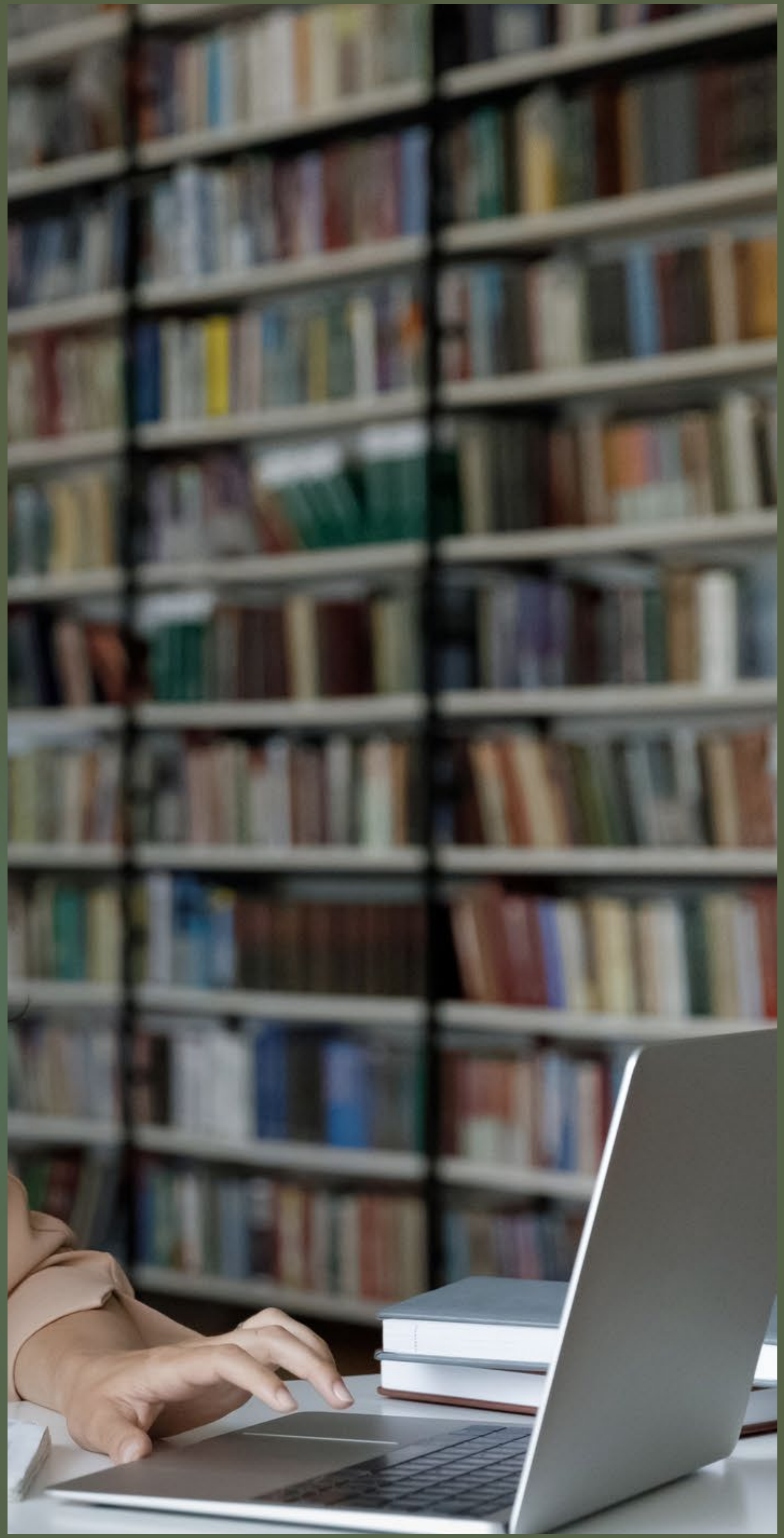
2024

NICOLE RAMOS, EA



LIVE EA
STUDY SESSION
Part 1: First Hour
Part 2: Second Hour

Hock international

PassKey Learning Systems

Forum Question

Claude owns Computer Relief, LLC, an accrual-based, calendar-year business that offers repairs and maintenance for high-end computer systems for various corporate customers. Claude reports his business on Schedule C. He receives several $5,000 payments in 2023 for one-year repair and warranty contracts, under which he agrees to repair or replace broken computer parts that have been manufactured and sold by unrelated parties. The warranty period will span into the following year (2024). When would Claude include the payments in gross income?

A. 2023
B. 2024
C. As he earns the income
D. He must report the income when he receives the customer's checks

Forum Question

Claude owns Computer Relief, LLC, an accrual-based, calendar-year business that offers repairs and maintenance for high-end computer systems for various corporate customers. Claude reports his business on Schedule C. He receives several $5,000 payments in 2023 for one-year repair and warranty contracts, under which he agrees to repair or replace broken computer parts that have been manufactured and sold by unrelated parties. The warranty period will span into the following year (2024). When would Claude include the payments in gross income?

A. 2023
B. 2024
C. As he earns the income
D. He must report the income when he receives the customer's checks

Forum Question

Question: In the aforesaid question, as the warranty period is extending into 2024, couldn't the taxpayer defer the income onto next year, at least partially if not fully? (as the warranty is still valid until next year and the probability that replacement of the material could be charged to the expense side of Income statement and related warranty revenue appears on the revenue side to appropriately match the income vs expenses)

ANSWER: This is an accrual-based taxpayer, so he is going to report the income <u>as he earns it,</u> which could potentially take him into the following year. But he can't choose to recognize all of it in 2024, because part of the income has already been earned in 2023.

PassKey Exam Question

Albatross Copiers, Inc. is an accrual-based, calendar-year corporation that sells commercial copiers to large businesses. Albatross Copiers offers copier service agreements to customers that purchase a commercial copier, but the service agreements are optional. On July 1, 2023, Albatross Copiers receives a $12,000 payment for a one-year service contract ($1,000 per month) that specifies the company will service and repair any copier components that break. How much would Albatross Copiers include in gross income for 2023 for the service agreements?

A. $6,000
B. $12,000
C. $0.00 if was included in the cost of the copier
D. Not enough information to answer

PassKey Answer

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B. $12,000
C. $0.00 if was included in the cost of the copier
D. Not enough information to answer

Forum Question

Sophia and Logan formed the Econix Corporation in 2023. As part of the capitalization of the newly-formed corporation, Sophia contributed $500,000 of cash, and Logan contributed land and a building with a fair market value of $700,000 and an adjusted basis of $450,000. Logan received $200,000 of cash from the corporation when the land and building were contributed. Sophia and Logan each receive 50% of the corporate stock after these contributions. What is the tax basis of the land and building to Econix Corporation?

A. $250,000
B. $500,000
C. $650,000
D. $700,000

Forum Answer

Sophia and Logan formed the Econix Corporation in 2023. As part of the capitalization of the newly-formed corporation, Sophia contributed $500,000 of cash, and Logan contributed land and a building with a fair market value of $700,000 and an adjusted basis of $450,000. Logan received $200,000 of cash from the corporation when the land and building were contributed. Sophia and Logan each receive 50% of the corporate stock after these contributions. What is the tax basis of the land and building to Econix Corporation?

A. $250,000
B. $500,000
C. $650,000
D. $700,000

Forum Question

Question: I don't understand why $650 000 is the correct answer. By starting with the contributing shareholders basis ($ 450 000) the inference is that this qualifies as a S 351 exchange ? Logan is the only one who contributes property in exchange for 50 % of the stock ….. Sophia contributes cash for her 50 % …… so I would not have thought S 351 would apply ?

Answer Because Sophia and Logan formed Econix corporation together as part of an integrated plan, the ownership percentages of the two founding shareholders can be added together to determine (as a group) whether or not the control test has been met under IRC Section 351.

Since they both contributed property (cash is also considered property under IRC Section 351), and collectively they own 100% of the shares of the newly formed Econix corporation, the control test has been met and IRC Sect. 351 applies to the transaction. However, as Logan received cash (boot) in addition to stock, some of Logan's realized gain will have to be recognized by Logan (see below).

Econix Corporation's basis in the land and building is $650,000. The contributing shareholder's basis in the property was $450,000, and any gain that is recognized by Logan must be added to the corporation's basis. Since Logan received cash in this transaction, he has to calculate gain. Logan's recognized gain is the lesser of: (1) his realized gain or (2) the boot received in the transaction. Logan's realized gain is $250,000 ($700,000 FMV – $450,000 basis). The boot he received was $200,000 in cash. Therefore, the gain recognized by Logan is $200,000, and the corporation's basis in the property is $650,000 ($450,000 carryover basis + the $200,000 income recognized by Logan).

In regards to Logan's basis in the stock, under IRC Section 358, the following formula is used to determine his basis in the stock:

- The adjusted basis of property issued to the corporation
- Plus: The amount of gain recognized by the shareholder (if any),
- Less: The amount of boot received.

Here, Logan contributed land and building with a basis of $450,000.

The $200,000 of gain recognized by Logan is added to the $450,000 of basis of the contributed property.

Finally, the $200,000 of cash boot received by Logan is subtracted.

Therefore, Logan's basis in the stock will be $450,000 ($450,000 + $200,000 – $200,000).

PassKey Exam Question

Brendan transfers a building to Plentywood Corporation in exchange for 50% of its outstanding stock; no one else received stock in the transaction. The remaining 50% of the stock is owned by an unrelated person. Prior to the contribution, Brendan did not own any stock in Plentywood Corporation. The building had an adjusted basis of $125,000 to Brendan and a fair market value of $300,000. The corporate stock that Brendan receives in the transfer has a fair market value of $300,000. How much gain or loss would Brendan recognize in this transfer?

A. $0
B. $175,000 gain
C. $175,000 loss
D. $300,000 gain

PassKey Exam Answer

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A. $0
B. $175,000 gain
C. $175,000 loss
D. $300,000 gain

PassKey Exam Question

Fabienne owns a warehouse. Her basis in the building is $50,000. She organizes a corporation when the warehouse has a fair market value of $125,000 and transfers the building to the corporation for all its authorized capital stock. How much gain must Fabienne and/or the corporation recognize on this transaction?

A. Corporation: $50,000 gain; Fabienne: $75,000.
B. Fabienne: $75,000 gain; corporation: $50,000.
C. Corporation: $75,000 gain; Fabienne: $0.
D. Fabienne: $0; corporation: $0.

PassKey Exam Answer

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A. Corporation: $50,000 gain; Fabienne: $75,000.
B. Fabienne: $75,000 gain; corporation: $50,000.
C. Corporation: $75,000 gain; Fabienne: $0.
D. Fabienne: $0; corporation: $0.

PassKey Exam Question

Alani is a CPA. She transfers a building worth $48,000 and renders accounting services valued at $4,000 to Gadsden Devices, Inc. in exchange for stock valued at $52,000. Right after the exchange, Alani owns 80% of the outstanding stock in Gadsden Devices. The other 20% of the stock in Gadsden Devices, Inc. is owned by another unrelated party. What is the correct statement about this transaction?

A. This is a qualified like-kind exchange.
B. She does not recognize income or gain from this transaction.
C. This is a qualified section 351 exchange.
D. She must recognize ordinary income of $4,000 as payment of services rendered to the corporation. There is no gain recognized on the exchange of property.

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Alani is a CPA. She transfers a building worth $48,000 and renders accounting services valued at $4,000 to Gadsden Devices, Inc. in exchange for stock valued at $52,000. Right after the exchange, Alani owns 80% of the outstanding stock in Gadsden Devices. The other 20% of the stock in Gadsden Devices, Inc. is owned by another unrelated party. What is the correct statement about this transaction?

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Partnership Guaranteed Payments & S Corporations Reasonable Compensation

PassKey Question

What are guaranteed payments in a partnership, and how are they reported to individual partners?

A. Guaranteed payments are reported on Schedule K-1. These are payments made to partners regardless of the partnership's profit or loss.
B. Guaranteed payments are reported on Form 1099-MISC. These are payments made to partners only when the partnership incurs a loss.
C. Guaranteed payments are reported on Form W-2. These are wages paid to a partner who provides services to the partnership.
D. Guaranteed payments are reported on Form 1099-NEC. These are payments made to partners based on their capital contribution.

PassKey Answer

What are guaranteed payments in a partnership, and how are they reported to individual partners?

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D. Guaranteed payments are reported on Form 1099-NEC. These are payments made to partners based on their capital contribution.

PassKey Question

Xavier is a 10% partner in Hartville Partnership. According to the partnership agreement, Xavier is entitled to a fixed annual guaranteed payment of $5,000. During the year, the Hartville Partnership has $55,000 of net ordinary income *before* deducting the guaranteed payment. How much partnership income should Xavier report on his individual return for this year?

A. $5,000
B. $10,000
C. $11,500
D. $16,000

PassKey Answer

Xavier is a 10% partner in Hartville Partnership. According to the partnership agreement, Xavier is entitled to a fixed annual guaranteed payment of $5,000. During the year, the Hartville Partnership has $55,000 of net ordinary income *before* deducting the guaranteed payment. How much partnership income should Xavier report on his individual return for this year?

A. $5,000
B. $10,000
C. $11,500
D. $16,000

PassKey Question

Carolyn and Jerome form a partnership. Each contributes $5,000 in cash for an equal partnership interest. Their partnership agreement states that they will share profit and losses equally (50/50). However, Carolyn is a licensed CPA who will provide ongoing accounting services to the partnership and receive a guaranteed payment each year of $21,000, regardless of the partnership's income or loss. The partnership earns $50,000 during the year, *before* deducting Carolyn's guaranteed payment. What is Jerome's distributive share of partnership profits for the year?

A. $0
B. $14,500
C. $22,500
D. $25,000

PassKey Answer

Carolyn and Jerome form a partnership. Each contributes $5,000 in cash for an equal partnership interest. Their partnership agreement states that they will share profit and losses equally (50/50). However, Carolyn is a licensed CPA who will provide ongoing accounting services to the partnership and receive a guaranteed payment each year of $21,000, regardless of the partnership's income or loss. The partnership earns $50,000 during the year, *before* deducting Carolyn's guaranteed payment. What is Jerome's distributive share of partnership profits for the year?

A. $0

B. $14,500

C. $22,500

D. $25,000

	Partnership	**Carolyn**	**Jerome**
Contribution to form Partnership		$5,000	$5,000
Partnership Income	$50,000		
Guarantee payments	($21,000)		
Partnership Adj Income	$29,000		
Distributive shares		**$14,500**	**$14,500**

Passkey Question

Halima is a 40% partner in the Vansant Partnership. Under the partnership agreement, Halima is to receive 40% of the partnership's income, but never less than $15,000 a year. The partnership's income for 2023 was $30,000 before considering Halima's minimum guarantee amount. What amount can the Vansant Partnership deduct as a guaranteed payment, and what amount of income is Halima required to report on her individual tax return?

A. Partnership: $12,000 Halima: $18,000
B. Partnership: $3,000 Halima: $15,000
C. Partnership: $15,000 Halima: $15,000
D. Partnership: $15,000 Halima: $27,000

Passkey Answer

Halima is a 40% partner in the Vansant Partnership. Under the partnership agreement, Halima is to receive 40% of the partnership's income, but never less than $15,000 a year. The partnership's income for 2023 was $30,000 before considering Halima's minimum guarantee amount. What amount can the Vansant Partnership deduct as a guaranteed payment, and what amount of income is Halima required to report on her individual tax return?

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B. Partnership: $3,000 Halima: $15,000
C. Partnership: $15,000 Halima: $15,000
D. Partnership: $15,000 Halima: $27,000

($30,000 × 40% = $12,000)

PassKey Question

Gena ran her restaurant business, Gena's Diner, as a sole-proprietorship for several years. In 2023, Gena gifted 50% of her restaurant business to her son, Daniel. After the gift, the business is considered a partnership. Capital is a material income-producing factor. The restaurant had a profit of $60,000 for the year. Gena performed managerial services for the partnership worth $24,000, which is reasonable compensation and was allocated to her as a guaranteed payment. Her son performed no services. What is Daniel's share of the partnership profit?

A. $0
B. $9,000
C. $18,000
D. $30,000

PassKey Answer

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A. $0
B. $9,000
C. $18,000
D. $30,000

Profit	$60,000
Guaranteed Payment	$24,000
Remaining profit	$36,000
50% capital interest	**$18,000**

PassKey Question

At the partnership level, how are guaranteed payments reported on Form 1065?

A. As a distribution.
B. As a business expense.
C. As a nonrecourse loan.
D. As business income.

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D. As business income.

PassKey Question

With regards to S corporations paying "reasonable compensation" to a shareholder, which of the following would be considered an employee?

A. A shareholder that provides substantial services to the corporation.
B. A shareholder that is a passive investor and not materially active in the business.
C. A family member of the shareholder under the family attribution rules.
D. A shareholder that is a majority shareholder and an investor.

PassKey Answer

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October Live Study Session Schedule:

Saturday, October 26th – 11am – 12pm (ET) Part 1 12-1pm (ET) Part 2
Wednesday, October 30th – 7pm Part 1

Please sent study subjects to:
- Nicole@hockinternational.com
- Post on Hock Student Forum
- Post on New and Enrolled EA Study Group FB page

Laura Stahl, EA Study Group on Facebook:
https://www.facebook.com/groups/eastudygroup