PRACTICE EXAM 28: ENROLLED AGENT SEE PART 1 — INDIVIDUALS SIMULATION (100 QUESTIONS)

This simulation exam contains 100 multiple-choice questions modeled on the IRS Special Enrollment Examination (SEE) Part 1 — Individuals. Select the single best answer for each question. Suggested time: 3.5 hours. An answer key with explanations follows the exam.

1. An enrolled agent's status must generally be renewed on a recurring cycle. How often must an enrolled agent generally renew their enrollment?

A. Every year, at the same time as PTIN renewal
B. Every three years, based on the last digit of the enrolled agent's Social Security number
C. Every five years, aligned with the CPA license renewal cycle
D. Only once, since enrollment does not expire once granted

2. An enrolled agent must generally complete a minimum number of continuing education hours during each three-year enrollment cycle. What is this general requirement, including the annual ethics component?

A. 36 hours total, with no annual minimum or ethics requirement
B. 100 hours total, including 10 hours of ethics per year
C. 24 hours total, completed entirely in the final year of the cycle
D. 72 hours total, including 16 hours per year, with 2 hours of ethics annually

3. A practitioner learns that a client failed to comply with a federal tax law in a prior year, resulting in an error or omission on a previously filed return. What does Circular 230 generally require the practitioner to do?

A. Immediately report the client's noncompliance directly to the IRS without informing the client first
B. Take no action, since the practitioner's duty extends only to future returns

C. Advise the client promptly of the fact and consequences of the noncompliance, error, or omission
D. Refuse to prepare any further returns for the client until the issue is resolved

4. A paid preparer transmits a client's return electronically using a five-digit PIN the preparer enters on the taxpayer's behalf after obtaining Form 8879. What e-file signature method does this describe?

A. The Practitioner PIN method
B. The Self-Select PIN method, used only when a taxpayer e-files without a preparer
C. The Electronic Return Originator method, which requires no PIN at all
D. The Modernized e-File method, which uses a digital certificate instead of a PIN

5. A paid preparer fails to provide a copy of the completed return to the taxpayer as required. What penalty exposure does the preparer face under Section 6695?

A. No penalty applies, since furnishing a copy is only a best practice, not a requirement
B. Automatic revocation of the preparer's EFIN, with no separate monetary penalty
C. A penalty applies only if the taxpayer files a formal written complaint
D. A per-failure penalty for failing to furnish the taxpayer a copy of the return

6. A paid preparer receives a client's refund check directly from the IRS and considers endorsing and cashing it on the client's behalf. What does Circular 230 generally say about this practice?

A. This practice is fully permitted as long as the client provides written authorization
B. This practice is permitted only for refunds below a certain dollar threshold
C. A practitioner is generally prohibited from endorsing or otherwise negotiating a client's refund check
D. This practice is permitted only if the preparer immediately forwards the full proceeds to the client

7. A complaint alleges that a practitioner violated a specific provision of Circular 230. Which IRS office generally has jurisdiction to investigate and pursue discipline against the practitioner?

A. The Office of Professional Responsibility (OPR)

B. The Taxpayer Advocate Service
C. The Return Preparer Office, exclusively
D. The IRS Whistleblower Office

8. A representative files multiple powers of attorney for different clients over the years. What number does the IRS assign to track the representative's authorizations across the Centralized Authorization File system?

A. A PTIN
B. A CAF number
C. An EFIN
D. A TIN

9. A taxpayer wants to know how long to retain records supporting the purchase of a stock that may later become a bad debt or worthless security claim. What is the generally recommended retention period for such records, longer than the typical three-year period?

A. Seven years, corresponding to the extended statute of limitations for bad debt and worthless security claims
B. One year, identical to most other supporting documentation
C. Three years, identical to the general assessment statute of limitations
D. There is no benefit to retaining records beyond the year of purchase

10. Under Circular 230, what types of conduct can generally subject a practitioner to censure, suspension, or disbarment from practice before the IRS?

A. Only a criminal conviction for tax fraud, with no other basis for discipline
B. Only a client complaint that is later substantiated by a state licensing board
C. Only a failure to complete continuing education, with no other basis for discipline
D. Incompetence and disreputable conduct, as specifically described in Circular 230

11. A representative's power of attorney authorization for a client's specific tax matter has expired according to its stated period. What is the general effect on the representative's authority?

A. The authorization automatically renews unless the client cancels it in writing
B. The authorization remains valid indefinitely, regardless of any stated period
C. The representative generally loses authority to act for the client on that matter once the authorization period ends
D. The authorization transfers automatically to any other representative at the same firm

12. A preparer wants to use client tax return information to create a database for the preparer's own future marketing purposes, beyond preparing the current return. What must generally be obtained first under Section 7216?

A. No consent is needed, since a preparer may freely use any information gathered while preparing a return
B. The client's knowing, voluntary, and specific written consent to that particular use of their information
C. Only verbal consent is required, since written consent is optional under Section 7216
D. IRS approval, obtained by filing a formal request with the Return Preparer Office

13. A paid preparer completes a client's return but forgets to sign it before it is filed. What is the general consequence under Section 6695?

A. No consequence, as long as the preparer's PTIN still appears on the return
B. Automatic criminal prosecution for filing an unsigned return
C. The return is automatically rejected and cannot be processed under any circumstances
D. A per-return penalty for failing to sign the return as required

14. How long does the authority granted through the Third Party Designee checkbox on Form 1040 generally remain in effect?

A. Indefinitely, until the taxpayer files a future return without checking the box

B. Generally until one year from the original due date of the return, regardless of extensions
C. Only for 30 days after the return is filed
D. Only until the return is accepted by the IRS, whichever comes first

15. Under Circular 230, may a practitioner generally use a former client's confidential information as the basis for a new advertisement soliciting other clients?

A. Yes, without restriction, once the client relationship has formally ended
B. Yes, but only if the former client is named directly in the advertisement
C. No, since Circular 230 generally requires practitioner communications to protect client confidentiality and avoid deceptive practices
D. Yes, but only for advertisements distributed exclusively by mail

16. As a general rule of thumb, how long should an individual taxpayer generally keep copies of filed tax returns and supporting records, absent special circumstances such as a bad debt claim?

A. At least three years, matching the general IRS assessment statute of limitations
B. Exactly one year, since records become irrelevant after that time
C. Indefinitely, with no shorter period ever being sufficient
D. Only until the refund, if any, has been received

17. A member of the U.S. Armed Forces serves in a designated combat zone during the year. How is military pay earned while serving in that combat zone generally treated?

A. Fully taxable, identical to pay earned outside a combat zone
B. Excluded only if the service member is also awarded a combat-related medal
C. Excluded from gross income, subject to certain limits for commissioned officers
D. Taxable only to the extent it exceeds the service member's base pay

18. A taxpayer licensed as a foster care provider receives qualified payments from a state agency for the care of a foster child placed in the home. How are these qualified foster care payments generally treated?

A. Excluded from gross income, up to the applicable per-child limits

B. Fully taxable as self-employment income subject to self-employment tax

C. Fully taxable as wages, since foster care is treated as an employment relationship

D. Excluded only if the foster child is later formally adopted by the taxpayer

19. A taxpayer receives a qualified disaster relief payment from a government agency to cover reasonable and necessary personal, family, living, or funeral expenses following a federally declared disaster. How is this payment generally treated?

A. Fully taxable as ordinary income, since government payments are generally not excludable

B. Excluded only if the taxpayer also itemizes deductions for the same disaster

C. Taxable only above a set annual dollar threshold

D. Excluded from gross income under Section 139, to the extent not otherwise compensated by insurance

20. A beneficiary receives a lump-sum payment of life insurance proceeds following the death of the insured. How is this payment generally treated for federal income tax purposes?

A. Fully taxable as ordinary income to the beneficiary in the year received

B. Excluded from the beneficiary's gross income

C. Taxable only to the extent the proceeds exceed the total premiums the insured paid

D. Excluded only if the beneficiary is the insured's spouse

21. A terminally ill policyholder receives accelerated death benefits from a life insurance policy before death, based on a physician's certification of a limited life expectancy. How are these benefits generally treated?

A. Fully taxable as ordinary income in the year received

B. Excluded from gross income, similar to ordinary life insurance death proceeds

C. Taxable only to the extent the benefits exceed the policy's cash surrender value

D. Excluded only if the policyholder is also receiving Social Security disability benefits

22. An employee injured on the job receives workers' compensation benefits under a state workers' compensation act. How are these benefits generally treated for federal income tax purposes?

A. Fully taxable as wages, since the payments replace lost work income
B. Taxable only to the extent the benefits exceed the employee's regular salary
C. Excluded from gross income
D. Excluded only if the employee is unable to return to work permanently

23. A taxpayer receives a court settlement that includes a specifically allocated amount compensating for medical expenses related to a physical injury. How is this specific medical expense portion generally treated?

A. Excluded from gross income, as part of the general physical injury damages exclusion
B. Fully taxable, since only punitive damages are ever excluded from a settlement
C. Excluded only if the taxpayer did not previously deduct any of those medical expenses
D. Taxable only to the extent the medical expenses were paid to an out-of-network provider

24. A taxpayer receives a monetary award from the IRS Whistleblower Office for information that led to the collection of unpaid taxes from another party. How is this award generally treated?

A. Excluded entirely, since it originates from a government enforcement action
B. Taxable only to the extent the award exceeds the whistleblower's original tax liability
C. Excluded up to a set annual dollar limit, with any excess taxable
D. Fully taxable as ordinary income to the whistleblower

25. An employee receives employer stock subject to a substantial risk of forfeiture, meaning the employee must forfeit the stock back to the employer if certain conditions are not met. Absent a special election, when is this stock generally taxable to the employee?

A. Immediately upon receipt, regardless of any forfeiture risk
B. When the stock is no longer subject to a substantial risk of forfeiture, generally when it vests
C. Never, since forfeitable property is permanently excluded from taxation

D. Only when the employee formally elects to recognize the income

26. A taxpayer surrenders a permanent life insurance policy for its cash surrender value, which exceeds the total premiums the taxpayer paid into the policy. How is the excess generally treated?

A. Taxable as ordinary income, to the extent the cash surrender value exceeds the taxpayer's basis in the policy
B. Fully excluded, since life insurance proceeds are always tax-free
C. Taxable as capital gain, regardless of the taxpayer's basis in the policy
D. Fully taxable, including the return of the taxpayer's own premiums paid

27. A taxpayer exchanges an existing life insurance policy for a new annuity contract, without receiving any cash in the transaction. How is this exchange generally treated?

A. As a fully taxable sale, with gain recognized immediately on the exchange
B. As a tax-free exchange, but only if both contracts are issued by the same insurance company
C. As a nondeductible personal transaction with no tax consequences to track
D. As a tax-free exchange under Section 1035, deferring any gain in the original contract

28. A taxpayer holds a tax-exempt municipal bond originally issued at a discount. How is the annual accretion of original issue discount on this tax-exempt bond generally treated?

A. Fully taxable as ordinary income each year, identical to taxable bond OID
B. Fully taxable only in the year the bond is sold or matures
C. Not taxable as income, but it increases the taxpayer's basis in the bond each year
D. Ignored entirely, with no effect on the bond's basis at any point

29. An employee receives restricted stock subject to a substantial risk of forfeiture and wants to be taxed on the stock's value now, at its low current value, rather than later when it vests at a potentially higher value. What must the employee generally do, and by when?

A. Nothing is required; the employee is automatically taxed at receipt
B. File a Section 83(b) election with the IRS within 30 days of receiving the restricted property
C. File the election within one year of receiving the restricted property
D. Wait until the property vests, since no earlier election is available

30. A company grants employees stock options that qualify under specific Code requirements, such as incentive stock options, as opposed to options that do not meet those requirements. What is the general term for options that do meet these specific Code requirements?

A. Nonstatutory stock options
B. Restricted stock units
C. Statutory stock options
D. Phantom stock awards

31. An employee receives sick pay benefits under a short-term disability plan for which the employer paid 100% of the premiums. How are these sick pay benefits generally treated for the employee?

A. Fully taxable as wages, since the employer paid the premiums
B. Fully excluded from income, regardless of who paid the premiums
C. Taxable only to the extent the benefits exceed the employee's regular salary
D. Excluded only if the employee has been continuously disabled for over six months

32. A taxpayer who lost their job due to increased imports receives Trade Adjustment Assistance benefits, in addition to regular unemployment compensation. How are these benefits generally treated?

A. Excluded entirely, since they compensate for job loss caused by foreign trade
B. Includible only if the taxpayer also receives regular unemployment benefits in the same year
C. Excluded up to a set annual dollar limit, with any excess includible
D. Fully includible in gross income, similar to regular unemployment compensation

33. A taxpayer receives a distribution from a qualified settlement fund established to resolve a class action lawsuit. How is this distribution generally treated for tax purposes?

A. Taxed according to the underlying nature of the claim the distribution is compensating, such as physical injury or lost wages

B. Always fully excluded from income, regardless of the nature of the underlying claim

C. Always fully taxable as ordinary income, regardless of the nature of the underlying claim

D. Always taxed as capital gain, regardless of the nature of the underlying claim

34. A self-employed taxpayer accepts virtual currency as payment for services rendered to a client. How is this payment generally treated for federal income tax purposes?

A. Excluded from income until the virtual currency is converted to U.S. dollars

B. Includible only if the virtual currency is later sold at a gain

C. Includible in gross income at the fair market value of the virtual currency on the date received

D. Excluded entirely, since virtual currency is not treated as property for tax purposes

35. A taxpayer makes an interest-free gift loan of $8,000 to a family member. How does the below-market loan imputed interest rule generally apply to this loan?

A. It fully applies, requiring imputed interest income regardless of the loan amount

B. It applies only if the loan is not repaid within one year

C. It applies only to loans made to a non-family member

D. It generally does not apply, since the loan falls under the $10,000 de minimis exception for certain gift loans

36. An employee of an educational institution receives a qualified tuition reduction for coursework taken at that institution below the graduate level. How is this benefit generally treated?

A. Fully taxable as wages, identical to ordinary compensation

B. Excluded from the employee's gross income

C. Excluded only if the employee is enrolled in a graduate-level program

D. Taxable only above a specific dollar threshold set annually by the IRS

37. A taxpayer who does not otherwise own a qualifying trade or business receives REIT dividends and income from a publicly traded partnership. How does this income generally interact with the Section 199A QBI deduction?

A. It is entirely ineligible for any QBI deduction, since the taxpayer has no qualifying trade or business

B. It is generally eligible for the 20% QBI deduction, even though the taxpayer has no other qualifying business

C. It is eligible for the QBI deduction only if combined with active business income

D. It is eligible for a QBI deduction of only 10%, half the standard rate

38. A self-employed taxpayer computes self-employment tax on Schedule SE. What above-the-line deduction is generally available related to this tax?

A. A deduction for the full amount of self-employment tax paid

B. No deduction is available for any portion of self-employment tax

C. A deduction for one-half of the self-employment tax, reducing adjusted gross income

D. A deduction limited to 25% of the self-employment tax paid

39. A student otherwise eligible for the American Opportunity Tax Credit has a felony drug conviction on their record as of the end of the tax year. How does this generally affect eligibility for the credit?

A. It has no effect on eligibility for the American Opportunity Tax Credit

B. It disqualifies the student only from the Lifetime Learning Credit, not the AOTC

C. It reduces, but does not eliminate, the available American Opportunity Tax Credit

D. It generally disqualifies the student from the American Opportunity Tax Credit for that year

40. A taxpayer's modified adjusted gross income exceeds the applicable threshold for their filing status. How does this generally affect the Child Tax Credit?

A. The credit generally phases out gradually as income rises above the threshold, rather than being lost all at once

B. The credit is entirely eliminated immediately once any threshold is exceeded

C. The credit is unaffected by income at any level for any filing status

D. The credit doubles once the threshold is exceeded, to offset the higher tax bracket

41. A taxpayer otherwise eligible for the Earned Income Tax Credit has a significant amount of investment income for the year, such as interest and dividends. How does this generally affect EITC eligibility?

A. Investment income has no effect on EITC eligibility at any level

B. Investment income disqualifies the taxpayer only if it exceeds the taxpayer's earned income

C. The taxpayer is generally disqualified from the EITC if investment income exceeds an annually adjusted limit

D. Investment income only reduces, but never eliminates, the available credit

42. An employer maintains a dependent care assistance program, and an employee elects to have $5,000 of pretax salary directed into the program during the year. How does this employer-provided exclusion generally interact with the Child and Dependent Care Credit?

A. The employee may fully claim both the $5,000 exclusion and the full dependent care credit on the same expenses

B. The dependent care credit is automatically doubled when combined with the employer exclusion

C. The employer exclusion has no effect on the amount of qualifying expenses available for the credit

D. Expenses reimbursed through the excluded employer benefit generally cannot also be used to calculate the separate dependent care credit

43. A taxpayer receives a settlement or judgment in an unlawful discrimination claim and pays related attorney fees. How are these specific attorney fees generally treated?

A. Deductible only as a miscellaneous itemized deduction, currently suspended under current law

B. Deductible above the line, reducing adjusted gross income, up to the amount of the related settlement or judgment includible in income

C. Not deductible under any circumstances, regardless of the type of claim

D. Deductible only if the taxpayer itemizes and exceeds the 2% of AGI floor

44. A taxpayer repays a substantial amount of income in the current year that was included in taxable income and taxed in a prior year under a claim of right. What relief may be available if the repayment exceeds $3,000?

A. A special computation under Section 1341, generally allowing either a current deduction or a credit based on the prior year's tax

B. No relief is available; the repayment simply provides no tax benefit at all

C. An automatic full refund of all tax paid on the item in the original year

D. The repayment must be treated as a new item of negative income in the current year with no special computation

45. A taxpayer suffers a deductible personal casualty loss from a federally declared disaster. What two reductions are generally applied before the loss becomes deductible?

A. A $100 per-casualty floor, and then a reduction by 10% of the taxpayer's adjusted gross income

B. A flat $500 floor only, with no further reduction based on income

C. A reduction of 50% of adjusted gross income only, with no separate per-casualty floor

D. No reductions apply; the full loss amount is always fully deductible

46. A taxpayer's property is stolen, but the taxpayer does not discover the theft until a later tax year. In which year is the resulting theft loss generally deductible?

A. The year the theft actually occurred, regardless of when it was discovered

B. The year the taxpayer files a police report, regardless of when discovered

C. The year the theft is discovered, rather than the year the theft actually occurred

D. Either year, at the taxpayer's election, with no default rule

47. A student's 529 plan distribution is used to pay for room and board costs. Under what condition are these room and board costs generally treated as qualified higher education expenses?

A. Room and board never qualifies as a qualified higher education expense under any circumstances

B. Generally only if the student is enrolled at least half-time

C. Room and board always qualifies, regardless of the student's enrollment status

D. Room and board qualifies only for students living in on-campus housing exclusively

48. A self-employed taxpayer purchases health insurance through the Marketplace and wants to claim the above-the-line self-employed health insurance deduction. Why can computing this deduction alongside the Premium Tax Credit involve a circular calculation?

A. There is no circularity; the two items are computed entirely independently of one another

B. Because the Premium Tax Credit must always be repaid in full once any deduction is claimed

C. Because self-employed taxpayers are categorically ineligible for the Premium Tax Credit

D. Because the deduction reduces AGI, which affects the Premium Tax Credit, while the credit itself affects the premiums used to compute the deduction

49. A taxpayer receives a distribution from a traditional IRA and wants to roll it over into another retirement account without current taxation. Within what general period must this rollover generally be completed?

A. 30 days from the date the distribution was received

B. One full year from the date the distribution was received

C. There is no time limit, as long as the funds are eventually redeposited

D. 60 days from the date the distribution was received

50. A taxpayer's taxable income exceeds the applicable threshold, and the taxpayer's business is not a specified service trade or business. How is the QBI deduction generally limited at this higher income level?

A. Limited to the greater of a percentage of W-2 wages paid, or a combination of W-2 wages and a percentage of qualified property basis

B. The deduction is eliminated entirely once any income threshold is exceeded, regardless of business type

C. The deduction is unaffected by any wage or property limitation at higher income levels

D. The deduction is limited strictly to 10% of taxable income, with no wage-based alternative

51. A taxpayer works as a school counselor for grades K-12 for at least 900 hours during the school year. Does this taxpayer generally qualify as an eligible educator for the educator expense deduction?

A. No, since only classroom teachers qualify as eligible educators
B. No, since the deduction is limited exclusively to elementary school teachers
C. Yes, since an eligible educator includes K-12 teachers, instructors, counselors, principals, or aides meeting the minimum hours requirement
D. Yes, but only if the counselor also holds a separate teaching credential

52. A taxpayer wants to make a one-time transfer of funds directly from a traditional IRA into a Health Savings Account without first taking a taxable IRA distribution. What transaction generally allows this?

A. This transaction is not permitted under any circumstances between an IRA and an HSA
B. A qualified HSA funding distribution, limited to the taxpayer's annual HSA contribution limit and generally allowed only once in a lifetime
C. An unlimited number of tax-free transfers may be made from an IRA to an HSA each year
D. The transfer is permitted, but is always fully taxable as an IRA distribution first

53. A taxpayer has funds remaining in a long-held 529 education savings plan that the beneficiary no longer needs for education expenses. Under current law, what option may allow a limited rollover of these funds into a Roth IRA for the beneficiary?

A. No rollover to a Roth IRA is available under any circumstances for 529 plan funds
B. A direct rollover to the beneficiary's Roth IRA, subject to a lifetime dollar cap and other requirements, including the account being open for a minimum period
C. An unlimited rollover amount may be transferred to a Roth IRA with no lifetime cap
D. The funds may only be withdrawn as a fully taxable, penalized nonqualified distribution

54. A taxpayer worked for two different employers during the year, and the combined Social Security tax withheld by both employers exceeds the annual maximum. What relief is generally available?

A. A credit for the excess Social Security tax withheld, claimed directly on the taxpayer's Form 1040

B. No relief is available; the excess withholding simply cannot be recovered

C. The taxpayer must request a refund separately from each employer directly

D. The excess is automatically applied to the following year's estimated tax payments only

55. A taxpayer age 73 makes a qualified charitable distribution directly from a traditional IRA to a qualified charity, in an amount equal to the taxpayer's entire required minimum distribution for the year. How does this generally affect the taxpayer's RMD requirement?

A. The RMD must still be separately withdrawn and included in income in addition to the QCD

B. The QCD has no effect on the RMD requirement, which must be met by a separate distribution

C. The qualified charitable distribution generally counts toward satisfying the RMD requirement, without being included in taxable income

D. The RMD requirement is permanently eliminated once any QCD has been made

56. A homeowner installs a qualifying solar electric system on their primary residence. What credit is generally available for this installation, and at what general percentage rate?

A. The Energy Efficient Home Improvement Credit, capped at a small annual dollar limit

B. No credit is available for solar installations under current law

C. A flat $500 credit, regardless of the system's actual cost

D. The Residential Clean Energy Credit, generally equal to 30% of qualifying costs, with no overall dollar cap

57. A taxpayer computes tax under both the regular tax system and the alternative minimum tax system. What is the general result if the tentative minimum tax exceeds the regular tax?

A. The taxpayer pays only the higher of the two amounts, never both combined

B. The AMT is simply ignored whenever it is lower than the regular tax result

C. The taxpayer generally owes the excess as an additional alternative minimum tax, on top of the regular tax

D. The taxpayer receives a credit equal to the entire AMT amount, offsetting it completely

58. A dependent child's unearned income for the year falls between two applicable dollar thresholds under the kiddie tax rules. How is the income within this middle range generally taxed?

A. Entirely at the parents' top marginal tax rate, with no amount taxed at the child's own rate
B. Entirely excluded from taxable income, regardless of the amount
C. At a flat 10% rate, regardless of either threshold
D. At the child's own tax rate, with only the amount above the upper threshold taxed at the parents' rate

59. A taxpayer whose spouse died two years ago wants to claim Qualifying Surviving Spouse filing status for the current year. In addition to the timing requirement, what condition must generally be met regarding a dependent child?

A. No dependent child requirement applies; the timing requirement alone is sufficient
B. The taxpayer must maintain a home that is the principal residence of a dependent child for the entire year
C. The dependent child must be at least age 18 by the end of the tax year
D. The taxpayer must have at least two dependent children living in the home

60. A taxpayer's Child Tax Credit exceeds their tax liability, and the taxpayer wants to claim the refundable Additional Child Tax Credit for the remainder. How is the refundable amount generally calculated?

A. Generally as a percentage of earned income above a set dollar threshold, up to a maximum refundable amount per child
B. As a flat dollar amount per child, regardless of the taxpayer's earned income
C. As the full remaining nonrefundable credit amount, with no separate calculation required
D. The Additional Child Tax Credit is never refundable under any circumstances

61. A taxpayer claimed Section 179 expensing on business equipment, and in a later year the equipment's business use drops to below 50%. What is the general consequence?

A. The taxpayer must generally recapture a portion of the Section 179 deduction as ordinary income

B. No consequence applies, as long as the taxpayer continues using the equipment at all

C. The taxpayer must fully repay the entire original purchase price of the equipment

D. The recapture applies only if the equipment is also sold in that same year

62. A member of the clergy receives a housing allowance excluded from income tax but must still generally pay self-employment tax on certain earnings. How does this general SE tax treatment for clergy differ from that of a typical employee?

A. Clergy are entirely exempt from both income tax and self-employment tax on ministerial earnings

B. Clergy are generally self-employed for Social Security tax on ministerial earnings despite being a church employee

C. Clergy pay only the employee half of Social Security tax, identical to a typical employee

D. Clergy pay self-employment tax only on earnings above a set high-income threshold

63. A taxpayer pays a household employee, such as a nanny, wages exceeding the annual threshold that triggers employment tax obligations. What is this general obligation commonly called, and what schedule is generally used to report it?

A. The self-employment tax, reported on Schedule SE by the household employer

B. No special reporting is required beyond issuing the employee a Form 1099-NEC

C. The 'nanny tax,' generally reported using Schedule H attached to the taxpayer's Form 1040

D. The household employee is always treated as an independent contractor, avoiding any employer tax obligation

64. A taxpayer who worked for two different employers during the year contributed more than the annual elective deferral limit to their combined 401(k) plans. What is the general consequence if the excess is not timely corrected?

A. No consequence applies, since 401(k) contribution limits apply separately to each employer's plan

B. The excess is automatically forfeited by the plan with no tax consequence to the employee

C. The excess is automatically converted to a Roth contribution with no further tax due

D. The excess deferral is generally taxable in the year contributed, and may be taxed again when eventually distributed if not corrected timely

65. A taxpayer under age 59½ wants to take penalty-free distributions from a retirement account before reaching normal retirement age, without qualifying for one of the standard specific penalty exceptions. What method may allow this?

A. Substantially equal periodic payments under Section 72(t), continued for the required minimum period

B. There is no way to avoid the 10% penalty before age 59½ without a standard specific exception

C. A one-time penalty-free withdrawal of any amount, available to every taxpayer regardless of circumstances

D. Converting the entire account to a Roth IRA, which always eliminates the early distribution penalty

66. A taxpayer paid alternative minimum tax in a prior year due to a timing-related preference item, such as the exercise of incentive stock options. What may allow the taxpayer to recover some of that AMT paid in a future year?

A. No mechanism exists to recover AMT paid in a prior year under any circumstances

B. An automatic full refund of the prior year's AMT, issued the following year with no election needed

C. The minimum tax credit, which may be carried forward to offset regular tax in a future year when AMT is not owed

D. A one-time itemized deduction equal to the AMT paid in the prior year

67. A taxpayer's joint refund is applied to the other spouse's separate, defaulted federal student loan debt through the Treasury Offset Program. What relief allows the non-liable spouse to claim their portion of the joint refund?

A. Injured spouse relief applies only to offsets for the other spouse's own separate tax debts

B. Innocent spouse relief, since Form 8379 does not apply to federal student loan offsets

C. No relief is available once the Treasury Offset Program has applied the refund

D. Injured spouse relief, requested using Form 8379, applicable to this type of federal debt offset as well as tax debts

68. A self-employed taxpayer's net self-employment income exceeds the Additional Medicare Tax threshold for their filing status. Unlike wage withholding, how is this threshold generally applied to self-employment income?

A. The threshold is automatically reduced to zero once any self-employment income exists

B. The threshold applies as usual, reduced by any wages separately earned as an employee that year

C. Self-employment income is entirely exempt from the Additional Medicare Tax under all circumstances

D. The threshold doubles for self-employment income compared to the wage-based threshold

69. A parent wants to elect, using Form 8814, to include a child's unearned income directly on the parent's own return instead of filing a separate return for the child. What is one general condition that must be met regarding the amount and type of the child's income?

A. The child's income must consist only of interest, dividends, and capital gain distributions within specific dollar limits

B. The child's income may be of any type or amount, with no specific limits applying

C. The election is available only if the child's total income exceeds a very high threshold

D. The child's income must consist entirely of wages from a part-time job

70. A married couple files a joint federal income tax return. What is the general rule regarding each spouse's liability for the total tax shown on that joint return?

A. Each spouse is liable only for the portion of tax attributable to their own individual income

B. Only the higher-earning spouse is liable for the entire joint tax liability

C. Each spouse is generally jointly and severally liable for the entire tax, not merely for their own proportionate share

D. Liability is automatically split 50/50 between the spouses, regardless of each spouse's income

71. A taxpayer is still legally married but has lived apart from their spouse for the entire last six months of the year. Under what circumstance might this taxpayer still be able to use Head of Household status, despite technically still being married?

A. A legally married taxpayer can never use Head of Household status under any circumstances

B. Simply living apart from a spouse for any period automatically qualifies the taxpayer as unmarried

C. The taxpayer must obtain a legal separation decree before qualifying for this exception

D. If the taxpayer is 'considered unmarried' under the specific requirements, such as maintaining a home for a qualifying child and the spouse not living there

72. A taxpayer who claims the standard deduction on their regular tax return computes alternative minimum taxable income. How is the standard deduction generally treated for AMT purposes?

A. Added back, since the standard deduction is not allowed in computing alternative minimum taxable income

B. Allowed in full, identical to its treatment for regular tax purposes

C. Allowed at half its regular value, rather than being fully added back

D. Doubled for AMT purposes to offset the general disallowance of other deductions

73. A taxpayer's return contains a substantial understatement of tax attributable to negligent recordkeeping, and the IRS proposes an adjustment on examination. What penalty may generally apply to the taxpayer directly, separate from any preparer penalty?

A. No penalty applies to the taxpayer directly; only the preparer can be penalized for return errors

B. The accuracy-related penalty, generally equal to 20% of the portion of the underpayment attributable to the negligence or substantial understatement

C. A flat penalty of $500, regardless of the size of the underpayment

D. Automatic criminal prosecution, with no separate civil penalty available

74. A participant in an employer retirement plan takes a loan from their account balance but fails to make the required payments, causing the loan to go into default. What is the general tax consequence of this default?

A. No tax consequence applies, since a plan loan is simply repaid to the participant's own account

B. The default automatically converts the loan into a permanently tax-free plan distribution

C. The outstanding loan balance is generally treated as a deemed taxable distribution, potentially subject to the 10% early distribution penalty

D. The plan is required to forgive the loan without any tax reporting to the participant

75. A client with significant retirement savings asks about differences in creditor protection between an employer 401(k) plan and a traditional IRA outside of bankruptcy. What should the advisor generally explain?

A. Both account types receive identical creditor protection under federal law in every state

B. An IRA always receives stronger creditor protection than any employer-sponsored plan

C. Neither account type receives any creditor protection under any circumstances

D. An employer plan generally receives broader federal ERISA creditor protection, while IRA protection outside bankruptcy often depends more on state law

76. A client wants to make a large charitable gift and has both cash and significantly appreciated stock available. What general advising point should be raised about which asset to give?

A. Cash and appreciated stock always produce an identical tax result when donated

B. Donating appreciated stock directly can avoid capital gains tax while still allowing a deduction for its full value

C. Donating appreciated stock is never advisable, since it eliminates any deduction

D. The client should always sell the stock first and donate the after-tax cash proceeds

77. A client wants to purchase Series I savings bonds and asks about using their federal tax refund to buy additional paper bonds beyond the standard electronic purchase limit. What should the advisor explain?

A. Tax refunds can never be used to purchase any type of savings bond

B. Using a refund to buy paper bonds replaces, rather than adds to, the electronic purchase limit

C. There is no limit at all on the amount of I bonds a taxpayer may purchase using a refund

D. A taxpayer may generally use part of their federal refund to purchase paper Series I bonds, in addition to the separate annual electronic purchase limit

78. A client founded a qualifying small business several years ago and is now considering selling their stock in the company. What advising point regarding Section 1202 should be raised before the sale?

A. Stock meeting the qualified small business stock requirements and held long enough may allow a significant portion of the gain to be excluded from tax

B. Section 1202 exclusion is available only to investors who purchased stock on a public stock exchange

C. All stock gain from any small business sale is automatically fully excluded from tax

D. Section 1202 applies only to stock held for less than one year

79. An elderly client purchases a qualified long-term care insurance policy and pays substantial annual premiums. What should the advisor explain about deducting these premiums?

A. The full premium amount is always fully deductible above the line, regardless of age

B. Long-term care insurance premiums are never deductible under any circumstances

C. A portion of the premiums, limited by age, may be deducted as a medical expense subject to the AGI floor

D. The premiums are deductible only if the client is currently receiving long-term care services

80. A client just received a grant of restricted stock from their startup employer, currently worth very little. What time-sensitive advising point should be raised immediately?

A. The client has a full year to decide whether to file a Section 83(b) election

B. The client has only 30 days from the grant date to elect current, low-value taxation

C. No election is available for restricted stock under any circumstances

D. The election, if desired, can be filed at any time before the stock is eventually sold

81. A client wants to convert a large traditional IRA balance to a Roth IRA but is concerned about pushing all the converted income into a much higher tax bracket in a single year. What should the advisor suggest?

A. Converting the entire balance in one year always produces the lowest total tax cost

B. Roth conversions must always be completed in a single transaction within one tax year

C. Spreading the conversion across multiple years to manage the amount of income recognized, and the resulting bracket, in any single year

D. There is no way to manage the tax bracket impact of a large Roth conversion

82. A client wants to name a trust, rather than an individual, as the beneficiary of a large traditional IRA. What should the advisor explain about the 'see-through trust' rules?

A. Naming any trust as an IRA beneficiary automatically requires the entire account to be distributed within one year

B. A trust can never be named as a retirement account beneficiary under any circumstances

C. Naming a trust as beneficiary always produces identical tax results to naming an individual directly

D. A trust meeting specific IRS requirements can generally be treated as having a designated beneficiary, preserving more favorable distribution options than an improperly structured trust

83. A business-owning client operates several related businesses, each individually falling short of the wage or property thresholds needed to maximize their QBI deduction at higher income levels. What planning strategy should the advisor raise?

A. Aggregating multiple businesses for QBI purposes is never permitted under any circumstances

B. Electing to aggregate the related businesses, where permitted, potentially allowing the combined wages and property to support a larger overall QBI deduction

C. Each business must always be treated entirely separately, with no aggregation option available

D. Aggregation is available only for businesses operating in entirely different industries

84. A client recently divorced but has not yet updated the beneficiary designation on their retirement account, which still names the former spouse. What should the advisor emphasize?

A. Beneficiary designations generally control over a will, so the outdated designation should be updated

B. A divorce automatically and immediately updates all retirement account beneficiary designations

C. The client's will automatically overrides any outdated beneficiary designation on the account

D. Beneficiary designations cannot be changed once originally established

85. A client owns rental properties generating income in several different states in addition to their home state. What should the advisor coordinate regarding estimated tax payments?

A. Only a single federal estimated payment is ever needed, regardless of how many states are involved

B. State estimated tax obligations are always eliminated once federal estimated payments are current

C. Only the state where the client resides ever requires any estimated tax payment

D. Estimated payments across the client's home state and each nonresident state where rental income is earned, to avoid underpayment penalties in multiple jurisdictions

86. A client holding nonqualified stock options expects significantly lower income next year due to an upcoming retirement. What timing point should the advisor raise about exercising the options?

A. Exercising in the lower-income year could result in the compensation income being taxed at a lower marginal rate than exercising in the current, higher-income year

B. The exercise date has no effect on the tax rate applied to the resulting compensation income

C. Nonqualified stock options must always be exercised within the same year they are granted

D. Waiting to exercise always eliminates any tax on the resulting compensation income

87. A client participates in an employer's Health Flexible Spending Account and is concerned about forfeiting unused funds at year-end. What should the advisor ask the client to check with their employer about?

A. Health FSA funds are never forfeited under any circumstances, regardless of the employer's plan design

B. All unused Health FSA funds are automatically refunded in cash to the employee at year-end

C. Whether the employer's plan offers a grace period or a limited carryover allowance, which can reduce funds otherwise lost under the general use-it-or-lose-it rule

D. Grace periods and carryover allowances are never permitted for any Health FSA plan

88. A nonresident alien decedent dies owning U.S.-situated property exceeding the applicable exemption. What federal estate tax return is generally required to be filed for this decedent's estate?

A. The standard Form 706, identical to the return filed for a U.S. citizen or resident decedent

B. Form 706-NA, United States Estate Tax Return, Estate of nonresident not a citizen of the United States

C. Form 1040-NR, filed on behalf of the deceased nonresident alien
D. No federal estate tax return is ever required for a nonresident alien decedent

89. A U.S. citizen receives a gift or bequest from a former U.S. citizen who is classified as a 'covered expatriate' under the expatriation tax rules. What may this U.S. recipient generally owe as a result?

A. No special tax applies to the recipient; the covered expatriate alone bears any tax consequence
B. Ordinary income tax on the full value received, as if it were compensation for services
C. The recipient must automatically renounce their own U.S. citizenship as a condition of accepting the gift
D. A special transfer tax under Section 2801, generally equal to the highest estate or gift tax rate applied to the value received

90. A U.S. person receives a gift exceeding $100,000 from a nonresident alien individual during the year. What is the U.S. recipient generally required to do?

A. Report the gift on Form 3520, even though no gift tax is owed by the U.S. recipient
B. Pay U.S. gift tax directly on the value of the gift received
C. Nothing is required, since only the foreign donor has any reporting obligation
D. File Form 709, the same form a donor would use to report a taxable gift made

91. A taxpayer creates an irrevocable trust but retains a reversionary interest, meaning trust property may revert back to the taxpayer, valued at more than 5% of the trust's value at the time of creation. How does this generally affect the trust's tax treatment?

A. The reversionary interest has no effect on the trust's tax classification
B. The trust automatically becomes fully revocable once any reversionary interest exists
C. The trust is generally treated as a grantor trust, with income taxed directly to the taxpayer
D. The reversionary interest disqualifies the trust from ever being valid under state law

92. A U.S. person fails to timely file a required FBAR for a foreign account. How does the potential civil penalty generally differ between a non-willful and a willful failure to file?

A. A non-willful failure generally carries a smaller penalty cap than a willful failure, which can carry a far larger penalty tied to the account's value
B. Both non-willful and willful failures carry an identical maximum civil penalty
C. Only a willful failure carries any civil penalty at all; a non-willful failure carries none
D. Only a non-willful failure carries any civil penalty at all; a willful failure carries none

93. A funeral home establishes small pre-need trusts to hold customer payments for future funeral services. What special tax election is generally available for these arrangements?

A. No special election is available; each pre-need trust must file a full separate Form 1041
B. An election to treat each trust as a Qualified Funeral Trust, allowing simplified income tax reporting
C. An automatic exemption from all federal income tax on trust earnings
D. An election to treat the trust as a grantor trust taxed to the funeral home operator

94. An estate incurs administration expenses, such as executor fees and legal costs, that are deductible for both estate tax and estate income tax purposes. What general election must the executor make regarding these expenses?

A. The expenses may always be fully deducted on both returns simultaneously with no election required
B. The expenses must always be deducted first on the estate's income tax return, with no alternative
C. Elect to deduct the expenses on either Form 706 or the estate's Form 1041, but generally not both
D. The expenses are never deductible on either return under current law

95. A decedent's outstanding medical expenses are paid by the estate within one year after the date of death. What special election may allow these expenses to be treated as though paid on the date incurred, for purposes of the decedent's final Form 1040?

A. No such election is available; medical expenses paid by the estate can never be deducted on the final Form 1040
B. The election is available only if the expenses are paid within 30 days of death
C. The expenses may only ever be deducted on the estate's own Form 1041, with no alternative

D. An election to treat the medical expenses as paid by the decedent at the time incurred, allowing them to be deducted on the final individual return

96. A grantor makes a gift to an irrevocable trust for a beneficiary's benefit, and the trust grants the beneficiary a temporary right to withdraw the contributed funds. What is the general purpose of including this withdrawal right?

A. To give the beneficiary permanent, unconditional ownership of the entire trust immediately

B. To convert what would otherwise be a future interest gift into a present interest gift, qualifying it for the annual gift tax exclusion

C. To disqualify the gift from any annual gift tax exclusion, ensuring it is fully taxable

D. To convert the irrevocable trust into a revocable trust for the grantor's benefit

97. A bank account is titled in one person's name 'in trust for' a named beneficiary, with the account owner retaining full control during their lifetime. How does this type of arrangement generally pass to the beneficiary at the owner's death?

A. Through the probate process, identical to an asset with no named beneficiary

B. Only if a separate will also names the same individual as a beneficiary

C. The funds automatically escheat to the state, regardless of any named beneficiary

D. Outside of probate, directly to the named beneficiary, similar to a payable-on-death designation

98. A trust wants to hold shares of an S corporation as a shareholder without disqualifying the corporation's S election. What two general types of trusts are generally permitted to hold S corporation stock for this purpose?

A. A Qualified Subchapter S Trust (QSST) and an Electing Small Business Trust (ESBT)

B. Any type of trust may hold S corporation stock without any special election required

C. Only a fully revocable grantor trust may ever hold S corporation stock

D. A charitable remainder trust and a qualified disability trust, exclusively

99. A special needs trust is funded with the disabled beneficiary's own assets, such as a personal injury settlement, rather than assets from a third party. What provision must this type of trust generally include?

A. No special provision is required if the trust is funded with the beneficiary's own assets

B. An automatic termination clause requiring the trust to end after five years

C. A Medicaid payback provision, reimbursing the state for benefits paid on the beneficiary's behalf upon the beneficiary's death

D. A provision requiring the trust's remaining assets to pass directly to the state immediately upon funding

100. An estate's governing instrument permanently sets aside a portion of estate income for a qualified charitable purpose, though the amount has not yet actually been paid out to the charity. How does the estate's charitable deduction generally differ from an individual's?

A. The estate is subject to the identical percentage-of-AGI limits that apply to an individual taxpayer

B. The estate may generally claim an unlimited charitable deduction for amounts permanently set aside for charity, without the percentage-of-income limits that apply to an individual taxpayer

C. The estate may never claim any charitable deduction until the funds are actually distributed

D. The estate's charitable deduction is capped at a flat dollar amount regardless of the estate's income

Answer Key and Explanations — Practice Exam 28

1. B — An enrolled agent must generally renew their enrollment every three years, on a staggered cycle determined by the last digit of the agent's Social Security number, separate from the annual PTIN renewal all paid preparers must complete. Failing to timely renew enrollment can result in the agent's enrollment becoming inactive.

2. D — An enrolled agent must generally complete 72 hours of continuing education over each three-year enrollment cycle, including a minimum of 16 hours in each individual year of the cycle, with at least 2 of those annual hours devoted to ethics or professional conduct, ensuring continuing education is spread throughout the cycle rather than completed all at once.

3. C — Circular 230 generally requires a practitioner who learns that a client failed to comply with federal tax law, or who made an error or omission on a previously filed return, to advise the client promptly of the fact and consequences of that noncompliance, error, or omission. The practitioner need not notify the IRS or amend the return unilaterally.

4. A — Under the Practitioner PIN method, a paid preparer transmitting a client's return electronically enters a PIN on the taxpayer's behalf after the taxpayer authorizes this on a signed Form 8879, while the Self-Select PIN method is instead generally used by a taxpayer e-filing independently, without a paid preparer, to sign their own electronically filed return.

5. D — Section 6695 imposes a per-failure penalty on a paid preparer who fails to furnish the taxpayer a copy of the completed return, one of several separate preparer penalties under that section, which also covers failures such as not signing the return, not including a PTIN, and not retaining required copies or a client list.

6. C — Circular 230 generally prohibits a practitioner from endorsing or otherwise negotiating a client's refund check, regardless of any client authorization, reflecting a bright-line rule intended to prevent preparers from diverting or improperly handling a client's refund proceeds, even temporarily or with the client's apparent consent, since the rule protects public confidence in preparers.

7. A — The Office of Professional Responsibility, commonly called OPR, generally has jurisdiction to investigate alleged violations of Circular 230 and to pursue disciplinary action against practitioners, including censure, suspension, or disbarment from practice before the IRS, separate from the Return Preparer Office's broader oversight of paid preparer compliance generally, and separate from state licensing boards.

8. B — The IRS assigns a CAF number, tied to the Centralized Authorization File, to track a representative's power of attorney and tax information authorizations across multiple clients and years. This number is separate from a PTIN, which identifies the individual as a paid preparer, and is instead specific to the representative's authorization history.

9. A — Because a claim for a loss from a bad debt or worthless security generally has a special seven-year statute of limitations, taxpayers are generally advised to retain supporting purchase records for at least seven years, longer than the typical three-year retention period recommended for most other ordinary supporting tax documentation.

10. D — Circular 230 identifies incompetence and disreputable conduct as general grounds that can subject a practitioner to censure, suspension, or disbarment from practice before the IRS, encompassing a range of specific conduct such as certain criminal convictions, willful failure to file returns, and knowingly providing false or misleading information to the IRS or to a client.

11. C — A power of attorney authorization is generally limited to the specific tax matters and periods stated on Form 2848, so once the stated period ends, the representative generally loses authority to act on the client's behalf for that matter, and a new Form 2848 must be filed to continue representation for any future periods.

12. B — Before using or disclosing a client's tax return information for a purpose beyond preparing the specific return, such as building a marketing database, Section 7216 generally requires the preparer to first obtain the client's knowing, voluntary, and specific written consent describing that particular intended use or disclosure of the information.

13. D — Section 6695 imposes a per-return penalty on a paid preparer who fails to sign a return they were required to sign, one of several separate mechanical preparer penalties under that section, distinct from the reasonable-basis and unreasonable-position penalties imposed under the related Section 6694 penalty provisions governing understated tax liability.

14. B — The authority granted through the Third Party Designee checkbox generally remains in effect until one year from the original due date of the return, without regard to extensions, allowing the designated preparer to discuss the specific return's processing with the IRS for that limited window before the authorization automatically expires.

15. C — Circular 230 generally requires a practitioner's communications and solicitations to remain truthful and non-deceptive, and using a former client's confidential information without consent as the basis for a new advertisement would generally conflict with the practitioner's ongoing confidentiality obligations, regardless of whether the client relationship has since ended or the information seems harmless.

16. A — As a general rule of thumb, an individual taxpayer should keep copies of filed returns and supporting records for at least three years, corresponding to the general statute of limitations for the IRS to assess additional tax, though longer retention is generally recommended for records supporting items such as property basis or a bad debt claim.

17. C — Military pay earned by a member of the U.S. Armed Forces while serving in a designated combat zone is generally excluded from gross income, with the exclusion for enlisted personnel generally unlimited but capped at a set dollar amount, tied to the highest enlisted pay grade, for commissioned officers, providing meaningful tax relief for deployed service members.

18. A — Qualified foster care payments a taxpayer receives from a state or qualified foster care placement agency for caring for a foster child placed in the home are generally excluded from gross income, up to applicable per-child difficulty-of-care and standard payment limits, since these payments primarily reimburse the cost of care rather than compensate an employee.

19. D — A qualified disaster relief payment received from a government agency to cover reasonable and necessary personal, family, living, or funeral expenses following a federally declared disaster is generally excluded from gross income under Section 139, to the extent the expense is not otherwise compensated by insurance or another source, without any specific dollar cap on the exclusion itself.

20. B — Life insurance proceeds paid to a beneficiary by reason of the insured's death are generally excluded from the beneficiary's gross income, regardless of the relationship between the beneficiary and the insured. However, any interest that accrues on the proceeds after death, such as when payment is delayed, is generally taxable to the beneficiary.

21. B — Accelerated death benefits paid to a terminally ill individual, certified by a physician as having a limited life expectancy, are generally excluded from gross income, treated similarly to ordinary life insurance proceeds paid by reason of death, recognizing that these payments serve the same underlying purpose even though received before the insured's actual death.

22. C — Amounts received as workers' compensation for a work-related injury or illness under a state workers' compensation act are generally excluded from gross income, whether paid directly to the injured employee or to a surviving family member, reflecting the payments' nature as compensation for a job-related injury rather than as taxable wage replacement.

23. A — A specifically allocated portion of a settlement compensating for medical expenses related to a physical injury is generally excluded from gross income as part of the broader exclusion for damages received on account of physical injury or sickness, though a taxpayer who previously deducted those same expenses must include the recovery to the extent of any tax benefit.

24. D — A monetary award a taxpayer receives from the IRS Whistleblower Office for providing information leading to the collection of unpaid taxes from another party is generally fully taxable as ordinary income to the whistleblower, though certain related attorney fees and costs may be separately deductible above the line in computing adjusted gross income.

25. B — Under Section 83, property such as employer stock that is subject to a substantial risk of forfeiture is generally not taxable to the employee upon receipt but instead becomes taxable, at its then fair market value, once it is no longer subject to that risk, typically at vesting, unless the employee makes a timely Section 83(b) election.

26. A — When a taxpayer surrenders a life insurance policy for its cash surrender value, the taxpayer generally recovers their basis, consisting of total premiums paid, tax-free, with any amount received above that basis generally taxable as ordinary income, reflecting the built-up gain inside the policy that was never previously subject to tax.

27. D — Under Section 1035, certain exchanges of life insurance, endowment, or annuity contracts, such as exchanging a life insurance policy for a new annuity contract, generally qualify for tax-free exchange treatment, deferring any gain built up in the original contract, provided the exchange meets specific requirements and no cash or other non-like-kind property is received by the taxpayer.

28. C — Original issue discount on a tax-exempt municipal bond is not taxable as income each year, unlike OID on a taxable bond, but it still accretes and increases the taxpayer's basis in the bond annually, which is important for correctly computing any gain or loss when the bond is eventually sold or matures.

29. B — An employee who wants to be taxed on restricted property at its value upon receipt, rather than waiting until it vests, must generally file a Section 83(b) election with the IRS within 30 days of receiving the property. This can be beneficial when current value is low, but it risks paying tax on property later forfeited without refund.

30. C — Stock options that meet specific requirements under the Internal Revenue Code, such as incentive stock options and options granted under an employee stock purchase plan, are generally referred to as statutory stock options, receiving more favorable tax treatment than nonstatutory stock options, which do not meet these specific Code requirements and are instead generally taxed as ordinary income at exercise.

31. A — Sick pay or short-term disability benefits an employee receives under a plan for which the employer paid 100% of the premiums are generally fully taxable as wages to the employee, since the employee did not bear the cost of the coverage with after-tax dollars, the opposite treatment of benefits received under a policy the employee paid for personally.

32. D — Trade Adjustment Assistance benefits, paid to workers who lost employment due to increased imports or a shift in production overseas, are generally fully includible in the recipient's gross income, treated similarly to regular unemployment compensation, and are generally reported to the recipient on Form 1099-G by the paying state agency each year.

33. A — A distribution a taxpayer receives from a qualified settlement fund is generally taxed according to the underlying nature of the claim it compensates, such as being excluded if it represents damages for a physical injury, or taxable as ordinary income if it represents lost wages, rather than receiving one uniform tax treatment for all fund distributions.

34. C — A self-employed taxpayer who accepts virtual currency as payment for services must include the fair market value of the virtual currency, measured in U.S. dollars on the date received, in gross income, exactly as if the payment had been received in cash, since virtual currency is treated as property, not currency, for federal tax purposes.

35. D — The below-market loan imputed interest rules generally include a de minimis exception for certain gift loans of $10,000 or less between individuals, meaning a taxpayer who makes an $8,000 interest-free gift loan generally is not required to recognize imputed interest income, provided the loan proceeds are not used to purchase income-producing property.

36. B — A qualified tuition reduction an educational institution provides to its employee for undergraduate-level coursework at that institution is generally excluded from the employee's gross income. Tuition reductions for graduate-level coursework are generally taxable unless the employee is engaged in teaching or research activities for the institution as part of the arrangement.

37. B — Qualified REIT dividends and qualified publicly traded partnership income are generally eligible for the 20% Section 199A deduction even for a taxpayer with no other qualifying trade or business, and this component is not subject to the wage and property limitations or specified service trade restrictions that can otherwise limit the deduction for business income.

38. C — A self-employed taxpayer is generally allowed an above-the-line deduction for one-half of the self-employment tax computed on Schedule SE, reducing adjusted gross income and roughly approximating the employer-equivalent portion of Social Security and Medicare tax that a traditional employee's employer would otherwise pay and separately deduct as an ordinary business expense.

39. D — A student with a felony drug conviction, for either possessing or distributing a controlled substance, as of the end of the tax year is generally disqualified from the American Opportunity Tax

Credit for that year, a specific eligibility restriction that does not apply to the separate Lifetime Learning Credit, which remains available regardless of this type of conviction.

40. A — The Child Tax Credit generally phases out gradually, reduced by a set amount for each increment of modified adjusted gross income above the applicable threshold for the taxpayer's filing status, rather than being eliminated entirely and immediately the moment income exceeds that threshold, allowing some taxpayers with income above the threshold to still claim a partial credit.

41. C — A taxpayer otherwise eligible for the Earned Income Tax Credit based on earned income and other requirements is generally disqualified from claiming the credit entirely if their investment income, such as interest, dividends, and capital gains, exceeds an annually adjusted dollar limit, regardless of how much earned income the taxpayer otherwise has for the year.

42. D — Because the same dependent care expenses cannot generate a double tax benefit, expenses reimbursed or paid through an employer's excluded dependent care assistance program generally reduce, dollar for dollar, the amount of qualifying expenses otherwise available to compute the separate Child and Dependent Care Credit, preventing the employee from claiming both benefits on the identical expenses.

43. B — Attorney fees and court costs a taxpayer pays in connection with an unlawful discrimination claim are generally deductible above the line, directly reducing adjusted gross income, up to the amount of the related judgment or settlement includible in the taxpayer's income, an exception to the general suspension of miscellaneous itemized deductions for legal fees under current law.

44. A — When a taxpayer repays income exceeding $3,000 that was included in taxable income and taxed under a claim of right in a prior year, Section 1341 generally allows the taxpayer to choose the more favorable of two methods: deducting the repayment currently, or claiming a credit for the additional tax paid on that amount in the earlier year.

45. A — A deductible personal casualty loss from a federally declared disaster is generally reduced first by a $100 floor for each separate casualty event, and the remaining amount, after combining all casualty losses for the year, is further reduced by 10% of the taxpayer's adjusted gross income, with only the amount exceeding both reductions actually deductible as an itemized deduction.

46. C — A theft loss is generally deductible in the year the taxpayer discovers the theft, rather than the year the theft actually occurred, since a taxpayer often cannot know a theft happened until sometime later; this discovery-year rule differs from the treatment of most other casualty losses, deductible in the year the casualty event itself occurred.

47. B — Room and board costs generally qualify as qualified higher education expenses for 529 plan distribution purposes only if the student is enrolled at least half-time, with the qualifying amount generally limited to the school's official cost of attendance allowance or the actual amount charged if the student lives in institution-owned or operated housing.

48. D — A circular calculation can arise because the self-employed health insurance deduction reduces adjusted gross income, which in turn affects the amount of Premium Tax Credit the taxpayer is eligible for, while the Premium Tax Credit itself affects the net premium amount available to be deducted, requiring an iterative worksheet computation to resolve both figures consistently.

49. D — A taxpayer who receives a distribution from a traditional IRA or other eligible retirement plan generally must complete a rollover into another eligible retirement account within 60 days of receiving the distribution to avoid current taxation and, if applicable, the 10% early distribution penalty, subject to limited exceptions such as certain hardship or IRS-granted waivers.

50. A — For a non-service trade or business once taxable income exceeds the applicable threshold, the Section 199A deduction is generally limited to the greater of 50% of W-2 wages paid, or the sum of 25% of W-2 wages plus 2.5% of the unadjusted basis immediately after acquisition of qualified property, rather than eliminated as for a specified service business.

51. C — An eligible educator for purposes of the educator expense deduction generally includes a kindergarten through grade 12 teacher, instructor, counselor, principal, or aide who works at least 900 hours during the school year, meaning a qualifying school counselor is generally eligible for the deduction on the same basis as a classroom teacher meeting the same hours requirement.

52. B — A qualified HSA funding distribution allows a taxpayer to make a one-time, direct trustee-to-trustee transfer from a traditional IRA into a Health Savings Account, tax-free, limited to the taxpayer's maximum annual HSA contribution limit, and generally available only once during the taxpayer's lifetime, providing a narrow bridge between the two types of tax-advantaged accounts.

53. B — Under current law, unused funds in a 529 education savings plan that has been maintained for a minimum required period may generally be rolled over directly into the designated beneficiary's Roth IRA, subject to a lifetime dollar cap and the beneficiary's normal annual Roth contribution limit, offering a way to repurpose leftover education savings without triggering tax or penalty.

54. A — A taxpayer who worked for two or more employers during the year, and whose combined Social Security tax withheld by those employers exceeds the annual maximum wage base amount, may generally claim a credit for the excess withholding directly on Form 1040, recovering the overwithheld amount without needing to contact each employer individually.

55. C — A qualified charitable distribution generally counts toward satisfying the taxpayer's required minimum distribution for the year, up to the applicable annual QCD limit, without the distributed amount being included in the taxpayer's taxable income, allowing a charitably inclined IRA owner to satisfy the RMD requirement while avoiding the income tax that would otherwise apply to a taxable distribution.

56. D — A homeowner who installs a qualifying solar electric system, along with certain other renewable energy property, on their residence may generally claim the Residential Clean Energy Credit, equal to 30% of qualifying costs with no overall dollar cap, distinct from the separate Energy Efficient Home Improvement Credit, which applies to items like insulation and carries smaller annual limits.

57. C — A taxpayer's total tax liability generally equals their regular tax plus any amount by which the tentative minimum tax, computed under the separate AMT system after applying the AMT exemption amount, exceeds that regular tax; when the tentative minimum tax does not exceed the regular tax, no additional AMT is owed for the year.

58. D — Under the kiddie tax rules, a dependent child's unearned income is generally taxed in tiers: a base amount is entirely tax-free, income within a middle range is taxed at the child's own rate, and only unearned income above the upper threshold is taxed at the parents' generally higher marginal rate, rather than the entire amount at the parents' rate.

59. B — In addition to the general requirement that surviving spouse status applies only for the two tax years following the year of the spouse's death, the taxpayer must also maintain a home serving as the principal residence for the entire year of a dependent child, and must have paid more than half the cost of maintaining that home.

60. A — The refundable Additional Child Tax Credit is generally calculated as 15% of the taxpayer's earned income above a set dollar threshold, up to a maximum refundable amount per qualifying child, allowing a taxpayer whose regular tax liability is too low to use the full nonrefundable Child Tax Credit to still receive some benefit as a refund.

61. A — When business-use percentage of property for which Section 179 expensing was claimed drops to 50% or below in a later year, before the end of the property's recovery period, the taxpayer must generally recapture the excess deduction, the amount claimed above what regular depreciation would have allowed, as ordinary income in the year the business use drops below that threshold.

62. B — A member of the clergy is generally treated as self-employed for Social Security and Medicare tax purposes on ministerial earnings, including any excludable housing allowance added back for this specific calculation, and pays self-employment tax under Schedule SE, even though the same individual may otherwise be treated as a common-law employee of the church for federal income tax withholding purposes.

63. C — A taxpayer who pays a household employee, such as a nanny or housekeeper, wages exceeding the annually adjusted threshold generally has employer tax obligations for Social Security, Medicare, and possibly federal unemployment tax, commonly called the 'nanny tax,' generally reported using Schedule H attached to the taxpayer's own Form 1040 rather than a separate business payroll return.

64. D — A taxpayer who contributes more than the annual elective deferral limit across all their 401(k) plans combined, often because of changing employers during the year, has an excess deferral generally taxable in the year contributed, and if not withdrawn by the corrective deadline, that same excess can effectively be taxed a second time when distributed.

65. A — A taxpayer under age 59½ may generally avoid the 10% early distribution penalty by taking a series of substantially equal periodic payments under Section 72(t), calculated using one of several IRS-approved methods, but must continue those payments for the longer of five years or until reaching age 59½, since modifying the payment schedule early generally triggers retroactive penalties.

66. C — A taxpayer who paid alternative minimum tax in a prior year due to certain timing-related preference items, such as the AMT preference generated by exercising incentive stock options, may generally be entitled to a minimum tax credit, carried forward to future years and used to offset regular tax liability in a year the taxpayer is not subject to AMT.

67. D — Injured spouse relief, requested using Form 8379, generally applies not only to offsets for the other spouse's separate tax debts, but also to offsets under the Treasury Offset Program for other federal debts, such as defaulted federal student loans or certain other federal agency debts, allowing the non-liable spouse to still claim their allocated share of the joint refund.

68. B — For a self-employed taxpayer, the Additional Medicare Tax threshold applicable to their filing status is generally reduced by any wages the taxpayer separately earned as an employee that year, since self-employment income and wages share a single combined threshold for the taxpayer's filing status rather than each type of income receiving its own separate full threshold amount.

69. A — The Form 8814 election allowing a parent to include a child's income directly on the parent's own return is generally available only if the child's income consists solely of interest, dividends, and capital gain distributions, all within specific dollar limits, and the child had no other type of income requiring a separate individual return.

70. C — Filing a joint return generally makes each spouse jointly and severally liable for the entire tax liability shown on that return, not merely liable for the portion attributable to their own individual income, meaning the IRS may generally pursue either spouse for the full amount, subject to potential relief such as innocent spouse relief in appropriate circumstances.

71. D — A taxpayer who is still legally married may nonetheless be treated as 'considered unmarried' for Head of Household purposes if specific requirements are met, generally including living apart from the spouse for the last six months of the year, filing a separate return, and maintaining a home that was a qualifying child's main home for over half the year.

72. A — A taxpayer who claims the standard deduction for regular tax purposes must generally add that same standard deduction amount back when computing alternative minimum taxable income, since the standard deduction, like several itemized deductions, is not an allowable deduction under the separate AMT system, which uses its own exemption amount instead.

73. B — A taxpayer whose return contains a substantial understatement of tax or reflects negligent disregard of rules and regulations may generally be subject to the accuracy-related penalty under Section 6662, equal to 20% of the portion of underpayment attributable to negligence or substantial understatement, imposed on the taxpayer directly and separate from any preparer penalty.

74. C — When a participant's retirement plan loan goes into default because required payments were not made, the outstanding loan balance is generally treated as a deemed taxable distribution to the participant, includible in gross income and potentially subject to the 10% early distribution penalty if the participant is under age 59½ and no exception applies.

75. D — An advisor should generally explain that an employer-sponsored plan such as a 401(k) typically receives broad, uniform creditor protection under federal ERISA law, while a traditional or

Roth IRA's protection from creditors outside of bankruptcy often depends more heavily on the specific state's own exemption laws, which can vary meaningfully in how much protection they provide.

76. B — An advisor should generally point out that donating appreciated stock held long-term directly to a qualified charity can avoid recognizing the gain on appreciation, while the client may still generally claim a deduction for the stock's full fair market value, subject to applicable AGI limits, often producing a better result than selling the stock and donating the after-tax proceeds.

77. D — An advisor should explain that a taxpayer may generally elect to use a portion of their federal income tax refund, via Form 8888, to purchase paper Series I savings bonds, in addition to, rather than instead of, the separate annual limit on electronically purchased I bonds, offering an additional avenue for a client interested in this particular savings vehicle.

78. A — An advisor should raise the Section 1202 qualified small business stock exclusion before a founder sells company stock, since stock meeting specific requirements, including original issuance by a qualifying C corporation and a sufficiently long holding period, generally over five years, may allow a substantial portion of the gain to be excluded from federal income tax.

79. C — An advisor should explain that premiums paid for a qualified long-term care insurance policy are generally treated as a deductible medical expense, but only up to an age-based dollar limit that increases with the taxpayer's age, and like other medical expenses, the deductible amount is still subject to the overall itemized medical expense floor of 7.5% of adjusted gross income.

80. B — An advisor should immediately raise the strict 30-day deadline for filing a Section 83(b) election, since a client who wants to be taxed on restricted stock's current, low value now, rather than its potentially higher value at vesting, must file this election with the IRS within 30 days of the grant, a deadline that cannot be extended.

81. C — An advisor should suggest spreading a large Roth conversion across multiple tax years, converting only the amount that keeps the client within a targeted tax bracket each year, rather than converting the entire balance in a single year and potentially pushing a large portion of the converted amount into a much higher marginal tax bracket than necessary.

82. D — An advisor should explain that a trust meeting specific IRS 'see-through trust' requirements, such as being valid under state law and having identifiable individual beneficiaries, can generally be treated as having a designated beneficiary for retirement account distribution purposes, while a trust failing to meet these requirements can result in much less favorable, accelerated distribution rules for the inherited account.

83. B — An advisor should raise the possibility of electing to aggregate certain commonly controlled and sufficiently interrelated businesses for Section 199A purposes, where the specific aggregation requirements are met, since combining the wages and qualified property of multiple related businesses can potentially support a larger overall QBI deduction than treating each business separately at higher income levels.

84. A — An advisor should emphasize that beneficiary designations on retirement accounts and life insurance policies generally control who receives those assets, regardless of what a more recently updated will might say, so a client who has experienced a major life event such as divorce should promptly review and update these designations rather than relying on the new will alone.

85. D — An advisor working with a client who owns rental properties in multiple states should coordinate estimated tax payments not only for the client's home state but also for each nonresident state where rental income is earned, since underpayment penalties can generally apply separately in each jurisdiction that taxes a portion of the client's rental income.

86. A — Because exercising a nonqualified stock option generates ordinary compensation income in the year of exercise, an advisor should raise the possibility of delaying exercise until the client's lower-income retirement year, if the options and market conditions allow, potentially resulting in that compensation income being taxed at a meaningfully lower marginal rate than exercising during a higher-income working year.

87. C — An advisor should ask the client to check whether their employer's Health FSA plan offers either a grace period, generally allowing additional time after year-end to incur and submit qualifying expenses, or a limited carryover allowance into the following plan year, since either feature can reduce the amount of unused funds lost under the use-it-or-lose-it rule.

88. B — The estate of a nonresident alien decedent who owned U.S.-situated property exceeding the applicable, generally much smaller, exemption amount is generally required to file Form 706-NA, a version of the estate tax return specifically designed for nonresident alien decedents, rather than the standard Form 706 used for a U.S. citizen or resident decedent's estate.

89. D — A U.S. citizen or resident who receives a gift or bequest from a covered expatriate, a former U.S. citizen or long-term resident who met specific net worth or tax liability thresholds upon expatriating, may generally owe a special transfer tax under Section 2801, calculated at the highest estate or gift tax rate applied to the value received.

90. A — A U.S. person who receives a gift exceeding $100,000 during the year from a nonresident alien individual or foreign estate is generally required to report the gift on Form 3520, even though the recipient owes no U.S. gift tax on the amount received, since gift tax generally falls on the donor and this filing is purely informational.

91. C — A grantor who retains a reversionary interest in a trust valued at more than 5% of the trust's value at creation generally causes the trust to be treated as a grantor trust for income tax purposes, meaning the trust's income, deductions, and credits are generally reported directly on the grantor's own return rather than taxed to the trust.

92. A — A non-willful failure to timely file a required FBAR generally carries a smaller civil penalty amount per violation, while a willful failure to file generally carries a far larger potential penalty, calculated as the greater of a substantial flat amount or a percentage of the unreported account's balance, reflecting the significantly greater culpability associated with a willful violation.

93. B — A trustee may generally elect to treat a small pre-need funeral trust as a Qualified Funeral Trust, allowing simplified income tax reporting for these numerous small trusts, often netting multiple qualifying trusts together on a single return rather than requiring the trustee to prepare a full separate Form 1041 for each individual pre-need funeral trust arrangement.

94. C — Administration expenses that qualify as deductible for both federal estate tax purposes on Form 706 and estate income tax purposes on the estate's Form 1041 generally require the executor to elect which return to claim them on, since double-deducting the same expense on both returns is generally not permitted, making this election an important part of estate tax planning.

95. D — A special election generally allows medical expenses of a decedent paid by the estate within one year after death to be treated as though paid by the decedent when the care was actually provided, allowing those expenses to be deducted as an itemized medical expense on the decedent's final individual Form 1040 rather than only on the estate's return.

96. B — A Crummey withdrawal right generally gives a trust beneficiary a temporary, limited right to withdraw a contribution shortly after it is made, converting what would otherwise be a future interest gift, generally ineligible for the annual gift tax exclusion, into a present interest gift qualifying for that exclusion, even though the beneficiary is expected not to exercise it.

97. D — A Totten trust, or informal bank account trust, generally passes directly to the named beneficiary outside of the probate process at the account owner's death, functioning much like a payable-on-death or transfer-on-death account designation, even though the original account owner retained complete control over the funds and could change the beneficiary at any time during their own lifetime.

98. A — A trust that wants to hold S corporation stock as a shareholder without disqualifying the corporation's S election generally must qualify, and make a timely election, as either a Qualified Subchapter S Trust, which must distribute all income currently to a single beneficiary, or an Electing Small Business Trust, which allows more flexibility but is taxed differently.

99. C — A special needs trust funded with the disabled beneficiary's own assets, sometimes called a first-party or self-settled special needs trust, generally must include a Medicaid payback provision, reimbursing the state for Medicaid benefits paid on the beneficiary's behalf from any trust assets remaining at death, a requirement not applicable to a third-party funded special needs trust.

100. B — An estate may generally claim a charitable contribution deduction, without the percentage-of-income limitations applying to an individual taxpayer's charitable deduction, for amounts of gross income permanently set aside for a qualified charitable purpose under the terms of the governing instrument, even before those amounts are actually paid to the charity, unlike rules applicable to individuals.