100%

Name: KB 7 ~~multiple choice~~

Accounting 385/685
Introduction to Taxation, Fall 2009
Final Exam
Ver B

Instructions: There are three longer problems at the end of the test worth a substantial number of points. Multiple choice questions are worth 6 points each, alt. answers are worth 2 points. 13 Problems, 6 pages. Please check.

1. Leonard Lambert's commercial building, which had an adjusted basis of $500,000, was partially destroyed by fire. The fair market value was $800,000 just before the fire and $600,000 immediately after. Leonard received $150,000 insurance proceeds and deducted a $50,000 casualty loss. What is Leonard's basis in the building after $150,000 of repairs are made?

a. $300,000
b. $350,000
c. $600,000
d. $500,000
e. $450,000
f. None of the above
Alt.______

ΔFMV = 800,000 − 600,000 = 200,000
Ins = 150,000 = repairs
Loss = <50,000>
BASIS = 500,000 − 50000 = 450,000
b/f

2. Tom Thompson traded in a station wagon (used in his business) which had an adjusted basis of $7,700 for a new one costing $26,900. The auto dealer allowed a trade-in allowance of $8,000 on the old station wagon and Tom paid $18,900 in cash. What is Tom's basis in the new station wagon?

a. $26,600
b. $15,700
c. $18,900
d. $26,900
e. None of the above
Alt.______

BASIS = 7700 + 18900 = 26,600
<10 $pd

3. Mickey buys a used truck (MACRS 5 year property) to use in his business on May 13, 2009 at a cost of $18,000. In November 2009, Mickey purchases additional used equipment, 7-year property, for $34,000. Assuming that none of this property is expensed under section 179, what is his 2009 maximum allowable cost recovery deduction?

a. $2,114
b. $15,500
c. $8,459
d. $12,086
e. $5,714
f. None of the above
Alt.______

34,000 / (34,000+18000) > 40% → mid qtr convention

Truck (May = 2nd Qtr)
18,000 × 1/5 × 2 × 5/8 = 4500

Equip (Nov = 4th Qtr)
34,000 × 1/7 × 2 × 1/8 = 1214

5714

Name:____

4. Margret Mildred, who has a salary of $50,000 during 2009, has a net long-term capital loss of $2,000 and a net short-term capital loss of $5,000 in 2009. What are her 2009 capital loss deduction and carryover?

a. $3,000 deduction; $4,000 STCL carryover,
b. $5,500 deduction; $2,000 LTCL carryover,
c. $3,000 deduction; no carryover
d. $3,000 deduction; $2,000 LTCL carryover, $2,000 STCL carryover
e. None of the above
Alt.______

LT <2000> → LTCL C/O = <2000>
ord ded
ST <5000> → <3,000> & <2000> STCL C/O

5. Tom Truman sells a business machine which he has owned for four years for $27,000. Tom purchased the machine for $42,000 and has taken $18,000 in depreciation. How much and what type of gain will result from this sale?

a. $3,000 long-term capital gain
b. $3,000 Section 1231 gain
c. $18,000 ordinary income; $3,000 long-term capital gain
d. $3,000 ordinary income
e. None of the above
Alt.______

S.P. 27,000
Cost 42,000
dep <18,000>
adj. Basis 24000 <24,000>
gn 3,000

dep > 3,000 → All ord.

6. During 2009, Norman Newhouse sold equipment used in his business for $11,000. The equipment cost $10,000 and Norman had properly claimed MACRS deductions totaling $4,000. Straight-line depreciation, if it had been used, would have been $2,500. What is the amount of gain that should be reported under Sections 1231 and 1245?

a. Section 1231: $1,000; Section 1245: $4,000
b. Section 1231: $3,500; Section 1245: $1,500
c. Section 1231: $5,000; Section 1245: $0
d. Section 1231: $0; Section 1245: $5,000
e. None of the above
Alt.______

SL - 2500
irrelevant to §1245

S.P. 11,000
cost 10,000
dep <4,000>
Basis 6,000 <6000>
gn 5,000

ord, §1245 4,000
§1231 1,000

Name:____

7. Johnny, a cash basis taxpayer, owns two rental properties. Based on the following information, compute the amount that he must include in his 2009 gross rental income.

		taxable
Property #1, security deposit received 2/1/09.	$ 500	0
Property #1, payment received 2/1/09 for last month of lease (2/15)	700	700
Property #1, rental income received in 2009 2/09-12/09	7,700	7,700
Property #2, rental income received in 2009 1/09-12/09	9,000	9,000
Property #2, security deposit received 1/1/09	750	0
Property #2, rent 1/09 received 12/28/08	800	0
		17,400

taxed in 08

a. $19,450
b. $18,650
c. $18,200
d. $17,400
e. None of the above
Alt.______

8. Alex Burg, a cash basis taxpayer, earned an annual salary of $80,000 at Ace Corp. in 2009, but elected to take only $50,000. Ace, which was financially able to pay Burg's full salary, credited the unpaid balance of $30,000 to Burg's account on the corporate books in 2009, and actually paid this $30,000 to Burg on April 25, 2010. How much of the salary is taxable to Burg in 2009?

a. $50,000
b. $80,000
c. $65,000
d. $60,000
e. None of the above
Alt.______

Sal 80,000 → all constructively received
All Earned in 2009
Would have to have changed
Contract in 2008, 2009 is too late

9. In September 2009, Bill and Linda, a married couple with $50,000 gross income, cashed qualified Series EE U.S. Savings Bonds which they had purchased in 2003. The proceeds were used to help pay for their son's 2009 college tuition. They received gross proceeds of $3,500, representing principal of $3,000 and interest of $500. The qualified higher education expenses they paid in 2009 totaled $4,000. Their modified adjusted gross income for the year was $20,000. How much of the $500 interest can Bill and Linda exclude from gross income in 2009?

a. $500
b. $200
c. $300
d. $0
e. None of the above
Alt.______

Not going to be asked

Name:____

10. Randi, a flight attendant, received wages of $30,000 in 2009. The airline provided transportation on a stand-by basis, at no charge, from her home in Detroit to the airline's hub in Chicago. The fair market value of the commuting flights was $5,000. Randi became disabled in November 2009 and received worker's compensation of $4,000. What amount must Randi include in gross income on her 2009 tax return?

a. $35,000

b. $34,000

c. $30,000 - salary only

d. $37,000

e. None of the above

Alt.______

flights, tax-free, no-additional.cost Services

work.comp. - tax-free, compensatory health Insurance

Name: ______________________________

Actual Dep
Basis = 2,000,000 − 1,000,000 = 1,000,000
SL = 800,000

This problem is worth 20 points.

11. John and Margaret are exchanging properties. John paid ~~$2,000,000~~ for an apartment building in 1985 and it is currently worth ~~$3,500,000~~. Under ACRS he has properly claimed ~~$1,000,000~~ of depreciation since 1985. Straight-line depreciation would have been $800,000. His property is subject to a mortgage of ~~$500,000~~. Margaret has an office building which she bought 2 years ago for ~~$2,750,000~~ on which she has properly claimed ~~$200,000~~ of depreciation. Her property is currently worth ~~$3,200,000~~. They are considering the following arrangement: They are to exchange properties and Margaret is to assume the mortgage on John's property. In addition John is to pay Margaret ~~$200,000~~.

2,550,000
2750,000 − 200,000

Actual dep → "SL" = Ex dep
1,000,000 → 800,000 = 200,000

Required: 1) Determine, under the proposed transaction, both parties' realized and recognized gains and/or losses and how they are taxed (1231, 25%, ordinary income) and their bases in properties received.

2) Suggest improvements to this plan. Be specific, and show all work as well as exactly what will result from your suggestions in terms of both parties' realized and recognized gains and/or losses and how they are taxed (1231, 25%, ordinary income) and their bases in properties received.

FMV = 3,500,000 Basis = 1,000,000
MORT = 500,000
$200,000

J → M

FMV = 3,200,000
Basis = 2,550,000

(2)
(1) Eq. FMV: 3,500,000 − 500,000 + 200,000 = 3,200,000 yes

(A) Real'd Gain

	J	M
FMV LK rec'd	3,200,000	3,500,000
Mort Rel	500,000	
" assumed	—	<500,000>
$ rec'd	—	200,000
$ given	<200,000>	
Basis given	<1,000,000>	<2,550,000>
Real'd gN	2,500,000	650,000

(8)

(B) Recog'd gN.

	J	M
debt rel.	300,000	
(none assumed) $ pd	<200,000>	
Excess debt rel.	300,000	
$ rec'd		200,000

(4)

(C) tax rates on gN.

(1) Excess dep.
Actual dep 1,000,000
"SL" <800,000>
→ 200,000

-0- (all SL) No ordinc, No Excess dep.

(3)

	J	M
Ord. inc	200,000	
SL dep − up to real'd gN − 25%	100,000	200,000
total recog'd gN	300,000	200,000

(2)

20 MAX

(D) Bases

	J	M
LK Basis given	1,000,000	2,550,000
gn recog'd	300,000	200,000
debt rel	<500,000>	500,000
" assumed	—	—
$ given	200,000	<200,000>
$ rec'd	—	
	1,000,000	3,050,000

(6)

	J	M
FMV LK rec'd	3,200,000	3,500,000
real'd gn 2,500,000		650,000
recog'd gn <300,000>		<200,000>
def'd gN 2,200,000	<2,200,000>	<450,000> 450,000
Basis	1,000,000	3,050,000

(E) Planning

(1) use 200,000 $, for John to pay down his mort

(2) (4) Mary can invest 300,000 in her prop so FMV → 3,500,000. & J pays down mort → 0 w/ $300,000 left.
If Both parties agree.

1

Name: ________________________________

This problem is worth 10 points.

12. Larry, who is in the 40% tax bracket, is considering participating in his company's cafeteria plan. Under the plan, which his union negotiated, he can get either $2000 in cash or $2000 in tax-free benefits, but if he takes benefits, then he can take no cash, and if he takes cash he must take it all and receive no tax-free benefits - it is an "all or nothing" proposition.

He can select among the following (but, can only get $2,000 worth in total): Life insurance ($500), Long-term Disability insurance ($500), Dental ($500), Eye-care ($500), Child-care ($1000), Education benefits ($500). First, assuming that all of these benefits are equally desirable to Larry and that he can buy them himself for the same cost on his own, advise him on which to buy with his company money and which to buy on his own. Be certain to precisely state on what you base your suggestion. Second, determine for him how much he saves by using the employer's plan versus taking the money and purchasing the same benefits on his own. Third, and finally, if Larry were only interested in the Education, Dental and Life insurance (that is, he has no use for and does not want any of the other benefits) what would you recommend he do, and why (show all work).

Choice \$2,000 (taxable) CASh, or 2,000 in benefits (tax free)

① what to buy. - KEy - Long term disability payments < taxable - Buy inside plan / tax free - Buy outside plan

total Benefit he can buy 2,000 → (can't Buy it All) total Benefits possible in plan 3,500 = 500 + 500 + 500 + 500 + 1000 + 500

(1)

→ What to leave out, what to get.

→ don't buy Long term disability w/ plan \$ → taxable

(3) Buy w/ outside money

② ~~TAX~~ \# SAVED. CAn do either of 2 ways.

ⓐ Pre tax dollars

NO ~~either~~ (4) Plan: 2000 tax free = \# (1-.4) taxable → \# = 3,333 (\# needed, after tax, to buy 2,000 of benefits) = 2000/(1-.4) → he saves (3,333-2000) = 1,333 Pre tax salary

ⓑ ~~after tax~~

~~2000 \# (1-.4) = 1,200 after tax value~~ ~~(could only buy this Amount w/ 2000 of pre-tax salary) - 2,000 actual tax-free benefit = 800 after tax savings.~~

③ If Larry only wants Education (500), Dental (500) & Life INS (500) = 1,500 should he take Benefits or \# and buy them himself?

(3) ~~PRETAX~~ \# if he takes 2,000 = 2,000 × (1-.4) = 1,200

→ 1200 is < 1,500 ∴ he cannot buy benefits

→ take benefits

NO ~~either~~

~~after tax~~

\# value

\#, taxable - chang outside plan

$\frac{1500}{(1-.4)}$ = 2500 → \$500 benefit = 2500 - 2000

Name: ______________________________

This problem is worth 10 points.

13. Bud's business is very profitable and has been growing steadily and he put several new assets to use in his business this year. The first is a machine with a three-year life and a cost of ~~$125,000~~, which was put into service on ~~January 10~~. The second is a warehouse, which cost ~~$1,250,000~~ and went into service on ~~February 11~~. The third is new office furniture, seven year life, which went into service on ~~August 12~~, and cost ~~$130,000~~. The final asset is another machine with a three-year life, costing ~~$200,000,~~ which went into service on ~~December~~ 12. What is the maximum amount of cost recovery that Bud can get this year? Ignore bonus depreciation. Be certain to show all of your work clearly.

7/8 5/8 3/8 1/8

QTR			In service
1st	3-yr machine	125,000	1/10/09
10½ mo.	39-yr warehouse	1,250,000	2/11/09
3rd	7-yr furniture	130,000	8/12/09
4th	3-yr machine	200,000	12/12/09

(1) mid-yr or mid Qtr

$\frac{200{,}000}{125{,}000 + 130{,}000 + 200{,}000} = 43.96\% > 40\%$

→ mid Qtr.

= 455,000 < 800,000 → NO §179 ded reduction. gets all 250,000

Effective depr. rates

(2)

3-yr machine: $\frac{1}{3} \times 2 \times \frac{7}{8} = 0.5833$

7-yr furniture $\frac{1}{7} \times 2 \times \frac{3}{8} = 0.1071$ ← Allocate 179 here — last / 2nd

3-yr machine $\frac{1}{3} \times 2 \times \frac{1}{8} = 0.0833$ ← " " " — 1st

depreciation = cost recovery

	D-ex-MACRS	§179 applied
Dec. machine 200,000 − 200,000 = 0	0	200,000
Aug. furniture (130,000 − 50,000) × 1/7 × 2 × 3/8 =	8571	50,000
Building: 1,250,000 × 1/(39×12) × 10.5 =	28,045	
JAN. machine (125,000 − 0) × 1/3 × 2 × 7/8 =	72,917	0
359,533 =	109,533 +	250,000

Allocate 179 (5)

250,000 total AVAIL.

Correct for 2009, Now only ....

depr. calculations (3)