PRACTICE EXAM 28: 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. Marisol Quintrell runs an alpaca-breeding operation reported on Schedule C. The activity has produced losses for six consecutive years, she keeps no formal books, drafts no business plan, and derives most of her income from a separate consulting practice. Under Treas. Reg. Section 1.183-2, which factor most strongly supports treating the alpaca activity as not engaged in for profit?

A. The activity generated losses for six straight years
B. She keeps no formal records and drafts no plan
C. She earns substantial income from unrelated consulting work
D. The activity involves livestock rather than manufactured products

2. Ophelia Brackenridge contributes a parcel of unencumbered real estate with an adjusted basis of $85,000 and a fair market value of $140,000 to a partnership solely in exchange for a partnership interest. No liabilities are involved, and the partnership recognizes no gain or loss on the contribution under Section 721. What is Ophelia's basis in her partnership interest immediately after the contribution?

A. $140,000, the fair market value of the property contributed
B. $0, because Section 721 nonrecognition eliminates any basis carryover

C. $55,000, the built-in gain inherent in the property at the time of contribution
D. $85,000, the same adjusted basis she held in the property before the contribution

3. Priya Vantsev is a 40% partner in Redshank Trading Partners. Her outside basis at the start of the year was $60,000. During the year, the partnership incurred $90,000 of recourse debt for which Priya bears the economic risk of loss under Section 752, and she received no distributions. What is Priya's ending outside basis before considering income or loss items?

A. $60,000, because partnership debt never affects outside basis
B. $96,000, reflecting only a portion of the new debt
C. $150,000, reflecting her full share of the new debt
D. $90,000, reflecting only the debt and not prior basis

4. Osric Thornbury receives a liquidating distribution of cash of $20,000 and land with an adjusted basis to the partnership of $45,000, in complete liquidation of his partnership interest. His outside basis immediately before the distribution was $50,000. Under Section 732(b), what basis does Osric take in the distributed land?

A. $30,000, the remaining outside basis after reducing for cash
B. $45,000, equal to the partnership's basis in the property
C. $50,000, equal to his full outside basis before distribution
D. $20,000, matching the cash portion of the distribution

5. Genevieve Larkspur is retiring from Cobblestone Advisory Partners, a general partnership in which capital is not a material income-producing factor. Her retirement payments include an amount for her share of unrealized receivables and an additional amount treated as a distributive share of future partnership income. Under Section 736, how is the second amount, tied to future income, characterized?

A. A capital gain distribution reducing her outside basis first
B. A Section 751 payment for unrealized receivables only
C. A tax-free return of capital under Section 731
D. A Section 736(a) payment taxed as ordinary income

6. Bartholomew Sikes provides ongoing management services to Ferrous Peak Partners and, under the partnership agreement, receives $6,000 monthly regardless of partnership profit or loss for the year. This payment is fixed in amount and not tied to partnership income. How is this payment properly characterized under Section 707(c)?

A. A tax-free capital contribution repayment to Bartholomew
B. A distributive share reported only on Schedule K-1
C. A guaranteed payment taxable as ordinary income to him
D. A Section 731 distribution reducing his outside basis

7. Ottoline Vasquez holds a limited partnership interest in Windward Grain Partners and has no management rights, no personal liability for partnership debts, and performs no services for the partnership. Her only role is as a passive capital investor. How does her distributive share of ordinary partnership income get treated for self-employment tax purposes under Section 1402(a)(13)?

A. Generally excluded from net earnings from self-employment
B. Fully subject to self-employment tax like any partner
C. Subject to self-employment tax only above a threshold
D. Treated as wages subject to FICA withholding instead

8. Halcyon Ridge Partners has two equal partners, Reinholt and Aster. Reinholt buys out Aster's entire interest, leaving Reinholt as the sole owner of the former partnership's assets and business. No other partners remain, and the entity ceases operating as a partnership for tax purposes. Under Section 708(b)(1), what is the tax consequence?

A. The partnership continues automatically under a technical rule
B. The partnership terminates because only one partner remains
C. The partnership converts to an S corporation by default
D. The partnership must file for bankruptcy protection first

9. Wilhelmina Trask and Corbin Ashgrove form Ashgrove Timber Partners and agree to maintain capital accounts under the rules of Treas. Reg. Section 1.704-1(b), with liquidation proceeds distributed according to those accounts and any deficit restoration obligation enforced. What primary purpose do these capital account rules serve for testing special allocations?

A. They establish whether an allocation has substantial economic effect
B. They determine each partner's self-employment tax liability annually
C. They set the partnership's required taxable year under Section 706
D. They fix the partnership's method of accounting for inventory

10. At the close of the tax year, Fenwick Hollow Partners allocates both taxable income and a nondeductible expense to partner Isolde Merriweather. Under Section 705, in what order must Isolde adjust her outside basis for these simultaneous items before any distribution basis limitation is applied?

A. Nondeductible expenses reduce basis before income increases it
B. Only the taxable income item affects basis at all
C. Distributions are applied before either item is considered
D. Basis is increased for income before being reduced for expenses

11. Percival Duskwood purchases Innes Farrow's entire interest in Copperfield Logistics Partners directly from Innes for a price exceeding Innes's share of inside basis. The partnership has a valid Section 754 election in effect for the year of the sale. What adjustment does Section 743(b) permit with respect to Percival's interest?

A. A partnership-wide basis increase shared by all partners equally
B. No adjustment, since 754 elections apply only to distributions
C. A basis adjustment to partnership property affecting only Percival
D. An automatic step-down in basis regardless of purchase price

12. Thaddeus Applecross operates a retail hardware store as a sole proprietorship reported on Schedule C. His average annual gross receipts exceed the threshold under Section 471(c), and he maintains substantial merchandise inventory that is a material income-producing factor. Which accounting method requirement generally applies to Thaddeus for inventory purposes?

A. He may use the cash method with no inventory tracking
B. He must use the accrual method to account for inventory
C. He must switch permanently to the completed-contract method
D. He must use mark-to-market accounting for all merchandise

13. Larkin Pemberton is allocated depreciation deductions attributable to nonrecourse financing at Grayhollow Properties Partners. The partnership agreement contains a minimum gain chargeback provision as required for the allocation to be respected under the Treasury Regulations. What situation does this chargeback provision address?

A. A partner contributing appreciated property with built-in loss
B. A retiring partner receiving Section 736(a) income payments
C. A limited partner performing more than minimal services
D. Partnership minimum gain decreasing, triggering an income allocation

14. Rosalind Kettering's Schedule C shows net profit of $80,000 for the year from her freelance architecture practice, with no other self-employment activity. Before applying the self-employment tax rate, what adjustment does Section 1402(a) require to her net profit figure?

A. Adding back all depreciation claimed during the year first
B. Multiplying net profit by 92.35 percent before applying rates
C. Subtracting the standard deduction from net profit amount
D. Excluding the first $20,000 of net profit entirely

15. Mordecai Ashworth and Talullah Brightwater form Brightwater Mercantile Partners, each contributing appreciated securities in exchange for partnership interests, with no partner receiving cash or other property. The partnership is not classified as an investment company for tax purposes. Under Section 721, what is the general tax treatment of these contributions?

A. Each partner recognizes gain equal to the built-in appreciation
B. Gain is deferred but taxed immediately at ordinary rates
C. No gain or loss is recognized by either contributing partner
D. Only the partner contributing the larger value recognizes gain

16. Cassius Iverwood acquired his interest in Hollowmere Ventures Partners three years ago in exchange for a contribution of a capital asset he had held for five years prior to contribution. Under Section 1223, what holding period does Cassius take in his partnership interest?

A. It includes the five-year holding period of the asset
B. It restarts entirely as of the date of contribution
C. It is measured only from the partnership's own formation
D. It depends solely on the partnership's chosen tax year

17. Newly formed Silverbrook Consulting Partners has partners with differing tax year ends and no natural business year. Absent a valid Section 444 election or established business purpose, which taxable year must the partnership generally adopt under Section 706(b)?

A. Any calendar or fiscal year the majority partner prefers
B. A year ending on the anniversary of formation always
C. The required year determined by reference to its partners
D. A short year that automatically renews every three years

18. Beatrix Colquhoun's outside basis in her interest in Thistledown Farms Partners is $12,000 before considering her distributive share of a $30,000 partnership loss for the year. She received no distributions and has no additional at-risk or passive activity limitations to apply. Under Section 704(d), how much loss may Beatrix currently deduct?

A. $12,000, limited to her adjusted outside basis amount
B. $30,000, the full distributive share regardless of basis
C. $18,000, representing the excess over her basis figure
D. $0, because partnership losses are never currently deductible

19. Marisol Yepez, Declan Fahey, and Priya Ramaswami form Coral Basin Corporation. Marisol contributes equipment for 50% of the stock, Declan contributes cash for 30%, and Priya contributes services worth the remaining 20%, receiving stock solely for those services. Immediately after the transfer, do Marisol and Declan satisfy the Section 351 control requirement?

A. No, because all three transferors must individually own at least 50% of the corporation's stock immediately after the exchange.

B. No, because Priya's stock issued for services disqualifies the entire transaction from Section 351 nonrecognition treatment automatically.

C. Yes, because any transferor who contributes appreciated property automatically satisfies the control requirement regardless of the other shareholders.

D. Yes, because Marisol and Declan together own 80% of the stock, satisfying the control requirement without counting Priya's shares.

20. Thornwell Corporation adopts a plan of complete liquidation and distributes a parcel of land with a fair market value of $410,000 and an adjusted basis of $260,000 to its sole shareholder, Odalys Brennan. Thornwell has no liabilities related to the land. How must Thornwell treat this distribution for tax purposes?

A. Thornwell recognizes no gain because liquidating distributions of appreciated property are always exempt from corporate-level taxation.

B. Thornwell recognizes $150,000 of gain as if the land had been sold to Odalys at its fair market value.

C. Thornwell recognizes $150,000 of loss because liquidating distributions are treated as sales at adjusted basis only.

D. Thornwell defers all gain recognition until Odalys later disposes of the land in a taxable transaction.

21. Halcyon Trading, Inc. is an S corporation with 97 shareholders, all of whom are unrelated individuals. The corporation is considering admitting five additional unrelated individual investors, which would bring the total shareholder count to 102. What is the effect on Halcyon's S corporation status?

A. The additional shareholders have no effect because S corporations may have an unlimited number of individual shareholders.

B. Halcyon's S election terminates automatically because the shareholder count would exceed the 100-shareholder limit under Section 1361.

C. Halcyon may keep its S election as long as the new shareholders each purchase stock directly from the corporation.

D. Halcyon must convert to a partnership within 90 days because exceeding 100 shareholders is treated as an inadvertent error.

22. Ferris Okonkwo-Lund incorporates Redshank Consulting, Inc. on March 1, and the corporation begins its first tax year that same day using a calendar year. By what date must Redshank file Form 2553 for the S election to be effective for its first tax year, absent a late-election relief request?

A. Redshank must file Form 2553 no later than December 31 of the corporation's first tax year to be timely.
B. Redshank must file Form 2553 within 30 days of incorporation, or the election is permanently barred for that year.
C. Redshank must file Form 2553 no later than May 15, which is two months and fifteen days after March 1.
D. Redshank must file Form 2553 before the end of the prior tax year, since S elections cannot apply retroactively.

23. Briallen Sarpong owns 40% of the stock of Pemberton Analytics, an S corporation. During the year, Pemberton earns $200,000 of ordinary business income and makes a $15,000 charitable contribution to a qualified organization. How must Pemberton report the charitable contribution to Briallen?

A. The $15,000 charitable contribution is separately stated and passed through to Briallen at her 40% share, or $6,000.
B. The charitable contribution is deducted entirely at the corporate level and reduces Pemberton's ordinary business income before pass-through.
C. The charitable contribution is disregarded for tax purposes because S corporations cannot claim charitable deductions of any kind.
D. The charitable contribution must be reported by Pemberton on a corporate return and cannot flow through to any shareholder.

24. At the start of the year, Wynstan Achterberg's basis in his S corporation stock of Larkspur Freight is $5,000. During the year, Larkspur earns $30,000 of ordinary income and makes a $12,000 distribution to Wynstan. In what order must Wynstan apply these items to determine his ending stock basis, and does any gain result from the distribution?

A. The distribution is applied first, reducing basis to zero and triggering $7,000 of capital gain before income increases basis.

B. Wynstan may choose either order, applying whichever sequence produces the smaller ending basis for his S corporation stock.

C. The distribution and income are averaged together before basis adjustments, producing no gain and an ending basis of $23,000.

D. Income increases basis first to $35,000, then the $12,000 distribution reduces basis to $23,000, with no gain recognized.

25. Genevra Okwuosa is the sole shareholder of Marrowstone Design, an S corporation that has never had any C corporation earnings and profits. Genevra's stock basis is $40,000 at the start of the year. Marrowstone distributes $55,000 in cash to Genevra during the year, and there is no other income or loss item. How is the distribution taxed?

A. The entire $55,000 distribution is taxed as an ordinary dividend because Marrowstone made a distribution exceeding its shareholder's basis.

B. The first $40,000 is a tax-free return of basis, and the remaining $15,000 is taxed as capital gain.

C. The distribution is entirely tax-free because S corporations without accumulated earnings and profits never generate taxable distributions.

D. The entire $55,000 is treated as wages subject to payroll tax because Marrowstone lacks any earnings and profits history.

26. Baltasar Quiroga forms Sablewood Ventures LLC, a domestic limited liability company with a single member, and does not file any entity classification election with the IRS. Under the check-the-box regulations, how is Sablewood Ventures classified for federal tax purposes by default?

A. Sablewood Ventures is disregarded as an entity separate from Baltasar and is treated as a sole proprietorship by default.

B. Sablewood Ventures is automatically classified as a C corporation because LLCs are corporations unless an election states otherwise.

C. Sablewood Ventures is automatically classified as an S corporation because single-member LLCs qualify for S status by default.

D. Sablewood Ventures must file Form 8832 within 75 days of formation or be treated as a partnership by default.

27. Kestrel Holdings acquires control of Alderbrook Fabricators, a corporation carrying significant net unrealized built-in gain in its assets, in a qualifying stock acquisition. Kestrel separately holds substantial net operating loss carryovers generated before the acquisition date. For the five-year period following the acquisition, what limitation does Section 384 impose?

A. Alderbrook may not use its pre-acquisition losses against post-acquisition income
B. Kestrel's pre-acquisition NOLs are permanently forfeited upon the change in control
C. The built-in gain limitation applies only if Kestrel is a foreign corporation
D. Kestrel's pre-acquisition losses generally may not offset Alderbrook's recognized built-in gains

28. Foxglove Hardware Corporation, a C corporation, converts to S corporation status effective January 1, 2024. At conversion, Foxglove holds an asset with a built-in gain. If Foxglove sells that asset in 2028, within the recognition period applicable under current law, how is the built-in gain treated?

A. The gain is never subject to corporate-level tax because S corporations are pass-through entities exempt from entity-level taxation.
B. The gain is subject to the built-in gains tax only if Foxglove sells the asset within two years of conversion.
C. The gain is subject to corporate-level built-in gains tax because the sale occurs within the five-year recognition period.
D. The gain escapes built-in gains tax entirely because the recognition period expired at the end of the conversion year.

29. Parent company Ashgrove Holdings owns 85% of the stock of its subsidiary, Wrenfield Systems. Wrenfield adopts a plan of complete liquidation and distributes all of its assets to Ashgrove in cancellation of its stock. What is the tax consequence to Ashgrove on receipt of the liquidating distribution?

A. Ashgrove recognizes gain to the extent the fair market value of the assets received exceeds its basis in the Wrenfield stock.
B. Ashgrove recognizes no gain or loss because it owns at least 80% of Wrenfield's stock, satisfying Section 332.
C. Ashgrove recognizes ordinary income equal to Wrenfield's accumulated earnings and profits immediately before the liquidation occurs.
D. Ashgrove must recognize loss if the assets received have a fair market value below its basis in the stock.

30. Redwood Fenwick Corp owns 25% of the outstanding stock of Marrow Point Corp and receives a $40,000 dividend distribution from Marrow Point during the year. Assuming no anti-abuse rules apply and the requisite holding period is satisfied, what percentage of the dividend may Redwood Fenwick generally deduct under the dividends-received deduction rules of Section 243?

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

31. Ottoline Braithwaite acquires original-issue stock in Quillfeather Corporation, a qualifying small business corporation, directly from the corporation for $45,000. Three years later, the stock becomes worthless, and Ottoline is unmarried. How much of her loss qualifies for ordinary loss treatment under Section 1244?

A. Up to $50,000 of the loss qualifies as an ordinary loss, with any remaining amount treated as a capital loss.
B. None of the loss qualifies as ordinary because Section 1244 applies only to losses from stock sales, not worthlessness.
C. The entire $45,000 loss is automatically treated as a capital loss regardless of the corporation's small business status.
D. Up to $100,000 of the loss qualifies as ordinary because Ottoline acquired the stock directly from the corporation itself.

32. Bettina Okonkwo sells qualified small business stock she has held for 14 months, realizing a $60,000 gain. She reinvests the entire sale proceeds in other qualified small business stock within 60 days of the sale. Under Section 1045, what is the effect of this reinvestment on Bettina's recognized gain?

A. She recognizes the full $60,000 gain because the holding period is insufficient
B. She recognizes 50% of the gain immediately and defers the remaining 50%
C. She permanently excludes the gain from taxation with no basis adjustment required

D. She defers recognition of the gain, reducing her basis in the replacement stock accordingly

33. Corvina Applewhite receives a $25,000 cash distribution from Drystone Manufacturing, a C corporation that has $18,000 of current earnings and profits and $40,000 of accumulated earnings and profits at year-end. How is the distribution classified for tax purposes under Section 316?

A. The entire $25,000 distribution is a dividend because it does not exceed the sum of current and accumulated earnings and profits.
B. Only the $18,000 attributable to current earnings and profits is a dividend, and the remaining $7,000 is nontaxable.
C. None of the distribution is a dividend because accumulated earnings and profits are disregarded when current earnings and profits exist.
D. The distribution cannot be classified until Corvina's basis in her Drystone stock is determined by the corporation's accountant.

34. Persimmon Retail Group, an S corporation, has a single class of common stock outstanding. All shareholders hold identical rights to distributions and liquidation proceeds. However, some shareholders have agreed among themselves, outside the corporate charter, to accept smaller distributions in certain years to help fund company operations. Does this side agreement violate the one-class-of-stock requirement?

A. Yes, because any variation in the amount of cash actually distributed to shareholders automatically creates a second class of stock.
B. Yes, because side agreements among shareholders are always treated as amendments to the corporate governing provisions for tax purposes.
C. No, because the one-class-of-stock test looks to the governing provisions, not to agreements outside the corporate documents.
D. No, because S corporations are permitted to maintain multiple classes of stock as long as voting rights remain identical.

35. Fenwick Corp merges into Ashdown Corp in a statutory merger under state law, with Fenwick's shareholders receiving 55% Ashdown voting stock and 45% cash for their Fenwick shares. For the transaction to qualify as a tax-free reorganization under Section 368(a)(1)(A), which requirement must be satisfied regarding the shareholders' continuing interest?

A. Fenwick's shareholders must receive solely Ashdown voting stock, since any cash consideration disqualifies a statutory merger reorganization entirely.

B. Fenwick's shareholders must receive at least 80% Ashdown stock, matching the control threshold applied to Section 351 transfers.

C. Fenwick's shareholders must retain their Fenwick shares for two years after closing to satisfy the continuity requirement.

D. Fenwick's shareholders must retain a meaningful continuing equity interest in Ashdown, generally measured by a substantial stock component.

36. Ferncliff & Rowe, P.C., a corporation providing legal services, wants to confirm it qualifies as a qualified personal service corporation for purposes of the mandatory cash method exception under Section 448. Which combination of criteria must the corporation satisfy under the function test and ownership test?

A. At least 50% of activities in a qualifying field, and 50% of stock held by current employees

B. At least 95% of activities in a qualifying field, and 95% of stock held by service-performing employees

C. At least 80% of activities in a qualifying field, with no stock ownership requirement at all

D. All gross receipts from one qualifying field, with no stock ownership test imposed

37. Brannigan Wholesale Distributors, a reseller with average annual gross receipts of $35 million, purchases goods for resale. Under Section 263A, what must Brannigan do with indirect costs like purchasing, storage, and handling?

A. Deduct all indirect costs currently, since UNICAP applies only to manufacturers, not resellers of purchased goods.

B. Capitalize the indirect costs into inventory, since UNICAP applies to resellers whose gross receipts exceed the small-business exemption.

C. Deduct all indirect costs currently, because resellers are exempt from UNICAP regardless of their average annual gross receipts.

D. Capitalize only direct labor costs, because Section 263A limits capitalization to costs directly identifiable with specific units produced.

38. Costa Home Builders sells lots from its inventory of residential building lots held for sale to customers in the ordinary course of its business, financed over five years. Can Costa report the gain on the installment method?

A. Yes, because any sale financed with deferred payments automatically qualifies for installment reporting under Section 453.

B. Yes, but only if Costa elects out of the accrual method for the specific lot sale transaction reported.

C. No, because property held for sale to customers in the ordinary course of business is excluded from installment reporting.

D. No, because installment reporting is limited exclusively to sales of intangible personal property and investment securities.

39. Delgado Bridge Contractors, which does not qualify as a small contractor, begins a bridge construction contract expected to span three years. Which accounting method must Delgado generally use for this contract?

A. Cash method, because construction contractors are permitted to use cash-basis reporting regardless of contract duration.

B. Completed-contract method, because Delgado may defer all income recognition until the contract is fully finished.

C. Installment method, because payments are received periodically over the multi-year duration of the construction contract.

D. Percentage-of-completion method, because the contract exceeds two years and Delgado does not meet the small-contractor exemption.

40. Everhart Consulting Group receives IRS consent to change from the cash to the accrual method, generating a positive Section 481(a) adjustment of $80,000. Over how many years must Everhart generally recognize this adjustment?

A. Four tax years, spreading the positive adjustment evenly beginning with the year of change.

B. One tax year, because positive adjustments must be fully recognized in the year of change.

C. Ten tax years, matching the recognition period used for negative adjustments under audit protection.

D. Two tax years, split evenly between the year of change and the immediately following year.

41. Farrow Storage LLC exchanges warehouse real property with an adjusted basis of $300,000 for like-kind warehouse real property worth $360,000 plus $50,000 cash, realizing a gain of $110,000. How much gain must Farrow recognize?

A. $110,000, because the entire realized gain is recognized whenever any boot is received in a like-kind exchange.

B. $0, because no gain is recognized when the properties exchanged are of like kind under Section 1031.

C. $50,000, because recognized gain equals the lesser of realized gain or boot received in the exchange.

D. $60,000, because recognized gain equals boot received reduced by the exchange's associated closing costs.

42. Grayson Freight Co.'s warehouse is destroyed by fire in Year 1, and Grayson receives insurance proceeds exceeding its adjusted basis, realizing gain. By when must Grayson replace the property to defer gain under Section 1033?

A. Within four years from the close of the tax year in which any part of the gain is realized.

B. Within six months from the date the insurance proceeds are actually received by Grayson Freight Co.

C. Within one year from the close of the tax year in which the fire destruction actually occurred.

D. Within two years from the close of the tax year in which any part of the gain is realized.

43. Holbrook Sales Corp receives a $200,000 commission payment in Year 1 under an unrestricted claim of right, though a customer dispute over entitlement to the funds remains unresolved. How should Holbrook report the payment?

A. Exclude the payment from income entirely until the customer dispute is fully and finally resolved.

B. Include the payment in gross income in Year 1, since it was received under a claim of right.

C. Report the payment as a deposit liability until Holbrook's legal right to retain it is confirmed.

D. Defer recognition using the installment method until the dispute's ultimate resolution establishes a fixed amount.

44. Ibarra Land Partners sells raw land for a contingent payment right whose fair market value cannot be reasonably ascertained at the time of sale. How should Ibarra report its gain on the sale?

A. Under the cost recovery method, treating payments as a nontaxable basis return until basis is fully recovered.
B. Under the accrual method, recognizing the full estimated present value of all contingent payments immediately upon sale.
C. Under the installment method, spreading gain ratably using the stated contract price divided by total payments due.
D. Under the completed-contract method, deferring all gain recognition until the contingent payment arrangement fully terminates completely.

45. Juniper Ventures is classified as a "tax shelter" under Section 448(d)(3) because more than 35% of its losses are allocable to limited partners. Which accounting method restriction applies to Juniper?

A. Juniper must use the accrual method, since tax shelters are barred from the cash method regardless of gross receipts.
B. Juniper may use the cash method freely, since the gross receipts test overrides the tax shelter classification entirely.
C. Juniper must use the completed-contract method exclusively, since tax shelters cannot use percentage-of-completion accounting under Section 460.
D. Juniper may choose either cash or accrual method, since tax shelter status has no effect on accounting method.

46. Kessler Equipment Sales sells farm equipment on a deferred payment installment contract, stating no interest, with payments due beyond six months. What consequence applies under Section 483?

A. No consequence arises, because Section 483 applies only to sales of publicly traded securities and inventory.
B. The full stated sales price is disqualified entirely from installment sale reporting due to the omitted interest.
C. Interest is imputed at the applicable federal rate, recharacterizing part of each payment as interest income.
D. The IRS automatically disallows the entire transaction, treating it instead as a taxable gift to the buyer.

47. Lindqvist Manufacturing wants to change its inventory valuation method and determines the change qualifies under an automatic change procedure listed in the applicable revenue procedure. What must Lindqvist do to make the change?

A. Nothing, because automatic change procedures eliminate any filing requirement with the IRS for the change.
B. File Form 3115 with its timely filed return, since automatic consent still requires the form to be filed.
C. Request a private letter ruling from the IRS National Office before implementing any automatic accounting method change.
D. Wait ninety days after filing for advance consent before implementing the automatic accounting method change requested.

48. Mercer Fine Art Gallery holds unique, non-fungible paintings as inventory, each individually identifiable and priced. Which inventory identification method is most appropriate for Mercer's cost of goods sold computation?

A. LIFO, because unique inventory items must always be matched with the most recently acquired identical item available.
B. Dollar-value LIFO, because it pools unique inventory items into broad categories for simplified valuation purposes.
C. FIFO, because unique items are automatically deemed sold in the order they were originally acquired chronologically.
D. Specific identification, because each unique item's actual cost can be directly matched to its specific sale.

49. Novak Home Construction, a small contractor whose average annual gross receipts fall below the applicable Section 460 threshold, builds custom single-family homes under contracts exceeding two years. Which method may Novak use?

A. Percentage-of-completion method only, because all contractors exceeding a two-year contract duration must use it.
B. Cash method exclusively, because small contractors are entirely exempt from all long-term contract accounting rules.

C. Installment method, because periodic draws received during construction qualify the contracts for deferred gain reporting.

D. Completed-contract method, because home construction contracts are exempt from the percentage-of-completion requirement under Section 460.

50. Ortiz Rentals exchanges rental real property with its wholly owned subsidiary in a like-kind exchange, and the subsidiary disposes of the received property fourteen months later. What is the tax consequence under Section 1031(f)?

A. Both parties' originally deferred gain is triggered and must be recognized because disposition occurred within two years.

B. No consequence arises, because related-party exchanges are entirely exempt from any post-exchange holding period requirement.

C. Only the subsidiary must recognize gain, while Ortiz Rentals retains full deferral on its original exchange transaction.

D. Gain recognition is deferred indefinitely as long as both related parties continue filing a consolidated tax return.

51. Ansel Portwright places into service a new office building for his consulting practice. Under MACRS, what is the applicable recovery period for straight-line depreciation of nonresidential real property?

A. 20 years

B. 27.5 years

C. 39 years

D. 45 years

52. Bristol Machine Works places $3,450,000 of qualifying Section 179 property in service during 2026, exceeding the phase-out threshold. How does this affect the maximum allowable Section 179 deduction?

A. The deduction is unaffected because the phase-out only applies to listed property

B. The maximum deduction is reduced dollar-for-dollar by the amount exceeding the threshold

C. The deduction is eliminated entirely once any threshold amount is exceeded

D. The deduction converts automatically into 100 percent bonus depreciation treatment instead

53. Delphine Okoro's corporation makes interior nonstructural improvements to the interior portion of an existing nonresidential building it has owned for six years. The improvements do not enlarge the building or modify the internal structural framework. How is this qualified improvement property classified under MACRS?

A. 39-year recovery period with no bonus depreciation eligibility
B. 15-year recovery period, straight-line, and eligible for bonus depreciation
C. 27.5-year recovery period identical to residential rental property
D. 5-year recovery period as tangible personal property

54. Trenton Vasquez purchases and places in service several pieces of equipment for his machine shop throughout the year, with none placed in service during the final three months of his tax year. Absent any exception, which depreciation convention applies to this MACRS personal property?

A. Half-year convention
B. Mid-quarter convention
C. Mid-month convention
D. Full-year convention

55. Marisol Fennimore's sole proprietorship has $18,000 of taxable income from the business before any Section 179 deduction, but she elected to expense $45,000 of qualifying equipment under Section 179. What happens to the portion of the deduction that exceeds her business taxable income limitation?

A. The excess amount is permanently disallowed and lost
B. The excess amount must be reclassified as bonus depreciation
C. The excess amount carries forward to succeeding tax years
D. The excess amount is deducted against unrelated portfolio income

56. Ferrovia Shortline Railroad Co., a Class II regional railroad, incurs $180,000 in qualified railroad track maintenance expenditures during the year. Under Section 45G, what is the general credit rate applied to these qualifying expenditures, subject to the applicable per-mile limitation?

A. 10 percent of qualified expenditures
B. 20 percent of qualified expenditures
C. 30 percent of qualified expenditures
D. 50 percent of qualified expenditures

57. Harriet Solberg acquires a competitor's customer list and a covenant not to compete as part of a business acquisition. Under the general rule for Section 197 intangibles, over what period must Harriet amortize these acquired assets?

A. 5 years using an accelerated method
B. 7 years using the double-declining balance method
C. 15 years on a straight-line basis
D. 20 years matching the covenant's stated term

58. Rosalind Deakins exchanges commercial real property she has depreciated for five years for replacement commercial real property of like kind in a qualifying Section 1031 exchange. How must Rosalind depreciate the carryover portion of her basis in the replacement property?

A. She restarts a full new 39-year recovery period for the entire basis
B. She must expense the entire carryover basis immediately under Section 179
C. She applies bonus depreciation to the full carryover basis automatically
D. She continues depreciating the carryover basis over the relinquished property's remaining period

59. Cassius Brennerman hires a new employee from a targeted group eligible for the Work Opportunity Tax Credit. Within how many days after the employee begins work must the employer submit the pre-screening notice, Form 8850, to the designated state workforce agency to preserve eligibility for the credit?

A. 7 days
B. 28 days
C. 45 days

D. 90 days

60. Winslow Aerodynamics wants to claim the research credit but lacks the detailed historical records needed to compute the credit under the traditional regular method. Which alternative method may Winslow elect that calculates the credit using a percentage of qualified research expenses exceeding a base amount tied to the three preceding years?

A. The Alternative Simplified Credit method
B. The Alternative Minimum Tax offset method
C. The Uniform Capitalization inventory method
D. The Modified Accelerated Cost Recovery method

61. Priscilla Ndiaye's partnership claims the Low-Income Housing Credit on a qualified residential rental project. For how many years must the project continue satisfying the low-income occupancy requirements to avoid recapture of previously claimed credit?

A. 15 years
B. 5 years
C. 10 years
D. 27.5 years

62. Desmond Okafor operates a non-SSTB manufacturing business and reports taxable income above the upper threshold for the applicable filing status. For a non-specified service business, how is the Section 199A deduction determined once income exceeds the threshold?

A. The deduction is denied entirely regardless of wages or property basis
B. The deduction is capped by a W-2 wage and property basis limitation
C. The deduction defaults automatically to a flat 10% of gross receipts
D. The deduction is limited solely to the entity's net operating loss

63. Genevieve Larkspur receives qualified REIT dividends and qualified publicly traded partnership income reported on her Schedule K-1. How is this income treated for purposes of the Section 199A deduction's W-2 wage and UBIA limitation?

A. It is combined with QBI and fully subject to the wage limitation
B. It is excluded entirely from any Section 199A deduction computation
C. It receives a separate 20% deduction not subject to the wage limitation
D. It is taxed at ordinary rates with no deduction available whatsoever

64. Roderick Van Zandt owns a specified service trade or business (SSTB), a tax preparation firm, and his taxable income falls within the phase-in range above the threshold amount for his filing status. What happens to his Section 199A deduction within this range?

A. The deduction remains completely unaffected by his taxable income level
B. The deduction is eliminated immediately at the first dollar above the threshold
C. The deduction automatically converts to the non-SSTB wage and UBIA formula
D. The deduction is proportionally phased out based on income within the range

65. Fitzgerald Emberton's business generates more general business credit than can be used against his current-year tax liability limitation. Under Section 39, how are unused general business credits generally treated?

A. Carried back one year and then forward twenty years
B. Carried back three years and forward five years indefinitely
C. Permanently forfeited if not used in the current tax year
D. Refunded immediately as an overpayment of estimated tax

66. Meridian Point Landscaping, LLC, an Ohio-based employer, pays its state unemployment tax (SUTA) in full and on time each quarter. The standard FUTA tax rate is 6.0% on the first $7,000 of each employee's wages. Assuming Ohio is not a credit reduction state for the year, what is Meridian Point's effective FUTA tax rate per employee after applying the maximum available credit?

A. 6.0%
B. 5.4%
C. 0.6%

D. 0.06%

67. Dara Okonkwo operates a freelance graphic design business and pays independent contractor Simeon Vance $3,400 during the year for logo design work. Vance fails to provide his correct Taxpayer Identification Number despite Dara's repeated requests. Under the backup withholding rules, what rate must Dara withhold from payments to Vance and remit to the IRS?

A. 22%
B. 28%
C. 32%
D. 24%

68. Priya Nakamura works exclusively as a full-time life insurance salesperson for Cascade Mutual Insurance Company, selling only Cascade's policies under a written agreement. Cascade withholds FICA tax from her commissions but does not withhold federal income tax, and issues her a Form W-2 with the statutory employee box checked. How does Priya report her business expenses for income tax purposes?

A. As an above-the-line adjustment to income on Schedule 1
B. On Schedule C, directly offsetting her statutory employee commission income
C. As unreimbursed employee business expenses on Schedule A, subject to limits
D. She may not deduct any expenses because she is a common-law employee

69. Tobias Reyes, a self-employed electrician, purchases a new pickup truck for $52,000 and uses it 80% for business. He elects the actual expense method and wants to claim depreciation. Which factor primarily limits the amount of depreciation Tobias may deduct annually on the vehicle?

A. The annual luxury automobile depreciation caps under Section 280F, prorated for business-use percentage
B. The vehicle's original purchase price divided evenly over a mandatory three-year period
C. The total mileage driven for personal purposes during the taxable year
D. The amount of gross income generated by the electrical business that year

70. Wendell Fairbanks operates a bookkeeping practice from a spare bedroom in his home. He uses the room daily for client work, but his children also use the same room several evenings a week to do homework and watch television. Can Wendell claim the home office deduction for this room?

A. Yes, because the room is used more than half the time for business purposes

B. Yes, because occasional personal use of a home office space is always disregarded

C. No, because the room fails the exclusive use requirement of Section 280A(c)(1)

D. No, because a spare bedroom can never qualify as a principal place of business

71. Colette Marchetti operates a small vegetable farm with gross farm income of $6,200 and net farm profit of $1,900 for the year. She wants to use the farm optional method to compute her self-employment tax so she can receive Social Security earnings credit for the year. Under this method, what amount of net earnings from self-employment may Colette report?

A. Her actual net profit of $1,900, since the optional method only applies below $1,000

B. Two-thirds of her gross farm income, capped at the annual dollar limit

C. The full amount of her gross farm income with no cap applied

D. The lesser of two-thirds of gross farm income or the annual dollar limit

72. Kettlebrook Staffing Inc. transfers its entire workforce to a newly formed related entity for the primary purpose of obtaining that entity's lower state unemployment tax experience rate, a practice commonly known as SUTA dumping. Under the SUTA Dumping Prevention Act, what is the general consequence for employers found to have engaged in this practice?

A. The state must assign the transferred workforce the highest applicable unemployment tax rate and may impose penalties

B. The IRS automatically revokes the employer's federal employer identification number for five years

C. The employer becomes permanently ineligible to claim the FUTA credit reduction offset

D. The transferred employees lose eligibility for state unemployment benefits going forward

73. Marisol Quintana is a licensed real estate agent who works under a written contract with Highcrest Realty Group stating that substantially all her pay is directly related to sales output rather than hours worked, and that she will not be treated as an employee for federal tax purposes. How is Marisol classified under Section 3508?

A. A common-law employee subject to FICA and income tax withholding
B. A statutory nonemployee treated as self-employed for all federal tax purposes
C. A statutory employee subject only to FICA tax withholding requirements
D. An independent contractor only if she also sells insurance products

74. Bartholomew Sinclair earns $210,000 in wages during the year from a single employer. With respect to FICA tax withholding, which statement correctly describes how the Social Security and Medicare portions apply to his wages?

A. Both the Social Security and Medicare portions of FICA stop once wages exceed the annual wage base amount
B. Neither the Social Security nor the Medicare portion is subject to any annual wage base limitation at all
C. Social Security tax stops once wages exceed the annual wage base, but Medicare tax continues on all wages earned
D. Medicare tax stops once wages exceed the annual wage base, but Social Security tax continues to apply on all wages

75. Nadia Petrov's regular place of business is in Denver, Colorado, where she also maintains her permanent residence. She travels to Salt Lake City for a five-day consulting project and incurs lodging and meal costs. For these costs to be deductible as travel expenses rather than nondeductible commuting or personal expenses, what condition must generally be met?

A. The trip must last longer than thirty consecutive calendar days each time
B. Nadia must own rather than rent her lodging while traveling away
C. The travel expenses must exceed a fixed dollar threshold set annually
D. Nadia must be traveling away from her tax home long enough to require sleep or rest

76. Elouise Bramwell, a self-employed sales consultant, travels frequently for business and wants to substantiate her lodging, meals, and incidental expenses without keeping every individual receipt.

Instead, she wants to use IRS-published per diem rates that vary based only on whether the travel destination is designated as a high-cost or standard-cost locality. Which substantiation method is she describing?

A. The actual expense method requiring contemporaneous receipts for every expenditure
B. The high-low per diem substantiation method for lodging and meals
C. The standard mileage rate method for vehicle expense substantiation
D. The accountable plan reimbursement method for employee expense advances

77. Thaddeus Okafor hires a new full-time employee, Rosalind Ferreira, at his manufacturing shop. Under federal new hire reporting requirements designed to assist child support enforcement, within how many days of Rosalind's hire date must Thaddeus generally report her to the state directory of new hires?

A. 10 days
B. 30 days
C. 15 days
D. 20 days

78. Genevieve Okonjo has operated her catering business as a sole proprietor using her Social Security number for tax filings. She now plans to hire her first employee. What must Genevieve do before she can begin withholding and depositing employment taxes for that employee?

A. Apply for an Employer Identification Number by filing Form SS-4 first
B. Register the catering business as a corporation with her home state
C. Wait until the new employee has worked ninety days before applying
D. Continue using her Social Security number since sole proprietors are exempt

79. Castellan Fabrication Inc. needs to determine whether it is a monthly or semiweekly depositor for federal employment tax deposits for the current calendar year. Which of the following determines this classification?

A. The total employment tax liability reported for the current calendar quarter

B. The number of employees on the payroll as of January 1 of the current year

C. The total employment tax liability reported during the four-quarter lookback period ending the prior June 30

D. Whether the employer voluntarily elects monthly or semiweekly status each January

80. The Hartwell Family Trust, a complex trust, paid $12,000 to a qualified charity during the tax year pursuant to the specific terms of its governing instrument. The payment was made from the trust's current-year gross income. Under which Code section may the trust claim an unlimited charitable deduction for this payment, without regard to the percentage limitations imposed on individual taxpayers?

A. Section 170, subject to the same adjusted gross income percentage limits that apply to individual donors

B. Section 642(c), which allows an unlimited deduction for amounts paid from gross income under the trust's governing instrument

C. Section 663(a), which excludes charitable payments entirely from the definition of a distribution to beneficiaries

D. Section 642(b), which permits only a fixed $100 exemption in lieu of any charitable contribution deduction

81. The trustee of the Delacroix Irrevocable Trust distributed $40,000 to the sole beneficiary on February 20, 2027, and wishes to treat the distribution as if it had been made on December 31, 2026, the last day of the trust's prior tax year. Which election allows the trustee to treat this timely post-year-end distribution as made in the earlier tax year?

A. The Section 645 election to treat a qualified revocable trust as part of the decedent's estate

B. The Section 642(c) election to designate a payment as a set-aside for charitable purposes

C. The Section 663(b) election to treat distributions made within 65 days after year-end as prior-year distributions

D. The Section 661(b) election to allocate distributable net income among multiple trust beneficiaries

82. The executor of Warren Castellano's estate is considering whether to value estate assets six months after the date of death instead of using date-of-death values. Which two conditions must both be satisfied before the executor may elect the alternate valuation date under Section 2032?

A. The estate must owe federal estate tax and the surviving spouse must consent in writing to the election

B. The estate must be worth more than $5 million and every asset must have appreciated since the date of death

C. The estate must file within nine months and every beneficiary must be a lineal descendant of the decedent

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

83. Percival Ostrander, age 72, transfers a commercial rental property worth $500,000 to his adult daughter in exchange for her unsecured promise to pay him a fixed sum annually for the rest of his life, with no security interest retained in the property. How is this private annuity arrangement generally treated for estate tax purposes if Percival survives the transfer by more than three years and retains no interest in the property?

A. The full value of the property remains includible in Percival's gross estate under the retained-interest rules

B. The property is generally excluded from Percival's gross estate because he retained no interest or security in it

C. The transaction is automatically recharacterized as a taxable gift subject to gift tax in the year of transfer

D. The daughter must include the property in her own estate immediately upon receiving it

84. Dorian Fitzwilliam created an irrevocable trust in which he retained a reversionary interest in the trust corpus that, at the time the trust was created, had a value exceeding 5% of the trust's value. Under the grantor trust rules, what is the income tax consequence of retaining this reversionary interest?

A. Dorian is treated as the owner of the trust portion subject to the reversion and must report its income

B. The trust becomes a simple trust automatically and must distribute all income currently to its beneficiaries

C. The reversionary interest has no income tax effect unless Dorian actually reclaims the property at trust termination

D. The trust is disregarded entirely for all federal tax purposes and files no separate fiduciary return whatsoever

85. The executor of the Beauchamp estate paid $18,000 in administration expenses that qualify as deductions under both Section 2053 for estate tax purposes and Section 212 for income tax purposes. Absent a waiver, what rule governs whether the estate may deduct these same expenses on both the estate tax return and the fiduciary income tax return?

A. The expenses may always be deducted in full on both returns since Congress intended full duplication of benefits

B. The expenses must be deducted only on the income tax return, since estate tax deductions are always secondary

C. The expenses must be split evenly between the two returns regardless of any waiver filed by the executor

D. Section 642(g) bars a double deduction unless the executor files a waiver relinquishing the estate tax deduction

86. Millbrook Family Foundation, a private nonoperating foundation, is calculating its excise tax liability under Section 4940 for the year. Which of the following items is included in the foundation's net investment income subject to this excise tax?

A. Interest, dividends, and net capital gain from the sale of investment assets

B. Program-related investment losses incurred in furthering the foundation's charitable mission

C. Contributions and grants received from the foundation's individual donors during the year

D. Unrealized appreciation on investment assets that have not yet been sold

87. Fairhaven Historical Society, organized as a tax-exempt trust, generated $30,000 of unrelated business taxable income after allowable deductions from operating a for-profit gift shop unrelated to its exempt purpose. At what rate structure is this unrelated business taxable income taxed under Section 511?

A. A flat 21% rate applies to all exempt organizations regardless of their underlying legal form

B. The income is entirely exempt from tax because it derives from an exempt organization's activities

C. Trusts pay tax on unrelated business income at the rates applicable to trusts, not corporations

D. Unrelated business income of a trust is taxed only if it exceeds $100,000 in a year

88. Cedar Hollow Community Church is a tax-exempt religious organization recognized under Section 501(c)(3). Which of the following statements correctly describes the church's obligation to file an annual information return with the IRS?

A. The church must file Form 990 annually once its gross receipts exceed $50,000

B. Churches are automatically exempt from the annual Form 990 filing requirement regardless of gross receipts

C. The church must file Form 990-EZ if it has fewer than five ordained ministers on staff

D. The church may file Form 990-N only if it has never applied for formal recognition of exemption

89. Bright Futures Youth Center seeks to qualify as a publicly supported organization under Section 509(a)(1) rather than a private foundation. Generally, what percentage of the organization's total support must come from governmental units, the general public, and other public charities to satisfy the standard public support test?

A. At least 10% of total support, with no facts-and-circumstances flexibility permitted under any test

B. At least 90% of total support, calculated solely from investment income over a one-year period

C. At least 50% of total support, measured only from membership dues collected in the current year

D. At least one-third of total support, measured over a rolling five-year computation period

90. Chandler Voss, a self-employed consultant, maintains a SEP-IRA and wants to know the maximum percentage of his net self-employment earnings that may be contributed to the plan for the current year, subject to the applicable dollar cap under Section 408(k). What is that maximum contribution percentage of compensation?

A. 25% of compensation, subject to the annual dollar limitation and net self-employment earnings adjustments

B. 50% of compensation, with no dollar limitation applying because SEPs are exempt from all statutory caps

C. 3% of compensation, matching the minimum nonelective contribution required under SIMPLE IRA plans

D. 100% of compensation, provided the participant is at least fifty years old under catch-up rules

91. Thornfield Manufacturing sponsors a traditional 401(k) plan. To confirm the plan does not disproportionately benefit highly compensated employees, the plan administrator compares the average deferral percentages of highly compensated and non-highly compensated employees each year. What is this required nondiscrimination test called?

A. The top-heavy test, which measures whether key employees hold more than 60% of total plan assets

B. The minimum coverage test, which measures whether enough non-highly compensated employees are eligible to participate

C. The actual deferral percentage test, comparing elective deferral rates of highly and non-highly compensated employees

D. The controlled group test, which aggregates commonly owned businesses for retirement plan eligibility purposes

92. Priya Nakamura, trustee of her company's qualified retirement plan, is considering having the plan purchase a rental property directly from her brother, a disqualified person under the plan. Under Section 4975, what is the tax consequence if this sale between the plan and the disqualified person proceeds?

A. An excise tax applies to the disqualified person on the amount involved in the prohibited transaction

B. No consequence arises because family sales to qualified plans are specifically exempted from all scrutiny

C. The plan automatically loses its qualified status only if the sale price exceeds fair market value

D. The disqualified person receives an automatic income tax deduction equal to the full sale price

93. Walter Pemberton turns 73 during the current year and has a traditional employer-sponsored qualified plan account. He is not a 5% owner of the sponsoring company and continues working full-time for that employer. Under Section 401(a)(9), by when must Walter generally begin taking required minimum distributions from this employer plan?

A. He must begin distributions by April 1 following the year he turns 73, regardless of employment status

B. He may generally delay distributions until April 1 following the year he actually retires from that employer

C. He must begin distributions immediately upon reaching age 73, with no exceptions available under any circumstance

D. He is permanently exempt from required minimum distributions because he continues working past normal retirement age

94. Estelle Marchetti, age 45, took a $15,000 distribution from her traditional IRA to pay unreimbursed medical expenses that exceeded 7.5% of her adjusted gross income for the year. Aside from including the distribution in gross income, what is the additional tax consequence under Section 72(t)?

A. A flat 25% additional tax applies because IRA distributions before age 59½ always incur a higher penalty

B. A 20% mandatory withholding tax applies automatically to any early distribution taken from a traditional IRA

C. No 10% additional tax applies because the distribution qualifies for the unreimbursed medical expense exception

D. A 10% additional tax applies with no exception available, since medical expenses only excuse plan loans

95. Osric Callendar, a farmer who received Commodity Credit Corporation loans during the year, incurs a net farming loss of $650,000 for the tax year, exceeding the applicable excess business loss threshold. Under Section 461(j), what special rule applies to farmers who received applicable subsidies when computing the disallowed excess farm loss?

A. The farmer's excess business loss is calculated using the general nonfarm threshold with no special adjustment

B. All farming losses are fully disallowed regardless of subsidies received, with no carryforward permitted

C. The farmer becomes permanently ineligible to claim any future farming losses once subsidies are received

D. The disallowed loss is limited to the greater of the general threshold or aggregate farming income

96. Odell Ferreira, a sole proprietor farmer, reports a net business loss of $650,000 for the current tax year, filing as single. Aside from at-risk and passive activity limits, which additional limitation may restrict the amount of this farming loss he can currently deduct against nonbusiness income?

A. The Section 469 material participation rules, which apply exclusively to rental real estate activities

B. The Section 461(l) excess business loss limitation, capping aggregate business losses deductible against nonbusiness income

C. The Section 1301 farm income averaging provision, which limits losses rather than spreading elected farm income

D. The Section 175 conservation expense cap, which restricts losses to 25% of gross farming income annually

97. Yolanda Brennan operates a farming business raising cattle for market. She wants to know whether her farming operation is subject to the uniform capitalization rules of Section 263A, which generally require capitalizing certain indirect costs into inventory or property produced for sale. What is the general treatment for farming businesses under Section 263A(d)?

A. Farmers must always capitalize all indirect costs regardless of the type of commodity or entity structure used

B. Farmers are exempt from UNICAP entirely with no requirement to use any particular depreciation method

C. Farmers may never elect out of UNICAP once a Section 263A method has been adopted for any asset

D. Property produced in a farming business is generally exempt from UNICAP, though electing out requires using the alternative depreciation system

98. Thaddeus Kowalczyk sold a dairy cow that he had held and used for breeding purposes for three years, realizing a gain on the sale. The cow was not held primarily for sale to customers in the ordinary course of his farming business. How is this gain generally characterized for federal income tax purposes?

A. Section 1231 gain, because livestock held for breeding, dairy, draft, or sporting purposes for the required holding period qualifies

B. Ordinary income entirely, because all livestock sales are treated as inventory sales regardless of the holding purpose

C. Capital loss automatically, because farm animals are excluded from the definition of property used in a trade or business

D. Section 1245 recapture in full, because livestock is always treated identically to depreciable farm machinery and equipment

99. Cordelia Ashcombe's will creates a trust for her surviving spouse that gives him all trust income for life and a general power to appoint the entire trust principal to himself or his estate, exercisable by him alone and in all events. No QTIP election is made or needed for this trust. Under Section 2056(b)(5), why does this trust qualify for the marital deduction despite being a terminable interest?

A. Because the trust automatically terminates within six months of the surviving spouse's death

B. Because the trustee, rather than the spouse, controls the ultimate disposition of the principal

C. Because the spouse's unrestricted general power of appointment satisfies the terminable interest exception

D. Because the trust was created during Cordelia's lifetime rather than under her will

100. Silverpine Charitable Foundation, a private foundation, wants to terminate its private foundation status without incurring the Section 507 termination tax. Which of the following actions allows the foundation to avoid this tax?

A. Simply filing a final Form 990-PF marked as a terminating return with the IRS

B. Distributing all of its net assets to one or more qualifying public charities

C. Reducing its annual grantmaking below the minimum distribution requirement for one year

D. Converting its investment portfolio entirely into tax-exempt municipal bond holdings

Answer Key and Explanations — Practice Exam 28, Part 2: Businesses

1. B — Under Treas. Reg. Section 1.183-2(b), whether a taxpayer conducts an activity in a businesslike manner, including keeping accurate books and records, is a key factor in assessing profit motive. Marisol's failure to keep records or draft a business plan indicates unbusinesslike conduct, supporting reclassification of the alpaca activity as a hobby under Section 183 rather than a trade or business.

2. D — Under Section 722, a partner's basis in a partnership interest received in exchange for a contribution of property equals the adjusted basis of the contributed property in the partner's hands immediately before the contribution, unchanged by the property's fair market value. This substituted basis carries over because Section 721 defers recognition of the built-in gain rather than eliminating it.

3. C — Under Section 752(a), an increase in a partner's share of partnership liabilities is treated as a contribution of money by that partner, increasing outside basis. Since Priya bears the economic risk of loss for the entire $90,000 recourse debt, her outside basis increases dollar-for-dollar by that amount, bringing her starting basis of $60,000 up to $150,000 before other adjustments.

4. A — Under Section 732(b), in a complete liquidating distribution, the partner's outside basis is allocated first to cash received, then any remaining basis is assigned to other distributed property. Osric's $50,000 outside basis is reduced by the $20,000 cash received, leaving $30,000 to be allocated as his basis in the distributed land, which is less than the partnership's own $45,000 basis.

5. D — Section 736 divides retirement payments into Section 736(b) payments for the partner's share of partnership property, including unrealized receivables, and Section 736(a) payments for everything else, including amounts tied to future income when capital is not material. Since Genevieve's second payment relates to future income rather than property, it is a Section 736(a) payment taxed as ordinary income.

6. C — Section 707(c) defines a guaranteed payment as an amount paid to a partner for services or capital use that is fixed without regard to partnership income. Because Bartholomew's $6,000 monthly payment is fixed regardless of profit or loss, it qualifies as a guaranteed payment, deductible by the partnership and reportable by him as ordinary self-employment income, not a distributive share.

7. A — Section 1402(a)(13) generally excludes a limited partner's distributive share of partnership income from net earnings from self-employment, except for guaranteed payments for services actually rendered. Because Ottoline has no management rights, no personal liability, and performs no services, her passive capital investment income from Windward Grain Partners falls within this exclusion and is not subject to self-employment tax.

8. B — Section 708(b)(1) provides that a partnership terminates for tax purposes when no part of any business continues to be carried on by any of its partners in a partnership. Once Reinholt buys out Aster's entire interest, only one owner remains, so Halcyon Ridge Partners ceases as a partnership, and Reinholt is treated as running a sole proprietorship going forward.

9. A — Treas. Reg. Section 1.704-1(b) provides safe harbor rules under which allocations are respected as having substantial economic effect when capital accounts are properly maintained, liquidation follows those accounts, and any deficit is restored or a qualified income offset applies. These rules primarily test whether special allocations, rather than the default profit-sharing ratio, will be respected for federal tax purposes.

10. D — Section 705 and its regulations require outside basis to be increased for income items, including tax-exempt income, before it is decreased for distributions and nondeductible, noncapital expenditures. This ordering matters because it maximizes basis available to absorb losses and distributions. Isolde's basis is therefore increased for taxable income first, then reduced for the nondeductible expense allocated to her.

11. C — Section 743(b) allows a partnership with a valid Section 754 election to adjust the basis of partnership property for a transferee partner who purchased an interest, when the transfer price differs from the transferee's share of inside basis. This adjustment is personal to Percival and does not affect the common basis of property shared by the other partners.

12. B — Under Section 471(c) and related regulations, a taxpayer whose average annual gross receipts exceed the applicable small-business threshold and who carries inventory that is a material income-producing factor generally must use an inventory method and the accrual method for purchases and sales of that merchandise, even though other parts of the business may otherwise qualify for simplified cash-method treatment.

13. D — The minimum gain chargeback rule under Treas. Reg. Section 1.704-2 requires that when partnership minimum gain attributable to nonrecourse liabilities decreases during a year, partners who were previously allocated nonrecourse deductions must be allocated income or gain to offset that decrease. This ensures nonrecourse deduction allocations, like those given to Larkin, are respected as having economic effect under the regulations.

14. B — Section 1402(a) requires net earnings from self-employment to be multiplied by 92.35 percent before applying the self-employment tax rate, reflecting an adjustment that approximates the employer-equivalent portion of FICA taxes a wage earner would not include as taxable earnings. Rosalind's $80,000 Schedule C net profit must first be reduced to this adjusted figure before computing her self-employment tax liability.

15. C — Section 721(a) provides that no gain or loss is recognized to a partnership or to any partner upon a contribution of property in exchange for a partnership interest, subject to limited exceptions such as investment company treatment under Section 721(b). Since no exception applies here, Mordecai and Talullah recognize no gain despite contributing appreciated securities to Brightwater Mercantile Partners.

16. A — Section 1223(1) provides that a partner's holding period for a partnership interest received in exchange for a contributed capital asset or Section 1231 property includes the holding period of the contributed asset. Because Cassius held the contributed asset for five years before contributing it, that period tacks onto his three-year ownership of the Hollowmere Ventures Partners interest for holding-period purposes.

17. C — Section 706(b) requires a partnership without an established business purpose or valid Section 444 election to adopt the required taxable year determined by reference to its partners, generally the year used by partners owning a majority interest, or otherwise the year of its principal partners or the calendar year. Silverbrook cannot simply choose a preferred fiscal year.

18. A — Section 704(d) limits a partner's deductible distributive share of partnership loss to the adjusted basis of the partner's interest at the end of the partnership year, before considering distributions. Beatrix's outside basis of $12,000 caps her currently deductible loss at that amount, with the remaining $18,000 suspended and carried forward until she obtains additional basis in future years.

19. D — Under Section 351(a) and 368(c), the control requirement is satisfied when persons transferring property own at least 80% of a corporation's stock immediately after the exchange. Marisol and Declan together hold 80% of Coral Basin's stock, meeting this threshold, so their exchange qualifies for nonrecognition even though Priya's service-based shares are excluded from the property transferors' group.

20. B — Section 336(a) requires a liquidating corporation to recognize gain or loss as though distributed property were sold to the shareholder at fair market value. Because the land's $410,000 fair market value exceeds Thornwell's $260,000 adjusted basis, Thornwell recognizes $150,000 of gain, reported on the corporation's final return before dissolution is complete.

21. B — Section 1361(b)(1)(A) limits an S corporation to a maximum of 100 shareholders, though certain family members may elect to be counted as one shareholder. Because Halcyon's shareholders are unrelated individuals, admitting five more would bring the total to 102, exceeding the statutory limit and causing the S election to terminate automatically.

22. C — Section 1362(b)(2) requires a new corporation's S election to be filed no later than two months and fifteen days after the beginning of the tax year for which it is to take effect. Since Redshank's first tax year began March 1, Form 2553 is timely if filed by May 15, satisfying the statutory deadline for a timely first-year election.

23. A — Section 1366(a)(1)(A) requires S corporation items with special tax character, such as charitable contributions, to be separately stated and passed through to each shareholder rather than deducted at the corporate level. Briallen reports her 40% share, or $6,000, on her individual return, subject to her own charitable deduction limitations for the year.

24. D — Under Section 1367(a), stock basis is increased for income items before being decreased for distributions during the same tax year. Wynstan's $5,000 basis rises to $35,000 with the $30,000 of income, and the $12,000 distribution then reduces it to $23,000, avoiding any gain recognition on the distribution itself for the tax year.

25. B — Under Section 1368(b), when an S corporation has no accumulated earnings and profits, a distribution is first a tax-free return of stock basis. Genevra's basis absorbs the first $40,000 of the $55,000 distribution, and the remaining $15,000, exceeding her basis, is taxed as capital gain from a deemed stock sale.

26. A — Under the check-the-box regulations of Reg. Section 301.7701-3, a domestic single-member LLC that does not file Form 8832 is classified by default as an entity disregarded from its owner. Sablewood Ventures is therefore treated as a sole proprietorship, with all income and expenses reported directly on Baltasar's individual tax return.

27. D — Section 384 generally prevents a corporation's preacquisition losses, including net operating loss carryovers, from offsetting recognized built-in gains of another corporation it acquires control of, or is acquired by, for the five-year period beginning on the acquisition date. This built-in gain limitation targets loss trafficking, distinct from the ownership-change loss limitation under Section 382.

28. C — Section 1374(d)(7) sets the built-in gains tax recognition period at five years, beginning with the first day of the corporation's first S corporation tax year. Because Foxglove converted effective January 1, 2024, a sale in 2028 falls within that five-year window, subjecting the recognized built-in gain to corporate-level tax immediately upon sale.

29. B — Section 332 provides nonrecognition treatment to a parent corporation on the receipt of property in complete liquidation of a subsidiary in which it owns at least 80% of the voting stock and value. Because Ashgrove owns 85% of Wrenfield, it recognizes no gain or loss on the liquidating distribution received.

30. C — Section 243 grants corporate shareholders a dividends-received deduction that scales with the shareholder's ownership percentage: less than 20% ownership permits a 50% deduction, at least 20% but less than 80% ownership permits 65%, and 80% or more, as an affiliated group member, permits a full 100% deduction. Redwood Fenwick's 25% stake qualifies for the 65% tier.

31. A — Section 1244 allows an unmarried individual shareholder to treat up to $50,000 of loss on qualifying small business stock as an ordinary loss rather than a capital loss, provided the stock was acquired directly from the issuing corporation. Because Ottoline's entire $45,000 loss falls under this cap, it is fully ordinary.

32. D — Section 1045 allows a taxpayer who sells qualified small business stock held more than six months to elect nonrecognition of gain if the proceeds are reinvested in other qualified small business stock within 60 days. The deferred gain reduces the basis of the replacement stock, distinguishing this rollover from the permanent exclusion available under Section 1202.

33. A — Section 316(a) defines a dividend as any distribution of property made by a corporation to its shareholders out of current or accumulated earnings and profits. Because Drystone's combined $58,000 of current and accumulated earnings and profits exceeds the $25,000 distributed, the entire distribution to Corvina is treated as a taxable dividend.

34. C — Under Reg. Section 1.1361-1(l), the one-class-of-stock test looks only to a corporation's governing provisions, such as its charter and bylaws. A private agreement among shareholders that is not part of those governing provisions and lacks a principal purpose of circumventing the requirement does not create a second class of stock.

35. D — To qualify as a Type A statutory merger under Section 368(a)(1)(A), the continuity of interest doctrine requires Fenwick's shareholders to retain a meaningful, continuing proprietary stake in Ashdown, typically satisfied when at least 40% of the consideration consists of acquiring corporation stock. Fenwick's 55% stock component clearly meets this threshold.

36. B — A corporation qualifies as a qualified personal service corporation under Section 448(d)(2) only if it satisfies both the function test, requiring that at least 95% of its activities involve services in a qualifying field such as law, health, or accounting, and the ownership test, requiring that at least 95% of its stock be held by employees performing those services.

37. B — Section 263A's uniform capitalization rules require resellers with average annual gross receipts above the small-business exemption to capitalize indirect costs such as purchasing, handling, and storage into inventory rather than deducting them currently. Because Brannigan's $35 million average exceeds the exemption threshold, its purchasing and storage costs must be capitalized, not expensed.

38. C — Section 453(b)(2) excludes dealer dispositions—property held for sale to customers in the ordinary course of business—from installment sale reporting. Because Costa's lots are inventory sold in its regular business, gain must be reported using its regular accounting method (accrual) in the year of sale rather than deferred as payments are collected.

39. D — Section 460 generally requires the percentage-of-completion method for long-term contracts expected to take more than two years, unless the taxpayer qualifies for the small-contractor exemption based on average annual gross receipts. Since Delgado's bridge contract spans three years and it isn't a small contractor, percentage-of-completion applies, recognizing income as work progresses.

40. A — A positive Section 481(a) adjustment resulting from a voluntary accounting method change is generally spread ratably over four tax years, beginning with the year of change, under the standard adjustment period rules in Rev. Proc. 2015-13. Everhart must therefore recognize $20,000 of the $80,000 adjustment in each of four years.

41. C — Under Section 1031, gain on a like-kind exchange of real property is recognized only to the extent of boot received, limited to the lesser of realized gain or boot. Farrow realized $110,000 of gain but received only $50,000 cash boot, so $50,000 is recognized and the remaining gain is deferred.

42. D — Section 1033(a)(2)(B) generally gives a taxpayer two years from the close of the first tax year in which any part of the gain is realized to acquire qualified replacement property and defer recognition. Because Grayson's loss resulted from fire (not condemnation of real property), the standard two-year replacement period applies here.

43. B — Under the claim of right doctrine established in North American Oil Consolidated v. Burnet, income received without restriction on its use must be reported in the year received, even though the taxpayer's right to keep it may later be challenged. Holbrook must include the $200,000 in Year 1 gross income.

44. A — When the fair market value of contingent consideration cannot be reasonably ascertained, the open transaction doctrine permits use of the cost recovery method: payments received are treated first as a tax-free return of basis, with gain recognized only after full basis recovery. Ibarra therefore defers gain until payments exceed its land basis.

45. A — Entities classified as tax shelters under Section 448(d)(3)—including those with more than 35% of losses allocable to limited partners or limited entrepreneurs—are barred from using the cash method regardless of their average annual gross receipts, unlike ordinary small businesses. Juniper must therefore use an accrual method of accounting for federal tax purposes going forward.

46. C — Section 483 imputes interest at the applicable federal rate on deferred payment sales lacking adequate stated interest, when payments are due more than six months after sale. Part of each payment Kessler receives is recharacterized as ordinary interest income rather than sale proceeds, even though the contract stated no interest.

47. B — Even automatic accounting method changes require the taxpayer to file Form 3115, Application for Change in Accounting Method, generally attached to the timely filed return for the year of change, along with a duplicate copy to the IRS. Automatic consent avoids the user fee and advance ruling process but not the filing itself.

48. D — Specific identification is required (or most appropriate) for inventory consisting of unique, non-fungible items whose individual costs can be directly traced, such as fine art or custom goods. Because each Mercer painting is distinct and identifiable, its actual acquisition cost—not an assumed FIFO or LIFO flow—determines cost of goods sold.

49. D — Section 460(e) exempts home construction contracts—along with contracts of small contractors meeting the applicable gross receipts threshold—from the mandatory percentage-of-completion method, permitting use of the completed-contract method or another permissible method instead. Because Novak's contracts qualify as home construction contracts, it may defer income recognition until each home is fully completed.

50. A — Section 1031(f) requires related parties to hold like-kind exchange property for at least two years after the exchange, or previously deferred gain is triggered and must be recognized by both parties. Because Ortiz Rentals' subsidiary disposed of the property after only fourteen months, the related-party rule causes recognition of the original gain.

51. C — Under Section 168(c), nonresidential real property is depreciated using the straight-line method over a 39-year recovery period under the general depreciation system. Residential rental property instead uses 27.5 years. Nonresidential real property must use straight-line depreciation exclusively; no accelerated method is permitted, regardless of the taxpayer's chosen depreciation system for other asset classes.

52. B — Under Section 179(b)(2), the dollar limitation is reduced, dollar-for-dollar, by the amount that qualifying property placed in service during the year exceeds the applicable investment threshold. Once cumulative qualifying purchases exceed the threshold by an amount equal to the maximum deduction, the Section 179 election is completely phased out, though bonus depreciation may still apply to the excess.

53. B — Section 168(e)(6) defines qualified improvement property as interior nonstructural improvements to nonresidential building interiors placed in service after the building was first placed in service. A legislative correction in the CARES Act assigned it a 15-year MACRS recovery period using straight-line depreciation, which also makes it eligible for bonus depreciation, unlike the original 39-year classification error.

54. A — Section 168(d)(1) establishes the half-year convention as the default rule for MACRS personal property, treating all property placed in service during the tax year as placed in service at the midpoint of that year. This convention applies unless the mid-quarter convention exception is triggered because more than 40 percent of qualifying property is placed in service during the last quarter.

55. C — Section 179(b)(3) limits the deduction to the taxpayer's aggregate taxable income derived from the active conduct of a trade or business. Any amount disallowed because it exceeds this taxable income limitation is not lost; instead, it carries forward indefinitely and may be deducted in a later year, subject again to that year's taxable income limitation.

56. D — Section 45G allows eligible Class II and Class III railroads, and other railroad track owners or lessees, a credit equal to 50% of qualified railroad track maintenance expenditures paid or incurred during the year, limited to a specified dollar amount per mile of railroad track assigned to the taxpayer for the period.

57. C — Section 197(a) requires most acquired intangible assets, including customer lists and covenants not to compete acquired in connection with a trade or business acquisition, to be amortized ratably over a fixed 15-year period beginning with the month of acquisition, regardless of the intangible's actual useful life or any shorter contractual term stated in the agreement.

58. D — Section 168(i)(7) generally requires that the carryover portion of basis in like-kind exchange replacement property continue to be depreciated as if the exchange had not occurred, using the relinquished property's remaining recovery period and method. Only the excess basis attributable to additional consideration paid is treated as newly placed in service property.

59. B — Section 51(d)(13) requires the employer to complete Form 8850, the pre-screening notice, on or before the day the job offer is made, and then submit it to the designated local agency no later than 28 days after the employee begins work. Missing this filing deadline generally disqualifies the employer from claiming the Work Opportunity Tax Credit for that hire.

60. A — Section 41(c)(5) permits taxpayers to elect the Alternative Simplified Credit, computed as 14 percent of qualified research expenses exceeding 50 percent of the average qualified research expenses for the three preceding tax years. This method avoids the burdensome fixed-base percentage calculations required under the regular credit method and is often used when older historical records are unavailable.

61. A — Section 42(i)(1) establishes a 15-year compliance period during which a low-income housing project must continue meeting the applicable set-aside and rent restriction requirements. Failing to maintain qualified low-income occupancy during this compliance period triggers recapture of a portion of the accelerated credit previously claimed, computed under the recapture rules of Section 42(j).

62. B — Section 199A(b)(2) limits the deduction for a non-specified service trade or business, once taxable income exceeds the threshold, to the greater of 50 percent of W-2 wages paid, or 25 percent of W-2 wages plus 2.5 percent of the unadjusted basis immediately after acquisition of qualified property, unlike an SSTB, which loses the deduction entirely above the phase-in range.

63. C — Qualified REIT dividends and qualified publicly traded partnership income are computed separately from qualified business income under Section 199A(b)(1)(B) and generally receive a 20 percent deduction. This component is not subject to the W-2 wage and unadjusted basis limitation that applies to qualified business income once taxable income exceeds the applicable threshold amount for the taxpayer's filing status.

64. D — Section 199A(d)(3) provides that an SSTB owner whose taxable income falls within the phase-in range does not lose the deduction entirely at the threshold. Instead, the applicable percentage of QBI, W-2 wages, and UBIA treated as attributable to the SSTB is proportionally reduced as income rises through the range, reaching zero once income exceeds the range's upper limit.

65. A — Section 39(a) generally allows unused general business credit to be carried back one year and, if not fully absorbed, carried forward for twenty taxable years following the year the credit arose. Credits are applied using a specific ordering rule, and any credit still unused after the twenty-year carryforward period expires and is permanently lost as a deduction against tax liability.

66. C — Employers that pay state unemployment tax timely and in full may claim a credit of up to 5.4% against the 6.0% FUTA rate under §3302, reducing the effective net rate to 0.6% on the first $7,000 of wages, unless the state is a credit reduction state, which lowers the available credit.

67. D — Under §3406, a payor must apply backup withholding when a payee fails to furnish a correct TIN, underreports interest or dividend income, or is otherwise notified by the IRS. The current backup withholding rate is 24%, matching the fourth individual income tax bracket, and applies to reportable payments including nonemployee compensation.

68. B — Statutory employees under §3121(d)(3), such as full-time life insurance salespeople, have Social Security and Medicare tax withheld like employees but report their income and related business expenses on Schedule C rather than as wages, allowing full deduction of ordinary and necessary expenses without being subject to the miscellaneous itemized deduction limitations.

69. A — Passenger vehicles, including many trucks and SUVs under a certain weight, are subject to annual depreciation caps under §280F, often called the luxury automobile limits. These dollar caps, adjusted for inflation, restrict the depreciation deduction regardless of the vehicle's cost, and must be prorated when business use is less than 100%.

70. C — Section 280A(c)(1) generally requires that a portion of the home be used exclusively and regularly for business to qualify for the home office deduction. Because the children's homework and television use is personal, not incidental to the business, the room fails the exclusive use test and Wendell cannot claim the deduction.

71. D — Under the farm optional method, a farmer with gross farm income at or below the applicable threshold may report net earnings from self-employment equal to the lesser of two-thirds of gross farm income or the indexed annual dollar limit, allowing a low-income farm year to still generate Social Security quarters of coverage for retirement purposes.

72. A — The SUTA Dumping Prevention Act of 2004 requires states to mandate the transfer of an employer's unemployment experience rating when there is common ownership or control, and to assign the highest rate the state allows, often with civil or criminal penalties, when a transfer is made primarily to obtain a lower rate, deterring this workforce-shifting manipulation.

73. B — Section 3508 designates qualified real estate agents and direct sellers as statutory nonemployees when substantially all compensation is tied to sales or output rather than hours worked and a written contract states they will not be treated as employees for federal tax purposes, making them self-employed for income and self-employment tax purposes.

74. C — The Social Security (OASDI) portion of FICA applies only up to an annually indexed wage base, after which no further Social Security tax is withheld. The Medicare portion has no wage base limit and continues to apply to all wages, with an Additional Medicare Tax also potentially applying above a separate income threshold.

75. D — To deduct travel expenses, a taxpayer must be traveling away from their tax home, meaning the trip requires being away substantially longer than an ordinary workday such that rest or sleep is needed before returning. Denver is Nadia's tax home, so her overnight trip to Salt Lake City satisfies this away-from-home requirement.

76. B — The high-low substantiation method is a simplified per diem approach under which the IRS publishes just two flat daily rates, one for designated high-cost localities and one for all other, standard-cost localities, allowing travelers to substantiate lodging, meals, and incidental expenses without tracking actual receipts for each expenditure incurred during travel.

77. D — Federal law under the Personal Responsibility and Work Opportunity Reconciliation Act requires employers to report newly hired employees to their state directory of new hires within 20 days of the hire date, providing information such as name, address, and Social Security number to assist state child support enforcement agencies in locating parents.

78. A — A sole proprietor who begins paying wages to employees must obtain an Employer Identification Number by filing Form SS-4, since an EIN, not a Social Security number, is used to report and deposit federal employment taxes, file employment tax returns such as Form 941, and issue Forms W-2 to employees.

79. C — An employer's deposit schedule for a calendar year is determined by its total employment tax liability during the lookback period, the four quarters ending the preceding June 30. Employers reporting $50,000 or less during that period are monthly depositors, while those exceeding $50,000 become semiweekly depositors under the deposit rules of Section 6302.

80. B — Section 642(c) allows a trust an unlimited income tax deduction for amounts of gross income paid to charity pursuant to the governing instrument, unlike the percentage caps under Section 170 applicable to individuals. The payment must trace to gross income, not corpus, and the governing document must authorize the payment for the deduction to apply.

81. C — Section 663(b) permits a fiduciary to elect treating any distribution made within the first 65 days of a new tax year as having been distributed on the last day of the preceding tax year. This 65-day rule gives trustees flexibility to finalize distributable net income figures after year-end while still meeting distribution needs of beneficiaries promptly.

82. D — Under Section 2032, an executor may elect the alternate valuation date only if doing so both decreases the value of the gross estate and decreases the combined estate and generation-skipping transfer tax liability. If either condition fails, the election is unavailable, and date-of-death values must be used consistently for the entire estate.

83. B — In a private annuity, a transferor exchanges property for the transferee's unsecured promise to make annuity payments for the transferor's life. Because no lien or security interest is retained in the property, the transferred asset is generally excluded from the transferor's gross estate under Section 2036, provided the annuity was actuarially fair and no retained interest exists.

84. A — Under Section 673, a grantor is treated as the owner of any trust portion in which the grantor holds a reversionary interest exceeding 5% of the value of that portion, measured at the trust's inception. This reversionary-interest rule triggers grantor trust status, requiring the grantor to report the trust's income directly on his own return.

85. D — Section 642(g) prohibits deducting administration expenses on both the estate tax return, Form 706, and the fiduciary income tax return, Form 1041, for the same amounts. The executor must choose one return, though a statement waiving the Section 2053 estate tax deduction permits claiming the expenses instead as an income tax deduction under Section 212.

86. A — Section 4940 imposes an excise tax on a private foundation's net investment income, which includes interest, dividends, rents, royalties, and net capital gain from the sale of investment assets, reduced by related expenses. Contributions received, program-related investment activity, and unrealized appreciation on unsold assets are not included in this net investment income calculation.

87. C — Section 511 imposes tax on unrelated business taxable income at corporate rates for organizations taxable as corporations, but exempt trusts are taxed at the rates applicable to trusts under Section 1(e). This distinction matters because trust rates reach the top bracket at much lower income levels than the flat 21% corporate rate applies.

88. B — Unlike most other Section 501(c)(3) organizations, churches, their integrated auxiliaries, and conventions or associations of churches are automatically exempt from the annual Form 990 information return filing requirement under Section 6033(a)(3), regardless of the amount of their gross receipts. This exemption applies without regard to whether the church has sought formal IRS recognition of its exempt status.

89. D — Under Section 170(b)(1)(A)(vi) and its regulations, an organization normally qualifies as publicly supported if at least one-third of its total support comes from governmental units, the general public, and other public charities, computed over a rolling five-year measuring period. Organizations between 10% and one-third may still qualify under a facts-and-circumstances test applied.

90. A — Section 408(k) permits employer contributions to a SEP-IRA of up to 25% of compensation, subject to an annual dollar limit adjusted for inflation. For self-employed individuals, compensation is net earnings from self-employment reduced by the deduction for one-half of self-employment tax and by the SEP contribution itself, effectively lowering the contribution percentage available.

91. C — The actual deferral percentage, or ADP, test compares the average elective deferral rates of highly compensated employees against non-highly compensated employees to ensure a traditional 401(k) plan does not discriminate in favor of higher earners. A related actual contribution percentage test applies the same comparison to employer matching and after-tax contributions made.

92. A — Section 4975 imposes an excise tax on a disqualified person who engages in a prohibited transaction with a qualified plan, such as a direct sale of property between the plan and a family member of a fiduciary. An initial tax applies to the amount involved, and a larger additional tax applies if the transaction is not timely corrected.

93. B — Under Section 401(a)(9), a non-5%-owner participant who continues working past the applicable required beginning date age may generally delay required minimum distributions from that employer's qualified plan until April 1 following the calendar year in which he actually retires. This still-working exception does not apply to 5% owners or to IRA accounts held.

94. C — Section 72(t) generally imposes a 10% additional tax on early distributions taken before age 59½, but the statute exempts distributions used to pay unreimbursed medical expenses exceeding the taxpayer's adjusted gross income threshold. Because Estelle's medical expenses exceed that threshold, her distribution qualifies for the exception and escapes the 10% early distribution penalty.

95. D — Section 461(j) provides a special excess farm loss limitation for farmers who received CCC loan proceeds or certain crop insurance and disaster payments during the year, applying instead of the general excess business loss rule. The disallowed loss is limited to the greater of the standard threshold amount or the taxpayer's aggregate net farming income for the preceding five years.

96. B — Section 461(l) limits the amount of aggregate net business losses, including farming losses, that a noncorporate taxpayer may deduct against nonbusiness income in a single year, with the excess treated as a net operating loss carryforward. This excess business loss limitation applies after the at-risk and passive activity loss rules are separately considered first.

97. D — Section 263A(d) generally exempts property produced in a farming business from the uniform capitalization rules that otherwise require capitalizing indirect production costs. However, a farmer who affirmatively elects out of UNICAP for certain plants or animals must use the alternative depreciation system to depreciate all property used predominantly in the farming business thereafter.

98. A — Livestock held for draft, breeding, dairy, or sporting purposes and held beyond the applicable holding period is treated as Section 1231 property, allowing gain on sale to potentially receive favorable capital gain treatment while losses remain ordinary. This differs from livestock held primarily for sale, which produces ordinary income when sold during regular farming operations.

99. C — Section 2056(b)(5) provides a marital deduction exception for a power of appointment trust in which the surviving spouse receives all trust income for life, payable at least annually, and holds a general power to appoint the principal to himself or his estate, exercisable alone and in all events, satisfying the terminable interest exception without any QTIP election.

100. B — A private foundation may avoid the Section 507 termination tax by distributing all of its net assets to one or more organizations described in Section 170(b)(1)(A), such as public charities, that have been in continuous existence for at least sixty months, thereby avoiding the tax otherwise imposed based on aggregate tax benefits received over the foundation's history.