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QUESTION 1

During 2001, Adler had the following cash receipts:

Wages	\$18,000
Interest Income from investments in municipal bonds	400
Unemployment compensation	1,500

What is the total amount that must be included in gross income on Adler's 2001 income tax return?

- A. \$18,000
- B. \$18,400
- C. \$19,500
- D. \$19,900

Correct Answer: C

Choice "c" is correct. The wages of \$18,000 and unemployment compensation are both includable in gross income on Adler's 2001 income tax return.

Choice "a" is incorrect. The unemployment compensation must be included in gross income.

Choice "b" is incorrect. Municipal bond interest income is excluded from gross income and the unemployment compensation must be included in gross income.

Choice "d" is incorrect. Municipal bond interest income is excluded from gross income.

QUESTION 2

Darr, an employee of Sorce C corporation, is not a shareholder. Which of the following would be included in a taxpayer's gross income?

- A. Employer-provided medical insurance coverage under a health plan.
- B. A \$10,000 gift from the taxpayer's grandparents.
- C. The fair market value of land that the taxpayer inherited from an uncle.
- D. The dividend income on shares of stock that the taxpayer received for services rendered.

Correct Answer: D

Choice "d" is correct. An individual receiving common stock for services rendered must recognize the fair

market value as ordinary income. Any dividends received on that stock would also result in income recognition.

Choice "a" is incorrect. Employer-provided medical insurance is a tax-free fringe benefit.

Choices "b" and "c" are incorrect. Gifts and inheritances are both tax-free to the recipient. (Remember tax is often paid by the person giving the gift or the estate at death.)

QUESTION 3

Conner purchased 300 shares of Zinco stock for \$30,000 in 1980. On May 23, 1994, Conner sold all the stock to his daughter Alice for \$20,000, its then fair market value. Conner realized no other gain or loss during 1994. On July 26, 1994, Alice sold the 300 shares of Zinco for \$25,000.

What was Alice's recognized gain or loss on her sale?

- A. \$0
- B. \$5,000 long-term gain.
- C. \$5,000 short-term loss.
- D. \$5,000 long-term loss.

Correct Answer: A

Choice "a" is correct. Alice has a realized gain of \$5,000 on the transaction: \$25,000 sales price less \$20,000 purchase price. However, she can reduce the gain, but not below zero, by the amount of loss her father could not deduct on the sale to her. Thus, Alice can reduce her gain by up to \$10,000, but not below zero. Here, the gain is \$5,000, so it is reduced to zero. Conner should have sold the stock in the open market so that he could deduct the entire loss. Alice could then have purchased the stock in the open market. Choice "b" is incorrect. \$5,000 is Alice's realized long-term gain on the sale. However, she can reduce the gain, but not below zero, by the amount of loss her father could not deduct on the sale to her. Choice "c" is incorrect. Alice has a realized gain of \$5,000 on the sale. However, since she is related to Conner, her holding period includes his holding period. Therefore, her realized gain is long-term. In addition, she can reduce the gain, but not below zero, by the amount of loss her father could not deduct on the sale to her. Choice "d" is incorrect. Alice can reduce the gain by the amount of loss her father could not deduct on the sale to her. However, she cannot reduce the gain below zero.

QUESTION 4

For a cash basis taxpayer, gain or loss on a year-end sale of listed stock arises on the:

- A. Trade date.
- B. Settlement date.
- C. Date of receipt of cash proceeds.
- D. Date of delivery of stock certificate.

Correct Answer: A

Choice "a" is correct. Trade date.

Gain or loss on a year-end sale of listed stock arises on the trade date.

Rule: Whether on the cash or accrual method of accounting taxpayers who sell stock or securities on an established securities market must recognize gains and losses on the trade date, rather than on the settlement date.

Choices "b", "c", and "d" are incorrect, per the above rule.

QUESTION 5

Dale received \$1,000 in 1990 for jury duty. In exchange for regular compensation from her employer during the period of jury service, Dale was required to remit the entire \$1,000 to her employer in 1990. In Dale's 1990 income tax return, the \$1,000 jury duty fee should be:

- A. Claimed in full as an itemized deduction.
- B. Claimed as an itemized deduction to the extent exceeding 2% of adjusted gross income.
- C. Deducted from gross income in arriving at adjusted gross income.
- D. Included in taxable income without a corresponding offset against other income.

Correct Answer: C

Choice "c" is correct. The \$1,000 jury duty fee that was required to be remitted to the employer may be deducted from gross income in arriving at adjusted gross income. This, in effect, washes out the \$1,000 income she will have to report as part of gross income for the jury duty fees paid to her. Choices "a" and "b" are incorrect. The amount remitted is allowed as an adjustment in arriving at AGI, not as an itemized deduction. Choice "d" is incorrect. A corresponding offset is allowed against other income as an adjustment in arriving at AGI.

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