wouldn't create hardship but would be unfair or create exceptional circumstances due to public policy or equity considerations. ETA is the most discretionary offer type. Examples include elderly taxpayers with limited income, serious illness, or situations where collection would undermine tax compliance norms. ETA offers are rare and require showing collection would be unconscionable despite ability to pay.

97. Correct Answer: B (Current compliance)

For an offer in compromise to be processable (accepted for consideration), the taxpayer must meet several requirements including: (1) current filing compliance (all required tax returns filed), (2) current payment compliance (estimated tax payments and federal tax deposits current), (3) not in open bankruptcy, (4) application fee paid (\$205 unless low-income waiver), (5) required payment included (20% for lump sum offers, first payment for periodic payment offers), and (6) complete Form 433-A or 433-B financial statement. Meeting these processability requirements doesn't guarantee acceptance—it means the IRS will investigate the offer. Failure to meet processability requirements results in the offer being returned without consideration.

98. Correct Answer: D (Comprehensive review)

Offer investigation includes comprehensive review of financial information, asset verification, income verification, expense analysis, and may include interviews, third-party contacts, and field investigations. The IRS thoroughly examines ability to pay before accepting offers. The comprehensive investigation ensures offers are appropriate and the government isn't compromising collectible liabilities. The process can take months as the IRS verifies all financial information submitted.

99. Correct Answer: A (Binding)

Offer acceptance creates a binding agreement between the taxpayer and the IRS. The agreement requires the taxpayer to comply with all terms including filing and paying taxes for specified future years (typically 5 years). The agreement is enforceable—failure to comply results in default and reinstatement of the full original liability. The binding nature ensures offers create meaningful compliance obligations beyond just paying the offer amount.

100. Correct Answer: C (Full reinstatement)

Offer default (failing to make required payments or comply with filing and payment obligations) results in full reinstatement of the original liability minus any payments made, plus interest from the original assessment date. The entire unpaid balance becomes immediately due and payable. Default also forfeits all payments already made under the offer (they're applied to the liability but don't reduce it dollar-for-dollar). The harsh consequence encourages compliance with offer terms.