

CHAPTER 1

UNDERSTANDING AND WORKING WITH THE FEDERAL TAX LAW

SOLUTIONS TO PROBLEM MATERIALS

DISCUSSION QUESTIONS

1. (LO 1) When enacting tax legislation, Congress often is guided by the concept of revenue neutrality so that any changes neither increase nor decrease the net revenues raised under the prior rules. Revenue neutrality does not mean that any one taxpayer's tax liability remains the same. Since this liability depends on the circumstances involved, one taxpayer's increased tax liability could be another's tax saving. Revenue-neutral tax reform does not reduce deficits, but at least it does not aggravate the problem.
2. (LO 2) Economic, social, equity, and political factors play a significant role in the formulation of tax laws. Furthermore, the IRS and the courts have had impacts on the evolution of tax laws. For example, control of the economy has been an important economic consideration in passing a number of laws (e.g., rapid depreciation, changes in tax rates). But, ultimately the tax law is written by Congress.
3. (LO 2) The tax law encourages technological progress by allowing immediate (or accelerated) deductions and tax credits for research and development expenditures.
4. (LO 2) Saving leads to capital formation and thus makes funds available to finance home construction and industrial expansion. For example, the tax laws provide incentives to encourage savings by giving private retirement plans preferential treatment.
5. (LO 2)
 - a. Section 1244 allows ordinary loss treatment on the worthlessness of small business corporation stock. Since such stock normally would be a capital asset, the operation of § 1244 converts a less desirable capital loss into a more attractive ordinary loss. Such tax treatment was designed to aid small businesses in raising needed capital through the issuance of stock.
 - b. The S corporation election allows the profits (or losses) of the corporation to flow through to its individual shareholders (avoiding the corporate income tax). In addition, the qualified business income deduction may apply to any flow-through profits (allowing a maximum 20% deduction to the shareholders). However, with the corporate tax rate being 21% (and individual marginal tax rates potentially being higher), individuals will need to compare the benefits of avoiding the corporate tax rate with the taxes on any S corporation flow-through profits.
6. (LO 2) Reasonable persons can, and often do, disagree about what is fair or unfair. In the tax area, moreover, equity is generally tied to a particular taxpayer's personal situation. For example, one equity difference relates to how a business is organized (i.e., partnership versus corporation). Two businesses may be equal in size, similarly situated, and competitors in the production of goods or services, but they may not be comparably treated under the tax law if one is a partnership and the other is a corporation. The corporation is subject to a separate Federal income tax of 21%; the partnership is not. The tax law can and does make a distinction between these business forms. Equity,

then, is not what appears fair or unfair to any one taxpayer or group of taxpayers. Equity is, instead, what the tax law recognizes.

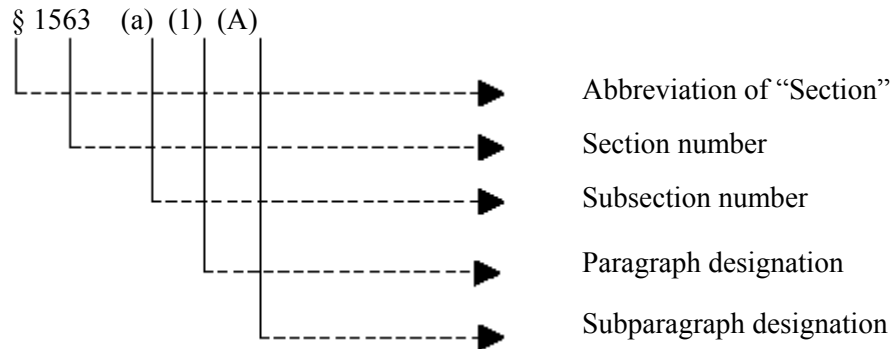
7. (LO 2) This deduction can be explained by social considerations. The deduction shifts some of the financial and administrative burden of socially desirable programs from the public (the government) sector to the private (the citizens) sector.
8. (LO 2) Preferential treatment of private retirement plans encourages saving. Not only are contributions to Keogh (H.R. 10) plans and certain Individual Retirement Accounts (IRA) deductible, but income from these contributions accumulates on a tax-free basis.
9. (LO 2) The availability of percentage depletion on the extraction and sale of oil and gas and specified mineral deposits and a write-off (rather than capitalization) of certain exploration costs encourage the development of natural resources.
10. (LO 2) Favorable treatment of corporate reorganizations provides an economic benefit. By allowing corporations to combine and split without adverse consequences, corporations are in a position to reduce their taxes and possibly more effectively compete with other businesses (both nationally and internationally).
11. (LO 2) Although the major objective of the Federal tax law is the raising of revenue, other considerations explain many provisions. In particular, economic, social, equity, and political factors play a significant role. Added to these factors is the impact the Treasury Department, the Internal Revenue Service, and the courts have had and will continue to have on the evolution of Federal tax law.
12. (LO 2) The deduction allowed for Federal income tax purposes for state and local income taxes is not designed to neutralize the effect of multiple taxation on the same income. At most, this deduction provides only partial relief. The \$10,000 overall limitation on state and local taxes also reduces the tax benefit of these taxes. Only allowing a full tax credit would achieve complete neutrality.
 - a. With the standard deduction, a taxpayer is, *indirectly*, obtaining the benefit of a deduction for any state or local income taxes he or she may have paid. The standard deduction is in lieu of itemized deductions, which include any allowed deductions for state and local income taxes.
 - b. If the taxpayer is in the 10% tax bracket, \$1 of a deduction for state or local taxes would save \$0.10 of Federal income tax liability. In the 32% tax bracket, the saving becomes \$0.32. The deduction approach (as opposed to the allowance of a credit) favors high-bracket taxpayers.
13. (LO 2) Under the general rule, a transfer of a partnership's assets to a new corporation could result in a taxable gain. However, if certain conditions are met, § 351 postpones the recognition of any gain (or loss) on the transfer of property by Heather to a controlled corporation.

The wherewithal to pay concept recognizes the inequity of taxing a transaction when Heather lacks the means with which to pay any tax. Besides, Heather's economic position would not change significantly should the transfer occur. Heather owned the assets before the transfer and still would own the assets after a transfer to a controlled corporation.
14. (LO 2) Yes, once incorporated, the business may be subject to the Federal corporate income tax. However, the 21% corporate tax rate *might* be lower than Heather's individual tax rates, especially if dividends are not paid to Heather.

The corporate income tax could be avoided altogether by electing to be an S corporation. An S corporation is generally not taxed at the corporate level; instead, the income flows through the corporate veil and is taxed at the shareholder level. An S election allows a business to operate as a corporation but be taxed like a partnership. With a partnership, there is no double tax. Income and expenses flow through to the partners and are taxed at the partner level.

15. (LO 2) Examples include like-kind exchanges, involuntary conversions, transfers of property to a controlled corporation, transfers of property to a partnership, and tax-free reorganization.
16. (LO 2) Generally, a recognized (taxable) gain cannot exceed the realized gain.
17. (LO 2) Recognition of gain ultimately occurs when the property is disposed of.
18. (LO 2) One year.
19. (LO 2) The installment method on the sale of property permits the gain to be recognized over the payout period.
20. (LO 2) Requiring a taxpayer to make a contribution to a Keogh retirement plan by the end of the year would force an accurate determination of net self-employment income long before the income tax return must be prepared and filed.
21. (LO 2) The difference between common law and community property systems centers around the property rights possessed by married persons. In a common law system, each spouse owns whatever he or she earns. Under a community property system, one-half of the earnings of each spouse is considered owned by the other spouse. Assume, for example, that Harold and Ruth are husband and wife and that their only income is the \$90,000 annual salary Harold receives. If they live in New York (a common law state), the \$90,000 salary belongs to Harold. If, however, they live in Texas (a community property state), the \$90,000 salary is divided equally, in terms of ownership, between Harold and Ruth.
22. (LO 2) Deterrence provisions include the following:
 - Alternative minimum tax.
 - Imputed interest rules.
 - Limitation on the deductibility of interest on investment indebtedness.
 - Gift and estate tax.
 - Unreasonable accumulated earnings tax.
 - Personal holding company tax.
23. (LO 4) Primarily concerned with business readjustments, the continuity of interest concept permits tax-free treatment only if the taxpayer retains a substantial continuing interest in the property transferred to the new business. Due to the continuing interest retained, the transfer should not have tax consequences because the position of the taxpayer has not changed. This concept applies to transfers to controlled corporations (Chapter 4), corporate reorganizations (Chapter 7), and transfers to partnerships (Chapter 10).
24. (LO 3) Under § 482, the IRS has the authority to allocate income and deductions among businesses owned or controlled by the same interests when the allocation is necessary to prevent the evasion of taxes or to clearly reflect the income of each business. Pursuant to § 482, therefore, the IRS might allocate interest income to White Corporation even though none was provided for in the loan agreement.
25. (LO 5) False. Federal tax legislation generally originates in the House of Representatives, where it is first considered by the House Ways and Means Committee. Only rarely does Federal tax legislation originate in the Senate. The Tax Equity and Fiscal Responsibility Act of 1982 originated in the Senate; its constitutionality was upheld by the courts.
26. (LO 5) A President's veto can be overridden by a two-thirds vote in both the House and Senate.

27. (LO 5)



28. (LO 5) Yes. Some Code Sections omit the subsection designation and use, instead, the paragraph designation as the first subpart [e.g., §§ 212(1) and 1221(1)].

29. (LO 5) When the 1954 Code was drafted, the omission of some Code section numbers was intentional. This omission provided flexibility to incorporate later changes into the Code without disrupting its organization. This technique is retained in the 1986 code.

30. (LO 6) Proposed, final, and Temporary Regulations are published in the *Federal Register* (**federalregister.gov**) and are reproduced in major tax services. Final Regulations are issued as Treasury Decisions (TDs).

31. (LO 6)

- a. A Temporary Regulation, with 1 referring to the type of regulation (i.e., income tax), 707 is the related code section number, 5 is the subsection number, T means temporary, (a) is the paragraph designation, and (2) is the subparagraph designation.
- b. Revenue Ruling number 11, appearing on page 174 of Volume 1 of the *Cumulative Bulletin* issued in 1960.
- c. Technical Advice Memorandum number 3 issued during the 37th week of 1988.

32. (LO 5) Raabe, Young, Hoffman, Nellen, & Maloney, CPAs
5191 Natorp Boulevard
Mason, OH 45040

October 18, 2019

Ms. Jennifer Olde
3246 Highland Drive
Clifton, VA 20124

Dear Ms. Olde:

In response to your recent request, the fact-finding determination of a lower trial court is binding on a Federal Court of Appeals. A Federal Court of Appeals is limited to a review of the record of trial compiled by a trial court. Rarely will an appellate court disturb a lower court's fact-finding determination.

Should you need more information, do not hesitate to contact me.

Sincerely,

Marilyn S. Crumbley
Tax Partner

33. (LO 5)
TAX FILE MEMORANDUM

DATE: September 4, 2019

FROM: Sarah Flinn

RE: Telephone conversation with Will Thomas regarding the failure of the IRS to appeal

I explained to Mr. Thomas that there were numerous reasons why the IRS may decide not to appeal a decision it loses in a District Court. For example, the workload may be too heavy. Or the IRS may have decided that this particular case is not a good decision to appeal (e.g., sympathetic taxpayer). Third, the IRS might not want to appeal this case to the appropriate Court of Appeals. I stressed that the failure to appeal does not necessarily mean that the IRS agrees with the results reached.

34. (LO 5, 8)
- a. If the taxpayer decides to choose a District Court as the trial court for litigation, the District Court of Utah would be the forum to hear the case. Unless the prior decision has been reversed on appeal, one would expect the same court to follow its earlier holding.
 - b. If the taxpayer decides to choose the Court of Federal Claims as the trial court for litigation, the decision previously rendered by this Court should have a direct bearing on the outcome. If the taxpayer selects a different trial court (i.e., the appropriate U.S. District Court or the U.S. Tax Court), the decision rendered by the Court of Federal Claims would be persuasive but not controlling. It is assumed that the results reached by the Court of Federal Claims were not reversed on appeal.
 - c. The decision of a Court of Appeals will carry more weight than one rendered by a trial court. Since the taxpayer lives in California, however, any appeal from a District Court or the U.S. Tax Court would go to the Ninth Court of Appeals. Although the Ninth Court of Appeals might be influenced by what the Second Court of Appeals has decided, it is not compelled to follow such holding.
 - d. Since the U.S. Supreme Court is the top appellate court, complete reliance can be placed on its decisions. Nevertheless, one should investigate any decision to see whether the Code has been modified to change the results reached. The rare possibility also exists that the Court may have changed its position in a later decision.
 - e. When the IRS acquiesces in a decision of the Tax Court, it agrees with the results reached. As long as such acquiescence remains in effect, taxpayers can be assured that this represents the position of the IRS on the issue involved. Keep in mind, however, that the IRS can change its mind and can, at any time, withdraw the acquiescence and substitute a nonacquiescence.
 - f. The issuance of a nonacquiescence reflects that the IRS does not agree with the results reached by a Tax Court decision. Consequently, taxpayers are placed on notice that the IRS will continue to challenge the issue involved.
35. (LO 6, 7) Aleshia has a number of approaches available, depending on the available materials. One approach is to begin with the keyword index in an online tax research service. Since the subject matter “§ 351 transfers” is somewhat self-contained, she could also start with the Internal Revenue Code and Treasury Regulations. The text identifies the major tax services that Aleshia could consult.

Another approach for Aleshia is to use CCH's *Federal Tax Articles*. After looking up "§ 351 transfers" in the subject index, she should be able to find a number of articles written about this subject. In addition, Thomson Reuters publishes the *Index to Federal Tax Articles* that is organized using RIA's paragraph index system. She also should check Bloomberg BNA *Tax Management Portfolios*.

36. (LO 7) Some tax researchers begin with a keyword search on an online tax service. If the problem is not complex, the researcher may bypass a tax service and turn directly to the Internal Revenue Code and the Treasury Regulations (both are available online; see Exhibit 1.7). For the beginner, this process saves time and will solve many of the basic problems. If the researcher does not have access to the Code or Regulations, the resources of a tax service may be necessary. Several of the major tax services publish paperback editions of the Code and Treasury Regulations that can be purchased at modest prices.
37. (LO 8)
- Primary source.
 - Secondary source.
 - Primary source.
 - Secondary source, but substantial authority for purposes of the accuracy-related penalty in § 6662.
 - Secondary source.
38. (LO 9) The key components of effective tax planning are as follows:
- Avoid the recognition of income (usually by resorting to a nontaxable source or nontaxable event).
 - Defer recognition of income (or accelerate deductions).
 - Convert the classification of income (or deductions) to a more advantageous form (e.g., ordinary income into capital gain).
 - Choose the business entity with the desired tax attributes.
 - Preserve formalities by generating and maintaining supporting documentation.
 - Act in a manner consistent with the intended objective.
- Don't just focus on tax considerations. Keep generally accepted accounting principles, sound business judgment, and overall economic outcomes in mind as well.
39. (LO 10) Simulations are task-based studies designed to test a candidate's tax knowledge and skills using real-life, work-related situations. Simulations include a four-function pop-up calculator, a blank spreadsheet with some elementary functionality, and authoritative literatures appropriate to the subject matter. The taxation database includes authoritative excerpts (e.g., Internal Revenue Code and Regulations, IRS publications, and Federal tax forms) that are necessary to complete the tax case study simulations.

PROBLEMS

40. (LO 2)

- a. Juniper has a realized gain of \$200,000 determined as follows:

Amount received on the exchange:		
FMV of real estate received	\$900,000	
Cash	<u>100,000</u>	\$1,000,000
Amount given up on the exchange:		
Basis of real estate		<u>(800,000)</u>
Realized gain		<u>\$ 200,000</u>

Juniper's recognized gain is limited to the *lesser* of realized gain of \$200,000 or the other property (boot) received of \$100,000. Thus, the recognized gain is limited to other property (boot) received of \$100,000 [the amount of cash (boot) received by Juniper]. Refer to § 1031.

- b. Birch has a realized loss of \$300,000, determined as follows:

Amount received on the exchange		\$1,000,000
Amounts given up on the exchange:		
Real estate (basis)	\$1,200,000	
Cash	<u>100,000</u>	
Basis of property given up		<u>(1,300,000)</u>
Realized loss		<u>\$ (300,000)</u>

None of Birch's realized loss can be recognized.

- c. Under the wherewithal to pay concept, forcing Juniper to recognize a gain of \$100,000 makes sense. Because of the \$100,000 cash received, not only has Juniper's economic position changed, but it now has the means to pay the tax on the portion of the realized gain that is recognized.

The disallowance of Birch's realized loss is consistent with the usual approach of the wherewithal to pay concept. This disallowance is the price that must be paid for tax-free treatment, and a carryover basis and adjustment under § 1031(d) prevents a deterioration of Birch's tax position. Note: After the exchange, Birch has a basis of \$1,300,000 in the real estate received from Juniper [i.e., \$1,200,000 (basis in the real estate given up) + \$100,000 (cash given up)].

41. (LO 2, 3)

- a. W. Wherewithal to pay concept.
- b. CE. Control of the economy.
- c. ESB. Encouragement of small business.
- d. SC. Social considerations.
- e. EI. Encouragement of certain industries.
- f. AF. Administrative feasibility.
- g. SC. Social considerations.

42. (LO 2)
- a. Louisiana, community property.
 - b. Virginia, common law.
 - c. Arizona, community property.
 - d. Rhode Island, common law.
 - e. Alaska, community property may be elected by spouses.
 - f. California, community property.
43. (LO 4) The real question is whether the parties acted in an arm's length manner. In other words, was the \$100,000 selling price the true value of the property?
- a. Where the parties to a transaction are related to each other, the IRS is quick to apply the arm's length concept. The IRS might, for example, find that the value of the property was less than \$100,000. In this event, the difference probably is dividend income to Benny.
 - b. The same danger exists even if Benny (the seller) is not a shareholder in Jet Corporation (the purchaser) as long as he is related to the one in control. If the value of the property is less than \$100,000, the IRS could argue for a constructive dividend to Benny's father of any difference. Because Benny ended up with the benefit, it follows that the father has made a gift to the son of such difference (see discussion in Chapter 5).
 - c. Since Benny is not a shareholder in Jet Corporation and is not related to any of its shareholders, the IRS probably would not question the \$100,000 selling price or the substance of the sale.
 - d. The student e-mail should summarize the items above. Look for proper grammar and e-mail etiquette in addition to the correct answer.
44. (LO 5)
- a. Letter rulings are issued for a fee by the National Office of the IRS upon a taxpayer's request and describe how the IRS will treat a proposed transaction for tax purposes. In general, they apply only to the taxpayer who asks for and obtains the ruling, but post-1984 rulings may be substantial authority for purposes of avoiding the accuracy-related penalties.
 - b. The National Office of the IRS releases technical advice memoranda (TAMs) weekly. TAMs resemble letter rulings in that they give the IRS's determination of an issue. Letter rulings, however, are responses to requests by taxpayers, whereas TAMs are issued by the National Office of the IRS in response to questions raised by taxpayers or IRS field personnel during audits. TAMs deal with completed rather than proposed transactions and are often requested for questions relating to exempt organizations and employee plans. Although TAMs are not officially published and may not be cited or used as precedent, post-1984 TAMs may be substantial authority for purposes of the accuracy-related penalties.
45. (LO 5)
- a. Revenue Procedure number 10, appearing on page 272 of Volume 1 of the *Cumulative Bulletin* for 2001.
 - b. Revenue Ruling number 14 appearing on page 31 of the 27th weekly issue of the *Internal Revenue Bulletin* for 2011.
 - c. The 30th letter ruling issued during the 25th week of 2011.

46. (LO 6)
- a. IRC.
 - b. FR, IRB, CB.
 - c. IRB, CB.
 - d. FR, IRB, CB.
 - e. IRB, CB.
 - f. NA, a court decision.
 - g. NA, a letter ruling.
47. (LO 5)
- a. Fifth Circuit.
 - b. Tenth Circuit.
 - c. Eleventh Circuit.
 - d. Ninth Circuit.
 - e. Second Circuit.
48. (LO 5)
- a. A
 - b. T
 - c. U
 - d. T
 - e. T
 - f. C
 - g. N
 - h. D
49. (LO 6)
- a. *United States Tax Reporter* is published by Research Institute of America, Thomson Reuters.
 - b. *Standard Federal Tax Reporter* is published by Commerce Clearing House, Inc.
 - c. *Federal Tax Coordinator 2d* is published by Research Institute of America.
 - d. *Mertens Law of Federal Income Taxation* is published by Thomson Reuters.
 - e. *Tax Management Portfolios* is published by Bloomberg BNA.
 - f. *CCH Tax Research Consultant* is published by Commerce Clearing House, Inc.

50. (LO 5, 8)
- a. P.
 - b. P.
 - c. P.
 - d. P.
 - e. S.
 - f. P.
 - g. S.
 - h. P.
 - i. B. Primary to the taxpayer to whom issued, but secondary for all other taxpayers.
 - j. P.
 - k. S. Cannot be cited as precedent.
 - l. P.
 - m. S.
 - n. S. Courts generally do not recognize proposed regulations.
51. (LO 5)
- a. For a regular decision of the U.S. Tax Court that was issued in 1970. The decision can be found in Volume 54, page 1514, of the *Tax Court of the United States Reports*, published by the U.S. Government Printing Office.
 - b. For a decision of the U.S. Second Circuit Court of Appeals that was rendered in 1969. The decision can be found in Volume 408, page 1117, of the *Federal Reporter*, Second Series (F. 2d), published by West Publishing Company.
 - c. For a decision of the U.S. Second Circuit Court of Appeals that was rendered in 1969. The decision can be found in Volume 1 for 1969, paragraph 9319, of the *U.S. Tax Cases*, published by Commerce Clearing House.
 - d. For a decision of the U.S. Second Circuit Court of Appeals that was rendered in 1969. The decision can be found in Volume 23, page 1090, of the Second Series of *American Federal Tax Reports*, now published by RIA (formerly P-H).
- [Note that the citations that appear in parts b., c., and d. are for the same case.]
- e. For a decision of the U.S. District Court of Mississippi that was rendered in 1967. The decision can be found in Volume 293, page 1129, of the *Federal Supplement Series*, published by West Publishing Company.
 - f. For a decision of the U.S. District Court of Mississippi that was rendered in 1967. The decision can be found in Volume 1 for 1967, paragraph 9253, of the *U.S. Tax Cases*, published by Commerce Clearing House.

- g. For a decision of the U.S. District Court of Mississippi that was rendered in 1967. The decision can be found in Volume 19, page 647, of the Second Series of *American Federal Tax Reports*, now published by RIA (formerly P-H).
[Note that the citations that appear in parts e., f., and g. are for the same case.]
- h. For a decision of the U.S. Supreme Court that was rendered in 1935. The decision can be found in Volume 56, page 289, of the *Supreme Court Reporter*, published by West Publishing Company.
- i. For a decision of the U.S. Supreme Court that was rendered in 1935. The decision can be found in Volume 1 for 1936, paragraph 9020, of the *U.S. Tax Cases*, published by Commerce Clearing House.
- j. For a decision of the U.S. Supreme Court that was rendered in 1935. The decision can be found in Volume 16, page 1274, of the *American Federal Tax Reports*, now published by RIA.
[Note that the citations that appear in parts h., i., and j. are for the same case.]
- k. For a decision of the former U.S. Court of Claims that was rendered in 1970. The decision can be found in Volume 422, page 1336, of the *Federal Reporter*, Second Series, published by West Publishing Company. This court is the Claims Court (renamed the Court of Federal Claims effective October 30, 1992), and current cases are in the *Federal Claims Reporter*.

RESEARCH PROBLEMS

- 1.
 - a. Section 6694(a) deals with the penalty for understatements due to taking an unreasonable position on a tax return.
 - b. Reg. § 1.6694-1(b) deals with the meaning of the term *tax preparer* for purposes of the tax preparer penalties.
 - c. Revenue Ruling 86-55 deals with tax return preparers and the assignment of refund checks.
 - d. PLR 8022027 deals with whether a tax return preparer is liable for a § 6694 penalty when he prepares a return claiming an IRA contribution that was not yet made and does not later ascertain that the contribution was made by the due date of the return.
- 2.
 - a. *rev'd* 929 F.2d 1252 (CA-8, 1991).
 - b. *aff'd* 734 F.2d 20 (CA-9, 1984), *cert. den.*, 469 U.S. 857 (1984).
 - c. *aff'd* 341 F.2d 341 (CA-5, 1965).
 - d. *aff'd per curiam*, 487 F.2d 515 (CA-8, 1973).
 - e. *rev'd* 335 F.2d 507 (CA-6, 1964).
- 3. The vacation may not be 100% free. Australia paid around \$2.7 million of the costs for the 300 vacations, but the trip is considered a taxable prize or award under IRC § 74(a) and not a nontaxable gift. Reg. § 1.74-1(a)(1) requires all amounts received as prizes and awards (unless such prizes or awards qualify as an exclusion from gross) to be included in gross income. Prizes and awards that are includible in gross

income include amounts received from radio and television giveaway shows. Reg. § 1.74-1(a)(2) further states that if the prize or award is not made in money but is made in goods or services, the fair market value of the goods or services is the amount to be included in income. Thus, the lucky recipients would have to pay taxes on the fair market value of the trip, not the amount actually paid for the trip by the Oprah show.

Oprah stated that she was paying any taxes of the lucky fans. Under *Old Colony Trust Co.*, 279 U.S. 716 (1929), the amount of any tax liability paid by Oprah is also taxable income. See Reg. § 1.61-14. If the initial tax liability is paid, another amount is taxable. Thus, an infinite amount of taxes would need to be paid by Oprah to make the vacation trip totally tax-free. The only way to make the prize tax-free is for Oprah to “gross up” the prize for any taxes due. Keep in mind there are also probably state taxes to be paid. All in all, this tax problem should create a lot of work for the accountant that Oprah chose to handle the tax problems of the 300 taxpayers.

Research Problems 4 and 5

These research problems require that students utilize online resources to research and answer the questions. As a result, solutions may vary among students and courses. You should determine the skill and experience levels of the students before assigning these problems, coaching where necessary. Encourage students to use reliable websites and blogs of the IRS and other government agencies, media outlets, businesses, tax professionals, academics, think tanks, and political outlets to research their answers.

CHECK FIGURES

40.a. Realized gain \$200,000; recognized gain
\$100,000.

40.b. Realized loss \$300,000; recognized loss
\$0.

SOLUTION TO ETHICS & EQUITY FEATURE

Choosing Cases for Appeal (p. 1-35). The issue is whether it is appropriate for the Government to select a case to appeal because of its potential for success (i.e., a reversal on appeal) rather than purely on its merits.

Without question, the tax laws treat taxpayers differently and often unfairly. Many laws are passed as the result of pressure from various groups (i.e., lobbying). “Don’t tax you, don’t tax me, tax that fellow behind the tree” is an appropriate statement of tax law development in many circumstances.

Part of the IRS’s function is to maximize revenue with the limited time and budget resources at its disposal. By litigating specific cases in order to develop judicial law, the IRS does “save” taxpayers’ dollars by avoiding marginal issues. And if the IRS position is sustained on appeal in Virginia, the judicial precedent might be important should the IRS choose to appeal the Iowa decision.

Certainly, there is an unfairness in such an approach. If the IRS decides to appeal the Virginia case, the CPA must bear the burden of litigation expenses (rather than the minister). Further, should the IRS position be sustained on appeal, the CPA’s trusts would be collapsed while the minister’s trusts may be allowed to remain—even though the tax issues are identical.