CPA-REGULATION Q&As

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QUESTION 1

Clark bought Series EE U.S. Savings Bonds after 1989. Redemption proceeds will be used for payment of college tuition for Clark\\'s dependent child. One of the conditions that must be met for tax exemption of accumulated interest on these bonds is that the:

A. Purchaser of the bonds must be the sole owner of the bonds (or joint owner with his or her spouse).

B. Bonds must be bought by a parent (or both parents) and put in the name of the dependent child.

C. Bonds must be bought by the owner of the bonds before the owner reaches the age of 24.

D. Bonds must be transferred to the college for redemption by the college rather than by the owner of the bonds.

Correct Answer: A

Choice "a" is correct. One of the conditions that must be met for tax exemption of accumulated interest on the bonds is that the purchaser of the bonds must be the sole owner of the bonds (or joint owner with his or her spouse). Choice "b" is incorrect. The bonds must be bought and put in the name of the owner or co-owner, not in the name of the dependent child. Choice "c" is incorrect. The owner must be at least 24 years old before the bonds issue date. Choice "d" is incorrect. There is no requirement that the bonds must be transferred to the college for redemption by the college rather than by the owner of the bonds.

QUESTION 2

DAC Foundation awarded Kent $75,000 in recognition of lifelong literary achievement. Kent was not required to render future services as a condition to receive the $75,000. What condition(s) must have been met for the award to be excluded from Kent\\'s gross income?

I. Kent was selected for the award by DAC without any action on Kent\\'s part.

II.

Pursuant to Kent\\'s designation, DAC paid the amount of the award either to a governmental unit or to a charitable organization.

A.

I only.

B.

II only.

C.

Both I and II.

D.

Neither I nor II.

Correct Answer: C

Choice "c" is correct. Generally, the fair market value of prizes and awards is taxable income. However, an exclusion from income for certain prizes and awards applies where the winner is selected for the award without entering into a contest (i.e., without any action on their part) and then assigns the award directly to a governmental unit or charitable organization. Therefore, conditions "I" and "II" must be met in order for Ken to exclude the award from his gross income.

Choice "a" is incorrect. "II" is a necessary condition as well. See explanation above.

Choice "b" is incorrect. "I" is a necessary condition as well. See explanation above.

Choice "d" is incorrect. "I" and "II" are both necessary conditions. See explanation above.

QUESTION 3

Ryan, age 57, is single with no dependents. On July 1, 1997, Ryan\\'s principal residence was sold for the net amount of $500,000 after all selling expenses. Ryan bought the house in 1963 and occupied it until sold. On the date of sale, the house had a basis of $180,000. Ryan does not intend to buy another residence. What is the maximum exclusion of gain on sale of the residence that may be claimed in Ryan\\'s 1997 income tax return?

A. $320,000

B. $250,000

C. $125,000

D. $0

Correct Answer: B

Choice "b" is correct. $250,000 maximum exclusion from taxable income.

Rule: An individual may exclude from income up to $250,000 gain provided that the property was the taxpayer\\'s primary residence for 2 of the last 5 years. Married taxpayers may exclude gains up to $500,000.

Choice "a" is incorrect. $320,000. Ryan, age 57, was not married. Thus, his exclusion was limited to $250,000.

Choice "c" is incorrect. The $125,000 exclusion was old law and eliminated for sales after 5/6/97.

Choice "d" is incorrect, per the above rule.

QUESTION 4

Under the uniform capitalization rules applicable to taxpayers with property acquired for resale, which of the following costs should be capitalized with respect to inventory if no exceptions have been met?

	Repackaging costs	Off-site storage costs
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

A. Option A

B. Option B

C. Option C

D. Option D

Correct Answer: A

Choice "a" is correct. Direct material, direct labor, and factory overhead (applicable indirect costs) are capitalized with respect to inventory under the uniform capitalization rules for property acquired for resale. Applicable indirect costs include depreciation and amortization, insurance, supervisory wages, utilities, spoilage and scrap, design expenses, repair and maintenance and rental of equipment and facilities (including offsite storage), some administrative costs, costs of bonus and other incentive plans, and indirect supplies and other materials (including repackaging costs).

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

QUESTION 5

Tom and Joan Moore, both CPAs, filed a joint 1994 federal income tax return showing $70,000 in taxable income. During 1994, Tom\\'s daughter Laura, age 16, resided with Tom. Laura had no income of her own and was Tom\\'s dependent. Determine the amount of income or loss, if any that should be included on page one of the Moores\\' 1994 Form 1040. The Moores had no capital loss carryovers from prior years. During 1994, the Moores had the following stock transactions, which resulted in a net capital loss:

	Date acquired	Date sold	Sales price	Cost
Revco	2/1/93	3/17/94	$15,000	$25,000
Abbco	2/18/94	4/1/94	8,000	4,000

A. $0

B. $500

C. $900

D. $1,000

E. $1,250

F. $1,300

G. $1,500

H. $2,000

I. $2,500

J. $3,000

K. $10,000

L. $25,000

M. $50,000

N. $55,000

O. $75,000

Correct Answer: J

"J" is correct. $3,000. The capital loss on Revco ($10,000 loss) is added to the capital gain on Abbco ($4,000) to produce a net capital loss of ($6,000). The Moores can claim $3,000 of the loss on their 1994 income tax return and carry the balance forward to 1995.