

**Test Bank for Federal Taxation 2013 7th Edition Pratt Kulsrud ISBN
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Federal Taxation 2013 7th Edition Pratt Test Bank

Chapter 2. Tax Practice and Research

2-23

- a. CA-7. This information is shown in the citation for the case.
- b. No. There is no Supreme Court citation listed.
- c. Tax Court and reported as a memorandum decision, as shown in the citation of the case.

2-24 It would be difficult to tell from the Citator alone exactly what effect the decision in *Arkansas Best v. Comm.* had on the *Corn Products, v. Comm.* case. For example, in the Prentice Hall Citator *Arkansas Best* and *Corn Products* are referenced by the symbol "k," which stands for "the cited and citing case principles are reconciled." It is probably best to read the two cases to see how they interrelate. The Citator does alert the reader to the fact that both cases address the same issue, however.

2-25

- a. The United States Court of Appeals for the Eleventh Circuit (CA-11) decided the *Robert Autrey, Jr. v. United States* case on appeal.
- b. A United States District Court originally tried the case.
- c. The Court of Appeals *affirmed* part of the District Court's decision and *reversed* part of it.

2-26

- a. The U.S. Tax Court tried the case of *Fabry v. Commissioner*.
- b. The judge used the following sources in framing his opinion:

- (1) Internal Revenue Code § 104;
- (2) Legislative History to § 104—83rd Cong., 2nd Sess. 15 (1954);
- (3) Various case citations; and
- (4) S.Rept. 1622, 83rd Cong, 2nd Sess. 15-16 (1954).

2-27

- a. No. The government won the case.
- b. Judge Atkins.
- c. Whether operating a farm with breeding cattle and incurring net losses qualified as a business activity and therefore the net losses were deductible, or as a hobby and therefore the losses were not deductible.

2-28

- a. 1998-51 I.R.B. 6
- b. *Lawrence W. McCoy*, 38 T.C. 841 (1962)
- c. *Reginald Turner*, 13 TCM 462, T.C. Memo 1954-38
- d. *RCA Corp. v. U.S.*, 81-2 USTC ¶9783 (CA-2, 1981)
- e. *RCA Corp. v. CAS.*, 48 AFTR2d 6164 (CA-2, 1981)
- f. *RCA Corp. v. U.S.*, 664 F.2d 881 (CA-2, 1981)
- g. *Conim. v. JFJ/cojc*, 66 S. Ct. 546 (USSC, 1946)
- h. *Thor Power Tool*, 79-1 USTC ¶9139 (USSC, 1979)
- i. *M.G. Anton*, 34 T.C. 842 (1960)
- j. *Brian E. Knutson*, 60 TCM 540, T.C. Memo 1990-440
- k. *Samuel B. Levin v. Comm.*, 43 AFTR2d 79-1057 (Ct. Cls., 1979)

2-29

- a. **Issue:** Whether Battelstein Investment Company unreasonably accumulated earnings so as to be subject to the § 531 accumulated earnings tax.
- b. **Issue 1:** Whether Code § 1034 fixes which of several sequential sales (within the statutory replacement period) is entitled to the benefit-of-gain exclusion on

the sale of a taxpayer's principal residence. Full cite is 47 TCM 904.

Issue 2: When gain goes unrecognized under § 1034(a), does § 1034(e) require that the basis of the new principal residence be reduced by the amount of the deferred gain?

- c. **Issue 1:** Was the amount paid to the taxpayer a dividend taxable as ordinary income, or was the transaction a redemption (i.e., treated as a sale-purchase) by the corporation of all of the taxpayer's stock?

Issue 2: Was the payment in question essentially equivalent to a dividend?

Issue 3: Was the payment in question a complete termination of the taxpayer/shareholder's interest, and therefore, to be treated as a qualifying redemption (i.e., sale)?

- d. **Issue:** Whether Code § 704(d) allows a former partner to deduct his payment to the partnership of a portion of his distributive share of partnership losses, which was not previously deductible while he was a partner because the basis of his partnership interest was zero.
- e. **Issue:** Whether the taxpayer permitted its earnings and profits to accumulate beyond the reasonable needs of the business. (Note that this case is similar to the *Battelstein Investment Co.* case cited in a above.)
- f. **Issue 1:** Whether the taxpayer is entitled to an interest deduction under Code § 163(a).

Issue 2: Whether the incorporating shareholders' 1968 advances to the corporation (the petitioner in this case) are considered bona fide loans or contributions to capital.

- g. Permanent citation should be 1985-1 C.B. 184.

Issue 1: Whether a grantor's receipt of the entire corpus of one irrevocable trust in exchange for an unsecured promissory note given to the trustee, the grantor's spouse, constituted an indirect borrowing of the trust corpus that caused the grantor to be the owner of the entire trust under § 675(3).

Issue 2: To the extent that a grantor is treated as the owner of a trust, whether the trust will be recognized as a separate taxpayer capable of entering into a sales transaction with the grantor. h. Permanent citation should be 1985-2 C.B. 716. This Revenue Procedure increases the operational standard mileage rate for the business use of an automobile and for when the automobile is used to render gratuitous service to a charitable organization.

- i. Permanent citation should be 84 T.C. 210.

Issue 1. Whether the taxpayers were engaged in an enterprise entered into for profit or whether their activity amounted to a hobby.

Issue 2. Whether certain nonrecourse notes may be included in the basis of equipment acquired by the taxpayer.

- j. Permanent citation should be 1986-2 C.B. 62.

Issue: Under a given set of circumstances, may a lump sum cash distribution from a deferred plan be rolled over tax-free into an IRA?

- k. Permanent citation should be 106 U.S. 522.

Issue: May a casino, on the accrual basis, deduct amounts guaranteed for payment on "progressive" slot machines but not yet won by playing patrons?

1. **Issue:** Issues relating to a spin-off of a corporate subsidiary.

2-30 T should be advised that he is not eligible for an office in the home deduction.

Section 280A provides that a taxpayer may take expenses incurred in the use of his or her home for business purposes if such expenses are attributable to the portion of the home used exclusively and regularly as

1. The principal place of business for any trade or business of the taxpayer;
2. A place of business that is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his or her trade or business; or
3. A separate structure, not attached to the dwelling unit, that is used in the taxpayer's trade or business.

First, this taxpayer probably fails the "exclusive use" test by using the den of his home for his work. The "exclusive use" test is strictly interpreted, so the use of the business portion of a home by the taxpayer or members of his family for purposes not related to business will result in the disallowance of the business expense deductions. Second, this taxpayer does not use his home office as the principal place of business in meeting or dealing with patients, clients, or customers in the normal course of his trade or business. It appears that the work the taxpayer brings home is simply additional work connected to the work he does during the day at the office. Third, the taxpayer has an office provided by his employer available to him at all times. There is case precedent holding that lack of amenities during the weekend and after hours does not produce an office in the home deduction for a taxpayer who chooses to work at home rather than in his or her office.

Because this is the first legal research problem the student has ever done, the

instructor should check the work as follows:

1. Make sure the citations are correct.
2. Correct spelling, punctuation, and grammar; and stress that unless the research is well-organized and well-written, it will never be read.

The instructor might also wish to introduce § 280A's treatment in CCH or RIA here by bringing the appropriate volume to class and going through its organization.

2-31 This research project is open-ended and therefore has no printed solution. The quality of the article depends on the extent of tax journals held by your library. The instructor is encouraged to evaluate the writing skills of the student as well as the quality of their tax research.

2-32 Answers to this question should be fairly standard because the legal issue is a relatively simple one. The student should show some ability to read and analyze the appropriate cases. Most students will find the cases through CCH or RIA. The instructor should stress that the cases themselves should be read and not simply the summaries in the reporters. Emphasis should be placed on evaluating the student's writing skills. The instructor should stress that the use of English writing skills is absolutely necessary in order to be an effective tax researcher. If time permits, the instructor should discuss the student's paper on an individual basis, since students vary so greatly in writing skills and analytical ability.

The following themes, based on the student's analysis of § 213, should be fairly standard in most papers:

- a. The expenditure is deductible to the extent it exceeds the increase in fair market value. Most of the cases on point support this deduction.
- b. Is the doctor's "strong recommendation" enough to sustain this deduction? Is something stronger required?
- c. Is the fact that there are no swimming pools nearby relevant?
- d. Will the courts question the \$15,000 expenditure? Can she obtain almost the same kind of facility for a lot less money?

Code § 213(a) provides a deduction for expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer. The Regulations at Reg. § 1.213-1(e)(1)(iii) provide that capital expenditures are generally not deductible for Federal income tax purposes. However, an expenditure that otherwise qualifies as a medical expense under § 213 shall not be disqualified merely because it is a capital expenditure.

The Internal Revenue Service itself has allowed a deduction in the case of

swimming pools. Rev. Rul. 83-33, 1983-1 C.B. 70 (modifying Rev. Rul. 54-57, 1954-1 C.B. 67) allowed a deduction for the cost of constructing a special exercise or lap pool to treat severe osteoarthritis. The amount of the deduction was the expenditure in excess of the resulting increase in the value of the taxpayer's related property. The Seventh Circuit has agreed with this approach in *C. H. Ferris*, 78-2 USTC ¶19646, 582 F.2d 1112 (CA-7, 1978), rev'g and rem'g 36 TCM 765. In *Ferris*, the taxpayer built a swimming pool for therapeutic purposes. The Appeals Court held that the taxpayer was entitled to a deduction for the minimally reasonable cost of a functionally adequate pool. Additionally, costs related to luxuries unrelated to the therapeutic use of the pool were disallowed. The Tax Court is in agreement with this approach, and has held (under similar circumstances) that the taxpayer is entitled to deduct the cost of building a swimming pool used for medical purposes to the extent that such costs exceed the amount by which the addition of the pool had increased the fair market value of the home. (See *C. L. W. Haines*, 71 T.C. 644, and *R A. Polacsek*, 42 TCM 1289.)

- 2-33 This problem should further introduce the beginning student to elements of tax research. Instructors should check students' writing style in addition to the technical tax analysis. Technically, the obstacle this taxpayer will encounter is that this course is part of an overall program of study that will prepare him for a new trade or business. [See Reg. § 1.162-5(b)(3).]

The cases the students will uncover will be against this taxpayer. [See *David Roeberg*, 29 TCM 1007, T.C. Memo 1970-236, and *Danielson v. Quinn*, 45 AFTR2d 80-1555, 482 F. Supp. § 275 (DC, 1980).]

The dicta in these and other cases may contain rays of hope for the taxpayer, but they are slight indeed when compared to the overwhelming authority against deductibility. You might ask the student if there is any hope for this taxpayer, and whether a tax preparer could ethically prepare a return if the client insists on taking this deduction.

2

Tax Practice and Research

Test Bank

True or False

- _____ 1. Once a tax law is enacted by Congress, any official interpretations of the law are by subsequent court decisions.
- _____ 2. The House Ways and Means Committee holds hearings on proposed revenue bills initiated by the Senate.
- _____ 3. The primary purpose of IRS regulations is to answer questions from taxpayers concerning specific tax problems.

- _____4. Although temporary regulations have the same binding effect as final regulations, proposed regulations have no force or effect.
- _____5. Unlike interpretative regulations, legislative regulations are not controlling on a court. Thus, the courts will not hesitate to substitute their own judgment for that of the Treasury Department.
- _____6. Both revenue rulings and revenue procedures are first published in the *Internal Revenue Bulletin* and then eventually published in the *Cumulative Bulletin*.
- _____7. The Internal Revenue Service may exercise discretion in determining whether to issue a letter ruling to a particular taxpayer.
- _____8. A letter ruling, or private ruling, is an individual response to a taxpayer, and it is generally understood to apply to all taxpayers.
- _____9. The three trial courts where tax matters may be litigated—the U.S. District Court, the U.S. Court of Federal Claims, and the U.S. Tax Court—are all courts of original jurisdiction.
- _____10. In the Small Claims Section of the U.S. Tax Court, the taxpayer forgoes the right to appeal the decision if she or he loses.
- _____11. An appeal of an adverse decision by the Tax Court may be taken as a matter of right to the appropriate U.S. Court of Appeals.
- _____12. Under the *Golsen* rule, the Tax Court follows the decisions of the Circuit Court to which a particular case would be appealed.
- _____13. It is not possible for the Appellate Court to affirm the decision of a lower court on one particular issue and reverse it on another.
- _____14. A Writ of Certiorari is the means by which the United States Court of Appeals grants review to a decision of the Tax Court.
- _____15. In the following citation, *Eugene Coloman*, 33 TCM 411, T.C. Memo ¶974-78, affd. in 76-2 USTC 19581, 38 AFTR2d 76-5523, 540 F.2d 427 (CA-9, 1976), the researcher would know that the original decision in the trial court was made by the Tax Court in a memorandum decision and that the case on appeal was affirmed by the Ninth Circuit, U.S. Court of Appeals.
- _____16. The IRS announces its acquiescence or nonacquiescence to the memorandum decisions of the Tax Court.
- _____17. A major difference between primary authorities and secondary authorities is that secondary sources are merely unofficial interpretations

of tax law and have no legal authority.

- _____ 18. A tax service has limited value because it only summarizes court decisions on a particular point of tax law.
- _____ 19. For a tax researcher, the weight (or value) accorded a particular court decision often may be determined by the reliance placed on that decision by other courts.
- _____ 20. Taxpayers are subject to a penalty if there is a substantial underestimate of tax attributable to a particular treatment for which they have no substantial authority, unless the treatment is disclosed on the tax return.

Multiple Choice

- _____ 21. The body or group that generally initiates revenue bills is
- a. The IRS
 - b. The House of Representatives
 - c. The Senate
 - d. The Joint Conference Committee on Taxation
 - e. The Ways and Means Committee
- _____ 22. Which of the following sources of authority would *most likely* contain a review of Congress's intentions with respect to a particular piece of tax legislation?
- a. Internal Revenue Code
 - b. Report of the House Ways and Means Committee
 - c. *Code of Federal Regulations*
 - d. Revenue procedures
 - e. Technical advice memoranda
- _____ 23. For the most accurate indication of Congressional intent for the enactment of a particular tax bill, a researcher would most likely consult the
- a. Report issued by the House Ways and Means Committee
 - b. Report issued by the Senate Finance Committee

- c. Report issued by the Joint Conference Committee on Taxation
- d. Records of debate on the bill
- e. Regulations and rulings of the Internal Revenue Service

- _____ 24. Which of the following statements is not a characteristic of the Internal Revenue Code?
- a. The basis of Congressional authority for the Federal income tax is the Sixteenth Amendment to the U.S. Constitution.
 - b. Changes made in the tax law after 1986 are incorporated into the *1986 Code as amended*.
 - c. Any change in the Internal Revenue Code generally starts in the House of Representatives.
 - d. When a tax advisor is citing a particular item within the Internal Revenue Code, citation of the section number alone is usually sufficient.
 - e. The reasons why Congress made a particular change or addition to the Internal Revenue Code are given within the Code itself.
- _____ 25. Which of the following administrative interpretations would be generally accorded the force and effect of law?
- a. Technical advice memoranda
 - b. Interpretative regulations
 - c. Letter rulings
 - d. Procedural regulations
 - e. Legislative regulations
- _____ 26. Which of the following best describes IRS interpretative regulations?
- a. They are binding on both the IRS and the courts.
 - b. They commit the IRS to a particular position on the Code.
 - c. They apply only to the particular person for whom they were written.
 - d. Both a. and b.
- _____ 27. Which one of the following types of Regulations *cannot* be cited as

authoritative?

- a. Proposed regulations
- b. Temporary regulations
- c. Procedural regulations
- d. Interpretative regulations
- e. Legislative regulations

_____ 28. Temporary regulations are generally issued

- a. Shortly after enactment of a major change in the tax law so that a taxpayer has guidance until final regulations are formulated
- b. To clarify existing regulations that are incomplete
- c. To deal with taxpayers living temporarily overseas who may be subject to tax treaties between the United States and foreign countries
- d. To define tax treatment for a general set of facts on which the Code is silent; they have the full force and effect of law until the Code addresses the issue
- e. To interpret the Code, but they do not have the same binding effect as final regulations

_____ 29. The difference between regulations and revenue rulings is that

- a. Revenue rulings are not limited to a given set of facts and regulations are limited.
- b. Revenue rulings are the direct law-making powers of Congress and regulations are not.
- c. Rulings require approval by the Secretary of the Treasury; regulations do not.
- d. Revenue rulings do not have the authority of regulations; regulations are a direct extension of the law-making powers of Congress.
- e. Only regulations are official pronouncements of the National Office of the IRS.

_____ 30. Which one of the following authorities is *not* correctly paired with a source where that authority might be found?

- a. Revenue procedures may be found in the *Cumulative Bulletin*.
- b. Legislative regulations may be found in the *Code of Federal Regulations*.
- c. Revenue rulings may be found in the *Internal Revenue Bulletin*.
- d. Revenue procedures may be found in the *Internal Revenue Bulletin*.
- e. Letter rulings may be found in the *Code of Federal Regulations*.

- _____ 31. Taxpayers who are in doubt about the particular tax consequences of a contemplated transaction may ask the IRS for a ruling on the tax question involved. Which one of the following statements is *not* true?
- a. The IRS may decline to issue a letter ruling.
 - b. Letter rulings apply only to the particular taxpayers with a particular set of facts asking for the ruling.
 - c. During the process of obtaining a ruling, the IRS may recommend changes in a proposed transaction to assist taxpayers in reaching the result they wish.
 - d. Letter rulings are available in digest form to allow other taxpayers to cite them as authority when they match the particular set of facts for which the letter ruling was issued.
 - e. None of the above; all are true.

- _____ 32. Letter ruling 201008048 was issued in which of the following months
- a. January 2010
 - b. February 2010
 - c. March 2010
 - d. April 2010
 - e. May 2010

- _____ 33. Before litigating a tax case in court, the taxpayer must
- a. Have exhausted the required administrative remedies available within the IRS
 - b. Convince the judiciary branch that the IRS misinterpreted tax law or wrongly applied it to the taxpayer's case

- c. Try to find a similar court decision from the past and present the case to that Court
- d. Enter into agreement with the IRS to use the Court as arbiter
- e. Not be guilty of fraud in the original or amended return at issue

- _____ 34. Which of the following could be a reason for a taxpayer not taking his tax case to a federal court of appeals?
- a. Too expensive
 - b. Failure to exhaust all the administrative remedies
 - c. No appealable decision from a trial court
 - d. All of the above
- _____ 35. The trial court that a taxpayer may *not* select is
- a. The Tax Court
 - b. The U.S. District Court
 - c. The U.S. Court of Federal Claims
 - d. The U.S. Court of Appeals
- _____ 36. Which of the statements below is *not* a characteristic of the Tax Court?
- a. Appeal is taken to the U.S. Court of Appeals.
 - b. A jury trial is not available.
 - c. The Court accepts only tax cases.
 - d. Taxpayers must pay the alleged deficiency and then sue for a refund.
 - e. The Court has nationwide jurisdiction.
- _____ 37. Which of the following is *not* a characteristic of U.S. District Courts?
- a. A District Court is not a national court.
 - b. A taxpayer need not pay any alleged deficiency in order to bring an action against the IRS.
 - c. The District Court hears many kinds of cases, including but not limited to tax cases.

- d. The District Court judges are appointed for life.
- e. The taxpayer may obtain a jury trial; the jury decides matters of fact but not matters of law.

_____38. A taxpayer may take a case into the District Court

- a. Only in the district where he or she resides
- b. Only if the disputed tax deficiency has not been paid
- c. Only to appeal the decision of the Tax Court or U.S. Court of Federal Claims
- d. Only if a Writ of Certiorari is granted
- e. Only if the Tax Court or U.S. Court of Federal Claims declines to hear the case

_____39. Although the Small Claims Section of the U.S. Tax Court allows a taxpayer to obtain a decision with little formality or expense, a disadvantage is that

- a. The taxpayer loses the right to appeal the decision.
- b. The case can be remanded to Tax Court.
- c. Special judges outside their area of expertise may be ruling.
- d. Priority on the trial calendars is not received.
- e. Cases eligible to be tried by the Court are limited to tax assessments of \$50,000 or less.

_____40. Which one of the following authorities is *not* correctly paired with a reporter or case system where that authority might be found?

- a. Regular decisions of the United States Tax Court may be found in the United States Tax Court Reports.
- b. A tax decision of the Court of Federal Claims may be found in the U.S. Tax Cases.
- c. A decision of the Small Claims Section of the Tax Court may be found in the United States Tax Court Reports.
- d. A decision of the Supreme Court of the United States may be found in the Supreme Court Reports (U.S.).

- e. A tax decision of the Court of Federal Claims may be found in the American Federal Tax Reports.

- _____ 41. Which one of the following is *not* true of the Supreme Court's appellate jurisdiction?
- a. Most of the time the Supreme Court indicates that it will accept a case by granting a Writ of Certiorari.
 - b. The Supreme Court reviews many tax cases during the year because of their national importance.
 - c. The Supreme Court often accepts cases when two or more Courts of Appeals are in conflict over an issue.
 - d. The Supreme Court does not conduct another trial but reviews the record of the trial court to determine if that court correctly applied the law to the facts.
 - e. The Supreme Court may accept a case where a Court of Appeals has settled an important question of Federal law and the Supreme Court feels such a question should have another review.
- _____ 42. In general, the Supreme Court only hears tax cases when one or more of certain conditions apply. These conditions *exclude* which of the following?
- a. The Courts of Appeals are in conflict on an issue.
 - b. A decision of a Court of Appeals is in apparent conflict with a decision of the Supreme Court.
 - c. The Supreme Court has already decided an issue but feels that the issue should be looked at again, possibly to reverse its previous decision.
 - d. The tax deficiency involved exceeds \$100,000.
 - e. The Court of Appeals has not used accepted or usual methods of judicial procedure or has sanctioned an unusual method by the trial court.
- _____ 43. Which of the following is *not* true of the Supreme Court's appellate jurisdiction?
- a. All cases reach the Supreme Court through the Court's granting a Writ of Certiorari.

- b. The Supreme Court will not hold another trial but merely reviews the records of the lower courts.
- c. Review by the Supreme Court is almost entirely discretionary.
- d. For most taxpayers, the final review is at the Court of Appeals level because the Supreme Court does not hear many tax cases.
- e. The Supreme Court's decision not to grant a Writ of Certiorari means that the decision of the lower court still stands.

- _____ 44. All of the following citations are to trial court decisions *except*
- a. *George E. Jones*, 21 B.T.A. 431 (1940)
 - b. *Harper Smith*, 511 F.2d 212 (CA-3, 1978)
 - c. *Jerome Prizant*, 30 TCM 817
 - d. *George F. Dowell v. U.S.*, 370 F. Supp. 69 (D. Ct. Tx, 1974)
 - e. *Raymond R. Windle*, 65 T.C. 483
- _____ 45. Which one of the following is *not* a citation to a Tax Court decision?
- a. *Simon Shield v. U.S.*, 19-1 USTC ¶8431
 - b. *Robert L. Lynch*, 84 T.C. _____, 29 (1984)
 - c. *James Pretzfelder*, T.C. Memo 1983-147
 - d. *Timothy Kirby*, 47 TCM 814
 - e. *Simpson Dean*, 35 T.C. 1083 (1961)
- _____ 46. Which of the choices below is the publisher in this citation: *Johnson v. Oregon*, 86-1, USTC ¶322 (D. Ct. Cal, 1986).
- a. Commerce Clearing House
 - b. Prentice Hall
 - c. West Publishing Co.
 - d. Research Institute of America
 - e. Senate Finance Committee
- _____ 47. Which one of the following is *not* a secondary source of tax authority?

- a. *The Accountant's Index*, American Institute of Certified Public Accountants
- b. Kulsrud, "The Alternative Minimum Tax: Its Operation and Effect after TEFRA," *The Review of Taxation of Individuals*, 1 (Summer, 1983)
- c. *Crane v. Comm.*, 47-1 USTC 9217, 35 AFTR 776, 331 U.S. 1 (USSC, 1947)
- d. Harris, "The Effect of the Installment Sales Revision Act of 1980 on Like-Kind Exchanges: Non-simultaneous Exchanges Reviewed," *Taxes—The Tax Magazine*, (July, 1981)
- e. *The Tax Law Review*

- _____ 48. Which one of the following is *not* a primary authority of tax law?
- a. Code § 1245(b)(3)
 - b. Regulations § 1.47-3(f)(2)
 - c. *May v. U.S.*, 81-1 USTC ¶9286, 47 AFTR2d 81-1124, 644 F.2d 578 (CA-6, 1981)
 - d. Bailey, "Using Voting Preferred Stock to Avoid CFC Status," *The International Tax Journal* 2 (January 1976) pp. 101-13
 - e. Revenue Rul. 80-219, 1980-2 C.B. 18
- _____ 49. Tax periodicals are an important source of information for the tax practitioner. Which of the following is *not* true about tax periodicals?
- a. They may be cited as authority in disputes with the IRS during administrative review or appeal.
 - b. They may give insight into recent court interpretations of tax laws.
 - c. They may provide question and answer sections to ensure that the reader comprehends the concepts and ramifications of recent rulings.
 - d. They generally offer concise summaries of new tax laws.
 - e. They serve to convey new tax planning opportunities.
- _____ 50. When researching a complex tax question, a researcher with little previous experience with the issue would be best served at the outset by consulting

- a. The Internal Revenue Code
- b. The Treasury Regulations
- c. The applicable legislative history
- d. A "tax service" (e.g., CCH, RIA)

- _____ 51. After completing basic research on a tax question, but before acting on the results of this research, it is wise to
- a. Check the newest updates to the "tax services."
 - b. Run a search on *LEXIS* or *WESTLAW* for the period not covered by your research sources.
 - c. Send a copy of the research to the IRS for validation.
 - d. Both a. and b.
- _____ 52. After doing extensive research on a tax question that involved certain matters that did not fall into established guidelines, the tax researcher made a filing that was based on what he reasonably believed the current law to be. This interpretation resulted in a substantial tax savings for his client. The return
- a. Should contain a statement disclosing the manner in which the "grey" tax question was treated
 - b. Should not contain any reference to a "grey" tax area in order to avoid arousing the IRS's curiosity
 - c. Should not be filed if any of it is based on assumptions by the tax researcher on what the law is "likely to be"
 - d. Both b. and c.
- _____ 53. Which of the following is true of revenue rulings?
- a. Although they represent the official policy of the IRS, courts may overrule them.
 - b. Lower courts are bound by them.
 - c. They are a subset of Treasury Regulations.
 - d. Once affirmed by an appellate court, they have the force of law.
 - e. All of the above are true.

- _____ 54. Which of the following statements is false?
- a. Tax benefits of an otherwise legal transaction may be denied if it lacks economic substance.
 - b. The economic substance doctrine is similar to the business purpose doctrine.
 - c. Reducing taxes is a good business purpose under the economic substance doctrine.
 - d. A transaction has economic substance if it changes the taxpayer's economic position or the taxpayer has a substantial business purpose.
 - e. More than one of the above statements is false.
- _____ 55. ASC 740 deals with which of the following.
- a. The financial accounting treatment of transactions that lack business purpose
 - b. The economic substance doctrine
 - c. The financial reporting of uncertainty related to positions taken in a tax return
 - d. None of the above
- _____ 56. Under ASC 740, a tax position is recognized for financial accounting purposes if it meets which of the following standards.
- a. More likely than not
 - b. Realistic possibility of success
 - c. Reasonable basis
 - d. None of the above
- _____ 57. In this year's tax return, T Corporation decided to account for certain international transactions in a specific matter. However, the tax treatment is not certain and there is a chance that if audited, the company would not prevail. Which of the following statement is false regarding the corporation's requirement to report the transaction for tax purposes (i.e., file Schedule UTP)?
- a. The corporation need not file if its assets are less than \$100 million.
 - b. The corporation need not file if it is an S corporation.

- c. The corporation need not file if it did not record a reserve for the position in its audited financial statements.
- d. The corporation need not file if it did not issue audited financial statements.
- e. More than one of the above is false.

ANS: True or False

1. False. Court decisions, IRS regulations and rulings also interpret tax laws. (See p. 2-6 and pp. 2-12 through 2-16.)
2. False. The House Ways and Means Committee structures a proposed bill initiated by the House of Representatives before it is presented for vote by the full House. (See pp. 2-6 and 2-7.)
3. False. The primary purpose of the Regulations is to explain and interpret particular Code sections. (See pp. 2-12 and 2-13.)
4. True. Temporary regulations have the same binding effect as final regulations until they are withdrawn or replaced. Proposed regulations have no force or effect; however, they do provide insight into how the IRS currently interprets a particular Code Section. (See p. 2-12 and 2-13.)
5. False. Legislative regulations have the force and effect of law. A court reviewing the regulations usually will not substitute its judgment for that of the Treasury Department unless the Treasury has clearly abused its discretion. (See p. 2-13.)
6. True. Revenue rulings and revenue procedures are published in the weekly issues of the *Internal Revenue Bulletin*, and then are published semiannually in the *Cumulative Bulletin*. (See p. 2-15.)
7. True. The IRS has discretion about whether to rule or not and has issued guidelines describing the circumstances for which it will issue a ruling. (See p. 2-15 and 2-16.)
8. False. In fact, letter rulings apply only to the particular taxpayer asking for the ruling and are not applicable to all taxpayers. (See p. 2-15.)
9. True. The courts of original jurisdiction are the courts where litigation begins. The taxpayer has a choice of forums in which to begin litigation. Since it is only in the

- Tax Court that the taxpayer may litigate without paying the tax deficiency, most tax matters are litigated in this court. (See pp. 2-17 and 2-18.)
10. True. By electing to use the Small Tax Division of the Tax Court, the taxpayer is able to obtain a decision with a minimum of formality, delay, and expense. However, the taxpayer must give up the right to appeal. (See p. 2-18.)
 11. True. If the taxpayer or government disagrees with the decision by the trial court, both parties may appeal to the Courts of Appeal as a matter of right and the courts must hear their cases. (See p. 2-17.)
 12. True. This practice is followed even if the Tax Court disagrees with a Circuit Court's view. See *Jack E. Golsen*, 54 T.C. 742 (1970). (See p. 2-19.)
 13. False. It is possible for the Appellate Court to affirm the decision of the lower court on one particular issue and reverse it on another. This is not a particularly unusual situation. Another possibility is for the Appellate Court to remand the case for another trial or for rehearing on another point not previously covered. (See p. 2-21.)
 14. False. Cases may be submitted to the Supreme Court of the United States through a request known as a Writ of Certiorari. If the Supreme Court decides to hear the case, it grants the Writ of Certiorari. If it decides not to hear the case, it denies the Writ of Certiorari. (See p. 2-21.)
 15. True. The case was originally decided in the Tax Court as a memorandum decision and was subsequently appealed to the Ninth Circuit Court of Appeals, which affirmed the Tax Court. (See pp. 2-29 and 2-30.)
 16. False. The IRS had adopted the practice of announcing its acquiescence to the *regular* decisions of the Tax Court. The IRS does not follow this practice for the decisions of the other courts or even for the memorandum decisions of the Tax Court. (See p. 2-22.)
 17. True. Secondary sources of tax information consist of books, periodicals, articles, newsletters, and editorial judgments. They have no binding legal authority, but are often consulted because they contain explanations of positions on important tax questions. (See p. 2-25.)
 18. False. A tax service generally contains either excerpts from or citations to the Code, Regulations, Court decisions, IRS releases, and explanations of these primary authorities by the editors. (See pp. 2-25 and 2-26.)
 19. True. The validity or value of a particular decision may be assessed by examining how the courts in subsequent cases viewed the cited decision. For example, subsequent cases may have agreed with, disagreed with, or distinguished the decision in question. (See p. 2-29.)

20. True. According to § 6662, "substantial authority" is difficult to define, but the standard probably lies somewhere between "reasonable support" and "more likely than not." (See pp. 2-34 through 2-35.)

Multiple Choice

21. b. The House of Representatives has the basic responsibility for initiating revenue bills. Tax bills generally do not originate in the Senate except when they are attached to other bills. The Ways and Means Committee considers and structures bills before they are presented for vote by the full House of Representatives, but the committee members do not initiate the bills. (See p. 2-6.)
22. b. Committees of Congress often generate records of the debates on a tax bill that are quite helpful in determining Congress's intention with respect to a particular piece of legislation. The House Ways and Means Committee, the Senate Finance Committee, and the Joint Conference Committee on Taxation all issue "committee reports" that at times may be helpful to the tax researcher trying to determine legislative intention. (See pp. 2-7 and 2-8.)
23. a. All of the choices, except e, shed light on the Congressional intent of a particular bill. However, the report issued by the House Ways and Means Committee provides the historical background of the proposed legislation along with the reasons for enactment and is usually one of the better sources of Congressional intent. (See pp. 2-7 and 2-8.)
24. e. Reasons for changes or additions are not given within the Internal Revenue Code itself. However, Congressional committees involved in the passage of the tax law changes often issue committee reports detailing the reasons for the change and Congressional intent in making the changes. These sources are very helpful to a researcher who is trying to determine Congressional intent for purposes of statutory interpretation. (See p. 2-6.)
25. e. Quite often, legislative regulations occur when there are virtually no Code sections governing the area such as consolidated returns. In these situations, the regulations in effect serve in lieu of the Code (e.g., the regulations dealing with filing a consolidated tax return). In this case and others where it occurs, the regulation has the force and effect of a law. A court reviewing the regulation will not substitute its judgment for that of the Treasury Department unless the Treasury has clearly abused its discretion. (See p. 2-13.)
26. b. Interpretative regulations do not have the force of law that legislative regulations do, but they nevertheless bind the IRS to a particular position. (See p. 13.)
27. a. Proposed regulations have no force or effect and are issued to elicit comment from interested parties. They can provide insight into how the IRS currently interprets a particular Code section but cannot be cited as authoritative. (See p. 2-13.)

28. a. Temporary regulations are issued after the enactment of a major change in tax laws. These temporary regulations have the same binding effect as final regulations until they are withdrawn or replaced. (See p. 2-13.)
29. d Regulations are a direct extension of Congressional authority whereas revenue rulings are an application of the administrative powers of the IRS. (See pp. 2-14 and 2-15.)
30. e Letter rulings appear in digests published by the leading tax commentators and publishers such as Commerce Clearing House and RIA. The *Code of Federal Regulations* reprints regulations but not letter rulings. (See p. 2-16.)
31. e All of the statements regarding private letter rulings are true. (See p. 2-15.)
32. b Citations for letter rulings and technical advice memorandums follow a multi-digit file number system. The IRS letter ruling number system works this way: 2010 is the year; 08 is the week (eighth week in the year—February); 048 is the number of the ruling issued that week. (See p. 2-16.)
33. a If the taxpayer has not exhausted administrative remedies, a court will deny a hearing because the claim filed in the court is premature. (See p. 2-16.)
34. d The procedure for getting a tax case into a federal court of appeals is: (1) exhaust IRS administrative remedies, (2) litigate the issue in one of the available trial courts and obtain an appealable decision. If the taxpayer disagrees with the trial court's decision, he may appeal as a matter of right. (See pp. 2-16 through 2-19.)
35. d. Choices a., b. and c. are trial courts in which a taxpayer may "try" his or her case. The taxpayer may select any one (and only one) of these courts to hear the case. An appeal may then be made to either the U.S. Court of Appeals or the U.S. Court of Appeals for the Federal Circuit. (See pp. 2-17 and 2-18.)
36. d. The taxpayer need not pay the tax deficiency to be heard in the Tax Court. (See p. 2-17.)
37. b. A taxpayer may take a case to District Court *only* if the disputed tax deficiency has first been paid. The District Court is a national court of specific jurisdiction in which the taxpayer may obtain a jury trial. (See pp. 2-17 and 2-18.)
38. a. The taxpayer can take the case to the District Court only in the district in which he or she resides. In addition, the taxpayer must pay the disputed tax deficiency before bringing an action to court. (See p. 2-17.)
39. a The taxpayer *does* lose the right to appeal the decision if the ruling goes against him or her. (See p. 2-17.)
40. c Opinions of the judges of the Small Claims Section of the Tax Court are

- published separately and are not a part of United States Tax Court Reports. Small Claims decisions cannot be appealed and are not reviewed by any other court or treated as precedents in any other case. (See p. 2-18.)
41. b The Supreme Court generally reviews only a very small number of tax cases. Taxpayers desiring a review of their trial court decision usually find it at the Court of Appeals level. (See p. 2-21.)
 42. d There is no minimum dollar amount that limits the cases the Supreme Court selects for reviews. (See p. 2-21.)
 43. a This response is false because "review by Appeal" *may* be available when a U.S. Court of Appeals has held that a state statute is in conflict with the laws or treaties of the United States, or when the highest court of a state has decided a case on the grounds that a Federal statute is invalid. Review by the Supreme Court is still discretionary, but the Writ of Certiorari is not involved. (See p. 2-12.)
 44. b. Answer b is a citation for a decision of the United States Court of Appeals for the Third Circuit, which is not a Trial Court but an Appellate Court. The other citations are as follows:
 - a. Citation to the Board of Tax Appeals, predecessor to the Tax Court.
 - b. Citation to the Tax Court—a Memorandum decision.
 - c. Citation to the District Court.
 - d. Citation to the Tax Court—a Regular decision.(See pp. 2-21 through 2-24.)
 45. a. The citation in a is to *U.S. Tax Cases*, published by Commerce Clearing House. This reporter reprints tax cases decided by the District Courts, Courts of Appeals, Court of Federal Claims, and the Supreme Court. (See p. 2-23.)
 46. a. The capital letters "USTC" in the citation indicate that the court decision can be found in *U.S. Tax Cases*, published by the Commerce Clearing House. (See p. 2-23.)
 47. c. The statutory law and its official interpretations constitute the primary sources of tax authority. Included in this category are interpretations by the courts. Secondary sources consist mainly of books, periodicals, articles, newsletters, and editorial judgments in tax services. Secondary sources are unofficial interpretations—mere opinions—and have no legal authority. Primary sources are authoritative, although not all have the same strength. (See pp. 2-5 and 2-25.)
 48. d. The statutory law and its official interpretations constitute the primary

- authorities of tax law. Secondary authorities of tax law consist mainly of books, periodicals, articles, newsletters, and editorial judgments in tax services. Secondary authorities are merely opinions and have no legal authority. (See pp. 2-5 and 2-25.)
49. a. Tax periodicals are secondary sources of information and may *not* be cited as authority. However, they offer concise summaries of new tax laws in a readable format, the latest IRS and judicial interpretations, and new ideas for tax planning. (See pp. 2-25 and 2-26.)
 50. d. While the sources listed in a through c would provide valuable information to a researcher, a "tax service" is usually the best place to begin if the researcher needs to have some of the concepts fleshed out and to get a better idea of how the particular issue fits into the overall tax picture. (See pp. 2-25 and 2-26.)
 51. d. The well-known dictum that ignorance of the law is no defense requires the prudent researcher to check the latest possible developments in the tax area. This can be accomplished by consulting the updates to the tax services and, if available, checking recent tax cases on one of the legal services. (See pp. 2-26 and 2-31.)
 52. a. The substantial understatement penalty exists for taxpayers who substantially understate tax based on a particular interpretation of tax law for which substantial authority does not exist. The understatement is considered substantial if it exceeds the larger of (1) 10 percent of the correct tax or (2) \$5,000. The penalty can be avoided if the taxpayer discloses the particular treatment when he files his return. (See pp. 2-34 through 2-35.)
 53. a. Revenue rulings are the outcome of IRS administrative reviews of specific tax cases. In this respect, they are similar to decisions in legal cases. Such administrative decisions are subject to judicial review, and if a court determines that the IRS reached its decision in an arbitrary or capricious manner that was not based on the facts, it will overturn the ruling. Contrast the revenue ruling to a Treasury Regulation, which is more like a law, in that it applies to all taxpayers and only prospectively. Treasury Regulations may only be overruled by a court when they are in conflict with the Code. (See p. 2-14 through 2-15.)
 54. e. Reducing taxes is not considered a "business" purpose. The economic substance test is met only if a transaction meets both requirements, it changes the taxpayer's economic position and the taxpayer had a substantial purpose for entering the transaction (other than for federal income taxes). (See pp. 2-36 and 2-37.)
 55. c. ASC 740 addresses the reporting of uncertain tax positions for financial accounting purposes. (See p. 2-37.)
 56. a. A tax position is recognized for financial accounting purposes only if it is "more likely than not" (i.e., greater than 50 percent chance) that the position will

be sustained upon examination by a taxing authority. (See p. 2-38.)

57. c. Although the corporation did not record a reserve, it still may be required to file Schedule UTP if it plans on litigating the position. (See p. 2-38.)

Comprehensive Problems

1. *Note:* This problem requires the use of a complete tax library. The average student will spend from 3 to 5 hours researching and writing this paper.

Taxpayer R is a full-time non-tenured tax professor at PT University, located in Fairfax, Virginia. R teaches four classes per year at the Arlington Campus (15 miles from the main campus in Fairfax). R is provided with an office at PTU-Fairfax and is required to keep formal office hours (one hour per week) at this location. R is *not* provided with an office at the Arlington Campus.

R's job requirements include research (50% to performance evaluation), teaching (25% to performance evaluation), and university service (25% to performance evaluation).

All research must be done at the Arlington campus library because of the inadequacy of the Fairfax campus library. All student consultations and teaching occurs at the Arlington campus. Service activities require minimal time and are conducted at the Fairfax campus. Required office hours at the Fairfax campus are not utilized by students at the Arlington Campus.

The employer-provided office is 10' × 15' and is furnished with a desk, chairs, and a phone. The office is inadequate to Taxpayer needs for required research because the location is 15 miles from the Arlington campus library. In addition, the office is not convenient for consultations with students at the Arlington campus.

R spends approximately eight hours per week teaching and consulting with students. One hour per week is spent at the Fairfax campus in formal office hours plus three service committee meetings per year. The majority of R's time is spent doing research in his home office. This amounts to approximately five hours/day, 25 hours per week.

R's home office is a segregated portion of his basement and is exclusively and regularly used for PTU-related activities. The office is 20' × 25' and is furnished with a desk, chairs, bookshelves/books used for research, a copier, a computer, and a telephone.

R deducted home office expenses of \$1,500 on his 2009 return. The IRS sent a

Notice of Deficiency stating that the amount was not deductible and did not meet the requirements of Code § 280A.

Question to Be Researched: May R deduct his office in the home expenses? Discuss all issues of law in a well written essay setting forth the reasons for your conclusion. You should use the research techniques discussed in the text.

2

Solutions to Comprehensive Problems

1. Code § 262(a) provides that a deduction is not allowed for personal, living, and family expenses, including expenses and losses attributable to a dwelling that is occupied by a taxpayer as his or her personal residence. Code § 280(a) restates the general rule that a deduction is not allowed with respect to a dwelling unit that is used by the taxpayer as a residence, except as provided in Code § 280A. The balance of Code § 280A provides the circumstances under which a taxpayer may claim deductions with respect to a residence.

In this case of taxpayer who exclusively uses a portion of his or her dwelling unit on a regular basis as a principal place of business for any trade or business of the taxpayer an allocable portion of expenses attributable to the residence is allowed as a deduction. Section 280A provides that a home office will qualify as a principal place of business for deducting expenses for its use if:

- (1) The taxpayer uses it exclusively and regularly for administrative or management activities of his or her trade or business, and
- (2) The taxpayer has no other fixed location where you conduct substantial administrative or management activities of his or her trade or business.

To qualify for a home office deduction, a taxpayer who is an employee must establish that the home office is used for the convenience of the employer. [See § 280A(c)(1).] The proposed regulations give no insight into what will satisfy the convenience requirement. The legislative history indicates that use that is merely appropriate and helpful to the employer's business does not satisfy this requirement. [See S. Rep. 938, 94th Cong., 2d Sess. 147 (1976)]. It appears that the key to satisfying the convenience of the employer requirement is providing proof that the employer provides either no facilities or inadequate facilities for the employee to perform activities that are crucial for successful job performance.

Both the Second and Seventh Circuits have held that the taxpayer need not prove that the employer strictly requires the maintenance of a home office. It seems that the taxpayer must establish only that a home office was a practical necessity and that the taxpayer could not perform his duties properly without performing work at home. If the taxpayer's employer expects the taxpayer to perform at least a portion of his work at a location other than the employer's premises, it can be readily established that the home office was for the

convenience of the employer.

If, however, the employer provides adequate facilities, but permits the taxpayer to work at home, the office is maintained for the taxpayer's convenience, not the employer's. If an employer provides adequate facilities for an employee to do her job, the employer ordinarily will want the employee to use those facilities.

In *Drucker v. Commissioner*, 715 F.2d 67 (CA-2 1983), the Second Circuit held that three concert musicians could deduct the cost of maintaining space in their apartments used exclusively for musical study and practice because their employer did not provide them with space for the essential task of individual practice. Thus, the maintenance of practice space met the convenience of their employer test because the use of the home for music studies was a business necessity, not simply a matter of personal convenience.

In *Weissman v. Commissioner*, 751 F.2d 512 (CA-2 1984), the Second Circuit held that a college professor had satisfied the convenience of the employer test where the professor established that he maintained his home office due to the lack of private working space on campus. Setting aside an argument that convenience of the employer could be found only where no work space was provided by the employer, the Second Circuit stated that the relevant fact was that the employer provided no "suitable" space for engaging in necessary employment-related activities.

Bases on the authorities discussed above, it appears that where a college professor is not provided appropriate office space, as in the circumstances described in the facts, he or she may claim an office in the home deduction under § 280A.