PRACTICE EXAM 24: SEE PART 2 — BUSINESSES (100 QUESTIONS)

This full-length simulation exam contains 100 multiple-choice questions covering SEE Part 2: Businesses, built to mirror the domain weighting of the official IRS Special Enrollment Examination. The official Part 2 exam, administered by PSI Services LLC, consists of 85 scored questions (plus unscored pretest questions) with a 3.5-hour time limit; this practice exam is expanded to 100 questions per the book's practical question-count override so that the total practice question bank across all Part 2 exams reaches a useful study volume, while domain weighting percentages are scaled proportionally from the official 85-question breakdown. For the most realistic practice, allow yourself 3.5 hours to complete this exam without interruption, using only scratch paper and a basic calculator as permitted at the PSI test center. The IRS-published passing score is a scaled score of 500 or higher on a 200-800 scale. Mark your answer for each question, then check your work against the Answer Key and Explanations section that follows. For an interactive, timed practice experience, use the Online Exam Simulator included with this book.

1. Renata operates a custom furniture refinishing activity as a sole proprietorship reported on Schedule C. She has shown a profit in 3 of the last 5 tax years, including the current year, and losses in the other two years. Under the profit-motive presumption for activities not engaged in for profit, what is the effect of this profit history?

A. The activity is automatically treated as a hobby, since sole proprietors cannot use this presumption at all.
B. The activity is presumed engaged in for profit, and the IRS bears the burden of proving otherwise.
C. The activity must show profit in four of the last five years before any presumption applies.
D. The presumption only applies when the activity earns a profit in all five consecutive years.

2. Marcus, a sole proprietor with no other earned income, has net profit from Schedule C of $80,000 for the year. Before applying the Social Security wage base or the additional Medicare tax, what percentage of his net profit is used as the base for computing self-employment tax under Section 1401?

A. 100% of net profit, since self-employment tax applies to the full reported amount without adjustment.
B. 50% of net profit, mirroring the employer-paid half of FICA taxes withheld from wage earners.

C. 65% of net profit, matching the effective rate after standard business expense adjustments.

D. 92.35% of net profit, reflecting the statutory reduction that approximates the employer-equivalent FICA deduction.

3. Wilson contributes appreciated land with a fair market value of $200,000 and an adjusted basis of $60,000 to a newly formed general partnership solely in exchange for a partnership interest, and the partnership assumes no liabilities in connection with the contribution. Under Section 721(a), what gain or loss does Wilson recognize?

A. No gain or loss is recognized on the contribution of property for a partnership interest.

B. Wilson recognizes $140,000 of capital gain immediately upon contributing the appreciated land.

C. Wilson recognizes ordinary income equal to the built-in gain inherent in the contributed land.

D. Wilson recognizes gain only to the extent the land's value exceeds $100,000 in total.

4. Meridian Partners, a partnership, makes a valid Section 444 election to retain a September 30 fiscal year rather than adopt the required calendar year, resulting in a deferral of income recognition to its partners. Under Section 7519, what must Meridian generally do to compensate the IRS for this deferral benefit?

A. Meridian must dissolve and reorganize as a calendar-year entity within five years of making the election.

B. Meridian's partners must each personally prepay their share of tax liability directly to the IRS every quarter.

C. Meridian must make an annual required payment approximating the tax deferral benefit its partners receive from the fiscal year.

D. Meridian must reduce its Section 179 deduction limit each year the fiscal-year election remains in effect.

5. Instead of receiving a capital interest, Delia receives a profits interest in a partnership in exchange for consulting services she performs for the partnership. The interest carries no right to a share of existing partnership capital if the partnership liquidated immediately after the grant. Under the safe harbor guidance for profits interests, what is the general tax treatment of the grant?

A. Delia recognizes ordinary compensation income equal to the discounted present value of future profit expectations.

B. Delia recognizes capital gain equal to the fair market value of the underlying partnership assets received.

C. The partnership must recognize gain as though it sold a proportionate share of its assets.

D. No taxable event occurs to Delia upon receipt, provided the safe harbor conditions continue to be met.

6. Partner Oscar's entire interest in the OPQ Partnership is completely liquidated on August 15, and OPQ continues to operate with its remaining partners for the rest of the calendar tax year. Under Section 706(c), what happens to the partnership's tax year with respect to Oscar?

A. The partnership's entire tax year closes for all partners, including those who continue after August 15.

B. The partnership tax year closes with respect to Oscar alone, ending his distributive share as of August 15.

C. The partnership tax year remains open for Oscar until the partnership's regular year-end in December.

D. The partnership must elect a new tax year for all partners following any complete liquidation.

7. Kestrel Partners LLC has a nonresident alien partner, Henrik, who holds a 20% interest and is allocated a share of the partnership's effectively connected taxable income for the year. What is the partnership generally required to do regarding this allocation under Section 1446?

A. Withhold and pay over tax on Henrik's allocable share of effectively connected income, regardless of actual distributions.

B. Withhold tax only in the year Henrik actually receives a cash distribution from the partnership.

C. Report the income to Henrik with no withholding obligation, since partnerships are flow-through entities.

D. Withhold tax at Henrik's individual marginal rate only if he fails to file a U.S. return.

8. Priya is a 30% partner in Cedar Grove Partnership and separately owns a warehouse that she leases to the partnership at a fair market rental rate under a standard commercial lease. She performs no partnership services related to this arrangement. How is this leasing arrangement treated for tax purposes under Section 707(a)(1)?

A. The rental payments are treated as a guaranteed payment for the use of Priya's capital.

B. The rental payments must be treated as a special allocation of partnership rental income.

C. Priya is treated as a party who is not a partner for purposes of this transaction.

D. The lease is disregarded entirely, and Priya reports no rental income from the arrangement.

9. A partnership is structured with a series of allocations and distributions that comply with the literal language of every Subchapter K provision but are designed principally to reduce the partners' aggregate federal tax liability in a manner inconsistent with the intent of the partnership tax rules. Under Reg. Section 1.701-2, what authority does the IRS have?

A. The IRS has no authority to challenge the arrangement if literal statutory language is satisfied.

B. The IRS may recast the transaction to achieve tax results consistent with the intent of Subchapter K.

C. The IRS must first obtain a court order before disregarding any partnership-level tax position.

D. The IRS may only impose a penalty but cannot alter the underlying tax treatment.

10. Two years after Faye contributes appreciated land with built-in gain to the FG Partnership, the partnership distributes that same land to a different partner, Grant, while Faye's own capital account remains fully intact and no distribution is made to her. Under Section 704(c)(1)(B), what is the tax consequence to Faye?

A. Faye recognizes no gain because the distribution was made to Grant rather than to her.

B. Grant recognizes the built-in gain as ordinary income upon receiving the distributed land.

C. The partnership recognizes gain at the entity level, and no gain passes through to any partner.

D. Faye recognizes the precontribution built-in gain that would have been allocated to her under Section 704(c).

11. Hillside Partnership incurs $53,000 of qualifying organizational expenditures in the year it begins business. Under Section 709(b), how much of this amount, if any, can Hillside immediately deduct as opposed to amortize, given the phase-out threshold applicable to the $5,000 first-year deduction?

A. Hillside may deduct $2,000 immediately, because the $5,000 allowance is reduced dollar-for-dollar by the $3,000 excess over $50,000, with the balance amortized.

B. Hillside may deduct the full $5,000 immediately, since organizational costs stay under the $60,000 total phase-out ceiling for eligibility.

C. Hillside may deduct nothing immediately, since any organizational costs exceeding $50,000 eliminate the entire first-year allowance completely.

D. Hillside may deduct $3,000 immediately, matching the exact dollar amount by which costs exceed the $50,000 phase-out threshold.

12. The HJ Partnership refinances its recourse debt in a manner that reduces partner Hank's share of partnership liabilities from $40,000 to $15,000, while his outside basis before the change, excluding any liability share, is otherwise unaffected. What is the tax consequence of this $25,000 reduction in Hank's share of liabilities under Section 752(b)?

A. Hank increases his outside basis by $25,000 because his personal liability exposure has decreased.

B. The partnership recognizes $25,000 of cancellation of debt income allocable to Hank alone.

C. Hank is treated as receiving a deemed cash distribution of $25,000, decreasing his outside basis.

D. No basis or distribution consequence occurs, since the underlying debt itself was merely refinanced.

13. Owen is the sole member of Falcon Ventures LLC, a disregarded entity for federal tax purposes. On July 1, Owen sells a 50% membership interest to Priscilla for cash, and the LLC continues operating with no other changes. Under Rev. Rul. 99-5, how is this conversion generally treated for federal income tax purposes?

A. Falcon Ventures continues to be disregarded, and Priscilla is treated as purchasing LLC assets directly.

B. Owen recognizes no gain at all, since disregarded entities cannot generate taxable transactions upon sale.

C. Owen is treated as selling a proportionate interest in each LLC asset, and a new partnership is formed.

D. The transaction is treated as a tax-free reorganization under the corporate reorganization provisions of Subchapter C.

14. The RS LLC, taxed as a partnership with two members, ceases to be a multi-member entity when member Sonia sells her entire 50% interest to the other member, Reuben, who becomes the sole remaining owner. Under Rev. Rul. 99-6, how is Reuben treated for federal tax purposes after the sale?

A. Reuben continues to hold a partnership interest, and the LLC files partnership returns going forward.

B. Reuben is treated as purchasing the LLC's assets, and the LLC becomes a disregarded entity.

C. Reuben must recognize no gain or loss, since LLC interest sales are always nonrecognition events.

D. The LLC is treated as liquidating into a newly formed C corporation automatically upon the sale.

15. Teresa's sole proprietorship generates $150,000 of qualified business income on Schedule C for the year, and her taxable income before any qualified business income deduction is well under the applicable threshold for wage and property limitations. Assuming no other limiting factors apply, what is the general Section 199A deduction available on this income?

A. 20% of the $150,000 of qualified business income, subject to Teresa's overall taxable income limitation.

B. 50% of the $150,000 of qualified business income, mirroring the wage-based limitation percentage.

C. 100% of the $150,000 of qualified business income, since sole proprietorships face no deduction cap.

D. 15.3% of the $150,000 of qualified business income, matching the self-employment tax rate applied.

16. Nadia uses 240 square feet of her home regularly and exclusively for her sole proprietorship consulting business and elects the simplified method for computing her home office deduction rather than tracking actual expenses. Under the simplified method, how is her deduction generally calculated?

A. Actual mortgage interest and utility bills are prorated based on the percentage of square footage used.

B. A flat $1,500 deduction applies automatically regardless of the actual square footage used for business.

C. Depreciation on the home is computed separately and added on top of the simplified square-footage rate.

D. A rate of $5 per square foot is applied, up to a maximum of 300 square feet.

17. Victor, a sole proprietor with no employees, wants to maximize his SEP-IRA contribution for the year based on his net self-employment earnings. Which adjustment must Victor make to his net Schedule C profit before applying the SEP contribution percentage, beyond simply using gross Schedule C income?

A. No adjustment is required; the full gross Schedule C receipts figure is used directly.

B. Net profit must be reduced by the deductible portion of self-employment tax before applying the SEP rate.

C. Net profit must be increased by the value of any employer matching contributions received.

D. Net profit must be reduced by the standard deduction before applying the SEP contribution rate.

18. Marguerite is a partner in an accounting firm organized as a limited liability partnership (LLP) under state law. A malpractice claim arises from the negligent acts of another partner, Theo, in which Marguerite had no involvement or supervisory role. What is Marguerite's general liability exposure for Theo's malpractice under typical LLP statutes?

A. Marguerite is fully personally liable for Theo's malpractice, identical to liability in a general partnership.

B. Marguerite has no liability protection at all, since LLP status only shields limited partners.

C. Marguerite is liable only for half of any judgment, regardless of her lack of involvement.

D. Marguerite is generally shielded from personal liability for Theo's malpractice under the LLP structure.

19. Falcon Manufacturing Corporation issues 1,000 shares of its own common stock to attorney Rita Delgado in exchange for legal services she performed in organizing the company. The shares have a fair market value of $40,000. Under Section 1032, what is Falcon Manufacturing's tax treatment of this stock issuance?

A. Falcon recognizes no gain or loss on the issuance, though it may deduct or capitalize $40,000 as compensation expense for the services received.

B. Falcon recognizes $40,000 of ordinary income because stock issued for services is treated as a taxable exchange of property.

C. Falcon recognizes capital gain equal to the excess of the stock's fair market value over its par value amount.

D. Falcon must recognize gain to the extent the stock's fair market value exceeds its adjusted basis in previously issued shares.

20. Harlan Cobb owns 100% of Cobb Fabrication Inc., a closely held C corporation. Over three years, Harlan advanced the corporation $300,000 with no written note, no fixed maturity date, no stated interest rate, and repayment made only when the corporation had excess cash. On audit, the IRS proposes reclassifying the advances as equity rather than debt. Which factor most strongly supports the IRS's position under the debt-versus-equity analysis?

A. The corporation used the advanced funds to purchase equipment used directly in its fabrication business operations.

B. Harlan reported the advances as a loan receivable on his personal financial statement each year.

C. The absence of a fixed repayment schedule and reliance on available cash flow resembles a shareholder's equity investment.

D. The corporation is organized as a C corporation rather than as a partnership or S corporation.

21. Meridian Holdings, a C corporation, sells 100% of the stock of its wholly owned subsidiary, Vantage Products Inc., to an unrelated individual buyer who does not join in a Section 338(h)(10) election. Meridian and Vantage instead want the sale treated as a disposition of Vantage's underlying assets for tax purposes. Which election allows this treatment even though the buyer is not a corporation?

A. A Section 338(g) election made unilaterally by the buyer corporation without Meridian's participation.

B. A Section 336(e) election made jointly by Meridian and Vantage to treat the stock sale as an asset sale.

C. A Section 355 spin-off election separating Vantage's assets before the stock sale closes.

D. A check-the-box election filed on Form 8832 changing Vantage's federal tax classification.

22. Redwood Corp, a corporate buyer, purchases 100% of the stock of Ashgrove Inc., an S corporation, from its sole shareholder. Both Redwood and Ashgrove's shareholder want the transaction treated as if Ashgrove sold its assets and liquidated, allowing the buyer a stepped-up basis in the assets while the target's shareholder reports gain on the deemed asset sale rather than the stock sale. What must occur for this treatment to apply?

A. Redwood alone files an election on its corporate return within one year of closing.

B. Ashgrove converts to a single-member LLC immediately before the stock closing occurs.

C. Ashgrove's shareholder personally guarantees Redwood's post-acquisition liabilities for two full years.

D. Redwood and Ashgrove's shareholder jointly make a timely Section 338(h)(10) election on Form 8023.

23. Blue Harbor Inc. terminated its S corporation election effective January 1, 2026. At the time of termination, its accumulated adjustments account balance was $85,000. During the one-year post-termination transition period, Blue Harbor distributes $60,000 cash to its sole shareholder, whose stock basis is $150,000. How is this distribution generally treated?

A. The entire $60,000 is taxed as an ordinary dividend because the corporation is now taxed as a C corporation.

B. The distribution is treated as wages subject to employment tax because the shareholder-employee relationship continued.

C. The distribution is tax-free and reduces stock basis to the extent it does not exceed the remaining AAA balance.

D. The distribution triggers immediate recognition of built-in gain under the Section 1374 recognition period rules.

24. Palisade Corp, an S corporation, owns 100% of Trailhead Inc., which has a valid QSub election in effect. Palisade sells 30% of Trailhead's stock to an outside investor, causing Trailhead to no longer be wholly owned by Palisade. What is the federal income tax result of this sale?

A. Trailhead's QSub election terminates, and Trailhead is treated as a new corporation formed via a deemed Section 351 contribution of assets.

B. Trailhead continues to be disregarded for federal tax purposes as long as Palisade retains voting control of the board.

C. Palisade must dissolve Trailhead entirely before any partial sale of its stock to an outside investor is permitted.

D. The sale is disregarded because QSub stock cannot legally be transferred to any party outside the parent's control group.

25. Ferncroft Partners LLC has two classes of membership interests: Class A units with preferred distribution rights and Class B units with standard rights. The LLC has three members, has not filed Form 8832, and no election has been made to be taxed as a corporation. How is Ferncroft classified for federal tax purposes?

A. As a partnership, because having multiple classes of membership interests does not change the default check-the-box classification for a multi-member LLC.

B. As an S corporation, because multiple classes of ownership interest automatically disqualify it from partnership status.

C. As a C corporation, because differing distribution rights among members violate the single-class default rule.

D. As a disregarded entity, because Class A's preferred rights effectively make it the sole economic owner.

26. Coldstream Utility Corp, a C corporation, receives a $200,000 payment from a real estate developer to help fund the extension of water lines to a new subdivision. The developer receives no stock or other equity interest in Coldstream in exchange. Under current law, how must Coldstream treat this contribution in aid of construction?

A. As a tax-free contribution to capital under Section 118, since Coldstream is a regulated public utility corporation.

B. As a reduction of Coldstream's basis in its existing water line assets rather than as income.

C. As a nontaxable capital contribution excluded from income because no stock was issued to the developer.

D. As gross income to Coldstream, since Section 118 no longer excludes contributions in aid of construction from nonshareholders.

27. Meadowlark Corp. has a $200,000 capital loss carryforward from a prior tax year. During the current year, Meadowlark undergoes an ownership change as defined in Section 382, triggering the related limitation under Section 383 on using this pre-change capital loss. What does Section 383 generally do?

A. It permanently disallows the entire pre-change capital loss carryforward, regardless of any capital gains recognized after the ownership change.

B. It caps the pre-change capital loss usable in each post-change year using a value-based formula tied to the long-term tax-exempt rate, mirroring Section 382.

C. It accelerates the capital loss carryforward, allowing the full amount to be used immediately in the year of the ownership change.

D. It converts the capital loss carryforward into an ordinary loss deduction, removing the usual capital loss carryover limitations entirely.

28. Ironwood Corp, a calendar-year C corporation, has taxable income of $500,000 before any charitable deduction and makes cash contributions of $65,000 to qualified public charities during the year. What is Ironwood's maximum current-year charitable contribution deduction, and what happens to any excess?

A. Ironwood may deduct the full $65,000 currently, and any amount disallowed in a future year is permanently lost.

B. Ironwood may deduct only $15,000 currently, and the remaining $50,000 is permanently disallowed with no carryforward permitted.

C. Ironwood may deduct $50,000 currently, limited to 10% of taxable income, and carry the remaining $15,000 forward up to five years.

D. Ironwood may deduct $65,000 currently because corporate charitable deductions are not subject to any taxable-income-based limitation.

29. Summit Ridge Corp incurs $52,000 of organizational expenditures, such as legal and accounting fees for drafting its corporate charter, in connection with its formation. How must Summit Ridge treat these costs under Section 248?

A. Because total organizational costs exceed $50,000, the $5,000 deduction phases out dollar for dollar, with the remainder amortized over 180 months.

B. The entire $52,000 must be capitalized permanently with no deduction or amortization ever allowed for corporate organizational costs.

C. Summit Ridge may deduct the full $52,000 immediately in the year the corporation begins active business operations.

D. Organizational expenditures must be amortized over exactly 60 months regardless of the total amount incurred by the corporation.

30. Cascade Corp generates a $400,000 net operating loss in 2025 and has $300,000 of taxable income (before any NOL deduction) in 2026. Cascade has no NOLs from tax years beginning before 2018. What is the maximum NOL deduction Cascade may claim on its 2026 return, and can it carry the loss back to 2024?

A. Cascade may deduct the full $300,000 in 2026, and it may also carry back any unused portion two years to 2024.

B. Cascade may deduct up to $240,000 in 2026, limited to 80% of taxable income, and generally may not carry the loss back at all.

C. Cascade may deduct up to $240,000 in 2026, and the unused $160,000 expires permanently after the current year with no further carryforward.

D. Cascade may deduct the full $400,000 in 2026 because post-2017 corporate net operating losses are not subject to any percentage limitation.

31. Cobalt Corp. adopts a plan of complete liquidation and, on a pro rata basis to all shareholders, distributes manufacturing equipment worth $250,000 with an adjusted basis of $90,000 to its shareholders in exchange for their stock. Under the general recognition rule of Section 336(a), what gain or loss must Cobalt report on this distribution?

A. Cobalt recognizes no gain, because a liquidating corporation never recognizes gain on distributing appreciated property to shareholders.

B. Cobalt recognizes ordinary income equal to the full fair market value of the equipment, without regard to its adjusted basis.

C. Cobalt recognizes gain only if a shareholder later resells the equipment within one year of the liquidating distribution.

D. Cobalt recognizes $160,000 of gain, as if it had sold the equipment to the shareholders for its fair market value.

32. Trader Simone holds two offsetting positions in actively traded property that together form a straddle under Section 1092. She closes the losing leg for a $14,000 loss while the offsetting leg remains open with $9,000 of unrecognized gain at year-end. How much of the $14,000 loss may Simone currently deduct?

A. The full $14,000 loss is currently deductible, since straddle positions are treated independently for tax purposes.

B. None of the $14,000 loss is deductible until both legs of the straddle are fully closed out.

C. Only $5,000 of the loss is currently deductible; the remaining $9,000 is deferred until the offsetting position closes.

D. The $14,000 loss is treated as long-term capital loss regardless of Simone's actual holding period in either leg.

33. Before opening its doors, newly formed Thistlewood Corp incurs $48,000 of investigatory and pre-opening expenses, including market research and employee training conducted prior to the start of active business. How are these start-up expenditures treated under Section 195?

A. The full $48,000 must be capitalized indefinitely, with no deduction allowed until the corporation is eventually liquidated or sold.
B. The full $48,000 is deductible immediately in the year incurred, regardless of when active business operations actually begin.
C. Thistlewood may deduct $5,000 immediately, subject to phase-out for costs over $50,000, and amortize the remainder over 180 months from when business begins.
D. Start-up costs must be amortized over exactly 60 months with no immediate deduction ever permitted in the first year.

34. Priya Nair owns 15% of the outstanding stock of Cardinal Services Inc., an S corporation, and works there as an employee. Cardinal Services pays $9,000 in health insurance premiums on Priya's behalf during the year. How must this premium payment be treated for federal tax purposes?

A. The $9,000 must be included in Priya's Form W-2 wages, though she may generally claim an offsetting above-the-line self-employed health insurance deduction.
B. The $9,000 is fully excludable from Priya's income because employer-paid health insurance is always tax-free to any corporate employee.
C. The $9,000 is treated as a nondeductible distribution to Priya and reduces her stock basis in Cardinal Services accordingly.
D. The $9,000 must be reported as self-employment income subject to self-employment tax on Priya's individual return.

35. Deacon Realty Corp, a C corporation, pays its sole shareholder, Marla Voss, monthly rent of $12,000 for office space she leases to the corporation, though comparable market rent for similar space is only $6,000 per month. How is the excess $6,000 monthly payment most likely characterized for tax purposes?

A. As additional deductible rent expense to Deacon Realty, since the parties freely negotiated the lease agreement terms.
B. As a tax-free return of capital to Marla, reducing her stock basis in Deacon Realty Corp.

C. As wages subject to employment tax withholding, since Marla is both landlord and shareholder of the corporation.

D. As a constructive dividend to Marla, nondeductible by Deacon Realty and taxable to her as ordinary dividend income.

36. Falcon Distributors, a U.S. company using the dollar as its functional currency, sells inventory to a foreign customer and is paid in euros 60 days later. Between the sale date and payment date, the euro strengthens against the dollar, producing a $3,000 foreign currency gain on the transaction. Under Section 988, how is this gain characterized?

A. As capital gain, because the gain arises from fluctuation in a foreign currency exchange rate.

B. As ordinary income, separately computed from the gain or loss on the underlying sale of inventory.

C. As a reduction to the cost of goods sold reported on the original inventory sale.

D. As tax-exempt income, because currency fluctuation gains are not includible in gross income.

37. Meridian Imports Inc. purchases inventory from its wholly owned foreign subsidiary and claims a customs value of $40 per unit for tariff purposes, while recording a cost basis of $55 per unit for U.S. income tax purposes on the same imported goods. Under Section 1059A, what is the maximum basis Meridian may use for U.S. tax purposes?

A. $55 per unit, because financial accounting cost is controlling regardless of customs valuation.

B. $47.50 per unit, the average of the customs and tax-reported values.

C. $40 per unit, because tax basis cannot exceed the value declared for customs purposes.

D. $55 per unit, adjusted upward for any freight and insurance costs incurred.

38. Voss Securities LLC is a registered dealer in securities that holds shares of Larkspur Corp. as inventory held primarily for sale to customers in the ordinary course of its dealer business. Voss sells the Larkspur shares at a loss and repurchases substantially identical shares within the inventory 25 days later. How does the wash sale rule of Section 1091 apply to this loss?

A. The wash sale rule does not apply, because Section 1091 excludes dealer-inventory securities sold in the ordinary course of business.

B. The wash sale rule fully disallows the loss and adds it to the basis of the repurchased shares.

C. The wash sale rule applies but permits Voss to deduct 50% of the disallowed loss immediately.
D. The wash sale rule applies only if Voss repurchases the shares within 15 days rather than 30 days.

39. Dalton Retail Corp. holds shares of a former supplier that became completely worthless during March of the current tax year, confirmed by identifiable events establishing zero value. Dalton did not sell or exchange the stock. Under Section 165(g), on what date is Dalton deemed to have sold this worthless stock for purposes of determining the tax year and holding period of the resulting loss?

A. March 2024, the specific date on which the stock actually became completely worthless.
B. January 1, 2024, the first day of the tax year in which worthlessness occurred.
C. The date Dalton formally writes off the stock in its accounting records.
D. December 31, 2024, the last day of the tax year in which the stock became worthless.

40. Prosper Holdings Inc. held a right under a supply contract that qualified as a capital asset in its hands. The counterparty terminated the contract before performance and paid Prosper $80,000 to settle its rights under the agreement. How is Prosper's $80,000 payment treated for tax purposes under Section 1234A?

A. Capital gain or loss, because termination of a right relating to a capital asset is treated as a sale or exchange.
B. Ordinary income, because payments received to settle contract rights are always treated as compensation for services rendered.
C. A nontaxable return of capital that simply reduces Prosper's basis in other, unrelated business assets.
D. Section 1231 gain, because the underlying contract involved the supply of depreciable business equipment.

41. Fenwick Logistics Corp., an accrual-method taxpayer, was found liable in a tort lawsuit and accrued a $200,000 liability on its books in November 2024 for damages owed to an injured claimant. Fenwick did not actually pay the claimant until February 2025. Under the all-events test, in which year does economic performance occur for this liability?

A. 2024, because the liability became fixed and determinable when the court entered judgment.

B. 2025, because economic performance for a tort liability occurs only when payment is actually made to the claimant.

C. 2024, under the recurring item exception, because tort settlements recur annually for most businesses.

D. 2025, but only if Fenwick elects to defer the deduction under Section 461(h).

42. Ridgemont Retail Corp. owned a commercial building that was condemned by the city in June 2024, and Ridgemont received condemnation proceeds exceeding its adjusted basis in the property. Ridgemont intends to defer gain recognition under Section 1033 by acquiring qualified replacement property. What is the deadline for Ridgemont to complete the replacement?

A. December 31, 2025, exactly 18 months after the close of the tax year of condemnation.

B. December 31, 2026, four full years after the close of the tax year of condemnation.

C. December 31, 2027, three years after the close of the tax year in which the condemnation gain was realized.

D. December 31, 2024, before the close of the tax year in which the condemnation occurred.

43. Copper Kettle Café Inc., a small accrual-eligible business, wants to report its inventory-related purchases and sales of merchandise using the accrual method while reporting its other income and expenses, such as rent and utilities, using the cash method. Under Reg. Section 1.446-1(c)(1)(iv), is this combination permitted?

A. No — a taxpayer must use one overall accounting method for every item reported on a single tax return.

B. Yes — combining accrual for inventory purchases and sales with cash for other items is permitted if it clearly reflects income.

C. Yes — but only C corporations with average gross receipts above $30 million may adopt a hybrid method.

D. No — hybrid accounting methods were eliminated for all taxpayers under the Tax Cuts and Jobs Act.

44. Falcon Fabrication Inc. placed several pieces of depreciable equipment in service during 2024. Of the total $500,000 basis of property placed in service during the year, $220,000 (44%) was placed in service during the fourth quarter. Which depreciation convention must Falcon apply to all of its 2024 property additions?

A. The half-year convention, because most business equipment defaults to this convention regardless of timing.

B. The mid-month convention, because more than 40% of basis was placed in service in the final quarter.

C. The full-month convention, because Falcon may elect any convention that minimizes current-year depreciation.

D. The mid-quarter convention, because more than 40% of total depreciable basis was placed in service in the year's final quarter.

45. A fire destroyed manufacturing equipment used in Beacon Print Shop's business, located in a federally declared disaster area. The equipment had an adjusted basis of $60,000 and a fair market value of $50,000 immediately before the fire, and zero value afterward. Beacon received $35,000 in insurance reimbursement for the loss. What is Beacon's deductible casualty loss before any percentage limitations?

A. $25,000, computed as the $60,000 adjusted basis reduced only by the $35,000 insurance reimbursement.

B. $15,000, computed as the lesser of adjusted basis or decline in fair market value, reduced by insurance proceeds received.

C. $50,000, the full pre-fire fair market value, without any reduction for insurance proceeds.

D. $10,000, computed as the fair market value decline reduced by both insurance proceeds and adjusted basis.

46. Rowan Hardware Supply Inc. deducted $18,000 in miscellaneous ordinary business expenses but lost the underlying receipts in an office flood. The expenses are not subject to the strict substantiation requirements of Section 274(d). Under the Cohan rule, how may Rowan support the deduction on examination?

A. Rowan cannot deduct any of the $18,000 without original receipts, regardless of other evidence.

B. Rowan must file Form 3115 to substitute an alternative accounting method for the lost records.

C. A court or examiner may allow a reasonable estimate of the expenses based on credible surrounding evidence.

D. Rowan must reduce the deduction to exactly 50% of the claimed amount as a substantiation penalty.

47. Sable Equipment Sales Inc. sold a piece of business machinery in 2024 for a gain, with payments to be received over the following three years, which would normally qualify for installment reporting under Section 453. Sable instead wants to report the entire gain on its 2024 return rather than spreading it over the payment years. What must Sable do?

A. Nothing; installment reporting is elective only for the buyer, never the seller of the property.

B. File Form 3115 to request a change in the seller's overall method of accounting for the sale.

C. Wait until all payments are collected, then amend the 2024 return to report the full gain.

D. Affirmatively elect out of the installment method under Section 453(d) by the due date of the 2024 return.

48. Timberline Home Builders Inc. constructs single-family residences and townhomes containing no more than four dwelling units each. Because its contracts qualify as home construction contracts under Section 460(e)(6), how are these contracts treated for long-term contract accounting purposes, regardless of Timberline's average annual gross receipts?

A. Home construction contracts are exempt from the percentage-of-completion requirement and may instead use the completed-contract or another permissible method.

B. Home construction contracts must always use percentage-of-completion, since only non-residential contracts qualify for any exemption.

C. Home construction contracts qualify for exemption only if Timberline's average annual gross receipts are below the small contractor threshold.

D. Home construction contracts are treated identically to inventory sales and must use the specific identification method exclusively.

49. Larkin Equipment Corp. purchased machinery from Delta Manufacturing on credit, financed by a note payable directly to Delta as the seller. Before Larkin made any payments, Delta agreed to reduce the outstanding note balance by $12,000 due to a pricing dispute, while Larkin remained solvent and outside bankruptcy. How should Larkin treat the $12,000 reduction under Section 108(e)(5)?

A. As ordinary cancellation of debt income includible in gross income in the year of the reduction.

B. As a capital gain recognized in the year the note is eventually paid off in full.

C. As tax-exempt income permanently excluded from Larkin's gross income under the insolvency exclusion.

D. As a purchase price reduction that decreases Larkin's basis in the machinery, rather than as income.

50. Quarry Industrial Corp. sold Section 1245 equipment in an installment sale, realizing $90,000 of gain, of which $70,000 represents depreciation recapture and $20,000 represents Section 1231 gain. Quarry will collect payments over four years. Under Section 453(i), how must Quarry report the $70,000 of depreciation recapture?

A. Spread ratably over the four years as payments are actually received from the buyer.

B. Deferred entirely and not recognized until the final installment payment is collected in year four.

C. Recognized in full as ordinary income in the year of sale, regardless of the installment payment schedule.

D. Excluded from income entirely because installment sale treatment eliminates recapture on Section 1245 property.

51. Owner-employee Marcus, age 52, participates in his S corporation's 401(k) plan. His FICA wages from the S corporation in the prior year exceeded $145,000 (indexed). Under the SECURE 2.0 Act's catch-up contribution rule effective for 2026, how must Marcus make his age-50 catch-up contribution for the current year?

A. Marcus may make the entire catch-up contribution pre-tax, since S corporation owner-employees are exempt from this rule.

B. Marcus must make the entire catch-up contribution as a Roth contribution, since his prior-year wages exceeded the indexed threshold.

C. Marcus may split the catch-up contribution evenly between pre-tax and Roth, regardless of his prior-year wage level.

D. Marcus is barred from making any catch-up contribution once his prior-year wages exceed the indexed threshold.

52. Ridgeline Partners leases an office building to a state government agency under a long-term lease that causes the building to be classified as "tax-exempt use property" under Section 168(h). How must Ridgeline depreciate this property?

A. Using the Alternative Depreciation System (ADS), because tax-exempt use property is statutorily required to use it

B. Using regular MACRS under the General Depreciation System (GDS) with the standard 39-year straight-line recovery period

C. Using GDS unless Ridgeline affirmatively elects ADS for the entire class of nonresidential real property

D. Using bonus depreciation to fully expense the entire property cost in the year of acquisition

53. Solaris Components Inc. manufactures eligible solar wafers and sells them to an unrelated third party during the tax year. The components qualify as "eligible components" under Section 45X. What is the general nature of the Section 45X advanced manufacturing production credit?

A. A per-unit production credit on eligible components produced domestically and sold, phasing down after 2029 for some

B. A one-time investment credit equal to 30% of the cost of the manufacturing facility used to produce the components

C. A credit available only to purchasers of domestically manufactured components, not to the manufacturers themselves

D. A deduction, rather than a credit, equal to the cost of domestic content used in production

54. Harbor Manufacturing hires Luis, a certified member of a WOTC targeted group, at $14 per hour. Luis works 350 hours during his first year of employment. Under the two-tier wage limitation of Section 51(i), what percentage of Luis's qualified first-year wages applies in computing Harbor's credit?

A. 40%, because any hours worked above 120 automatically qualifies for the maximum rate

B. 50%, the flat rate applicable to all WOTC targeted groups regardless of hours worked

C. 0%, because employees must work a minimum of 400 hours before any credit is allowed

D. 25%, because Luis worked at least 120 but fewer than 400 hours during the year

55. Architect Priya Nair designs energy-efficient HVAC and lighting systems for a new public elementary school owned by a local school district. Because the school district cannot use the Section 179D deduction itself, how may the deduction be treated?

A. The deduction is permanently lost because government-owned buildings are wholly ineligible for Section 179D

B. The school district may allocate the Section 179D deduction to Priya, the designer of the energy-efficient systems

C. The deduction may only be allocated to the general contractor who physically installed the systems

D. The deduction automatically passes to the school district's taxpayers through a refundable credit mechanism

56. A Qualified Opportunity Fund purchases an existing warehouse in a qualified opportunity zone for $800,000 (excluding land value of $150,000). To satisfy the "original use or substantial improvement" requirement without meeting original use, what must the fund do within 30 months?

A. Spend at least $150,000 improving the property, an amount matching the land's allocated value

B. Spend any amount on improvements at all, since no minimum threshold applies to existing buildings

C. Spend more than $800,000 (the building's adjusted basis, excluding land) on improvements to substantially improve the property

D. Sell the property and reinvest the proceeds in a new original-use asset within the same zone

57. An investor holds a Qualified Opportunity Fund investment for more than ten years before selling it. What is the primary tax benefit available upon disposition due to satisfying the ten-year holding requirement?

A. The investor may elect a basis step-up to fair market value, excluding post-acquisition appreciation from gain

B. The originally deferred gain is permanently forgiven and never recognized in any circumstance

C. The investor receives an automatic 15% basis increase applied only at the ten-year mark

D. The ten-year holding period eliminates the requirement to have invested capital gains within 180 days

58. A farming business elects out of the Section 163(j) business interest expense limitation to preserve full interest deductibility. As a required consequence of this election, how must the business depreciate property used predominantly in the farming business?

A. Using GDS combined with 100% bonus depreciation for all qualifying farm assets

B. Using GDS with the mid-quarter convention automatically applied to all farm equipment

C. Using Section 179 exclusively, since ADS is unavailable to electing farming businesses

D. Using ADS for any property with a recovery period of 10 years or more

59. Vance sold his business and recognized a gain on the disposition of purchased goodwill that had been amortized under Section 197 since acquisition. How is this gain characterized for depreciation recapture purposes?

A. Entirely Section 1231 gain, because goodwill is never subject to any depreciation recapture rules

B. Entirely capital gain, because intangible assets are excluded from the recapture rules altogether

C. Section 1245 ordinary income recapture up to prior amortization, with any excess as Section 1231 gain

D. Section 1250 recapture computed using the applicable straight-line percentage reduction formula each year

60. Marta exchanges real property with an adjusted basis of $200,000, subject to a $60,000 mortgage, for like-kind real property worth $310,000 subject to a $40,000 mortgage assumed by the other party, plus $10,000 cash received. What is treated as boot received in this like-kind exchange?

A. Only the $10,000 cash, because liability relief never constitutes boot in a like-kind exchange

B. The $10,000 cash plus the $20,000 net liability relief ($60,000 relieved minus $40,000 assumed)

C. The full $60,000 liability relieved, without offsetting the $40,000 liability assumed

D. Nothing, because liabilities and cash are disregarded when both properties are real property

61. A qualified small business with no income tax liability and gross receipts under the statutory threshold wants to benefit from its Section 41 research credit in the current year. What election allows the business to realize immediate value from the credit?

A. An election to carry the credit back five years against prior income tax liability

B. An election under Section 41(h) to apply up to $500,000 against payroll tax liability

C. An election to convert the credit into a refundable income tax credit paid by the Treasury

D. An election to sell the unused research credit to an unrelated corporation for cash

62. Before considering the Section 199A deduction, a single taxpayer has combined QBI of $150,000 from a qualified trade or business, taxable income of $120,000, and no capital gains. How is the taxpayer's Section 199A deduction ultimately limited?

A. To the lesser of 20% of QBI ($30,000) or 20% of taxable income minus capital gain ($24,000)

B. To exactly 20% of QBI regardless of the taxpayer's overall taxable income for the year

C. To the greater of 20% of QBI or 20% of taxable income, whichever produces the larger deduction

D. To 20% of taxable income only, since QBI never factors into the final limitation

63. Beacon Utility installs a standalone battery energy storage system with at least 5 kilowatt-hours of capacity, not connected to a co-located solar facility. Under current law, how is this energy storage property treated for investment tax credit purposes?

A. It is ineligible for any Section 48 credit because storage must be paired with a solar or wind facility

B. It qualifies only for accelerated depreciation, since storage technology was permanently excluded from Section 48

C. It qualifies for the credit only if it stores electricity generated exclusively from a fossil fuel source

D. It independently qualifies as energy property for the Section 48 credit, without requiring co-location with renewable generation

64. Meridian Café, a small business meeting the eligibility requirements for the Disabled Access Credit, incurs $9,000 of eligible access expenditures in the current year to comply with ADA accessibility requirements. What is the maximum disabled access credit Meridian may claim?

A. $9,000, equal to 100% of all eligible expenditures incurred during the year

B. $2,250, computed as 25% of the eligible expenditures with no dollar cap applied

C. $4,375, computed as 50% of eligible expenditures exceeding $250, capped at a $5,000 credit

D. $5,000, the flat statutory credit amount regardless of the expenditures actually incurred

65. Kessler Builders holds several parcels of land that it regularly subdivides and sells to individual homebuyers in the ordinary course of its business. When one parcel is sold at a gain, how is that gain characterized?

A. Section 1231 gain, because all real property held longer than one year automatically qualifies

B. Section 1250 recapture income, because land is treated as depreciable real property under Section 1250

C. Section 1245 ordinary income recapture, since land held for sale is treated as personal property

D. Ordinary income, because property held for sale to customers in the ordinary course of business is excluded

66. Nina sells cosmetics door-to-door for Bright Glow Products under a written contract stating she will not be treated as an employee for federal tax purposes. Substantially all her compensation is directly related to sales volume rather than hours worked. How should Bright Glow treat Nina under federal employment tax rules?

A. As a common-law employee subject to full FICA and FUTA withholding
B. As a statutory employee subject to FICA but exempt from FUTA
C. As a statutory nonemployee, not subject to income tax or FICA/FUTA withholding
D. As an independent contractor requiring Section 530 relief documentation

67. A newly hired employee fails to submit a completed Form W-4 before the first payroll date. Under IRC Section 3402(f)(2)(B), how must the employer compute federal income tax withholding for this employee until a valid W-4 is furnished?

A. Withhold as if the employee were single with no other adjustments claimed
B. Withhold at the highest supplemental wage flat rate of 37%
C. Withhold nothing until the employee submits a completed W-4
D. Withhold using the employee's prior employer's last W-4 on file

68. An employer provides an employee a company vehicle with a fair market value at first availability that does not exceed the IRS's annual maximum threshold for this method. The employee drives at least 10,000 miles per year and the vehicle is regularly used in the employer's business. Which method may the employer use to value the personal-use portion of the vehicle as a fringe benefit?

A. The commuting valuation rule based on a flat $1.50 per one-way trip
B. The cents-per-mile rule using the standard mileage rate for personal miles driven
C. The lease value table method regardless of the vehicle's fair market value
D. The unrestricted use method exempting all personal mileage from income

69. An employer discovers in March, after already filing Forms W-2 and W-3 with the Social Security Administration for the prior year, that an employee's Social Security wages were understated. What must the employer do to correct this error?

A. File Form W-2c with a transmittal Form W-3c and furnish a copy to the employee

B. File an amended Form 941-X only, since W-2 corrections are automatic

C. Wait until the following year-end to correct the figures on the next W-2

D. Issue a corrected Form 1099-NEC in place of the original W-2

70. Casey's Diner paid FICA tax on $18,000 of reported employee tips during the year. Of that amount, $6,500 represented the portion of tips considered necessary to bring employee wages up to $5.15 per hour (the frozen federal minimum wage used for this calculation). What is the maximum Section 45B FICA tip credit Casey's Diner may claim, based on the employer's 7.65% FICA rate?

A. 7.65% of the full $18,000 in reported tips

B. 7.65% of the $6,500 minimum-wage-offset portion only

C. 7.65% of the $11,500 remaining after subtracting the minimum-wage-offset portion

D. A flat credit equal to 100% of employer FICA tax paid on tips

71. An employer contributes to the Health Savings Accounts of its employees outside of a cafeteria plan. Employee A works full-time and Employee B works part-time, and both are HSA-eligible with self-only coverage. Under the HSA comparability rules, how must the employer structure its contributions to avoid a 35% excise tax?

A. Contribute a higher dollar amount to full-time employees than part-time employees automatically

B. Contribute only to employees who have not yet met their deductible

C. Contribute based solely on each employee's individual account balance

D. Contribute the same dollar amount or same percentage of the deductible to all comparable participating employees

72. An airline allows its employees to fly on a standby basis at no charge, using seats that would otherwise remain empty, at no substantial additional cost to the airline. How is this benefit treated for federal employment tax purposes?

A. Fully taxable wages subject to FICA and income tax withholding
B. Excludable from wages as a no-additional-cost service fringe benefit
C. Taxable only to the extent the seat's retail value exceeds $50
D. Excludable only if offered exclusively to highly compensated employees

73. Harold works as a cashier in the retail hardware store owned and operated by his daughter as a sole proprietorship. How should the wages paid to Harold be treated for federal employment tax purposes?

A. Exempt from FICA and FUTA because Harold is a family member
B. Subject to FICA and income tax withholding, but exempt from FUTA
C. Subject to FUTA and income tax withholding, but exempt from FICA
D. Subject to FICA, FUTA, and income tax withholding with no exceptions

74. A business hired an employee on March 1, 2020, and the employee's employment was terminated on February 1, 2024. Under federal recordkeeping requirements for Form I-9, Employment Eligibility Verification, until what date must the employer retain the completed form?

A. February 1, 2025 — one year after termination, since it is later than three years after hire
B. March 1, 2023 — three years after the hire date regardless of termination
C. February 1, 2024 — immediately upon termination of employment
D. March 1, 2027 — seven years after the hire date

75. Dr. Alvarez, a self-employed physician, performs surgeries at three different hospitals but has no fixed office space at any of them. She uses a dedicated room in her home exclusively and regularly to handle billing, scheduling, and patient records, with no other fixed location where she conducts these administrative activities. Does Dr. Alvarez's home office qualify as her principal place of business?

A. No, because performing surgery, not administrative work, is her principal business activity
B. No, because a home office can never qualify when substantial services are performed elsewhere
C. Yes, because she uses the space exclusively and regularly for administrative activities with no other fixed location available for them

D. Yes, but only if she elects the actual expense method instead of the simplified method

76. A self-employed contractor purchases a new SUV with a gross vehicle weight rating (GVWR) of 6,800 pounds and uses it 100% for business. Because the vehicle exceeds 6,000 pounds GVWR, it is not subject to the luxury automobile depreciation limits of Section 280F. However, what special limitation still applies specifically to Section 179 expensing for this heavy SUV?

A. No Section 179 deduction is allowed for any vehicle exceeding 6,000 pounds
B. Section 179 expensing is capped at 50% of the vehicle's purchase price
C. The vehicle must be depreciated over a mandatory 10-year recovery period instead
D. Section 179 expensing for the SUV is capped at a specific annual dollar limit under Section 179(b)(5)

77. A farming operation pays cash wages to agricultural workers throughout the year and meets the wage threshold requiring federal employment tax reporting. Which form must this agricultural employer file annually to report income tax withholding and both employee and employer shares of Social Security and Medicare tax, instead of the quarterly form used by most employers?

A. Form 941, filed quarterly like all other employers
B. Form 944, filed annually only for very small non-agricultural employers
C. Form 940, which reports only federal unemployment tax
D. Form 943, Employer's Annual Federal Tax Return for Agricultural Employees

78. A U.S. business hires a foreign individual, a nonresident alien, as an independent contractor to perform services entirely outside the United States. The contractor submits a completed Form W-8BEN certifying foreign status. How should the business treat payments to this contractor for federal withholding purposes?

A. Apply 24% backup withholding because no Form W-9 was submitted
B. Apply neither backup withholding nor Chapter 3 withholding, since the income is foreign-source
C. Apply the standard 30% Chapter 3 nonresident alien withholding rate
D. Apply both backup withholding and Chapter 3 withholding simultaneously

79. The IRS examines a restaurant's records and determines that employees underreported tip income for FICA purposes. Under Section 3121(q), when does the employer become liable for the additional employer share of FICA tax on these previously unreported tips?

A. Only after the IRS issues a formal notice and demand for the tax
B. Immediately when the underreporting occurs, regardless of IRS action
C. Only if the employer voluntarily self-assesses the tax on an amended return
D. Never, because employers are not liable for tax on unreported employee tips

80. The Ashgrove Family Trust's governing instrument permanently and irrevocably sets aside $40,000 of current-year trust income for the American Red Cross, a qualified public charity, but the funds will not actually be paid out until the following tax year. Under what provision may the trustee claim a current-year deduction for the set-aside amount?

A. Section 661 distributable net income deduction for amounts paid
B. Section 663(a) separate share rule for multiple beneficiaries
C. Section 642(c) charitable set-aside deduction for amounts permanently set aside
D. Section 645 election to treat a trust as part of the estate

81. Decedent Harold Vance owned a traditional IRA worth $200,000 at his death. His estate paid federal estate tax attributable to the IRA. When Harold's daughter, the named beneficiary, withdraws funds from the inherited IRA, how is the income in respect of a decedent treated for income tax purposes?

A. The distributions are entirely tax-free because the estate already paid tax
B. The distributions retain ordinary income character, and estate tax on the IRD may be deducted
C. The distributions receive a full basis step-up eliminating income tax entirely
D. The distributions are treated as capital gain under basis step-up rules

82. Grandmother Elena Cruz transfers $18,000 annually into a trust for her 10-year-old grandson. The trust permits the trustee to use income and principal for the minor's benefit before age 21, and any remaining trust property must be distributed to the minor at age 21 (or to his estate if he dies earlier). What allows these transfers to qualify for the annual gift tax exclusion despite the minor having no present right to immediate possession?

A. Section 2503(c) minor's trust exception, deeming the transfer a present interest under its statutory requirements

B. The Crummey withdrawal power granted to the minor's legal guardian

C. Section 2032A special use valuation applied to trust corpus

D. The generation-skipping transfer tax annual exclusion under Section 2642(c)

83. The Whitfield Foundation, a private foundation, purchases a used company vehicle from Marcus Whitfield, a substantial contributor and foundation manager, paying him $22,000, which independent appraisers confirm is fair market value. Is this transaction self-dealing under Section 4941?

A. No, because the price paid was confirmed to equal fair market value

B. No, because Marcus Whitfield does not qualify as a disqualified person

C. No, because the transaction amount falls below the $25,000 threshold

D. Yes, because any sale between a foundation and a disqualified person is self-dealing regardless of price

84. Executive Priya earns $450,000 in compensation this year from the sponsor of her employer's qualified profit-sharing plan. For purposes of calculating the employer's contribution and allocation to Priya's account, Section 401(a)(17) limits the compensation taken into account to what amount for 2024?

A. The full $450,000, since Section 401(a)(17) applies only to defined benefit plans, not profit-sharing plans.

B. $200,000, an amount Priya's employer sets internally without reference to any statutory limit.

C. $345,000, the annually indexed statutory compensation limit applicable to qualified plans for 2024.

D. $69,000, the same dollar figure as the Section 415(c) annual additions limit for that year.

85. Community Outreach Ministries is a central organization holding a group exemption letter that covers 45 affiliated local chapters sharing its purpose and general supervision. How do the subordinate chapters typically satisfy their annual information return filing requirement under Section 6033?

A. Each subordinate must independently apply for its own Section 501(c)(3) determination letter

B. The central organization may file one group return covering authorizing subordinates, satisfying their Section 6033 obligation

C. Subordinates are permanently exempt from any Form 990-series filing once covered by the group exemption

D. Subordinates must each file Form 1023 annually to maintain group exemption status

86. Retiree Wilma Osgood, age 74, directs her IRA custodian to transfer $12,000 directly from her traditional IRA to her local food bank, a qualified public charity. Wilma's required minimum distribution for the year is $10,000. How does this qualified charitable distribution affect her taxable income and RMD?

A. The $12,000 is excluded from Wilma's gross income and satisfies her entire $10,000 RMD for the year

B. Wilma must report the full $12,000 as income but may claim an itemized charitable deduction

C. Only $10,000 of the QCD is excluded from income, with the excess $2,000 taxable

D. Wilma may not use a QCD because she has not yet reached age 75

87. The executor of Frank Delgado's estate is considering the Section 2032 alternate valuation date election. The estate's assets declined in value during the six months after Frank's death. Which condition must be satisfied for the executor to make this election?

A. The election is available only if the estate is not required to file Form 706

B. The election may be made separately for each asset the executor chooses

C. The election must decrease both the value of the gross estate and the total estate and GST tax liability

D. The election is automatically applied whenever asset values decline after death

88. Married couple Rajesh and Anika Patel wish to gift $34,000 to their adult daughter this year. Rajesh made the entire transfer from his separately owned brokerage account. If they elect gift splitting under Section 2513 on a timely filed gift tax return, how is the gift treated for gift tax purposes?

A. Only Rajesh is treated as the donor, and the full $34,000 is subject to gift tax reporting

B. Gift splitting is unavailable because the funds came entirely from Rajesh's separate account

C. The gift is automatically split without any election or consent required from Anika

D. Each spouse is treated as having made half of the gift, allowing both annual exclusions to apply

89. Trustee Diane Marsh distributes appreciated stock with a fair market value of $50,000 and an adjusted basis of $30,000 from a complex trust to a beneficiary, in satisfaction of a discretionary distribution, without making any special election. How is the distribution generally treated under Section 643(e)?

A. The trust recognizes $20,000 of taxable gain, and the beneficiary takes a fair market value basis

B. The trust does not recognize gain, and the beneficiary takes a carryover basis limited to fair market value

C. The beneficiary immediately recognizes $20,000 of ordinary income upon receiving the property

D. The distribution is entirely tax-free to both the trust and the beneficiary with no basis carryover

90. Farmer Gus Holloway markets his wheat through a farmer cooperative and receives a $6,000 patronage dividend in the form of a qualified written notice of allocation for the year. How must Gus generally treat this patronage dividend for federal income tax purposes?

A. As a nontaxable return of capital reducing the basis of his cooperative membership

B. As a tax-exempt agricultural subsidy excluded under Section 175 rules

C. As long-term capital gain regardless of the character of the underlying cooperative business

D. As ordinary income in the year received, tied to his farming business dealings with the cooperative

91. Marisol qualifies as a real estate professional and owns interests in four separate rental real estate activities, materially participating in only one of them individually. Under Reg. Section 1.469-9(g), what election is available to help her satisfy material participation across all four activities?

A. She may elect to treat all of her interests in rental real estate as a single combined activity for material participation purposes.

B. She may elect to exclude the three activities in which she does not materially participate from passive loss treatment entirely.

C. She may elect to convert the three nonparticipating activities into portfolio income, removing them from the passive activity rules altogether.

D. She may elect to treat each activity as a separate trade or business exempt from the passive activity loss limitations.

92. Dr. Susan Byrne owns a medical office building and rents it to her own professional corporation, in which she materially participates. The rental generates $15,000 of net income this year. How must this rental income be treated under the passive activity self-rental rules?

A. As passive income, freely available to absorb losses from Susan's other passive activities

B. As tax-exempt income because it is between related commonly controlled entities

C. As nonpassive income under the self-rental recharacterization rule, unavailable to offset other passive losses

D. As portfolio income subject to the net investment income tax exclusively

93. Employee Nora Fitzgerald, age 40, began participating in her employer's SIMPLE IRA plan eight months ago. She now takes an early withdrawal of $5,000 from the SIMPLE IRA and does not qualify for any penalty exception. What early distribution penalty rate applies to this withdrawal?

A. 10%, the standard early withdrawal penalty applicable to all IRA types

B. 0%, because SIMPLE IRA distributions are never subject to an early withdrawal penalty

C. 20%, the mandatory withholding rate applicable to qualified plan distributions

D. 25%, because the withdrawal occurs within the first two years of plan participation

94. The Larkspur Arts Foundation is organized and operated exclusively to support a named public university, is controlled by individuals who also control the university's board, and carries out its purpose by making distributions to the university. Under what classification does Larkspur avoid private foundation status despite lacking broad public financial support?

A. Section 509(a)(3) supporting organization, based on its relationship with the university

B. Section 501(c)(4) social welfare organization, based on its community activities

C. Section 4947(a)(1) nonexempt charitable trust, based on its trust instrument

D. Section 501(c)(6) business league, based on its membership structure

95. Husband Oscar Reyes dies in 2023, having used only $6 million of his $12.92 million applicable exclusion amount. His executor timely files Form 706 and elects portability. Oscar's widow, Marisol, later makes large lifetime gifts. How may Marisol use Oscar's unused exclusion?

A. She cannot use it because portability only applies to estate tax, never gift tax
B. She may add Oscar's deceased spousal unused exclusion to her own applicable exclusion amount
C. She may use it only if she remarries within two years of Oscar's death
D. The unused exclusion automatically passes to their children, not to Marisol

96. A complex trust accumulates income for several years and then makes a large distribution to a U.S. beneficiary. Domestic trusts are generally no longer subject to the throwback rule for such accumulation distributions. Under what circumstance do throwback rules still commonly apply?

A. Whenever a trust has more than five current beneficiaries
B. Whenever a domestic trust makes a distribution exceeding accumulated DNI
C. When the accumulation distribution comes from a foreign trust, still subject to throwback rules
D. Only when the trust was created before 1969 under grandfathered rules

97. Cash-method farmer Owen pays $85,000 in December for feed, seed, and other farm supplies he will not use until the following growing season. His other deductible farm expenses for the current year total $60,000. Under Section 464, what is the general limitation on Owen's current-year deduction for these prepaid farm supplies?

A. The full $85,000 is deductible currently, since cash-method farmers face no limitation on prepaid supply expenses.
B. None of the $85,000 is deductible currently; prepaid farm supplies must always be deducted in the year used.
C. Only 10% of the $85,000, or $8,500, is deductible currently, with the remainder deducted as the supplies are used.
D. Generally, only 50% of Owen's other deductible farm expenses, or $30,000, is deductible currently, with the excess deferred.

98. Investor Carla Whitfield owns limited partnership interests in two separate publicly traded partnerships (PTPs), Partnership X and Partnership Y. Partnership X generates a $9,000 passive loss this year, while Partnership Y generates $7,000 of passive income. Carla also has $5,000 of passive losses from an unrelated rental real estate activity. How may Carla use the Partnership X loss?

A. Against passive income from Partnership Y, the rental activity, or any other passive activity she owns

B. Only against Partnership X's own future passive income, since PTP losses cannot offset other activities' income

C. Against her nonpassive wage income and portfolio income without any limitation

D. Against Partnership Y's income this year, but never carried forward if unused

99. The Hartwell Community Foundation, a sponsoring organization, maintains a donor-advised fund for the Hartwell family. At the family's recommendation, the fund distributes $8,000 to an individual for personal travel expenses unrelated to any charitable purpose. What is the consequence under Section 4966?

A. No consequence, because donor-advised fund distributions are never taxed once contributed

B. The distribution is treated as a qualified charitable distribution automatically exempt from tax

C. The distribution is a taxable distribution, subjecting the sponsoring organization and approving fund managers to excise tax

D. Only the individual recipient is taxed on the funds as ordinary wage income

100. Meridian Manufacturing adopts a 401(k) plan using a Qualified Automatic Contribution Arrangement (QACA) safe harbor design, automatically enrolling eligible employees at an initial deferral rate that increases annually, paired with a safe harbor matching contribution. What is the primary benefit Meridian receives from adopting this QACA safe harbor design?

A. Deemed satisfaction of ADP/ACP nondiscrimination testing and top-heavy plan requirements

B. Elimination of all vesting requirements for the safe harbor matching contributions

C. Exemption from the Section 402(g) elective deferral limit for all participants

D. Automatic exclusion of highly compensated employees from plan participation entirely

Answer Key and Explanations — Practice Exam 24, Part 2: Businesses

1. B — Section 183(d) presumes an activity is for-profit if it shows a profit in at least three of the last five tax years, shifting the burden to the IRS to disprove profit motive. Option A wrongly denies sole proprietors this presumption, C overstates the requirement as four years, and D wrongly demands profit in all five years.

2. D — Section 1401 computes self-employment tax on net earnings from self-employment, defined by Section 1402(a) as net profit multiplied by 92.35%, approximating the employer share excluded for wage earners. Option A ignores this reduction, B confuses it with the later SE tax deduction, and C uses an incorrect, invented percentage not found in the Code.

3. A — Section 721(a) provides general nonrecognition treatment when a partner contributes property solely in exchange for a partnership interest, regardless of the built-in appreciation involved. Option B incorrectly recognizes the built-in gain immediately, C mischaracterizes any recognized amount as ordinary income, and D invents an arbitrary dollar threshold that does not exist under Section 721.

4. C — Section 7519 requires an electing Section 444 partnership to make an annual required payment to the IRS, approximating the value of the tax deferral its partners receive from the fiscal year. This payment, computed under a specified formula, is refundable if the deferral benefit later shrinks, and is unrelated to Section 179 limits.

5. D — Under the safe harbor described in Rev. Proc. 93-27 and Rev. Proc. 2001-43, receipt of a profits interest for services generally is not a taxable event, since it carries no claim to existing capital. Option A wrongly treats it as immediate compensation income, B mischaracterizes it as a capital interest, and C incorrectly triggers gain at the partnership level.

6. B — Section 706(c)(2)(A) closes the partnership tax year with respect to a partner whose entire interest is liquidated, so that partner's distributive share is determined through the liquidation date only. Option A wrongly closes the year for continuing partners as well, C incorrectly keeps Oscar's share open until year-end, and D describes no such mandatory election requirement.

7. A — Section 1446 requires a partnership with effectively connected taxable income allocable to a foreign partner to pay withholding tax on that allocable share, whether or not any cash is actually distributed. Option B wrongly ties withholding to distributions, C incorrectly denies any withholding obligation exists, and D wrongly conditions withholding on the partner's own filing failures.

8. C — Under Section 707(a)(1), a partner who transacts with the partnership other than in a partner capacity, such as a fair-market lease, is treated as an outside third party. Option A wrongly labels the rent a guaranteed payment, B incorrectly forces a special allocation, and D wrongly disregards the lease and its income entirely.

9. B — The Section 1.701-2 anti-abuse rule allows the IRS to recast a transaction that satisfies literal Subchapter K requirements but is used to achieve a tax result inconsistent with the intent of partnership taxation rules. Option A wrongly assumes literal compliance insulates the arrangement, C invents an unnecessary court-order requirement, and D wrongly limits the remedy to penalties alone.

10. D — Section 704(c)(1)(B) requires the contributing partner to recognize the remaining built-in gain if contributed property is distributed to another partner within seven years, preventing the mixing bowl strategy of shifting built-in gain away from the contributor. Option A wrongly excuses Faye entirely, B misattributes the gain to Grant, and C incorrectly taxes the partnership rather than the partner.

11. A — Section 709(b) allows a $5,000 first-year deduction for organizational expenditures, reduced dollar-for-dollar by the amount total expenditures exceed $50,000; here the $3,000 excess reduces the allowance to $2,000, with the remaining $51,000 amortized over 180 months. Option B ignores the phase-out, C wrongly eliminates the allowance, and D confuses the excess amount with the deductible amount.

12. C — Section 752(b) treats any decrease in a partner's share of partnership liabilities as a deemed cash distribution to that partner, which reduces outside basis dollar-for-dollar and may trigger gain if the distribution exceeds basis. Option A incorrectly increases basis instead of decreasing it, B invents cancellation of debt income that does not apply here, and D wrongly ignores the consequence.

13. C — Rev. Rul. 99-5 treats adding a second member to a single-member LLC as a sale by the original owner of a proportionate interest in each asset, followed by contribution of the assets to a newly formed partnership. Option A wrongly keeps the entity disregarded, B ignores the gain Owen realizes, and D incorrectly applies unrelated corporate rules.

14. B — Rev. Rul. 99-6 treats the departure of one member, leaving a single remaining owner, as a deemed purchase of the partnership's assets by the remaining member, terminating the partnership and creating a disregarded entity going forward. Option A wrongly continues partnership status, C incorrectly assumes automatic nonrecognition for Sonia, and D wrongly invokes an unrelated corporate liquidation.

15. A — Section 199A generally allows a deduction equal to 20% of qualified business income from a sole proprietorship, limited to 20% of taxable income minus net capital gain, before wage and property limitations become relevant below the threshold. Option B confuses the figure with an unrelated wage-limitation percentage, C wrongly assumes full deductibility, and D incorrectly borrows the self-employment tax rate.

16. D — The simplified home office method permits a deduction of $5 per square foot of qualified business use, capped at 300 square feet, producing a maximum deduction of $1,500 without tracking actual expenses. Option A describes the actual-expense method instead, B wrongly treats $1,500 as a flat automatic amount, and C incorrectly layers separate depreciation onto the simplified calculation.

17. B — A self-employed individual computing SEP-IRA contribution limits must first reduce net Schedule C profit by the deductible one-half of self-employment tax, since that adjusted figure, not gross income, is the base for the contribution percentage. Option A wrongly uses unadjusted gross receipts, C invents an employer-matching adjustment that does not apply, and D improperly subtracts the standard deduction.

18. D — An LLP structure generally shields a partner from personal liability for another partner's malpractice or negligence when uninvolved, though each partner remains liable for personal acts and the firm's contractual obligations. Option A wrongly equates LLP liability to a general partnership, B incorrectly denies any protection, and C invents an arbitrary fifty-percent split.

19. A — Under Section 1032, a corporation never recognizes gain or loss on issuing its own stock, regardless of what it receives, including services. Falcon instead deducts or capitalizes the $40,000 as compensation expense. Options B, C, and D wrongly treat the issuance as a taxable event to the issuing corporation, contrary to Section 1032.

20. C — Courts weigh factors such as a fixed maturity date, written instrument, stated interest rate, and independent repayment terms when distinguishing debt from equity. Repayment tied only to available cash flow with no fixed schedule closely resembles an equity investment rather than a bona fide loan. How the funds were used, personal recordkeeping, and entity type do not affect this characterization.

21. B — Section 336(e) allows the selling shareholder group and target corporation to jointly elect asset-sale treatment for a qualifying stock disposition, and unlike Section 338(h)(10), it does not require the purchaser to be a corporation. Section 338(g) requires purchasing-corporation action alone, Section 355 governs distributions of controlled subsidiary stock, and Form 8832 addresses entity classification, not sale characterization.

22. D — A Section 338(h)(10) election requires a joint election by the purchasing corporation and the selling shareholders, here Ashgrove's S corporation shareholder, filed on Form 8023, to treat a qualifying stock purchase as a deemed asset sale followed by liquidation. A unilateral election under Section 338(g) does not achieve this, and entity conversion or personal guarantees are irrelevant to qualifying.

23. C — During the post-termination transition period, cash distributions up to the corporation's remaining AAA balance are treated as if the S election were still in effect, reducing stock basis tax-free rather than as a taxable dividend. Option A ignores this PTTP relief provision, B misclassifies the distribution as compensation, and D confuses PTTP treatment with the unrelated built-in gains tax rules.

24. A — A QSub election requires 100% ownership by the parent S corporation, so selling any portion of the subsidiary's stock automatically terminates the QSub election. Trailhead is then treated as a new corporation that received its assets from Palisade in a deemed Section 351 contribution immediately before the sale. Continued disregard, mandatory dissolution, and a transfer prohibition all misstate the rule.

25. A — Unlike S corporations, which are barred from having more than one class of stock, an LLC's default partnership classification under the check-the-box regulations is unaffected by multiple classes of membership interests with differing economic rights. Absent a Form 8832 election, a multi-member LLC remains a default partnership. Options B, C, and D misapply the S corporation single-class rule here.

26. D — Section 118 was narrowed so that contributions to capital by a nonshareholder, including contributions in aid of construction, are no longer excludable and must be included in the corporation's gross income when received. The absence of stock issuance creates no exclusion. Options A and C rely on the pre-amendment rule, and B incorrectly treats the payment as a basis adjustment.

27. B — Section 383 extends the Section 382 ownership-change limitation to capital loss carryforwards and certain credits, capping the amount usable in each post-change year under the same value-times-tax-exempt-rate formula. Meadowlark cannot use its full pre-change loss at once; only the annually capped amount offsets post-change gains, with any unused excess continuing to carry forward.

28. C — A C corporation's charitable contribution deduction is generally limited to 10% of taxable income computed before the charitable deduction itself, so Ironwood's limit here is $50,000. The disallowed $15,000 excess is not lost but may be carried forward for up to five succeeding tax years. Options A, B, and D misstate either the limitation percentage or the carryforward availability.

29. A — Section 248 allows an initial $5,000 deduction for organizational expenditures, phased out dollar for dollar once total costs exceed $50,000, with the remaining balance amortized ratably over 180 months starting when the corporation begins business. Because Summit Ridge's costs exceed $50,000, the $5,000 allowance shrinks, leaving only $3,000 deductible. Options B, C, and D misstate the phase-out and amortization rules.

30. B — For NOLs arising in tax years beginning after 2017, a corporation's deduction is limited to 80% of taxable income computed before the NOL deduction, here $240,000, and the loss generally cannot be carried back but instead carries forward indefinitely. Option A wrongly allows a carryback, C wrongly lets the unused balance expire, and D ignores the 80% limitation entirely.

31. D — Section 336(a) generally requires a liquidating corporation to recognize gain or loss as if distributed property were sold to the distributee at fair market value. Cobalt's equipment has a $250,000 fair market value and a $90,000 basis, so Cobalt recognizes $160,000 of gain on the distribution, taxed at the corporate level before any shareholder-level gain is determined.

32. C — Under the Section 1092 straddle rules, a loss on one leg of a straddle is deductible only to the extent it exceeds unrecognized gain in offsetting positions. Simone's $14,000 loss is reduced by the $9,000 of unrecognized gain in the still-open leg, so only $5,000 is currently deductible; the deferred $9,000 carries forward until that position closes.

33. C — Section 195 permits a corporation to deduct up to $5,000 of start-up expenditures in the year active business begins, phased out dollar for dollar once total costs exceed $50,000, with the remaining balance amortized over 180 months. Thistlewood's costs are under this threshold, so the full $5,000 allowance applies. Options A, B, and D misstate the deduction and amortization rules.

34. A — Because Priya owns more than 2% of Cardinal Services' stock, the S corporation fringe benefit rules treat her health insurance premiums as wages includible in her Form W-2 income, though she may claim an above-the-line deduction on her individual return. The fringe benefit exclusion in option B does not apply to greater-than-2% shareholders, and C and D misstate the treatment.

35. D — When a corporation pays a shareholder an amount exceeding the fair value of what it receives, such as excessive rent, the excess is treated as a constructive dividend, nondeductible to the corporation and taxable as ordinary dividend income to the shareholder. Option A wrongly allows a full deduction, B misapplies return-of-capital treatment, and C incorrectly recharacterizes the payment as wages.

36. B — Section 988 generally treats foreign currency gain or loss on a nonfunctional-currency transaction, such as a euro-denominated receivable, as ordinary income or loss, separate from gain or loss on the underlying sale. Falcon's $3,000 currency gain from the euro's strengthening between the sale and payment dates is ordinary, not capital, and is computed independently of the inventory sale gain.

37. C — Section 1059A caps the income tax basis of property imported from a related person at the value declared to U.S. Customs, preventing taxpayers from understating customs duty while overstating tax basis and depreciation. Meridian's basis is limited to $40 per unit, the lower customs-declared amount, regardless of the higher figure recorded internally for tax purposes.

38. A — Section 1091 specifically exempts losses realized on securities disposed of in the ordinary course of a dealer's business from the wash sale disallowance rule. Because Voss held the Larkspur shares as dealer inventory rather than as an investment, the loss is fully deductible despite the repurchase; Options B, C, and D describe wash sale mechanics that do not apply here.

39. D — Section 165(g) deems worthless securities sold or exchanged on the last day of the taxable year in which they became worthless, regardless of the actual month worthlessness occurred. This fixed year-end deemed sale date determines the holding period and the tax year in which Dalton reports the resulting capital loss, rather than the specific date the stock lost all value.

40. A — Section 1234A treats gain or loss from the cancellation, lapse, or termination of a right relating to property that is, or would be, a capital asset as gain or loss from a sale of a capital asset. Because Prosper's contract right was capital in nature, the $80,000 payment produces capital gain, not ordinary income or Section 1231 gain.

41. B — For liabilities arising from torts, workers' compensation, and similar claims, Reg. Section 1.461-4(g)(2) provides that economic performance occurs only when the taxpayer actually makes payment to the claimant. Fenwick therefore cannot deduct the $200,000 liability until the 2025 payment is made, even though the liability was fixed and accrued on its books in 2024.

42. C — Section 1033(g) provides an extended three-year replacement period, rather than the standard two-year period, for condemned real property held for business or investment use. Since the condemnation occurred in 2024, Ridgemont has until the end of 2027, three years after the close of that tax year, to acquire replacement property and defer the gain.

43. B — Reg. Section 1.446-1(c)(1)(iv) expressly permits a hybrid method that combines accrual accounting for purchases and sales of merchandise with cash accounting for other income and expense items, provided the combination clearly reflects income and is used consistently from year to year. No corporate-size restriction or TCJA repeal applies to this combination.

44. D — Under Section 168(d)(3), the mid-quarter convention applies to depreciable property placed in service during the year, other than real property, when more than 40% of total basis is placed in service in the final quarter. Because Falcon placed 44% of its basis in the fourth quarter, it must use mid-quarter convention for its 2024 additions, not the default half-year convention.

45. B — A business casualty loss is measured as the lesser of the property's adjusted basis or its decline in fair market value, then reduced by any insurance reimbursement received. Here, the decline in value ($50,000) is less than adjusted basis ($60,000), so the starting point is $50,000, minus the $35,000 reimbursement, leaving a $15,000 deductible loss.

46. C — The Cohan rule permits a court or the IRS to estimate deductible business expenses based on credible testimony and other surrounding evidence when records are unavailable, so long as there is a reasonable basis for the estimate. This exception does not apply to travel, meals, or listed property expenses governed by the strict substantiation rules of Section 274(d).

47. D — Section 453(d) allows a seller to elect out of installment reporting and instead report the entire gain in the year of sale, using the fair market value of any deferred payment obligations. The election must be made on or before the due date, including extensions, of the return for the year the sale occurs, and once made is generally irrevocable.

48. A — Section 460(e)(6) provides a categorical exemption for home construction contracts, defined as contracts where at least 80% of costs relate to dwelling units in buildings with four or fewer units, allowing use of the completed-contract or another permissible method regardless of the contractor's size. This differs from the separate small-contractor exception, which depends on average annual gross receipts.

49. D — Section 108(e)(5) treats a debt reduction between a solvent, non-bankrupt purchaser and the seller who financed the purchase as a purchase price adjustment rather than cancellation of debt income, provided the debt arose directly from the purchase. Larkin therefore reduces its machinery basis by $12,000 instead of recognizing taxable income, avoiding the ordinary COD income treatment that otherwise applies.

50. C — Section 453(i) requires that any depreciation recapture income under Sections 1245 or 1250 be recognized in full in the year of sale, even when the sale otherwise qualifies for installment reporting. Only the remaining $20,000 of Section 1231 gain in excess of recapture may be reported under the installment method as payments are collected in future years.

51. B — Under SECURE 2.0, a participant whose prior-year FICA wages from the sponsoring employer exceeded the indexed threshold, originally $145,000, must make any age-50 catch-up contribution as a Roth contribution rather than pre-tax. Because Marcus's prior-year wages exceeded that threshold, his entire catch-up amount must be contributed to the plan on an after-tax Roth basis.

52. A — Section 168(g)(1)(B) mandates ADS for tax-exempt use property regardless of any taxpayer election; this is a required use, not an elective one, distinguishing it from farming or electing real property trades. GDS options B and C wrongly treat ADS as elective here, and bonus depreciation in D is unavailable because ADS property is ineligible.

53. A — Section 45X provides a per-unit production credit for eligible components (e.g., solar wafers, battery cells) that are produced in the U.S. and sold, with statutory phase-down percentages for sales after 2029 for some components. B describes an investment credit, C misidentifies the credit recipient, and D mischaracterizes it as a deduction.

54. D — Section 51(i)(3) applies a 25% rate to qualified wages when the employee works at least 120 but fewer than 400 hours, and 40% only at 400 hours or more; employees under 120 hours generate no credit. Luis's 350 hours falls in the 25% tier, making A, B, and C incorrect statements of the rule.

55. B — Government and certain tax-exempt building owners cannot use Section 179D themselves, so the deduction may be allocated to the designer (architect, engineer, or contractor) primarily responsible for creating the energy-efficient design. A incorrectly excludes government buildings entirely, C wrongly limits allocation to contractors only, and D describes a mechanism that does not exist.

56. C — Existing property fails "original use," so a QOF must substantially improve it by spending, within 30 months, more than the property's adjusted basis (excluding land) — here, more than $800,000. Option A misapplies the land value, B ignores the required threshold, and D describes reinvestment, not the improvement test itself.

57. A — Under Section 1400Z-2(c), holding a QOF investment more than ten years lets the investor elect a basis step-up to fair market value on disposition, excluding post-acquisition appreciation from taxable gain. B overstates the benefit for the original deferred gain (which was already recognized by 2026), C misstates a discontinued 15% basis rule, and D confuses an unrelated requirement.

58. D — A farming business that elects out of the Section 163(j) interest limitation must use ADS for property with a recovery period of 10 years or more, per Section 163(j)(7)(B) and 168(g)(1)(G). This trade-off makes options A and B incorrect since GDS and bonus depreciation are foreclosed for that property, and C misstates Section 179 availability.

59. C — Amortizable Section 197 intangibles, including purchased goodwill, are treated as Section 1245 property, so gain is recaptured as ordinary income to the extent of amortization claimed, with remaining gain treated as Section 1231 gain. A and B wrongly exempt goodwill from recapture, and D misapplies the Section 1250 real property recapture rule to an intangible asset.

60. B — In a like-kind exchange, net liability relief is treated as boot, offsetting relieved and assumed liabilities before adding cash received. Marta's boot equals $10,000 cash plus $20,000 net liability relief ($60,000 − $40,000), totaling $30,000. A incorrectly excludes liability relief entirely, C fails to net the liabilities, and D disregards well-established boot rules.

61. B — Section 41(h) allows a qualified small business (generally under $5 million in gross receipts, within its first five years) to apply up to $500,000 of its research credit against payroll tax liability. A misstates carryback rules, C describes a refundable credit that doesn't exist here, and D wrongly implies credit transferability under Section 41.

62. A — The Section 199A deduction is capped at the lesser of 20% of QBI or 20% of taxable income minus net capital gain; here that is the lesser of $30,000 and $24,000, yielding $24,000. B ignores the taxable-income ceiling, C incorrectly uses the greater amount, and D wrongly discards QBI from the computation entirely.

63. D — Legislative changes made standalone energy storage technology (minimum 5 kWh capacity) independently eligible for the Section 48 investment tax credit, removing the prior requirement that storage be paired with renewable generation. A and B state the outdated co-location requirement, and C invents a fossil-fuel restriction that does not exist under the current rule.

64. C — The Disabled Access Credit equals 50% of eligible access expenditures exceeding $250, up to a maximum credit of $5,000 (expenditures capped at $10,250). Here, 50% of ($9,000 − $250) = $4,375. A ignores the 50% rate and floor, B applies the wrong percentage, and D wrongly treats $5,000 as a flat amount unrelated to actual spending.

65. D — Section 1231 property specifically excludes property held primarily for sale to customers in the ordinary course of business, meaning inventory-type land held by a builder-developer produces ordinary income, not capital or 1231 gain. A ignores this exclusion, and B and C incorrectly apply depreciation recapture rules to land, which is never depreciable.

66. C — Direct sellers meeting the statutory nonemployee test — compensation tied to sales output rather than hours, and a written contract stating they are not employees — are treated as self-employed for all federal tax purposes. No income tax, FICA, or FUTA withholding applies; Nina reports her earnings and pays self-employment tax directly.

67. A — When a new employee does not furnish a Form W-4, the employer cannot leave wages unwithheld. IRC Section 3402(f)(2)(B) requires withholding as though the employee is single with no adjustments, using the current withholding tables, until the employee submits a valid Form W-4 reflecting actual filing status and adjustments. This default rule applies regardless of the employee's true circumstances.

68. B — For vehicles whose fair market value falls under the IRS's annual ceiling for this method, and that meet the regular-use or mileage tests, employers may value personal use by multiplying personal miles driven by the current standard mileage rate. This cents-per-mile amount is included in the employee's wages as a fringe benefit.

69. A — Once original Forms W-2 and W-3 have been filed with the SSA, an employer must correct wage errors by filing Form W-2c, Corrected Wage and Tax Statement, accompanied by transmittal Form W-3c. The employer must also furnish the corrected W-2c to the employee promptly so the employee can amend their return if needed.

70. C — Section 45B allows a credit for the employer's share of FICA tax paid on tips exceeding the amount needed to bring wages to $5.15 per hour. Subtracting the $6,500 offset from $18,000 leaves $11,500 in creditable tips; multiplying by 7.65% produces the allowable credit, since the offset portion is excluded from the calculation.

71. D — Outside a cafeteria plan, HSA comparability rules under Section 4980G require employers to make comparable contributions — either the same dollar amount or the same percentage of the deductible — to all comparable participating employees within each category, such as full-time versus part-time. Noncompliance triggers a 35% excise tax on the employer.

72. B — Services an employer offers to employees at no substantial additional cost to the employer, using excess capacity such as unsold seats, qualify as a no-additional-cost service under Section 132(a) and (b). These benefits are excludable from wages for income tax and FICA purposes, provided the service is one the employer regularly sells to customers.

73. B — Wages paid by a child to a parent working in the child's trade or business are subject to FICA and federal income tax withholding like any other employee's wages. However, Section 3306(c)(5) specifically excepts services performed by an individual in the employ of a son or daughter from FUTA coverage, regardless of the work performed.

74. A — Employers must retain Form I-9 until the later of three years after the date of hire or one year after termination of employment. Three years after the March 1, 2020 hire date is March 1, 2023; one year after the February 1, 2024 termination date is February 1, 2025 — the later, controlling retention date the employer must observe.

75. C — Under the administrative-or-management-activities test, a home office qualifies as the principal place of business if the taxpayer uses it exclusively and regularly for administrative or management activities and has no other fixed location to conduct substantial administrative work, even though income-producing services are performed elsewhere, such as at hospitals or client sites.

76. D — Heavy SUVs between 6,000 and 14,000 pounds GVWR escape the Section 280F luxury auto caps, but Section 179(b)(5) imposes its own separate dollar cap on Section 179 expensing for these vehicles, adjusted annually for inflation, to prevent taxpayers from fully expensing large SUVs used primarily for business purposes rather than depreciating them over time.

77. D — Employers of farmworkers report federal income tax withholding and FICA tax on Form 943, Employer's Annual Federal Tax Return for Agricultural Employees, filed once per year rather than quarterly. This differs from Form 941, used by most nonagricultural employers, and Form 940, which separately reports only federal unemployment tax liability.

78. B — Backup withholding applies only when a payee subject to U.S. reporting fails to certify a taxpayer identification number on Form W-9; it does not apply to foreign persons who certify status on Form W-8BEN. Because the services were performed entirely outside the United States, the compensation is foreign-source and not subject to Chapter 3 withholding either.

79. A — Under Section 3121(q), an employer's liability for the employer share of FICA tax on tips an employee failed to report arises only upon the IRS issuing a notice and demand for the tax. Unlike ordinary payroll tax obligations, this liability is not self-assessed and does not accrue automatically when underreporting occurs.

80. C — Section 642(c) allows a trust to deduct amounts of gross income permanently set aside for a qualified charitable purpose under the governing instrument, even without actual payment, provided the set-aside is irrevocable. Section 661 requires actual distribution to beneficiaries, Section 663(a) governs separate shares, and Section 645 concerns combining a trust with a decedent's estate for filing purposes.

81. B — Under Section 691(a), income in respect of a decedent retains the same character it would have had to the decedent, so IRA distributions remain ordinary income to the beneficiary. Section 691(c) permits a deduction for estate tax attributable to the IRD, avoiding double taxation. IRD assets do not receive a Section 1014 basis step-up, unlike other inherited property.

82. A — Section 2503(c) treats a gift to a trust for a beneficiary under age 21 as a present interest, qualifying for the annual exclusion, if trust property and income may be spent for the minor before 21 and passes to the minor (or estate) at 21. No Crummey withdrawal power is required, and Option D concerns the unrelated GST exclusion.

83. D — Section 4941 treats any sale or exchange of property between a private foundation and a disqualified person as self-dealing per se, even at fair market value; only a lease of property to the foundation at no charge is excepted. Marcus, as a substantial contributor and manager, is clearly a disqualified person, and no dollar threshold exempts the sale.

84. C — Section 401(a)(17) caps the compensation a qualified plan may take into account when calculating contributions and allocations, indexed annually; for 2024 the limit is $345,000. Even though Priya earns $450,000, her employer's profit-sharing contribution formula may only be applied to the first $345,000 of her compensation, separate from the Section 415(c) annual additions limit.

85. B — Under a group exemption, the central organization may file a single group return on behalf of subordinate organizations that authorize inclusion, satisfying each subordinate's Section 6033 annual filing requirement without separate individual returns. Subordinates do not need separate determination letters, and group exemption does not eliminate filing entirely or require annual Form 1023 refiling.

86. A — A qualified charitable distribution allows an IRA owner age 70½ or older to transfer up to the annual QCD limit directly to charity, excluding the amount from gross income while counting toward the RMD. Since the $12,000 QCD exceeds her $10,000 RMD, it satisfies the RMD fully and the entire amount is excluded, not merely $10,000.

87. C — Section 2032 permits an executor to value the gross estate six months after death instead of the date of death, but only if the election decreases both the gross estate's value and the combined estate and generation-skipping transfer tax liability. It applies to the entire estate, not asset-by-asset, is elective rather than automatic, and typically requires a filed Form 706.

88. D — Section 2513 allows spouses to elect gift splitting so that a gift made by one spouse to a third party is treated as made one-half by each, regardless of which spouse actually owned the transferred property. Both spouses must consent on a timely filed return; the election is not automatic, and separate ownership of funds does not bar the election.

89. B — Under Section 643(e), absent an election to recognize gain, a trust distributing appreciated property in kind does not recognize gain, and the beneficiary takes a carryover basis equal to the lesser of the trust's adjusted basis or fair market value. The distribution's value is included in DNI. The trustee could elect to recognize gain, but did not here.

90. D — Patronage dividends from a farmer cooperative, when paid in cash or a qualified written notice of allocation, are includible as ordinary income in the year received to the extent attributable to the patron's trade or business activity with the cooperative. They are not a basis return, not a Section 175 subsidy, and not automatically capital gain regardless of source.

91. A — Reg. Section 1.469-9(g) allows a qualifying real estate professional to elect to aggregate all interests in rental real estate into a single activity for material participation testing. Marisol's election lets her combine hours across all four properties, potentially meeting material participation for the combined activity even though she individually satisfies the test in only one property.

92. C — Under the self-rental rule, net rental income from property leased to a business in which the taxpayer materially participates is recharacterized as nonpassive income, so it cannot be offset by losses from unrelated passive activities. This prevents taxpayers from generating artificial passive income to absorb passive losses. The income is neither tax-exempt nor limited only to portfolio treatment.

93. D — Early distributions from a SIMPLE IRA taken within the first two years of an employee's initial participation are subject to a heightened 25% additional tax, rather than the standard 10% penalty that applies to distributions after the two-year period. The 20% mandatory withholding rate applies only to certain qualified plan distributions, not SIMPLE IRAs, and the penalty is not zero.

94. A — Section 509(a)(3) allows an organization to qualify as a supported public charity, rather than a private foundation, based on its organizational and operational relationship to one or more public charities, rather than on broad public financial support. Options B and D describe unrelated exemption categories, and Section 4947(a)(1) applies to nonexempt charitable trusts, not supporting organizations like Larkspur.

95. B — Portability allows a surviving spouse to add a deceased spouse's unused exclusion (DSUE) amount to her own applicable exclusion amount, usable for both lifetime gift tax and future estate tax purposes, provided the executor timely elected portability on a filed Form 706. The exclusion does not pass to children, is not gift-tax-only, and has no remarriage time limit requirement.

96. C — Congress repealed the throwback rule for most domestic trusts, but foreign trusts remain subject to it under Sections 665 through 668, so accumulation distributions from a foreign trust to a U.S. beneficiary can still trigger throwback taxation and the interest charge regime. Beneficiary count, pre-1969 creation date, and mere excess-of-DNI distributions from domestic trusts do not trigger throwback.

97. D — Section 464 generally limits a cash-method farmer's current deduction for prepaid farm supplies to 50% of the farmer's other deductible farm expenses for the year, absent an exception. Owen's other farm expenses total $60,000, so only $30,000 of his $85,000 prepaid supply cost is currently deductible; the remaining $55,000 is deferred and deducted in the year the supplies are used.

98. B — Special passive activity rules for publicly traded partnerships prevent a loss from one PTP from offsetting income from another PTP or from any other passive activity; each PTP's losses may only be suspended and carried forward to offset that same PTP's future passive income. The loss cannot offset nonpassive wages or portfolio income, and unused losses are not forfeited.

99. C — Section 4966 imposes an excise tax on a sponsoring organization for any taxable distribution from a donor-advised fund made to a natural person or for a non-charitable purpose. Fund managers who knowingly approve such a distribution face a separate excise tax. The distribution is not automatically exempt, is not a QCD, and taxation is not limited to the individual recipient.

100. A — A QACA safe harbor design combining automatic enrollment with required contributions deems the plan to satisfy ADP/ACP nondiscrimination testing and, generally, top-heavy requirements, relieving the employer of running those separate annual tests. Safe harbor QACA contributions may still require a two-year vesting schedule rather than immediate vesting, and it does not exempt deferrals from Section 402(g) limits or exclude HCEs.