

Chapter 01: An Introduction To Taxation and Understanding the Federal Tax Law

1. The Federal income tax on individuals generates more revenue than the Federal income tax on corporations.

- a. True
- b. False

ANSWER: True

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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2. Because the law is complicated, most individual taxpayers are not able to complete their Federal income tax returns without outside assistance.

- a. True
- b. False

ANSWER: True

RATIONALE: More than 50% use tax return preparers and about 33% purchase tax return software.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-02 - LO: 1-02

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3. The ratification of the Sixteenth Amendment to the U.S. Constitution was necessary to validate the Federal income tax on corporations.

- a. True
- b. False

ANSWER: False

RATIONALE: The Sixteenth Amendment validated only the tax on *individuals*. The income tax on corporations had been previously sanctioned by the courts.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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4. Before the Sixteenth Amendment to the Constitution was ratified, there was no valid Federal income tax on individuals.

a. True

b. False

ANSWER: False

RATIONALE: There existed a Federal income tax during the Civil War that was sanctioned by the U.S. Supreme Court.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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5. The first income tax on individuals (after the ratification of the Sixteenth Amendment to the Constitution) levied tax rates from a low of 2% to a high of 6%.

a. True

b. False

ANSWER: True

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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6. The pay-as-you-go feature of the Federal income tax on individuals conforms to Adam Smith's canon (principle) of certainty.

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- a. True
- b. False

ANSWER: False

RATIONALE: Pay-as-you-go refers to the withholding provisions applicable to wages and other types of income and adds *convenience* to the tax system.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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7. The FICA tax (Medicare component) on wages is *progressive* since the tax due increases as wages increase.

- a. True
- b. False

ANSWER: False

RATIONALE: The FICA tax (Medicare component) is *proportional* because the rate is constant regardless of the wages earned.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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8. The Federal estate and gift taxes are examples of *progressive* taxes.

- a. True
- b. False

ANSWER: True

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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9. The Federal excise tax on cigarettes is an example of a *proportional* tax.

- a. True
- b. False

ANSWER: True
RATIONALE: The tax is a flat \$1.01 per pack.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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10. Currently, the Federal income tax is less *progressive* than it ever has been in the past.

- a. True
- b. False

ANSWER: False
RATIONALE: Currently, the Federal income tax has six rates. At one time, it had two rates.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-03 - LO: 1-03
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11. Mona inherits her mother's personal residence, which she converts to a furnished rental house. These changes should

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affect the amount of *ad valorem* property taxes levied on the properties.

- a. True
- b. False

ANSWER: True

RATIONALE: Conversion from residential to rental use will increase the taxes. Furthermore, Mona's mother may have had a senior citizen exemption on the property, which will no longer be appropriate. Lastly, the furnishings in the rent house could now be subject to an *ad valorem* tax on personalty.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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12. A *fixture* will be subject to the *ad valorem* tax on *personalty* rather than the *ad valorem* tax on *realty*.

- a. True
- b. False

ANSWER: False

RATIONALE: By definition, a fixture becomes part of the real estate to which it is attached.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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13. Even if property tax rates are not changed, the amount of *ad valorem* taxes imposed on *realty* may not remain the same.

- a. True
- b. False

ANSWER: True

RATIONALE: Property taxes will vary in accordance with changes in the assessed value of the property.

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DIFFICULTY: Easy
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HAS VARIABLES: False
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14. The *ad valorem* tax on personal use personalty is more often avoided by taxpayers than the *ad valorem* tax on business use personalty.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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15. A Federal excise tax is no longer imposed on admission to theaters.

- a. True
- b. False

ANSWER: True
RATIONALE: Such tax has been rescinded.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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16. There is a Federal excise tax on hotel occupancy.

a. True

b. False

ANSWER: False
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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17. The Federal gas-guzzler tax applies only to automobiles manufactured overseas and imported into the U.S.

a. True

b. False

ANSWER: False
RATIONALE: No such restriction is imposed. Although many of the European luxury and sports car manufacturers were initially hit hard by the tax, the law is silent on this matter.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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18. Like the Federal counterpart, the amount of the state excise taxes on gasoline varies from state to state.

a. True

b. False

ANSWER: False
RATIONALE: The Federal excise tax rate on gasoline remains constant.

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POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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19. Not all of the states that impose a general sales tax also have a use tax.

- a. True
- b. False

ANSWER: False
RATIONALE: Every state that has a general sales tax also has a use tax. There are no states with only a sales or use tax.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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20. Sales made by mail order are not exempt from the application of a general sales (or use) tax.

- a. True
- b. False

ANSWER: True
RATIONALE: They are not exempt but compliance is sporadic.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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21. Two persons who live in the same state but in different counties may not be subject to the same general sales tax rate.

- a. True
- b. False

ANSWER: True
RATIONALE: This possibility could exist if local jurisdictions exact additional sales taxes.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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22. States impose either a state income tax *or* a general sales tax, but not both types of taxes.

- a. True
- b. False

ANSWER: False
RATIONALE: Many states impose both.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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23. A safe and easy way for a taxpayer to avoid local and state sales taxes is to make the purchase in a state that levies no such taxes.

- a. True
- b. False

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ANSWER: False
RATIONALE: A review of the Example 5 discussion shows that this may not always be successful.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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24. On transfers by death, the Federal government relies on an estate tax, while states impose an estate tax, an inheritance tax, both taxes, or neither tax.

- a. True
- b. False

ANSWER: True
RATIONALE: The Federal government relies on an estate tax while states impose an estate tax, an inheritance tax, both taxes, or neither tax.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
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25. An inheritance tax is a tax on a decedent's right to pass property at death.

- a. True
- b. False

ANSWER: False
RATIONALE: What is described is an estate tax. An inheritance tax is a tax on an heir's right to receive property from a decedent.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False

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26. One of the major reasons for the enactment of the Federal estate tax was to prevent large amounts of wealth from being accumulated within the family unit.

- a. True
- b. False

ANSWER: True

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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27. Under Clint's will, all of his property passes to either the Lutheran Church or to his wife. No Federal estate tax will be due on Clint's death in 2017.

- a. True
- b. False

ANSWER: True

RATIONALE: A combination of the charitable and marital deductions will eliminate Clint's taxable estate.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

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28. Under the usual state inheritance tax, two heirs, a cousin and a son of the deceased, would not be taxed at the same rate.

- a. True
- b. False

ANSWER: True

RATIONALE: The more closely related the heir is to the decedent, the larger the exemption allowed and/or the lower the tax rate imposed.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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29. The annual exclusion, currently \$14,000, is available for gift and estate tax purposes.

- a. True
- b. False

ANSWER: False

RATIONALE: The annual exclusion is not available for estate tax purposes.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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30. In 2017, José, a widower, sells land (fair market value of \$100,000) to his daughter, Linda, for \$50,000. José has not made a taxable gift.

- a. True
- b. False

ANSWER: False

RATIONALE: \$100,000 (value of land) – \$50,000 (consideration received) – \$14,000 (per donee annual

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exclusion) = \$36,000 (taxable gift).

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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31. Julius, a married taxpayer, makes gifts to each of his six children. A maximum of twelve annual exclusions could be allowed as to these gifts.

- a. True
- b. False

ANSWER: True
RATIONALE: If Julius can obtain the consent of his wife to make the election to split the gifts, twelve per donee annual exclusions are available.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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32. One of the motivations for making a gift is to save on income taxes.

- a. True
- b. False

ANSWER: True
RATIONALE: This presumes that income-producing property is involved and that the donee is in a lower tax bracket than the donor.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
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33. The formula for the Federal income tax on corporations is the same as that applicable to individuals.

a. True

b. False

ANSWER: False
RATIONALE: For example, an AGI determination is required only for individual taxpayers.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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34. A state income tax *can* be imposed on *nonresident* taxpayers who earn income within the state on an itinerant basis.

a. True

b. False

ANSWER: True
RATIONALE: Highly-paid taxpayers (e.g., entertainers, athletes) are often subject to a state's income tax. The so-called "jock tax" has been criticized since it singles out highly-paid and well known personalities and is not imposed on the average business traveler.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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35. For state income tax purposes, a majority of states allow a deduction for Federal income taxes.

- a. True
- b. False

ANSWER: False

RATIONALE: Only a minority allow the deduction.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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36. Some states use their state income tax return as a means of collecting unpaid sales and use taxes.

- a. True
- b. False

ANSWER: True

RATIONALE: Often a table is provided that suggests an amount to be used.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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37. No state has offered an income tax amnesty program more than once.

- a. True
- b. False

ANSWER: False

RATIONALE: One state has had at least four.

POINTS: 1

DIFFICULTY: Easy

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HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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38. For Federal income tax purposes, there never has been a general amnesty period.

- a. True
- b. False

ANSWER: True
RATIONALE: Limited amnesty has been made available as to various tax penalties in certain tax shelter situations.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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39. Under state amnesty programs, all delinquent and unpaid income taxes are forgiven.

- a. True
- b. False

ANSWER: False
RATIONALE: The taxes and interest are not forgiven. Only the penalties are forgiven.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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40. When a state decouples from a Federal tax provision, it means that this provision will *not* apply for state income tax purposes.

a. True

b. False

ANSWER: True

RATIONALE: In view of tight state finances, decoupling from various Federal tax cuts has become quite common.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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41. The principal objective of the FUTA tax is to provide some measure of retirement security.

a. True

b. False

ANSWER: False

RATIONALE: This is the objective of the FICA tax.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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42. Currently, the tax base for the Social Security component of the FICA is *not* limited to a dollar amount.

a. True

b. False

ANSWER: False

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RATIONALE: There is no dollar amount limitation on the Medicare component of FICA.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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43. A parent employs his twin daughters, age 17, in his sole proprietorship. The daughters are *not* subject to FICA coverage.

- a. True
- b. False

ANSWER: True
RATIONALE: An exemption exists for taxpayer's children who are *under age 18*.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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44. Unlike FICA, FUTA requires that employers comply with state as well as Federal rules.

- a. True
- b. False

ANSWER: True
RATIONALE: This is a major difference between FICA and FUTA.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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45. A major advantage of a flat tax type of income tax is its simplicity.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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46. The value added tax (VAT) *has not* had wide acceptance in the international community.

- a. True
- b. False

ANSWER: False
RATIONALE: Its use in 140 countries seems to represent "wide acceptance."
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
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47. If more IRS audits are producing a greater number of *no change* results, this indicates increased compliance on the part of taxpayers.

- a. True
- b. False

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ANSWER: False
RATIONALE: It indicates that the IRS is not always choosing the right returns to audit (i.e., those that contain errors).
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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48. The amount of a taxpayer's itemized deductions *will* increase the chance of being audited by the IRS.

- a. True
- b. False

ANSWER: True
RATIONALE: If the taxpayer has itemized deductions that are unusually large, the chances of being selected for audit increase.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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49. In an office audit, the audit by the IRS takes place at the office of the taxpayer.

- a. True
- b. False

ANSWER: False
RATIONALE: What is described is a field audit. An office audit takes place at the office of the IRS.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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50. The IRS agent auditing the return *will* issue an RAR even if the taxpayer owes no additional taxes.
a. True
b. False

ANSWER: True
RATIONALE: An RAR can result in no change, a deficiency, or a refund.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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51. If a “special agent” becomes involved in the audit of a return, this indicates that the IRS suspects that fraud is involved.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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52. If a taxpayer files early (i.e., before the due date of the return), the statute of limitations on assessments begins on the date the return is filed.

- a. True
- b. False

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ANSWER: False
RATIONALE: If begins on the due date of the return.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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53. For omissions from gross income in excess of 25% of that reported, there is no statute of limitations on additional income tax assessments by the IRS.

- a. True
- b. False

ANSWER: False
RATIONALE: Unless fraud is involved, the statute of limitations in this case is six years.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
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54. If an income tax return is *not* filed by a taxpayer, there is no statute of limitations on assessments of tax by the IRS.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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55. If fraud is involved, there is no time limit on the assessment of a deficiency by the IRS.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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56. The IRS is required to redetermine the interest rate on underpayments and overpayments once a year.

- a. True
- b. False

ANSWER: False
RATIONALE: Interest rates are determined quarterly by the IRS.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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57. A calendar year taxpayer files his 2016 Federal income tax return on March 4, 2017. The return reflects an overpayment of \$6,000, and the taxpayer requests a refund of this amount. The refund is paid on May 16, 2017. The refund need not include interest.

- a. True
- b. False

ANSWER: True
RATIONALE: Because 45 days have not gone by since the *due date* of the return, interest need not be

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paid on the refund.

POINTS:

1

DIFFICULTY:

Easy

QUESTION TYPE:

True / False

HAS VARIABLES:

False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

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KEYWORDS:

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58. For individual taxpayers, the interest rate for income tax refunds (overpayments) *is* the same as that applicable to assessments (underpayments).

a. True

b. False

ANSWER:

True

RATIONALE:

There exists no difference in the applicable interest rates for *individual* taxpayers.

POINTS:

1

DIFFICULTY:

Easy

QUESTION TYPE:

True / False

HAS VARIABLES:

False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

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59. During any month in which both the failure to file penalty and the failure to pay penalty apply, the failure to file penalty is *increased* by the amount of the failure to pay penalty.

a. True

b. False

ANSWER:

False

RATIONALE:

The failure to file penalty *is reduced* by the amount of the failure to pay penalty.

POINTS:

1

DIFFICULTY:

Easy

QUESTION TYPE:

True / False

HAS VARIABLES:

False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

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60. When interest is charged on a deficiency, any part of a month counts as a full month.

- a. True
- b. False

ANSWER: False
RATIONALE: Interest accrues daily.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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61. For the negligence penalty to apply, the underpayment must be caused by intentional disregard of rules and regulations without intent to defraud.

- a. True
- b. False

ANSWER: True
RATIONALE: In the negligence penalty situation, there is no intent to defraud requirement.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
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62. Upon audit by the IRS, Faith is assessed a deficiency of \$40,000 of which \$25,000 is attributable to negligence. The 20% negligence penalty will apply to \$25,000.

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- a. True
- b. False

ANSWER: True
RATIONALE: The negligence penalty applies only to \$25,000.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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63. If the tax deficiency is attributable to fraud, the negligence penalty will not be imposed.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
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64. The *civil* fraud penalty can entail large fines and possible incarceration.

- a. True
- b. False

ANSWER: False
RATIONALE: What is described is *criminal* fraud. Civil fraud involves a monetary penalty of 75% of the deficiency attributable to fraud.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False

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KEYWORDS: Bloom's: Comprehension

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65. Even though a client refuses to correct an error on a past return, it may be possible for a practitioner to continue to prepare returns for the client.

- a. True
- b. False

ANSWER: True

RATIONALE: However, if the error is material and carries over to the current year, the preparer should consider withdrawing from the engagement.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics

STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Comprehension

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66. In preparing an income tax return, the use of a client's estimates is *not* permitted.

- a. True
- b. False

ANSWER: False

RATIONALE: Estimates are allowed if reasonable and not given the appearance of greater accuracy than is the case.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics

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67. In preparing a tax return, all questions on the return must be answered.

- a. True
- b. False

ANSWER: False

RATIONALE: The question need not be answered if the information requested is not readily available, the answer is voluminous, or the question's meaning is uncertain.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics

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68. A CPA firm in California sends many of its less complex tax returns to be prepared by a group of accountants in India. If certain procedures are followed, this outsourcing of tax return preparation is proper.

- a. True
- b. False

ANSWER: True

RATIONALE: Confidentiality must be secured; accuracy verified; and clients advised of the procedure.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics

STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Knowledge

OTHER: Time: 2 min.

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69. The objective of *pay-as-you-go* (*paygo*) is to improve administrative feasibility.

- a. True
- b. False

ANSWER: True

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

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LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 2 min.

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70. When Congress enacts a tax cut that is phased in over a period of years, revenue neutrality is achieved.

- a. True
- b. False

ANSWER: False

RATIONALE: No tax cut is revenue neutral unless accompanied by a revenue offset. A phase-in merely postpones some of the revenue loss caused by the tax cut.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 2 min.

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71. A tax cut enacted by Congress that contains a *sunset provision* will make the tax cut temporary.

- a. True
- b. False

ANSWER: True

RATIONALE: The sunset provision rescinds the change and reinstates former law.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

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72. The tax law provides various tax credits, deductions, and exclusions that are designed to encourage taxpayers to obtain additional education. These provisions can be justified on both economic and equity grounds.

- a. True
- b. False

ANSWER: False

RATIONALE: The justification is social and economic.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

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73. Various tax provisions encourage the creation of certain types of retirement plans. Such provisions can be justified on both economic and social grounds.

- a. True
- b. False

ANSWER: True

RATIONALE: The economic justification is attributable to the savings that result. In terms of social justification, private retirement plans supplement the meager benefits provided by Social Security and, thereby, circumvent the need for public assistance.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

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74. To lessen, or eliminate, the effect of multiple taxation, a taxpayer who is subject to both foreign and U.S. income taxes on the same income is allowed either a deduction or a credit for the foreign tax paid.

- a. True
- b. False

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ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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75. To mitigate the effect of the annual accounting period concept, the tax law permits the carryforward to other years of the excess charitable contributions of a particular year.

- a. True
- b. False

ANSWER: True
RATIONALE: This is also the case with excess capital losses.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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76. Jason's business warehouse is destroyed by fire. As the insurance proceeds exceed the basis of the property, a gain results. If Jason shortly reinvests the proceeds in a new warehouse, no gain is recognized due to the application of the wherewithal to pay concept.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

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STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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77. As it is consistent with the wherewithal to pay concept, the tax law requires a seller to recognize gain in the year the installment sale occurs.

- a. True
- b. False

ANSWER: False
RATIONALE: The seller is taxed in the years the installment payments are received.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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78. Stealth taxes have the effect of generating additional taxes from all taxpayers.

- a. True
- b. False

ANSWER: False
RATIONALE: Stealth taxes phase out (or eliminate) certain tax benefits from *higher income* taxpayers.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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79. A provision in the law that compels accrual basis taxpayers to pay a tax on prepaid income in the year received and

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not when earned is consistent with generally accepted accounting principles.

- a. True
- b. False

ANSWER: False

RATIONALE: It is inconsistent with accounting rules, although it can be justified for tax purposes under the wherewithal to pay concept.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Communications

STATE STANDARDS: United States - AK - AICPA: FN-Reporting

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 2 min.

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80. As a matter of administrative convenience, the IRS would prefer to have Congress decrease (rather than increase) the amount of the standard deduction allowed to individual taxpayers.

- a. True
- b. False

ANSWER: False

RATIONALE: Just the opposite is the case.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: True / False

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Research

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 2 min.

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81. In cases of doubt, courts have held that tax relief provisions should be broadly construed in favor of taxpayers.

- a. True
- b. False

ANSWER: False

RATIONALE: Such provisions should be *narrowly* construed *in favor of* taxpayers.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: True / False

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HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Research
KEYWORDS: Bloom's: Comprehension
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82. On occasion, Congress has to enact legislation that clarifies the tax law in order to change a result reached by the U.S. Supreme Court.

- a. True
- b. False

ANSWER: True
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: True / False
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Research
KEYWORDS: Bloom's: Comprehension
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83. Which, if any, of the following statements best describes the history of the Federal income tax?

- a. It did not exist during the Civil War.
- b. The Federal income tax on corporations was held by the U.S. Supreme Court to be allowable under the U.S. Constitution.
- c. The Federal income tax on individuals was held by the U.S. Supreme Court to be allowable under the U.S. Constitution.
- d. Both the Federal income tax on individuals and on corporations was held by the U.S. Supreme Court to be contrary to the U.S. Constitution.
- e. None of these.

ANSWER: b
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-02 - LO: 1-02
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Research
KEYWORDS: Bloom's: Knowledge

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84. Which, if any, is *not* one of Adam Smith's canons (principles) of taxation?

- a. Economy in collection
- b. Certainty
- c. Convenience of payment
- d. Simplicity
- e. Equality

ANSWER: d
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-03 - LO: 1-03
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge
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85. Which, if any, of the following taxes are *proportional* (rather than *progressive*)?

- a. State general sales tax
- b. Federal corporate income tax
- c. Federal estate tax
- d. Federal gift tax
- e. All of these

ANSWER: a
RATIONALE: Sales taxes are applied at a constant rate that does not progress.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-03 - LO: 1-03
NATIONAL STANDARDS: United States - BUSPROG: Comprehension - BUSPROG: Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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86. Which, if any, of the following transactions will *increase* a taxing jurisdiction's revenue from the *ad valorem* tax imposed on real estate?

- a. A resident dies and leaves his farm to his church.
- b. A large property owner issues a conservation easement as to some of her land.
- c. A tax holiday issued 10 years ago has expired.
- d. A bankrupt motel is acquired by the Red Cross and is to be used to provide housing for homeless persons.
- e. None of these.

ANSWER: c

RATIONALE: Although a farm was probably subject to reduced valuation (due to its agricultural use), it will now be fully exempt since it is owned by a church (choice a.). Property that is subject to a conservation easement is usually appraised at a lower value (choice b.). The expiration of a tax holiday means that the property involved can now be taxed (choice c.). The motel has been converted from business property to exempt charitable use (choice d.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

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87. Which, if any, of the following transactions will *decrease* a taxing jurisdiction's *ad valorem* tax revenue imposed on real estate?

- a. A tax holiday is granted to an out-of-state business that is searching for a new factory site.
- b. An abandoned church is converted to a restaurant.
- c. A public school is razed and turned into a city park.
- d. A local university sells a dormitory that will be converted for use as an apartment building.
- e. None of these.

ANSWER: a

RATIONALE: Choice a. has an effect since the tax holiday was granted. Choice b. will increase taxes as the church was abandoned and previously exempt. Choice c. converts one tax-exempt property (i.e., school) into another (i.e., public park). Choice d. probably places the building on the tax rolls because it is no longer owned by a tax-exempt institution.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -

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KEYWORDS: AICPA: FN-Measurement
Bloom's: Comprehension
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88. Which, if any, of the following is a typical characteristic of an *ad valorem* tax on personalty?
- a. Taxpayer compliance is greater for personal use property than for business use property.
 - b. The tax on automobiles sometimes considers the age of the vehicle.
 - c. Most states impose a tax on intangibles.
 - d. The tax on intangibles generates considerable revenue since it is difficult for taxpayers to avoid.
 - e. None of these.

ANSWER: b
RATIONALE: Taxpayer compliance is greater with business use property (choice a.). Very few states impose a tax on intangibles (choice c.) because it is easily avoided and does not generate much revenue (choice d.).

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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89. Federal excise taxes that are *no longer imposed* include:
- a. Tax on air travel.
 - b. Tax on wagering.
 - c. Tax on the manufacture of sporting equipment.
 - d. Tax on alcohol.
 - e. None of these.

ANSWER: e
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge

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90. Taxes *not imposed* by the Federal government include:

- a. Tobacco excise tax.
- b. Customs duties (tariffs on imports).
- c. Tax on rental cars.
- d. Gas guzzler tax.
- e. None of these.

ANSWER: c
RATIONALE: The Federal government imposes an excise tax on tobacco (choice a.), customs duties (choice b.), and a gas guzzler tax (choice d.). It does not impose a tax on rental cars (choice c.).
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge
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91. Taxes levied by *both* states and the Federal government include:

- a. General sales tax.
- b. Custom duties.
- c. Hotel occupancy tax.
- d. Franchise tax.
- e. None of these.

ANSWER: e
RATIONALE: Choices a., c., and d. are levied at the state or local level. Choice b. is strictly a Federal levy.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge

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92. Taxes levied by *all* states include:

- a. Tobacco excise tax.
- b. Individual income tax.
- c. Inheritance tax.
- d. General sales tax.
- e. None of these.

ANSWER: a
RATIONALE: All states impose a tobacco excise tax (choice a.). Most states impose individual income taxes (choice b.) and general sales taxes (choice d.), and only some states impose inheritance taxes (choice c.).
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge
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93. A use tax is imposed by:

- a. The Federal government and all states.
- b. The Federal government and a majority of the states.
- c. All states and not the Federal government.
- d. Most of the states and not the Federal government.
- e. None of these.

ANSWER: d
RATIONALE: A use tax is a complement to a general sales tax. Consequently, it is imposed by most states because only a few states do not have a general sales tax. At this point, the Federal government has no general sales tax.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement

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94. Burt and Lisa are married and live in a common law state. Burt wants to make gifts to their four children in 2017. What is the maximum amount of the annual exclusion they will be allowed for these gifts?

- a. \$14,000.
- b. \$28,000.
- c. \$56,000.
- d. \$112,000.
- e. None of these.

ANSWER: d
RATIONALE: $4 \text{ (number of donees)} \times \$14,000 \text{ (annual exclusion)} \times 2 \text{ (number of donors)} = \$112,000$. It is assumed that Lisa will make the election to split the gifts.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
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95. Property can be transferred within the family group by gift or at death. One motivation for preferring the gift approach is:

- a. To take advantage of the higher unified transfer tax credit available under the gift tax.
- b. To avoid a future decline in value of the property transferred.
- c. To take advantage of the per donee annual exclusion.
- d. To shift income to higher bracket donees.
- e. None of these.

ANSWER: c
RATIONALE: The per donee annual exclusion is only available for gift tax purposes (choice c.). Ideally, gifts should involve property that is expected to *appreciate* in value (choice b.). A higher unified tax credit is not available for gift tax purposes (choice a.). Usually the donor is trying to shift future income to *lower* bracket donees (choice d.).
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
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96. Indicate which, if any, statement is *incorrect*. State income taxes:

- a. Can piggyback to the Federal version.
- b. Cannot apply to visiting nonresidents.
- c. Can decouple from the Federal version.
- d. Can provide occasional amnesty programs.
- e. None of these.

ANSWER: b

RATIONALE: Many states piggyback to the Federal system (choice a.). Some states, due to revenue shortfalls, have decoupled from various provisions of the Federal version (choice c.). The "jock tax," although much criticized, is very much in being (choice b.). Some states have had more than one amnesty period (choice d.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 5 min.

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DATE MODIFIED: 5/11/2017 12:50 PM

97. State income taxes *generally* can be characterized by:

- a. The same date for filing as the Federal income tax.
- b. No provision for withholding procedures.
- c. Allowance of a deduction for Federal income taxes paid.
- d. Applying only to individuals and not applying to corporations.
- e. None of these.

ANSWER: a

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

Chapter 01: An Introduction To Taxation and Understanding the Federal Tax Law

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Knowledge

OTHER: Time: 5 min.

DATE CREATED: 11/28/2016 3:10 PM

DATE MODIFIED: 5/11/2017 12:50 PM

98. A characteristic of FICA is that:

- a. It does not apply when one spouse works for the other spouse.
- b. It is imposed only on the employer.
- c. It provides a modest source of income in the event of loss of employment.
- d. It is administered by both state and Federal governments.
- e. None of these.

ANSWER: e

RATIONALE: FICA is imposed on *both* the employer and the employee (choice b.). Spouses who work for each other are not exempt from the tax (choice a.). Its objective is retirement income, not loss of employment (choice c.). It is administered only by the Federal government (choice d.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Knowledge

OTHER: Time: 5 min.

DATE CREATED: 11/28/2016 3:10 PM

DATE MODIFIED: 5/11/2017 12:50 PM

99. A characteristic of FUTA is that:

- a. It is imposed on both employer and employee.
- b. It is imposed solely on the employee.
- c. Compliance requires following guidelines issued by both state and Federal regulatory authorities.
- d. It is applicable to spouses of employees but *not* to any children under age 18.
- e. None of these.

ANSWER: c

RATIONALE: FUTA is imposed only on the employer (choices a. and b.). Choice d. refers to FICA. Because the administration of FUTA is shared by Federal and state governments, employers must comply with the rules issued by each (choice c.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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100. The U.S. (either Federal, state, or local) *does not* impose:

- a. Franchise taxes.
- b. Severance taxes.
- c. Occupational fees.
- d. Custom duties.
- e. Export duties.

ANSWER: e
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Knowledge
OTHER: Time: 2 min.
DATE CREATED: 11/28/2016 3:10 PM
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101. The proposed *flat tax*:

- a. Would eliminate the income tax.
- b. Would simplify the income tax.
- c. Would tax the increment in value as goods move through the production and manufacturing stages to the marketplace.
- d. Is a tax on consumption.
- e. None of these.

ANSWER: b
RATIONALE: There is only a single rate. The tax base is simplified by taxing only limited types of income. Many deductions and credits would be eliminated.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -

Chapter 01: An Introduction To Taxation and Understanding the Federal Tax Law

KEYWORDS: AICPA: FN-Measurement
Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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102. A VAT (value added tax):
- Is regressive in its effect.
 - Has not proved popular outside of the U.S.
 - Is *not* a tax on consumption.
 - Is used exclusively by third world (less developed) countries.
 - None of these.

ANSWER: a
RATIONALE: Both the VAT and a general sales tax are taxes on consumption (choice c.) and are regressive in effect (choice a.). The VAT has been adopted by many countries (choice b.), many of which (e.g., Japan, Denmark) *are not* third world countries (choice d.).
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
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103. Characteristics of the "Fair Tax" (i.e., national sales tax) include which, if any, of the following:
- Abolition of the Federal individual (but not the corporate) income tax.
 - Abolition of all Federal income taxes but retention of payroll taxes (including the self-employment tax).
 - Abolition of all Federal income taxes and payroll taxes but retention of the Federal estate and gift taxes.
 - Abolition of all Federal income and payroll taxes as well as the Federal estate and gift taxes.
 - None of these.

ANSWER: d
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPROG: Comprehension - BUSPROG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension

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OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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104. In terms of probability, which of the following taxpayers would be *least likely* to be audited by the IRS?

- a. Taxpayer owns and operates a check-cashing service.
- b. Taxpayer is an employed electrician.
- c. Taxpayer just received a \$3 million personal injury award as a result of a lawsuit.
- d. Taxpayer just won a \$1 million slot machine jackpot at a Las Vegas casino.
- e. Taxpayer has been audited several times before.

ANSWER: b
RATIONALE: Employees are subject to income tax withholding and have little opportunity to avoid reporting income (choice b.). Casino gambling income is subject to Form 1099 reporting (choice d.).
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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105. Which of the following *is* a characteristic of the audit process?

- a. Most taxpayer audits involve “special” agents.
- b. Self-employed taxpayers are less likely to be selected for audit than employed taxpayers.
- c. Less important issues are handled by means of a correspondence audit.
- d. If a taxpayer disagrees with the IRS auditor’s finding, the only resort is to the courts.
- e. None of these.

ANSWER: c
RATIONALE: Special agents are assigned to an audit only when fraud might be involved (choice a.). Self-employed persons have more flexibility in manipulating income and deductions than do employed taxpayers (choice b.). The next step after an initial audit would be the Appeals Division within the IRS (choice d.). Settlement at this level could avoid costly litigation.
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

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KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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106. David files his tax return 45 days after the due date. Along with the return, David remits a check for \$40,000 which is the balance of the tax owed. Disregarding the interest element, David's total failure to file and to pay penalties are:

Failure to pay penalty [$0.5\% \times \$40,000 \times 2$ (two months violation)] \$ 400

Plus: Failure to file penalty [$5\% \times \$40,000 \times 2$ (two months violation)] \$4,000

Less: Failure to pay penalty (400) 3,600

Total penalties \$4,000

Failure to pay penalty [$0.5\% \times \$40,000 \times 2$ (two months violation)] \$ 400

Plus: Failure to file penalty [$5\% \times \$40,000 \times 2$ (two months violation)] \$4,000

Less: Failure to pay penalty (400) 3,600

Total penalties \$4,000

Failure to pay penalty [$0.5\% \times \$40,000 \times 2$ (two months violation)] \$ 400

Plus: Failure to file penalty [$5\% \times \$40,000 \times 2$ (two months violation)] \$4,000

Less: Failure to pay penalty (400) 3,600

Total penalties \$4,000

- a. \$400.
- b. \$3,600.
- c. \$4,000.
- d. \$4,400.
- e. None of these.

ANSWER: c

RATIONALE: Following the procedure identified in Example 20, the penalty is determined as follows:

Failure to pay penalty [$0.5\% \times \$40,000 \times 2$ (two months violation)] \$ 400

Plus: Failure to file penalty [$5\% \times \$40,000 \times 2$ (two months violation)] \$4,000

Less: Failure to pay penalty (400)

Failure to File Penalty 3,600

Total penalties \$4,000

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POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

107. A characteristic of the fraud penalties is:

- a. When negligence and civil fraud apply to a deficiency, the negligence penalty predominates.
- b. Criminal fraud can result in a fine and a prison sentence.
- c. The criminal fraud penalty is 75% of the deficiency attributable to the fraud.
- d. The IRS has the same burden of proof in the case of criminal fraud than with civil fraud.
- e. None of these.

ANSWER: b

RATIONALE: Choice b. describes criminal fraud, while choice c. describes civil fraud. When both negligence and civil fraud exists as to the same deficiency, both penalties cannot apply and the civil fraud penalty predominates (choice a.). In the case of criminal fraud, the IRS must also show willfulness on the part of the taxpayer (choice d.).

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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108. Regarding proper ethical guidelines, which (if any) of the following is correct?

- a. The use of client estimates in preparing a return may be acceptable.
- b. Under no circumstances should a question on a tax return be left unanswered.
- c. If a client has made a mistake in a prior year's return and refuses to correct it, you should withdraw from the engagement.
- d. If the exact amount of a deduction is not certain (e.g., around mid-\$600s), it *should* be recorded as an odd amount (i.e., \$649) so as to increase the appearance of greater certainty.
- e. None of these.

ANSWER: a

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RATIONALE: In some cases, the use of client estimates is acceptable (choice a.), but they should not give the appearance of certainty (choice d.). Questions can be left blank if their meaning is uncertain or the answer is not readily available or voluminous (choice b.). Withdrawal is not necessary if the error is not material or does not have a carryover effect on the current year return (choice c.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics

STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 5 min.

DATE CREATED: 11/28/2016 3:10 PM

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109. Both economic and social considerations can be used to justify:

- a. Favorable tax treatment for accident and health plans provided for employees and financed by employers.
- b. Disallowance of any deduction for expenditures deemed to be contrary to public policy (e.g., fines, penalties, illegal kickbacks, bribes to government officials).
- c. Various tax credits, deductions, and exclusions that are designed to encourage taxpayers to obtain additional education.
- d. Allowance of a deduction for state and local income taxes paid.
- e. None of these.

ANSWER: c

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

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110. Social considerations can be used to justify:

- a. Allowance of a credit for child care expenses.
- b. Allowing excess capital losses to be carried over to other years.
- c. Allowing accelerated amortization for the cost of installing pollution control facilities.
- d. Allowing a Federal income tax deduction for state and local sales taxes.
- e. None of these.

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ANSWER: a
RATIONALE: Equity considerations justify choices b. and d., and economic considerations justify choice c.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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111. Allowing a domestic production activities deduction for certain manufacturing income can be justified:
- As mitigating the effect of the annual accounting period concept.
 - As promoting administrative feasibility.
 - By economic considerations.
 - Based on the wherewithal to pay concept.
 - None of these.

ANSWER: c
RATIONALE: The deduction will encourage U.S. manufacturing. It also will lead to job growth and discourage the outsourcing of labor to overseas.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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112. Provisions in the tax law that promote energy conservation and more use of alternative (non-fossil) fuels can be justified by:
- Political considerations.
 - Economic and social considerations.
 - Promoting administrative feasibility.
 - Encouragement of small business.
 - None of these.

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ANSWER: b

RATIONALE: Although it may be “good politics” to promote measures that ease the problem of global warming (choice a.), the real justification is economic (curtail dependence on foreign oil) and social (reduce pollution)—choice b. The encouragement of small business (choice d.) is a byproduct of these conservation provisions, but is not their justification.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 5 min.

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113. Which, if any, of the following provisions *cannot* be justified as mitigating the effect of the annual accounting period concept?

- a. Nonrecognition of gain allowed for involuntary conversions.
- b. Net operating loss carryback and carryover provisions.
- c. Carry over of excess charitable contributions.
- d. Use of the installment method to recognize gain.
- e. Carry over of excess capital losses.

ANSWER: a

RATIONALE: The involuntary conversion provision is based on the wherewithal to pay concept (choice a.).

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Multiple Choice

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 5 min.

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114. Which, if any, of the following provisions of the tax law *cannot* be justified as promoting administrative feasibility (simplifying the task of the IRS)?

- a. Penalties are imposed for failure to file a return or pay a tax on time.
- b. Prepaid income is taxed in the year received and not in the year earned.
- c. Annual adjustments for indexation increases the amount of the standard deduction allowed.

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- d. Casualty losses must exceed 10% of AGI to be deductible.
- e. A deduction is allowed for charitable contributions.

ANSWER: e
RATIONALE: Choices a. through d. aid the IRS in administering the tax laws. Choice e., particularly when trying to value property contributions, will add to the audit effort required by the IRS.
POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
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115. A landlord leases property upon which the tenant makes improvements. The improvements are significant and are not made in lieu of rent. At the end of the lease, the value of the improvements are not income to the landlord. This rule is an example of:

- a. A clear reflection of income result.
- b. The tax benefit rule.
- c. The arm's length concept.
- d. The wherewithal to pay concept.
- e. None of these.

ANSWER: d
POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Multiple Choice
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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116. Taylor, a widow, makes cash gifts to her five married children (including their spouses) and to her seven grandchildren. What is the maximum amount Taylor can give for calendar year 2017 without using her unified transfer tax credit?

ANSWER: \$238,000. $\$14,000 \text{ (annual exclusion)} \times 17 \text{ donees} = \$238,000$.
POINTS: 1
DIFFICULTY: Easy

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QUESTION TYPE: Subjective Short Answer
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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117. For the tax year 2017, Noah reported gross income of \$300,000 on his timely filed Federal income tax return.

- Presuming the general rule applies, when does the statute of limitations on assessments normally expire?
- Suppose Noah inadvertently omitted gross income of \$76,000. When does the statute of limitations on assessments expire?
- Suppose the omission was deliberate and not inadvertent. When does the statute of limitations on assessments expire?

ANSWER:

- Three years from April 16, 2018.
- If more than 25% of gross income is omitted, a six-year statute applies (i.e., 6 years from April 16, 2018). Here, it does as \$76,000 is more than \$75,000 ($25\% \times \$300,000$).
- If fraud is involved, the statute never expires.

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Subjective Short Answer
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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118. Without obtaining an extension, Pam files her income tax return 55 days after the due date. With her return, she pays an additional tax of \$60,000. Disregarding any interest element, what is Pam's penalty for failure to pay and to file?

ANSWER: \$6,000. Disregarding the interest element, Pam's total penalties are as follows:

Failure to pay penalty ($0.5\% \times \$60,000 \times 2$ months)		\$ 600
Plus: Failure to file penalty ($5\% \times \$60,000 \times 2$ months)	\$6,000	
Less failure to pay penalty for same period	<u>-(600)</u>	<u>5,400</u>
Total penalties		<u>\$6,000</u>

POINTS: 1

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DIFFICULTY: Moderate
QUESTION TYPE: Subjective Short Answer
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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119. On his 2017 income tax return, Andrew omitted income and overstated deductions to the extent that his income tax was understated by \$500,000. Disregarding any interest element, what is Andrew's penalty if the understatement was due to:

- a. Negligence.
- b. Civil fraud.
- c. Criminal fraud.

ANSWER:

- a. \$100,000 ($20\% \times \$500,000$).
- b. \$375,000 ($75\% \times \$500,000$).
- c. Various fines and/or prison sentence.

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Subjective Short Answer
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
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120. Several years ago, Logan purchased extra grazing land for his ranch at a cost of \$240,000. In 2017, the land is condemned by the state for development as a highway maintenance depot. Under the condemnation award, Logan receives \$600,000 for the land. Within the same year, he replaces the property with other grazing land. What is Logan's tax situation if the replacement land cost:

- a. \$210,000?
- b. \$360,000?
- c. \$630,000?
- d. Why?

ANSWER:

- a. The full realized gain of \$360,000 [$\$600,000$ (condemnation proceeds) – $\$240,000$ (cost of land)] must be recognized, as only \$210,000 was reinvested. The

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condemnation proceeds of \$600,000 exceed the amount reinvested by more than \$360,000.

- b. As only \$360,000 was reinvested in replacement property, \$240,000 (\$600,000 – \$360,000) of the gain must be recognized.
- c. As the full \$600,000 was reinvested, no realized gain need be recognized.
- d. If some of the gain is not reinvested, consistent with the wherewithal to pay concept, there exists the ability to pay the tax. Thus, gain is recognized to the extent the proceeds are not reinvested.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Subjective Short Answer

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Application

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

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121. Paige is the sole shareholder of Citron Corporation. During the year, Paige leases a building to Citron for a monthly rental of \$80,000. If the fair rental value of the building is \$60,000, what are the income tax consequences to the parties involved?

ANSWER: The rent charged by Paige is not “arms length”; as such, Citron Corporation’s rent deduction is \$60,000 (not \$80,000). The \$20,000 difference is a nondeductible dividend distribution. For Paige, the change merely requires reclassification. Instead of \$80,000 of rent income, she has \$60,000 of rent income and \$20,000 of dividend income.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Subjective Short Answer

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Application

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

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122. In 1986, Roy leased real estate to Drab Corporation for 20 years. Drab Corporation made significant capital improvements to the property. In 2006, Drab decides not to renew the lease and vacates the property. At that time, the value of the improvements is \$800,000. Roy sells the real estate in 2017 for \$1,200,000 of which \$900,000 is attributable to the improvements. When is Roy taxed on the improvements made by Drab Corporation?

ANSWER: Roy is not subject to taxation on the improvements until he disposes of the property (i.e., 2017). After a controversial Supreme Court decision years ago, Congress clarified the tax

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law to make it more consistent with the wherewithal to pay concept.

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Subjective Short Answer
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Application
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

123. The Federal income tax is based on a pay-as-you-go system and has become a “mass tax.” Explain this statement.

ANSWER: The pay-as-you-go system is present in the wage and other withholding procedures. In the case of self-employed persons, it is manifested in the required quarterly payments for estimated taxes. The income tax became a mass tax during World War II when its coverage was extended to 74% of the population (from less than 6% in 1939).

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-02 - LO: 1-02
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Research
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

124. In terms of Adam Smith's canons of taxation, how does the Federal income tax fare as far as *economy* is concerned?

ANSWER: Economy is present only if the collection procedure of the IRS is considered. Economy is not present, however, if the focus is on taxpayer compliance effort and costs.

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-03 - LO: 1-03
NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Reporting
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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125. Due to the population change, the Goose Creek School District has decided to close one of its high schools. Since it has no further need of the property, the school is listed for sale. The two bids it receives are as follows:

United Methodist Church	\$1,700,000
Planet Motors	1,600,000

The United Methodist Church would use the property to establish a sectarian middle school. Planet, a well-known car dealership, would revamp the property and operate it as a branch location.

If you were a member of the School District board, what factors would you consider in evaluating the two bids?

ANSWER: Although the bid from the United Methodist Church is higher, several other factors need to be considered. Does, for example, Goose Creek School district exempt property owned by churches from its *ad valorem* taxes? If so, losing this property from the tax base could prove very costly over the long run. Also, it is probable that income-producing property (such as a car dealership) would be taxed at a higher rate than that owned by a nonprofit organization (a school operated by a church). This assumes, of course, that the school would be taxed at all. The auto dealership also would generate sales tax.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

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126. Morgan inherits her father's personal residence including all of the furnishings. She plans to add a swimming pool and sauna to the property and rent it as a furnished house. What are some of the *ad valorem* property tax problems Morgan can anticipate?

ANSWER: The real estate taxes probably will increase for several reasons. The capital improvements and the conversion from residential to rental will trigger the increase. Furthermore, the furnishings may generate an *ad valorem* tax on personalty. (Depending on applicable law, furniture might not be subject to tax unless used for business purposes—such as in this case.)

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

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KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
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127. In 2015, Deborah became 65 years old. In 2016 she added a swimming pool, and in 2017 she converted the residence to rental property and moved into an assisted living facility. Since 2014, Deborah's *ad valorem* property taxes have decreased once and increased twice. Explain.

ANSWER: The decrease probably came in 2015 when Deborah reached age 65. The increases probably occurred in 2016 when she added the pool and in 2017 when the residence was converted to rental property with the property reassessed due to change in use and/or removal of the homestead exemption.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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128. A lack of compliance in the payment of use taxes can be resolved by several means. In this regard, comment on the following:

- a. Registration of automobiles.
 - b. Reporting of Internet purchases on state income tax returns.
- ANSWER:**
- a. As reflected in Example 5, re-registration of a car purchased out-of-state is the occasion for the owner's home state to collect the use tax.
 - b. Completing the state income tax return reminds (or forces) the taxpayer to pay use tax on out-of-state purchases.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVE CMPV.SWFT.LO: 1-04 - LO: 1-04
S:
NATIONAL STANDARD United States - BUSPORG: Comprehension - BUSPORG:Comprehension
S: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement

United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension

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OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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129. What are the pros and cons of the following state and local tax provisions?

- a. An *ad valorem* property tax holiday made available to a manufacturing plant that is relocating.
- b. Hotel occupancy tax and a rental car surcharge.
- c. A back-to-school sales tax holiday.

ANSWER:

- a. Such a holiday is designed to attract new industry to the area. This means more jobs and growth in consumption. On the other hand, if the tax holiday is too generous, this places a strain on available public revenue. The result could be that schools and capital maintenance (roads, public services) will suffer.
- b. The hotel occupancy tax and car rental surcharges are popular because they mainly impact visitors. Also, they can generate considerable revenue to finance major capital improvements. If these taxes become excessive, however, they could discourage major events (such as conventions).
- c. Such holidays are very popular with both merchants and consumers and serve the social need of defraying some of the costs of sending children to school. Once established, however, they are difficult to get rid of. Thus, they become an annual drain on sales tax revenue.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Analysis
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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130. What is a severance tax? How productive can it be in terms of generating revenue?

ANSWER: A severance tax is one imposed when natural resources (e.g., oil, gas, iron ore, coal) are extracted. It is based on the notion that the state has an interest in such resources. For some states, the revenue from severance taxes can be significant. Alaska, for example, relies heavily on its severance taxes and has been able to avoid both a state income tax and a general sales tax.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

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NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Evaluation

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

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131. What is the difference between an inheritance tax and an estate tax? Who imposes these taxes?

ANSWER: An inheritance tax is a tax on the right to receive property from a decedent. An estate tax is imposed on the right to pass property at death. The Federal government imposes estate taxes, while states impose inheritance taxes. Some states impose both, while others impose neither.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Evaluation

OTHER: Time: 5 min.

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132. Logan dies with an estate worth \$20 million. Under his will, \$10 million passes to his wife while \$10 million goes to his church. What is Logan's Federal estate tax result?

ANSWER: None. After a marital deduction of \$10 million and a charitable deduction of \$10 million, Logan's taxable estate is \$0.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Application

OTHER: Time: 5 min.

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133. With regard to state income taxes, explain what is meant by the "jock tax"?

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ANSWER: Although states have a right to levy an income tax on all nonresidents who earn income within the state, they usually do so only on highly paid visitors. Such persons are often athletes, hence the designation of “jock tax.”

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

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134. Virtually all state income tax returns contain checkoff boxes for donations to various causes. On what grounds has this procedure been criticized?

ANSWER: In many cases the procedure is overused (i.e., a multiplicity of boxes). This overuse adds complexity to the return. Also, in most cases the donation is being drawn from any income tax refund that might be due. Thus, taxpayers may not fully appreciate that they are paying for such checkoffs.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

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135. State and local governments are sometimes forced to find ways to generate additional revenue. Comment on the pros and cons of the following procedures:

- Decouple what would be part of the piggyback format of the state income tax.
- Tax amnesty provisions.
- Internet shaming.

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ANSWER:

- a. The decoupling process is easily accomplished as to new Federal tax changes that have never taken effect at the state level. Taxpayers are not apt to miss what they never have enjoyed.
- b. Tax amnesty provisions generate considerable revenue. It also unmasks many taxpayers who have not previously paid taxes. Now that the taxing jurisdiction is aware of their existence, they will tend to pay taxes in the future.
- c. By use of a public Web site, the taxing authority posts the names of those taxpayers that are delinquent as to various taxes (e.g., sales, income). This public humiliation (or threat of) very often results in compliance.

POINTS:

1

DIFFICULTY:

Moderate

QUESTION TYPE:

Essay

HAS VARIABLES:

False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS:

Bloom's: Evaluation

OTHER:

Time: 10 min.

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136. Briana lives in one state and works in the adjoining state. Both states tax the income she earns from her job. Does Briana have any relief from this apparent double taxation of the same income?

ANSWER:

Most states allow their residents some form of tax credit for the income taxes paid to other states. In Briana's case, the credit would be allowed by the state where she lives for the taxes paid to the state where she works.

POINTS:

1

DIFFICULTY:

Easy

QUESTION TYPE:

Essay

HAS VARIABLES:

False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS:

Bloom's: Comprehension

OTHER:

Time: 10 min.

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137. In late June 2017, Art is audited by the state and a large deficiency is assessed. In November of the same year, his Federal income tax return is audited by the IRS. What has probably happened?

ANSWER: The IRS has been notified by the state concerning the results of the June audit.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

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138. Two months after the burglary of his personal residence, Eric is audited by the IRS. Among the items taken in the burglary was a shoe box containing approximately \$50,000 in cash. Eric is the owner and operator of a cash-and-carry liquor store. Eric wonders why he was audited. Can you help explain?

ANSWER: Although Eric's audit by the IRS could be the result of sheer chance, this appears unlikely. Press coverage of the burglary, particularly if the items stolen were enumerated, could have put the IRS on notice. Why would anyone keep such a large amount of cash at his personal residence? Also, Eric is in a business where tax evasion is easily accomplished.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

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139. Rick, the sole proprietor of an adult entertainment club, is audited by the IRS. On the third day of the field audit, the regular IRS agent is accompanied by a special agent. Should Rick be concerned by this new development? Explain.

ANSWER: Yes, he should. Special agents rarely appear during an audit unless the regular agent suspects that fraud may be involved. Considering the type of business Rick conducts, the heavy use of cash probably exists. With cash involved, tax evasion is easier to carry out.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

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HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
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140. Tracy has just been audited and the IRS agent has issued an RAR that assesses a large deficiency. Since Tracy disagrees with the result, her next step is to go to court. Do you agree?

ANSWER: Tracy might save herself time and expense by going to the Appeals Division of the IRS. Here, the IRS has the authority to negotiate a settlement based on the “hazards of litigation” (i.e., the probabilities of winning or losing). If a settlement is reached, resort to the courts is avoided.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
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141. Brayden files his Federal income tax return by April 15, but does not pay the tax. Although he expects to pay interest on the large amount of tax he still owes, he feels that the timely filing has avoided any penalties. Is Brayden’s assumption correct?

ANSWER: Although Brayden has avoided the failure to file penalty, the failure to pay penalty will apply. It is 0.5% per month up to a maximum of 25% of the tax due as shown on the return.

POINTS: 1
DIFFICULTY: Moderate
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension

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142. Melinda has been referred to you by one of your clients. In the past, she has prepared her own income tax returns, but she has become overwhelmed by the increased complexity of the tax law. Consequently, Melinda wants you to prepare her return for calendar year 2017. In reviewing her 2016 return, you note that she has claimed as a deduction the entire cost of a business building that should have been capitalized and depreciated. What course of action should you follow?

ANSWER: You should recommend to Melinda that an amended return be filed for 2016 correcting the error. If she refuses, you should assess the gravity of the error and how it impacts on your ability to file an accurate return for 2017. If you cannot do so, then you must decline the engagement.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06
NATIONAL STANDARDS: United States - BUSPROG: Ethics
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Reporting
United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
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143. Your client, Connie, won \$12,000 in a football office pool. She sees no reason to include it in her income for several reasons. First, the amount won will not be reported to the IRS. Second, as an average income employee, she is unlikely to be audited by the IRS. Third, she feels that she has probably lost this much in other past office pools. How do you respond?

ANSWER: As a practitioner, you cannot play the audit lottery. You must presume she will be audited irrespective of the probabilities. Although the use of estimates is allowed, Connie's assumptions as to her losses are not realistic. Even if they were reliable, gambling losses cannot be offset against gambling winnings but must be separately deducted. Thus, the \$12,000 must be reported as income or you cannot prepare Connie's return.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06
NATIONAL STANDARDS: United States - BUSPROG: Ethics
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Reporting
United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
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144. Under what conditions is it permissible, from an ethical standpoint, for a CPA firm to outsource tax return preparation to a third party?

ANSWER: First, the clients' confidentiality must be preserved. Second, the CPA firm must verify the accuracy of the work. Third, the clients must be advised as to the practice.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-06 - LO: 1-06

NATIONAL STANDARDS: United States - BUSPROG: Ethics
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Reporting
United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Knowledge

OTHER: Time: 10 min.

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145. In terms of revenue neutrality, comment on a tax cut enacted by Congress that:

- a. contains revenue offsets.
- b. includes a sunset provision.

ANSWER:

- a. Ideally, to achieve revenue neutrality all tax cuts should be accompanied by revenue offsets.
- b. A sunset provision does not account for the immediate revenue losses generated by a tax cut. It merely provides that such losses will not continue beyond a specified date when the tax cut expires and the former tax law is reinstated.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Comprehension - BUSPROG:Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

DATE MODIFIED: 5/11/2017 12:50 PM

146. The tax law contains various tax credits, deductions, and exclusions that are designed to encourage taxpayers to obtain additional education. On what grounds can these provisions be justified?

ANSWER: Social and economic considerations. As to the latter, a better educated workforce carries a

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positive economic impact.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

147. The tax law contains various provisions that encourage home ownership.

- a. On what basis can this objective be justified?
- b. Are there any negative considerations? Explain.

ANSWER:
a. Home ownership can be justified on economic and social grounds.
b. Granting tax advantages to persons who are purchasing their homes places the taxpayers who rent at a disadvantage. The result is inequality in treatment.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

148. The tax law allows an income tax deduction (or a credit) for foreign income taxes. Explain why.

ANSWER: The deduction (or a credit) for foreign income taxes can be justified on the grounds that it mitigates the double tax imposed on the same income.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

Chapter 01: An Introduction To Taxation and Understanding the Federal Tax Law

STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 5 min.
DATE CREATED: 11/28/2016 3:10 PM
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149. The tax law allows, under certain conditions, deferral of gain recognition for involuntary conversions.

- a. What is the justification for this relief measure?
- b. What happens if the proceeds are not entirely reinvested?

ANSWER:

- a. By recognizing that the taxpayer's relative economic situation has not changed and that he or she lacks the wherewithal to pay a tax, any recognition of realized gain is deferred.
- b. If the proceeds from an involuntary conversion are not fully reinvested in property that is similar or related in service or use, recognized gain results. Such recognized gain cannot exceed realized gain and will be limited to the amount of the proceeds not reinvested. Recognition is based on the notion that the taxpayer now has the wherewithal to pay the tax that results.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement - AICPA: FN-Measurement
United States - AK - AICPA: FN-Reporting
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
DATE MODIFIED: 5/11/2017 12:50 PM

150. How do the net operating loss provisions in the tax law mitigate the effect of the annual accounting concept?

ANSWER: Without the allowance of carryback and/or carryover provisions that apply the excess losses to profitable years, the losses would disappear. As shown by Example 24, this result places a business with profit and loss fluctuations on a more level playing field with one that maintains a stable income pattern.

POINTS: 1
DIFFICULTY: Easy
QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

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STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Reporting

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 10 min.

DATE CREATED: 11/28/2016 3:10 PM

DATE MODIFIED: 5/11/2017 12:50 PM

151. In connection with facilitating the function of the IRS in the administration of the tax laws, comment on the utility of the following:

- a. An increase in the amount of the standard deduction.
- b. Dollar and percentage limitations on the deduction of personal casualty losses.
- c. Availability of interest and penalties for taxpayer noncompliance.

ANSWER:

- a. An increase in the amount of the standard deduction reduces the number of taxpayers who choose to itemize their personal deductions. This, in turn, cuts down on the deductions the IRS has to check.
- b. Limitations placed on casualty and theft losses curtail the number of taxpayers who can claim the deduction.
- c. The imposition of extra penalties, in addition to the tax owed, definitely deters taxpayer noncompliance.

POINTS: 1

DIFFICULTY: Moderate

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 20 min.

DATE CREATED: 11/28/2016 3:10 PM

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152. Congress reacts to judicial decisions that interpret the tax law in different ways. When it approves of a decision, Congress may act to amend the Code to incorporate the holding. When it disapproves, Congress may amend the Code to nullify its effect. Give an example of each one of these congressional reactions.

ANSWER: Congress approved of the judicial conclusion that most stock dividends should be nontaxable and amended the Code to this effect. However, it disagreed as to when leasehold improvements should be taxed to a lessor. Consistent with the wherewithal to pay concept, the improvements are to be taxed on the termination of the lease. Thus, Congress overturned a judicial holding that would have taxed such improvements in the year they are made by the lessee.

POINTS: 1

DIFFICULTY: Moderate

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QUESTION TYPE: Essay
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-08 - LO: 1-08
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
United States - AK - AICPA: FN-Reporting
KEYWORDS: Bloom's: Comprehension
OTHER: Time: 10 min.
DATE CREATED: 11/28/2016 3:10 PM
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Match the statements that relate to each other. Note: Some choices may be used more than once or not at all.

- a. Deferral of gains from involuntary conversions
- b. Carryback and carryforward of net operating losses
- c. "No change" is one possible result
- d. State income tax applied to visiting nonresident
- e. IRS special agent
- f. Undoing the "piggyback" result
- g. Ideal budget goal as to new tax legislation
- h. Every state that has a general sales tax has one
- i. Imposed by all states and the Federal government
- j. Imposed by some states but not the Federal government
- k. Imposed only by the Federal government
- l. No correct match provided

DIFFICULTY: Easy
QUESTION TYPE: Matching
HAS VARIABLES: False
LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-04 - LO: 1-04
NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG: Comprehension
United States - BUSPROG: Technology: Technology: - BUSPROG: Technology
STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement
United States - AK - AICPA: FN-Reporting
United States - AK - AICPA: FN-Risk Analysis
KEYWORDS: Bloom's: Knowledge
OTHER: Time: 2 min.
DATE CREATED: 11/28/2016 3:10 PM
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153. Jock tax

ANSWER: d

POINTS: 1

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154. Decoupling

ANSWER: f

POINTS: 1

155. Discriminant Index Function (DIF)

ANSWER: l

POINTS: 1

156. Tax fraud suspected

ANSWER: e

POINTS: 1

157. Revenue neutrality

ANSWER: g

POINTS: 1

158. Revenue Agent's Report (RAR)

ANSWER: c

POINTS: 1

159. Wherewithal to pay concept

ANSWER: a

POINTS: 1

160. Mitigation of the annual accounting period concept

ANSWER: b

POINTS: 1

161. Tax on transfers at death (inheritance type)

ANSWER: j

POINTS: 1

162. Excise tax on tobacco

ANSWER: i

POINTS: 1

163. Use tax

ANSWER: h

POINTS: 1

164. Income tax amnesty

ANSWER: j

POINTS: 1

165. Import taxes (customs duties)

ANSWER: k

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POINTS: 1

166. "Pay-as-you-go" (paygo)

ANSWER: g

POINTS: 1

167. Export taxes

ANSWER: l

POINTS: 1

Using the choices provided below, show the justification for each provision of the tax law listed.

a. Economic considerations

b. Social considerations

c. Equity considerations

d. Both a. and b.

DIFFICULTY: Easy

QUESTION TYPE: Matching

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-07 - LO: 1-07

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - TX - AICPA: FN Measurment
United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 2 min.

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168. A tax credit for amounts spent to furnish care for children while the parent is at work.

ANSWER: b

POINTS: 1

169. Additional depreciation deduction allowed for the year the asset is acquired.

ANSWER: a

POINTS: 1

170. Tax brackets are increased for inflation.

ANSWER: c

POINTS: 1

171. A small business corporation can elect to avoid the corporate income tax.

ANSWER: a

POINTS: 1

172. A deduction for contributions by an employee to certain retirement plans.

ANSWER: d

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POINTS: 1

173. A deduction for qualified tuition paid to obtain higher education.

ANSWER: d

POINTS: 1

174. A deduction for certain expenses (interest and taxes) incident to home ownership.

ANSWER: d

POINTS: 1

175. A Federal deduction for state and local income taxes paid.

ANSWER: c

POINTS: 1

176. A deduction for certain income from manufacturing activities.

ANSWER: a

POINTS: 1

177. A bribe to the local sheriff, although business related, is not deductible.

ANSWER: b

POINTS: 1

178. Contributions to charitable organizations are deductible.

ANSWER: b

POINTS: 1

179. A Federal deduction for state and local sales taxes paid.

ANSWER: c

POINTS: 1

180. Tax credits available for the purchase of a vehicle that uses alternative (non-fossil) fuels.

ANSWER: a

POINTS: 1

181. Tax credits for home improvements that conserve energy.

ANSWER: a

POINTS: 1

182. More rapid expensing for tax purposes of the costs of installing pollution control devices.

ANSWER: a

POINTS: 1

Match the statements that relate to each other. Note: Some choices may be used more than once.

- a. 3 years from date return is filed
- b. 3 years from due date of return
- c. 20% of underpayment
- d. 5% per month (25% limit)

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- e. 0.5% per month (25% limit)
- f. Conducted at IRS office
- g. Conducted at taxpayer's office
- h. 6 years
- i. 45-day grace period allowed to IRS
- j. No statute of limitations (period remains open)
- k. 75% of underpayment
- l. No correct match provided

DIFFICULTY: Easy

QUESTION TYPE: Matching

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

NATIONAL STANDARDS: United States - BUSPORG: Comprehension - BUSPORG:Comprehension

STATE STANDARDS: United States - AK - AICPA: FN-Measurement -
AICPA: FN-Measurement

United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Knowledge

OTHER: Time: 2 min.

DATE CREATED: 11/28/2016 3:10 PM

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183. Office audit

ANSWER: f

POINTS: 1

184. Field audit

ANSWER: g

POINTS: 1

185. Failure to file penalty

ANSWER: d

POINTS: 1

186. Failure to pay penalty

ANSWER: e

POINTS: 1

187. Negligence penalty

ANSWER: c

POINTS: 1

188. Criminal fraud penalty

ANSWER: l

POINTS: 1

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189. Fraud and statute of limitations

ANSWER: j

POINTS: 1

190. Early filing and statute of limitations (deficiency situations)

ANSWER: b

POINTS: 1

191. Late filing and statute limitations (deficiency situations)

ANSWER: a

POINTS: 1

192. No return and statute limitations

ANSWER: j

POINTS: 1

193. More than 25% gross income omission and statute of limitations

ANSWER: h

POINTS: 1

194. Interest due on refund

ANSWER: i

POINTS: 1

195. Can a taxpayer start the 3-year statute of limitations on additional assessments by the IRS by filing his income tax return early (i.e., before the due date)? Can the period be shortened by filing late (i.e., after the due date)?

ANSWER: The answer is *no* in both cases. When filing early, the statute starts to run on the due date of the return. When filing late however, the filing date controls.

POINTS: 1

DIFFICULTY: Easy

QUESTION TYPE: Essay

HAS VARIABLES: False

LEARNING OBJECTIVES: CMPV.SWFT.LO: 1-05 - LO: 1-05

NATIONAL STANDARDS: United States - BUSPROG: Technology: Technology: - BUSPROG: Technology

STATE STANDARDS: United States - AK - AICPA: FN-Risk Analysis

KEYWORDS: Bloom's: Comprehension

OTHER: Time: 5 min.

DATE CREATED: 11/28/2016 3:10 PM

DATE MODIFIED: 5/11/2017 12:50 PM