McGraw-Hill's Taxation of Individuals and Business Entities 2023 Edition 14th edition Spilker Test Bank

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CORRECT ANSWERS ARE LOCATED IN THE 2ND HALF OF THIS DOC.

TRUE/FALSE - Write 'T' if the statement is true and 'F' if the statement is false.

1) Corporations are required to file a tax return annually regardless of their taxable income.
   - ◎ true
   - ◎ false

2) The tax return filing requirements for individual taxpayers only depend on the taxpayer's filing status.
   - ◎ true
   - ◎ false

3) If a taxpayer is due a refund, she does not have to file a tax return.
   - ◎ true
   - ◎ false

4) If April 15th falls on a Saturday, the due date for individual tax returns will be on Monday, April 17th (assuming it is not a holiday).
   - ◎ true
   - ◎ false

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5) If an individual taxpayer is unable to file a tax return by its original due date, the taxpayer can request an automatic nine-month extension to file the return.
   - ◎ true
   - ◎ false

6) An extension to file a tax return does not extend the due date for tax payments.
   - ◎ true
   - ◎ false

7) The statute of limitations for IRS assessment generally ends four years after the date a tax return is filed.
   - ◎ true
   - ◎ false

8) For fraudulent tax returns, the statute of limitations for IRS assessment is 10 years.
   - ◎ true
   - ◎ false

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9) The IRS DIF system checks each tax return for mathematical mistakes and errors.
   - ◎ true
   - ◎ false

10) Joel reported a high amount of charitable contributions as a deduction on his individual tax return relative to taxpayers with similar income levels. The information matching program is the IRS program most likely to identify Joel's tax return for audit.
   - ◎ true
   - ◎ false

11) Office examinations are the most common type of IRS audit.
   - ◎ true
   - ◎ false

12) The three basic types of IRS examinations are computer exams, office exams, and business exams.
   - ◎ true
   - ◎ false

13) The "30-day" letter gives the taxpayer the opportunity to request an appeals conference or agree to a proposed IRS adjustment on the taxpayer's income tax return.
   - ◎ true
   - ◎ false

14) The "90-day" letter gives the taxpayer the opportunity to pay a proposed IRS tax adjustment or file a petition in the U.S. District Court to contest the adjustment and hear the case.
   - ◎ true
   - ◎ false

15) If a taxpayer has little cash and a very technical tax case about which she feels very strongly that the tax rules are "on her side," she should prefer to have her case tried in the U.S. Tax Court.
   - ◎ true
   - ◎ false

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16) In researching a tax issue, Eric finds that the U.S. Circuit Court of Appeals for the Federal Circuit previously has ruled in favor of his tax position, whereas the 11th Circuit (Eric's circuit) previously has ruled against his tax position. If Eric is contemplating litigating his tax position with the IRS, he should prefer to have his case first tried by the U.S. Tax Court.
- ◎ true
- ◎ false

17) If a taxpayer loses a case at the circuit court level, he is granted an automatic appeal hearing with the Supreme Court.
- ◎ true
- ◎ false

18) Secondary authorities are official sources of the tax law with a lesser "weight" than primary authorities.
- ◎ true
- ◎ false

19) Revenue rulings and revenue procedures are examples of primary authorities.
- ◎ true
- ◎ false

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20) The Internal Revenue Code and tax treaties are examples of statutory authorities.
- ◎ true
- ◎ false

21) Because the U.S. District Court hears a broader set of cases, decisions by the U.S. District Court may be considered to have more authoritative weight than those by the U.S. Court of Federal Claims.
- ◎ true
- ◎ false

22) Temporary regulations have more authoritative weight than revenue rulings.
- ◎ true
- ◎ false

23) Proposed and temporary regulations have the same authoritative weight.
- ◎ true
- ◎ false

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24) An acquiescence indicates that the IRS lost a court case and that it has decided to follow the court's ruling in the future.
- ◎ true
- ◎ false

25) The Internal Revenue Code of 1986 is the name of the current income tax code of the United States of America.
- ◎ true
- ◎ false

26) As required by the Constitution, all tax bills are supposed to originate in the House of Representatives.
- ◎ true
- ◎ false

27) The Senate Ways and Means Committee is in charge of drafting tax bills in the U.S. Senate.
- ◎ true
- ◎ false

28) Closed facts are especially conducive to tax planning.
- ◎ true
- ◎ false

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29) Of the two basic types of tax services, beginning tax researchers often prefer topical tax services.
- ◎ true
- ◎ false

30) In researching a question of fact, the researcher should focus her efforts on identifying authorities with fact patterns similar to her client's facts.
- ◎ true
- ◎ false

31) Under the Statements on Standards for Tax Services, a CPA may recommend a tax return position if the position is frivolous and the position is not disclosed on the tax return.
- ◎ true
- ◎ false

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32) In general, a CPA will satisfy his professional responsibilities under the Statements on Standards for Tax Services when recommending a tax return position if he complies with the standards imposed by the applicable tax authority.
- ◎ true
- ◎ false

33) Under the tax law, taxpayers may be subject to both civil and criminal penalties for underpaying their tax liability (e.g., due to fraud).
- ◎ true
- ◎ false

34) A taxpayer can avoid an underpayment penalty if there is substantial authority that supports her tax return position.
- ◎ true
- ◎ false

35) If the IRS assesses additional tax on a tax return upon audit, a taxpayer may be subject to interest and penalties on the underpayment.
- ◎ true
- ◎ false

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MULTIPLE CHOICE - Choose the one alternative that best completes the statement or answers the question.

36) Which of the following is not a factor that determines whether a taxpayer is required to file a tax return?
- A) Filing status
- B) Taxpayer's gross income
- C) Taxpayer's employment
- D) Taxpayer's age
- E) None of the choices are correct.

37) If Paula requests an extension to file her individual tax return in a timely manner, the latest she could file her return without a failure-to-file penalty is:
- A) September 15th.
- B) October 15th.
- C) August 15th.
- D) November 15th.
- E) None of the choices are correct.

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38) If Lindley requests an extension to file her individual tax return in a timely manner, the latest she could pay her tax due without penalty is:
A) April 15th.
B) October 15th.
C) August 15th.
D) November 15th.
E) None of the choices are correct.

39) Corporations are required to file a tax return only if their taxable income is greater than:
A) $0.
B) $1,000.
C) $600.
D) $750.
E) None of the choices are correct. Corporations are always required to file a tax return.

40) Generally, if April 15th falls on a Saturday, individual tax returns will be due on:
A) April 14th.
B) April 15th.
C) April 16th.
D) April 17th.
E) None of the choices are correct.

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41) Dominic earned $1,500 this year, and his employer withheld $200 of federal income tax from his salary. Assuming that Dominic is single, 30 years old, and will have zero tax liability this year, he:
A) is required to file a tax return.
B) is not required to file a tax return but should file a return anyway.
C) is required to file a tax return but should not file because he owes no tax.
D) is not required to file a tax return and should not file a return.
E) None of the choices are correct.

42) Greg earned $25,500 in 2022 and had $1,500 of federal income taxes withheld from his salary. Assuming that Greg is single, 25 years old, and will have a total tax liability of $1,301 (and thus will receive a $199 refund), he:
A) is required to file a tax return.
B) is not required to file a tax return but should file a return anyway.
C) is required to file a tax return but should not file because he owes no tax.
D) is not required to file a tax return and should not file a return.
E) None of the choices are correct.

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43) Bill filed his 2022 tax return on March 15th, 2023. The statute of limitations for IRS assessment on Bill's 2022 tax return should end:
A) March 15th, 2025.
B) April 15th, 2025.
C) March 15th, 2026.
D) April 15th, 2026.
E) None of the choices are correct.

44) Henry filed his 2022 tax return on May 15th, 2023. The statute of limitations for IRS assessment on Henry's 2022 tax return should end:
A) May 15th, 2025.
B) April 15th, 2025.
C) May 15th, 2026.
D) April 15th, 2026.
E) None of the choices are correct.

45) Allen filed his 2022 tax return on May 15th, 2023, and underreported his gross income by 30 percent. Assuming Allen's underreporting is not due to fraud, the statute of limitations for IRS assessment on Allen's 2022 tax return should end:
A) May 15th, 2025.
B) April 15th, 2025.
C) May 15th, 2026.
D) April 15th, 2026.
E) None of the choices are correct.

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46) Andy filed a fraudulent 2022 tax return on May 1, 2023. The statute of limitations for IRS assessment on Andy's 2022 tax return should end:
A) May 1st, 2026.
B) April 15th, 2026.
C) May 1st, 2029.
D) April 15th, 2029.
E) None of the choices are correct.

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47) Martin has never filed a 2022 tax return despite earning approximately $30,000 providing landscaping work in the community. In what tax year, will the statute of limitations expire for Martin's 2022 tax return?

A) 2025
B) 2026
C) 2029
D) 2030
E) None of the choices are correct.

48) Which of the following is not a common method that the IRS uses to select returns for audit?

A) DIF system
B) Tax Select system
C) Information matching
D) Document perfection
E) None of the choices are correct.

49) Leslie made a mathematical mistake in computing her tax liability. Which audit program will likely catch Leslie's mistake?

A) DIF system
B) Mathematical correction
C) Document perfection
D) Information matching
E) None of the choices are correct.

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50) Tyrone claimed a large amount of charitable contributions as a tax deduction relative to taxpayers with similar levels of income. If Tyrone's tax return is chosen for audit because of his large charitable contributions, which audit program likely identified Tyrone's tax return for audit?

A) DIF system
B) Deduction Detective
C) Document perfection
D) Information matching
E) None of the choices are correct.

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51) Ramon's tax return was randomly selected for audit. Which IRS program likely selected Ramon's return for audit?
A) DIF system
B) National Research Program
C) Document perfection
D) Information matching
E) None of the choices are correct.

52) Which of the following audits is the most common and typically less comprehensive?
A) Correspondence
B) Random
C) Office
D) Field
E) None of the choices are correct.

53) Which of the following audits is the least common, broadest in scope, and typically most complex?
A) Correspondence
B) Targeted
C) Office
D) Field
E) None of the choices are correct.

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54) Dan received a letter from the IRS that gave him the choice of (1) requesting a conference with an appeals officer or (2) agreeing to a proposed tax adjustment. Dan received the:
A) 30-day letter.
B) 90-day letter.
C) Appeals letter.
D) Tax adjustment letter.
E) None of the choices are correct.

55) Basu received a letter from the IRS that gave him the choice of (1) paying a proposed deficiency or (2) filing a petition with the U.S. Tax Court. Basu received the:
A) 30-day letter.
B) 90-day letter.
C) Appeals letter.
D) Tax adjustment letter.
E) None of the choices are correct.

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56) Which of the following courts is the only court that provides for a jury trial?
A) Tax Court
B) U.S. Court of Federal Claims
C) U.S. District Court
D) U.S. Circuit Court of Appeals
E) None of the choices are correct.

57) Lavonda discovered that the 5th Circuit (where Lavonda resides) has recently issued a favorable opinion with respect to an issue that she is going to litigate with the IRS. Lavonda should choose which of the following trial courts to hear her case?
A) Tax Court only
B) U.S. Court of Federal Claims only
C) U.S. District Court only
D) Tax Court or the U.S. District Court
E) Tax Court or the U.S. Court of Federal Claims

58) Lavonda discovered that the U.S. Circuit Court of Appeals for the Federal Circuit has recently issued a favorable opinion with respect to an issue that she is going to litigate with the IRS. Lavonda should choose which of the following trial courts to hear her case?
A) Tax Court only
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B) U.S. Court of Federal Claims only
C) U.S. District Court only
D) Tax Court or the U.S. District Court
E) Tax Court or the U.S. Court of Federal Claims

59) Rowanda could not settle her tax dispute with the IRS at the appeals conference. If she wants to litigate the issue but does not have sufficient funds to pay the proposed tax deficiency, Rowanda should litigate in the:
A) U.S. District Court
B) U.S. Circuit Court of Appeals
C) U.S. Court of Federal Claims
D) Tax Court
E) None of the choices are correct.

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60) Which of the following is not considered a primary authority?
A) Tax Court case
B) Treasury Regulation
C) Revenue ruling
D) Tax service
E) None of the choices are correct.

61) Which of the following is not considered a secondary authority?
A) Textbook
B) Private letter ruling
C) Tax article
D) Tax service
E) None of the choices are correct.

62) Which of the following has the highest authoritative weight?
A) Textbook
B) Private letter ruling
C) Revenue ruling
D) Tax service
E) Tax article

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63) Which of the following has the highest authoritative weight?
A) Legislative regulation
B) Private letter ruling
C) Revenue ruling
D) Action on decision
E) Revenue procedure

64) Josephine is considering taking a six-month rotation in Paris for her job. Which type of authority may be especially helpful in determining the tax consequences of Josephine's job in Paris?
A) Determination letter
B) Private letter ruling
C) Tax treaty
D) Regulation
E) Revenue procedure

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65) Generally, code sections are arranged (grouped together):
- A) chronologically.
- B) by topic.
- C) randomly.
- D) by length.
- E) None of the choices are correct.

66) Which of the following has the lowest authoritative weight?
- A) Legislative regulation
- B) Private letter ruling
- C) Revenue ruling
- D) Interpretative regulation
- E) Revenue procedure

67) Which judicial doctrine means that a court will rule consistently with its previous rulings and the rulings of higher courts with appellate jurisdiction?
- A) Judicial hierarchy
- B) The *Goldman* rule
- C) Judicial consistency
- D) Stare decisis
- E) None of the choices are correct.

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68) The regulation with the lowest authoritative weight is the:
- A) procedural regulation.
- B) interpretative regulation.
- C) proposed regulation.
- D) legislative regulation.
- E) None of the choices are correct.

69) Princess, who resides in the 2nd Circuit, recently found a circuit court case that is favorable to her income tax research question. Which of the following circuits would she prefer to have issued the opinion?
- A) 2nd Circuit
- B) Federal Circuit
- C) 1st Circuit
- D) 2nd Circuit or the Federal Circuit
- E) None of the choices are correct.

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70) Jaime recently found a "favorable" *trial-level* court opinion directly on point for her tax question. Which *trial-level* court would she prefer to have issued the opinion?
A) Tax Court
B) District Court
C) Circuit Court
D) Divorce Court
E) None of the choices are correct.

71) Which of the following committees typically initiates tax legislation?
A) House Ways and Means Committee
B) Joint Conference Committee
C) Senate Finance Committee
D) Senate Tax Committee
E) None of the choices are correct.

72) Edie would like to better understand a new code section enacted four weeks ago. Which of the following authorities will help Edie understand the newly enacted code section?
A) IRS regulations
B) U.S. Tax Court cases
C) Committee reports
D) IRS revenue rulings
E) None of the choices are correct.

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73) If the president vetoes tax legislation, Congress:
A) cannot override the president's veto.
B) can override the president's veto with a 50 percent positive vote in the House and Senate.
C) can override the president's veto with a two-thirds positive vote in the House and Senate.
D) can override the president's veto with a 75 percent positive vote in the House and Senate.
E) None of the choices are correct.

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74) Jeremy has a new client. He has identified a research question that relates to a transaction that the client completed several months ago. This type of research question will primarily involve:
A) open facts.
B) new facts.
C) old facts.
D) closed facts.
E) None of the choices are correct.

75) In a planning context,
A) closed facts are preferred to open facts.
B) new facts are preferred to old facts.
C) old facts are preferred to new facts.
D) open facts are preferred to closed facts.
E) None of the choices are correct.

76) Which of the following types of tax services is arranged by code section?
A) Legal tax service
B) Annotated tax service
C) Professional tax service
D) Topical tax service
E) None of the choices are correct.

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77) Which of the following is not a common tool used in conducting tax research?
A) Citator
B) Annotated tax service
C) Topical tax service
D) Keyword search
E) None of the choices are correct.

78) Which of the following is not a source of a tax practitioner's professional responsibilities?
A) AICPA Code of Professional Conduct
B) Statements on Standards for Tax Services
C) Circular 230
D) State board of accountancy statutes
E) None of the choices are correct.

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79) According to Statements on Standards for Tax Services No. 1, a tax practitioner can recommend a tax return position:
A) if the position is frivolous and disclosed on the tax return.
B) if the position complies with the standards imposed by the applicable tax authority.
C) only if the position meets the "more likely than not" standard.
D) only if the position meets the "clear and convincing evidence" standard.
E) None of the choices are correct.

80) Circular 230 was issued by:
A) AICPA.
B) State boards of accountancy.
C) American Bar Association.
D) IRS.
E) None of the choices are correct.

81) Which of the following is a false statement? A taxpayer filing a fraudulent tax return:
A) is potentially subject to criminal penalties.
B) is potentially subject to civil penalties.
C) is potentially subject to fines and a prison sentence.
D) will have an unlimited statute of limitations for the fraudulent tax return.
E) None of the choices are correct.

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82) For which of the following tax violations is a civil penalty not imposed on taxpayers?
A) Failure to file a tax return
B) Failure to pay tax owed
C) Fraud
D) Failure to make estimated tax payments
E) None of the choices are correct.

83) A taxpayer can avoid a substantial understatement of tax penalty:
A) if the position is frivolous and disclosed on the tax return.
B) if the position has a realistic possibility of being sustained by the IRS or courts.
C) if there is substantial authority to support the position.
D) if the position has a reasonable basis and is not disclosed on the tax return.
E) None of the choices are correct.

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84) A taxpayer can avoid a substantial understatement of tax penalty:
- A) if the position is frivolous and disclosed on the tax return.
- B) if the position has a realistic possibility of being sustained by the IRS or courts.
- C) if the position is not frivolous and disclosed on the tax return.
- D) if the position has a reasonable basis and is disclosed on the tax return.
- E) None of the choices are correct.

85) Which types of penalties are only imposed after normal due process including a trial?
- A) Criminal penalties
- B) Civil penalties
- C) Criminal and civil penalties
- D) Failure-to-file penalty
- E) None of the choices are correct.

86) A tax practitioner can avoid IRS penalty relating to a tax return position:
- A) if the position is frivolous and disclosed on the tax return.
- B) if the position has a realistic possibility of being sustained by the IRS or courts.
- C) if there is substantial authority to support the position.
- D) if the position has a reasonable basis and is not disclosed on the tax return.
- E) None of the choices are correct.

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87) A tax practitioner can avoid IRS penalty relating to a tax return position:
- A) only if the position has a more likely than not chance of being sustained by the IRS or courts.
- B) if the position has a realistic possibility of being sustained by the IRS or courts.
- C) if there is not substantial authority to support the position.
- D) if the position has a reasonable basis and is disclosed on the tax return.
- E) None of the choices are correct.

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

88) Tina has a very complex tax return and it looks like she will not be able to file her tax return by its due date. When is her tax return due? What are Tina's options for paying her tax due and filing her tax return this year? What are the consequences if Tina does not file or pay her tax in a timely manner? Be specific.

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89) For the following taxpayers, indicate whether the taxpayer should file a tax return and why.

a. Robert earned $50,000 this year as a staff accountant. His estimated tax liability is $4,500, and he expects to receive a $500 tax refund.
b. Amy earned $4,000 this year working part-time. She will have no federal tax liability and has not made any federal tax payments.
c. Ty earned $2,500 this summer and had $200 of federal taxes withheld from his paycheck. He will have no federal tax liability this year.
d. Startup Corporation had a $50,000 loss this year.
e. The Walker Family Trust earned $500 of gross income this year.

90) For the 2022 tax returns, indicate when the statute of limitations expires and why.

a. Phoenix filed his tax return on February 28, 2023.
b. Jill and Randy filed their tax return on August 16, 2023.
c. Although required to file, Catherine chose not to file a tax return this year because she was expecting a tax refund and could not pull together all the information needed to file the return.
d. Jerry filed his tax return on May 22, 2023, but has accidentally underreported his taxable income by 30 percent.

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91) For the 2022 tax returns, indicate when the statute of limitations expires and why.

a. Simon filed his tax return on April 10, 2023.
b. Billy and Barbara filed their tax returns late on December 1, 2023.
c. Pearson earns a living through various illegal activities. He filed his tax return on March 14, 2023, but did not report his illegal income on his tax return.
d. Luther filed his tax return on July 17, 2023, but has accidentally underreported his gross income by 20 percent.

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92) For the following tax returns, identify the method the IRS likely used to select the return for audit.
   a. Dan made a mistake in adding his income on his tax return.
   b. Juanita failed to report her salary from her second job on her tax return.
   c. Michael and Venita deducted a relatively large amount of travel expenses on their tax return for their business. The travel expense is large relative to other taxpayers in similar businesses with similar levels of income.
   d. Paul and Melissa recently went through a very nasty divorce. One of the issues was Paul's less than forthright accounting of his income in determining the appropriate level of alimony.

93) For the following tax returns, identify which of the three audit types will most likely be utilized.
   a. The IRS selected Don's return for audit because of his high itemized deductions. The IRS would like documentation of these deductions.
   b. Large Public Corporation is a very large publicly traded corporation. It is involved in many complex transactions that have significant tax ramifications.
   c. George and Barbara operate a small business out of their home. The IRS has identified a couple of issues that may relate to their business.
   d. The IRS selected Bill and Hillary's tax return for review because of some of their investment sales. They would like a better understanding of the transactions and parties involved.

94) The IRS has recently completed its audit of Lorene's corporation. As a tax novice, she has very little understanding regarding the audit process and what happens next. Describe the post-audit process for Lorene and identify her options.

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95) Mel recently received a 30-day letter from the IRS. Although his tax return being audited has several potential large issues (potential tax consequences of $70,000 – $80,000), the IRS agent auditing his return only identified one item that will require a modest adjustment of $10,000. Mel feels strongly that the $10,000 adjustment would not hold up in court and was surprised that the IRS agent did not identify some of the other potential larger issues. What are Mel's choices with respect to the 30-day letter and what factors should influence his decisions?

96) Kim has decided to litigate a tax issue with the IRS. Describe the trial-level courts that Kim may use to litigate the case.

97) For the following taxpayers, please recommend the most advantageous trial-level court(s) to litigate a tax issue with the IRS.

a. Joe is litigating a tax issue with the IRS that is considered a question of fact (i.e., the answers depend on the facts of the case). There is not a lot of authority on point for this case, but Joe has a very appealing story to justify his position that is likely to be viewed sympathetically by his peers.
b. The Circuit Court of Appeals for the Federal Circuit recently issued an opinion that is very favorable to the issue that Jesse plans to litigate with the IRS.
c. The Circuit Court of Appeals for the Federal Circuit recently issued an opinion that is not favorable to the issue that Hank plans to litigate with the IRS.
d. The 7th Circuit (where Elizabeth resides) recently issued an opinion that is very favorable to the issue that Elizabeth plans to litigate with the IRS.

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98) A client has recently learned of a proposed tax bill that would increase the tax rates on investment gains by 5 percent. The president does not support this increase. Please describe for your client the process by which new tax legislation is created and how the president's disapproval may influence the enactment of the bill.

99) Chris and Chuck were recently debating whether the Internal Revenue Code is "logical." Chris offers that she has briefly reviewed the Code and could hardly understand its organizational structure, if there is one. Please describe the basic organization of the Code and how understanding its organization may be especially beneficial to the tax researcher.

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100) Carey was researching a tax issue and located what appears to be a favorable IRS regulation. He knows that regulations serve different purposes and are issued in different forms. Which purpose and which form of regulation would provide Carey the most confidence that he has found an authority that carries a lot of weight for the long term? How could Carey check the status of this regulation?

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101) Campbell was researching a tax issue and found a favorable tax court opinion and an IRC Code Section that appear to answer the question. Is she finished with the research process? If so, why? If not, what must she do?

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102) Roddy was researching an issue and found a favorable tax court decision that addresses his issue. He also determined that there was a nonacquiescence for the case. Who issued the nonacquiescence? What is it? What does it mean and how would it affect Roddy's reliance on the court case?

103) Raul was researching an issue and found two tax court decisions issued within six months of each other, one for a taxpayer residing in California and the other for a taxpayer residing in New York, whose rulings were inconsistent. Raul knows that the federal tax law does not differ by state and the issue was exactly the same in both cases. Raul is confused because he thought that a basic judicial doctrine was that a court is supposed to rule consistently. Name and describe this judicial doctrine that requires judicial consistency and discuss why the tax court may have intentionally ruled inconsistently in this example.

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104) Rebecca is at a loss. A new tax law was recently passed, and she needs to get a better understanding of why the tax law was passed and the intent of the law from an official authority. Describe what authorities may be especially helpful to Rebecca and why she can't find many authorities that discuss the new law.

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105) Lakeisha, a first-year staff accountant, was researching a tax issue and found what appears to be the answer to her question in her introductory tax textbook that she bought three years ago. She is thrilled because she thought it would take much longer to find her answer. What type of authority is the textbook? What are other examples of this type of authority? Can Lakeisha base her research conclusion on the textbook or similar authorities? Any suggestions for Lakeisha?

106) Kodak is a beginning tax researcher. He knows that the first step of the research process is to get an understanding of the facts surrounding the transaction being researched. Describe the two basic types of facts, the sources of facts for a research project, and any advice that may help Kodak.

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107) Caitlin is a tax manager for an accounting firm, and Duff is a first-year staff accountant. Describe the differences in the manner in which Caitlin and Duff may identify research issues and in general how one may identify research questions.

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108) Lindy, a tax intern, is beginning her first tax research case for her employer. Her manager has given her a basic understanding of the facts and has identified the basic research question. Lindy is now ready to begin searching for relevant tax authorities. Describe the different types of research tools available to help a tax researcher locate relevant authority and identify which type may be especially useful for Lindy.

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109) Hong, an introductory tax student, is beginning his first research project. He has a complete understanding of the relevant facts for his project and has identified the initial research questions. He is now ready to begin using a tax service to identify relevant authorities. What are some suggestions for him on how to use tax services to identify relevant authorities?

110) Mary Ann is working on a pretty big research project. Her manager has alerted her to the possibility that some of her research questions are likely to be questions of fact, whereas others are likely to be questions of law. Explain the difference between the two types of questions and how this would influence her research.

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111) Nolene suspects that one of her new clients may be intentionally underreporting his taxable income. What are the potential ramifications to her client for this behavior? What are the consequences to Nolene if she assists the client in underreporting income? Any advice for Nolene?

112) Houston has found conflicting authorities that address a research question for one of his clients. The majority of the authorities provide a favorable answer for his client. Nonetheless, there are several authorities that provide an unfavorable answer. Houston estimates that if the client takes the more favorable position on its tax return there is approximately a 60 percent chance that the position will be sustained upon audit or judicial proceeding. If the client takes this position on its tax return, will Houston be subject to penalty? Will the client potentially be subject to penalty?

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Answer Key

Test name: Chapter 02

1) TRUE
2) FALSE
3) FALSE
4) TRUE
5) FALSE
6) TRUE
7) FALSE
8) FALSE
9) FALSE
10) FALSE
11) FALSE
12) FALSE
13) TRUE
14) FALSE
15) TRUE
16) FALSE
17) FALSE
18) FALSE
19) TRUE
20) TRUE
21) FALSE
22) TRUE
23) FALSE
24) TRUE
25) TRUE
26) TRUE
27) FALSE
28) FALSE
29) TRUE
30) TRUE
31) FALSE
32) TRUE
33) TRUE
34) TRUE
35) TRUE
36) C

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37) B
38) A
39) E
40) D
41) B
42) A
43) D
The statute of limitations (SOL) ends three years from the later of (1) the date the tax return was filed or (2) the tax return's original due date.

44) C
The statute of limitations (SOL) ends three years from the later of (1) the date the tax return was filed or (2) the tax return's original due date.

45) E
Because Allen underreported his gross income by 30 percent, the statute of limitations (SOL) ends six years from the later of (1) the date the tax return was filed or (2) the tax return's original due date.

46) E
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There is no statute of limitations for fraudulent tax returns.

47) E
There is no statute of limitations if a taxpayer fails to file a tax return.

48) B
49) C
50) A
51) B
The National Research Program randomly selects returns for audit to provide the necessary input into the DIF system.

52) A
53) D
54) A
55) B
56) C
57) D
The Tax Court and the U.S. District Court will appeal to the 5th Circuit.

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58) B
The U.S. Court of Federal Claims will appeal to the U.S. Circuit Court of Appeals for the Federal Circuit.

59) D
60) D
61) B
62) C
63) A
64) C
65) B
66) B
67) D
68) C
69) D
70) A
71) A
72) C
Of the authorities listed, only committee reports will be available to aid in understanding a new code section.

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73) C
74) D
75) D
76) B
77) E
78) E
79) B
80) D
81) E
82) E
83) C
84) D
85) A
86) C
87) D
88) Essay

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Tina's tax return is due on April 15th. Tina may request an automatic six-month extension to file her tax return (i.e., until October 15th). Extensions allow the taxpayer to delay filing a tax return but ***do not*** extend the due date for tax payments. If a taxpayer fails to pay the entire balance of tax owed by the original due date of the tax return, the IRS charges the taxpayer interest on the underpayment from the due date of the return until the taxpayer pays the tax. The interest rate charged depends on taxpayer type (e.g., individual versus corporation) and varies quarterly with the federal short-term interest rate. The interest rate for tax underpayments for individuals equals the federal short-term rate plus three percentage points. Penalties are also imposed when a taxpayer fails to file a tax return. Also, there is no statute of limitations if Tina fails to file her return.

89) Essay

a. Because his gross income exceeds the applicable gross income threshold, Robert is required to file a tax return.
b. Amy is not required to file a tax return because her income is below the applicable gross income threshold.
c. Ty is not required to file a tax return because his gross income is below the applicable gross income threshold. However, he should file a tax return to receive a refund of the $200 of taxes withheld.
d. Startup Corporation is required to file a tax return as all corporations are required to file an annual tax return regardless of their profitability.
e. Because the trust's income is below the applicable threshold, the Walker Family Trust is not required to file a tax return this year.

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90) Essay

f. April 15, 2026. The statute of limitations expires three years from the later of the original due date of the return or the date the return was filed.
g. August 16, 2026. The statute of limitations expires three years from the later of the original due date of the return or the date the return was filed.
h. Because Catherine failed to file a tax return, the statute of limitations will not lapse for her 2022 tax return.
i. May 22, 2029. Because Jerry underreported his gross income by 30 percent, the statute of limitations is extended to six years.

91) Essay

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j. April 15, 2026. The statute of limitations expires three years from the later of the original due date of the return or the date the return was filed.
k. December 1, 2026. The statute of limitations expires three years from the later of the original due date of the return or the date the return was filed.
l. Because Pearson filed a fraudulent tax return, the statute of limitations will not lapse for his 2022 tax return.
m. July 17, 2026. Because Luther accidentally underreported his gross income by only 20 percent, the statute of limitations will expire three years from the date the return is filed (i.e., the statute of limitations is not extended to six years).

92) Essay
n. Document perfection
o. Information matching
p. DIF system
q. Spousal tip.

93) Essay
r. Correspondence examination
s. Field examination
t. Office examination
u. Correspondence examination and possibly an office examination.

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94) Essay

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After the examination, the IRS agent provides a list of proposed adjustments (if any) to the taxpayer for review. If the taxpayer agrees to the proposed changes, the taxpayer signs an agreement form (Form 870) and pays the additional tax owed (or receives the proposed refund). If the taxpayer disputes the proposed changes, the taxpayer will receive a "30-day letter," which instructs the taxpayer that he or she has 30 days to either (1) request a conference with an appeals officer, who is independent and resides in a separate IRS division from the examining agent or (2) agree to the proposed adjustment. An appeals officer would consider the merits of the unresolved issues as well as the "hazards of litigation"—that is, the probability that the IRS will lose if the case is brought to court and the resulting costs of a taxpayer-favorable ruling. If the taxpayer chooses the appeals conference and reaches an agreement with the IRS there, the taxpayer can then sign the Form 870. If the taxpayer and IRS still do not agree on the proposed adjustment at the appeals conference, or the taxpayer chooses not to request an appeals conference, the IRS will then send the taxpayer a "90-day letter." The 90-day letter (also known as a statutory notice of deficiency) explains that the taxpayer has 90 days to either (1) pay the proposed deficiency or (2) file a petition in the U.S. Tax Court to hear the case. If the taxpayer would like to litigate the case but would prefer that the case be heard in the local U.S. District Court or the U.S. Court of Federal Claims, the taxpayer must pay the tax deficiency first and then sue the IRS for refund in the court.

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95) Essay

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The "30-day letter" instructs the taxpayer that he or she has 30 days to either (1) request a conference with an appeals officer, who is independent and resides in a separate IRS division from the examining agent or (2) agree to the proposed adjustment. An appeals officer would consider the merits of the unresolved issues as well as the "hazards of litigation"—that is, the probability that the IRS will lose if the case is brought to court and the resulting costs of a taxpayer-favorable ruling. Thus, the appeals officer has a bit more latitude to settle cases than examining agents. Because the appeals division is independent, it may be possible for the taxpayer to receive a more favorable resolution as the appeals officer is less emotionally invested in the audit. On the downside, the appeals officer may raise new issues, and thus, increase the taxpayer's tax exposure. In addition, the longer the dispute continues without resolution, the more interest will accrue on the assessment. In Mel's case, the potential risk of the appeals officer raising additional questions probably outweighs the potential benefits of appeal. Thus, it may be better for him to forgo the appeals conference and either agree to the proposed adjustment or litigate the case.

96) Essay

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There are three trial-level courts that hear federal tax cases: the U.S. Tax Court, the U.S. District Court, and the U.S. Court of Federal Claims. The U.S. District Court is the only court that provides for a jury trial; the U.S. Tax Court is the only court that allows tax cases to be heard before the taxpayer pays the disputed liability and is the only court with a small claims division (hearing claims involving disputed liabilities of $50,000 or less); the U.S. Tax Court judges are tax experts, whereas the U.S. District Court and U.S. Court of Federal Claims judges are generalists. Both the U.S. Tax Court and local U.S. District Court cases appeal to the specific circuit court based on the taxpayer's residence. In contrast, all U.S. Court of Federal Claims cases appeal to the U.S. Circuit Court of Appeals for the Federal Circuit.

97) Essay

v. U.S. District Court because it is the only court that offers a jury trial.
w. The U.S. Court of Federal Claims because its appellate court is the Circuit Court of Appeals for the Federal Circuit.
x. The U.S. Tax Court or the U.S. District Court because they will not appeal to the Circuit Court of Appeals for the Federal Circuit.
y. The U.S. Tax Court or the U.S. District Court because they will appeal to the 7th Circuit.

98) Essay

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As required by the U.S. Constitution (Article 1, Section 7), "All bills for raising revenue shall originate in the House of Representatives." The Senate may propose tax legislation, but the first to formally consider a bill will be the House, typically within its Ways and Means Committee. After the committee debates the proposed legislation and drafts a bill, the bill is sent to the House of Representatives for debate and ultimately a vote (either yea or nay without modification). If the bill is approved, it becomes an "act" and is sent to the Senate, which refers the act to the Senate Finance Committee. Not to be outdone by the House, the Senate Finance Committee typically amends the act during its deliberations. After the revised act passes the Senate Finance Committee, the act is sent to the Senate for debate and vote. Unlike the process in the House of Representatives, Senators may modify the proposed legislation during their debate. If the Senate passes the act, both the House and Senate versions of the legislation are sent to the Joint Conference Committee, which consists of members of the House Ways and Means Committee and the Senate Finance Committee. During the Joint Conference Committee deliberations, committee members debate the two versions of the proposed legislation. Possible outcomes for any specific provision in the proposed legislation include adoption of the Senate version, House version, or some compromise version of the two acts. Likewise, it is possible that the Joint Conference Committee will simply choose to eliminate specific provisions from the proposed legislation or fail to reach a compromise on the proposed legislation, thereby terminating the legislation. After the Joint Conference Committee approves the act, the revised legislation is sent to the House and Senate for vote. If approved by both the House and Senate, the act is sent to the president for his or her signature. If the president signs the act, it becomes law and is incorporated into the Internal Revenue Code of 1986 (i.e., Title 26 of the United States Code, which contains *all* codified laws of the U.S.). If the president vetoes the legislation, Congress may override the veto with a two-thirds positive vote in both the House of Representatives and Senate. Given the president's disapproval of the proposed tax increase and supermajority required to override a presidential veto, the legislation most likely will not be enacted.

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99) Essay

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The Internal Revenue Code is segregated into subtitles, chapters, subchapters, parts, subparts, and sections. All existing and any new tax laws are placed in the Code within a specific subtitle, chapter, subchapter, part, subpart, and section of the Code. When referencing a tax law, the researcher generally refers to the law simply by its code section. Code sections are numbered from 1 to 9834, with gaps in the section numbers to allow new code sections to be added to the appropriate parts of the Code as needed. Each code section is further segregated into subsections, paragraphs, subparagraphs, and clauses to allow more specific reference or citation.
One must understand the organization of a code section (i.e., into subsections, paragraphs, subparagraphs, and clauses) to be able to cite the respective law correctly (e.g., IRC Section. 162(b)(2)). Many provisions in the Code apply only to specific parts of the Code. If one does not understand what laws are encompassed in the chapter, it would be very difficult to interpret the code section and determine its applicability to a research question. Finally, the Code has been arranged such that, in general, similar code sections are grouped together. Understanding this organization allows the researcher to be much more efficient in locating relevant code sections.

100) Essay

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Regulations are the Treasury Department's official interpretation of the Internal Revenue Code and have the highest authoritative weight. Regulations are issued in three different forms: proposed, temporary, and final. Final regulations are regulations that have been issued in final form, and thus, until revoked, they represent the Treasury's interpretation of the Code. Temporary regulations, as the name suggests, have a limited life (three years for regulations issued after November 20, 1988). Nonetheless, during their "life," they carry the same authoritative weight as final regulations. Finally, proposed regulations are, as the name suggests, "proposed," and thus do not carry the same authoritative weight as temporary or final regulations.

In addition to being issued in three different forms, regulations also serve three basic purposes: interpretative, procedural, and legislative. Most regulations are issued as interpretative or procedural regulations. As the names suggest, interpretative regulations represent the Treasury's interpretation of the Code. Procedural regulations explain Treasury Department procedures as they relate to administering the Code. Legislative regulations, the rarest type, are issued when Congress specifically directs the Treasury Department to create regulations to address an issue in an area of law. In these instances, the Treasury is actually writing the law instead of interpreting the Code. Because legislative regulations actually represent tax law instead of an interpretation of tax law, legislative regulations generally have been viewed to have more authoritative weight than interpretative and procedural regulations. However, in *Mayo Foundation for Medical Education & Research v. U.S.*, 131 S.Ct. 704 (2011), the Supreme Court held (subject to specific conditions) that all Treasury regulations warrant deference.

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Checking the status of regulations is a bit complicated. Most tax services alert researchers if a regulation has not been updated for certain changes in the Code. If this is the case, the researcher should evaluate whether the changes in the Code make the regulation obsolete.

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101) Essay

Campbell is not finished. Once the tax researcher has identified relevant authorities, she must make sure that the authorities are still valid and up to date. For court cases, a citator can be used to review the history of the case to find out, for example, whether it was subsequently appealed and overturned and to identify subsequent cases that cite the case. Favorable citations strengthen a case, while unfavorable citations weaken the case. Citators can also be used to check the status of revenue rulings, revenue procedures, and other IRS pronouncements. Checking the status of the Code is fairly simple: just locate the current version.

102) Essay

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Except for Supreme Court cases, whenever the IRS loses, it may issue an acquiescence or nonacquiescence as guidance for how the IRS intends to respond to the loss. An acquiescence indicates that the IRS has decided to "follow" the court's adverse ruling in the future—i.e., the IRS will no longer litigate this issue. A nonacquiescence has the exact opposite implications. A nonacquiescence alerts taxpayers that the IRS plans to continue to litigate this issue. Roddy can still rely on the favorable tax court case but should alert his client that the IRS has stated very clearly that it does not agree with the tax court opinion and will continue to litigate this issue.

103) Essay

In rendering court decisions, all courts apply the judicial doctrine of *stare decisis*. This doctrine means that a court will rule consistently with (a) its previous rulings (i.e., unless, due to evolving interpretations of the tax law over time, they decide to overturn an earlier decision) and (b) the rulings of higher courts with appellate jurisdiction (i.e., the courts their cases are appealed to). The implication of *stare decisis* is that a circuit court will abide by Supreme Court rulings and its own rulings, whereas a trial-level court will abide by Supreme Court rulings, its respective circuit court's rulings, and its own rulings. For example, a district court in California would follow 9th Circuit and Supreme Court rulings as well as the court's own rulings.

The doctrine of *stare decisis* presents a special problem for the U.S. Tax Court because it appeals to different circuits based on the taxpayer's residence. To implement the doctrine of *stare decisis*, the tax court applies the Golsen rule. The Golsen rule simply states that the tax court will abide by rulings of the circuit court that has appellate jurisdiction for a case. The implication of the Golsen rule is that tax courts may issue conflicting opinions in different circuits, and thus most likely explains the differing tax court decisions that Raul located.

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104) Essay

The House Ways and Means Committee, Senate Finance Committee, and Joint Conference Committee each produce a committee report that explains the current tax law, proposed change in the law, and justification for the change. These committee reports are considered "statutory" sources of the tax law and may be very useful in interpreting tax law changes and understanding congressional intent. This is especially important after new legislation has been enacted because, with the exception of the Code, there will be very little authority interpreting the new law (i.e., no judicial or administrative authorities because of the time it takes for the new law to be litigated or for the IRS to issue interpretative guidance—e.g., regulations, etc.).

105) Essay

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There are two broad categories of tax authorities: primary authorities and secondary authorities. Primary authorities are "official" sources of the tax law generated by the legislative branch (i.e., statutory authority issued by Congress), judicial branch (i.e., rulings by the U.S. District Court, U.S. Tax Court, U.S. Court of Federal Claims, U.S. Circuit Court of Appeals, or U.S. Supreme Court), or executive/administrative branch (i.e., IRS pronouncements). Secondary authorities are "unofficial" tax authorities that interpret and explain the primary authorities, such as tax research services, tax articles, newsletters, and textbooks. Secondary authorities may be very helpful in understanding a tax issue, but they hold little weight in a tax dispute (hence the term "unofficial" tax authorities). Thus, tax advisors should always be careful to verify their understanding of tax law by examining primary authorities directly and never citing a secondary authority in a research memo. In Lakeisha's case, this is particularly important because her textbook is three years old. Thus, not only is the textbook not an "official" tax authority, it may also be out of date.

106) Essay

To answer a tax question, you must understand the question. To understand the question, you must know the facts. There are two basic types of facts: open facts and closed facts. Open facts have not yet occurred, such as the facts associated with a proposed transaction. Closed facts have already occurred. The distinction between open and closed facts is important because unlike closed facts, open facts can be altered, and different facts may result in very different tax consequences. Open facts allow the taxpayer to arrange a transaction to achieve the most advantageous outcome. Thus, they are especially important in tax planning.

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There are several sources of facts for the typical research projects. Common sources include interviewing clients, speaking with third parties (e.g., attorneys, brokers), and reviewing client documents (contracts, prior tax returns, wills, trust documents, deeds, corporate minutes, etc.). When interviewing clients, you must remember that many clients are not tax experts. Thus, it is up to the tax researcher to ask the correct initial and follow-up questions to obtain all the relevant facts. Within a tax planning context, one should also consider nontax factors, such as a client's personal values or objectives, as these often put constraints on tax planning strategies.

107) Essay

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A tax researcher's ability to identify issues is largely a function of his or her type of tax expertise. A tax expert in a particular area will typically be able to identify quickly the specific tax issues that relate to transactions in that area. For example, an expert in corporate acquisitions would quickly identify the tax consequences and specific issues of alternative acquisition types. A novice, on the other hand, would likely identify broader issues first and then more specific issues as he researched the relevant tax law.

The best method to identify tax issues is to first get a good understanding of the client's facts. Then combine your understanding of the facts with your knowledge of the tax law. For an expert in this particular area, the issues will be immediately evident. For a novice, the initial response to a set of facts may take the form of a series of general questions: (1) Is this item of expense deductible? (2) Is that item of income taxable? (3) In what year should the expense be deducted? (4) In what year should the item of income be taxed? etc. After you identify these types of general issues, your research will enable you to identify the more specific issues that ultimately determine the tax ramifications of the transaction being researched.

108) Essay

Tax services aid the researcher in identifying relevant authorities. There are two basic types of tax services: annotated tax services and topical tax services. Annotated tax services are arranged by code section, i.e., for each code section, an annotated service includes the code section, a listing of the code section history, copies of congressional committee reports that explain changes to the code section, a copy of all the regulations issued for the specific code section, the service's "unofficial" explanation of the code section, and brief summaries (called annotations) of relevant court cases, revenue rulings, revenue procedures, letter rulings, etc., that address issues specific to the code section. Two examples of annotated tax services are Commerce Clearing House's (CCH) Standard Federal Tax Reporter and RIA's United States Tax Reporter.

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Topical tax services are arranged by topic (e.g., taxable forms of income, tax-exempt income, trade or business expenses, etc.). For each topic, the services identify tax issues that relate to the topic, and then explain and cite authorities relevant to the issue (code sections, regulations, court cases, revenue rulings, etc.). Beginning tax researchers (like Lindy) often prefer topical services, as they generally are easier to read. Some examples of topical federal tax services include BNA's Tax Management Portfolios, CCH's Tax Research Consultant, and RIA's Federal Tax Coordinator.

109) Essay

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A novice may conduct a keyword search in the service, use the tax service's topical index, or "browse" the tax service to identify the relevant portions. Some suggestions for identifying keywords: try to describe the transaction in three to five words. An ideal keyword search typically includes (1) the relevant area of law and (2) a fact or two that describes the transaction. Try to avoid keywords that are too broad (e.g., income, deduction, taxable, etc.) or that may be too narrow.

If keyword searching is not proving beneficial, check your spelling, make sure you are searching the correct database, rethink your keywords, use another research method, use another tax service, or as a last resort, take a break.

While utilizing keyword searches or other research methods to identify potentially relevant areas of law and tax authorities, you must constantly ask yourself whether you are indeed in the correct area of law. Once the answer to this question is an authoritative "yes," you can delve deeper into the area of law and related authorities to answer the question.

110) Essay

Two basic types of issues that researchers will encounter are questions of fact and questions of law. The answer to a question of fact hinges upon the facts and circumstances of the taxpayer's transaction. For example, whether a trade or business expense is "ordinary," "necessary," and "reasonable," and thus deductible, is a question of fact. If you are researching a question of fact, it is important for the researcher to understand which facts determine the answer—in this case, which facts make an expense "ordinary," "necessary," and "reasonable" and which facts do not. In this type of question, the researcher will focus much of her efforts toward understanding how various facts affect the research answer and identifying authorities with fact patterns similar to her client's fact pattern.

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The answer to a question of law hinges upon the interpretation of the law, such as interpreting a particular phrase in a code section. If a researcher is faced with this type of question, she will spend much of her time researching the various interpretations of the code section and taking note of which authorities interpret the code differently and why.

111) Essay

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There are serious ramifications for committing fraud for both the taxpayer and the tax practitioner. First, there is no statute of limitations on assessing tax due to fraudulent reporting. Thus, Nolene's client will be at risk for additional tax, interest, penalties, etc., for the period of time he commits fraud. Second, the penalties associated with fraud are substantial. In addition to having to pay the assessed tax and interest on the assessed tax (which can be quite substantial), the client may be subject to both civil and criminal penalties for fraud. Both penalties carry potentially substantial monetary fines, and the criminal penalty may include a prison term.
For Nolene, assisting in fraud will clearly violate her professional responsibilities established by the Statements on Standards for Tax Services, Circular 230, and her state board of accountancy. She will also be subject potentially to both civil and criminal penalties.
Nolene should discuss the severe negative consequences of committing tax fraud (civil and criminal penalties) as well as her own professional standards with her client. If Nolene suspects that her client is not fully reporting his income, she should carefully consider terminating the client relationship.

112) Essay
A tax preparer (Houston) may recommend any tax return position and avoid penalty if there is substantial authority that supports the tax return position. Substantial authority suggests that the probability that the taxpayer's position is sustained upon audit or litigation is in the 35 to 40 percent range or above. The tax practitioner can also avoid penalty if the tax return position has a reasonable basis (i.e., supported by one or more tax authorities) and the position is disclosed on the taxpayer's return. Given that there is a 60 percent chance that the position will be sustained upon audit or by the courts, Houston should not be subject to penalty and no disclosure is required.
Taxpayers are subject to the same standards as tax practitioners (substantial authority without disclosure; reasonable basis with disclosure). Thus, Houston's client will not need to disclose the position on its tax return to avoid penalty.

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