CPA-REGULATION[Q&As]

CPA Regulation

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QUESTION 1

On December 31, 1989, a building owned by Pine Corp. was totally destroyed by fire. The building had fire insurance coverage up to $500,000. Other pertinent information as of December 31, 1989 follows:

Building, carrying amount	$520,000
Building, fair market value	550,000
Removal and clean-up cost	10,000

During January 1990, before the 1989 financial statements were issued, Pine received insurance proceeds of $500,000. On what amount should Pine base the determination of its loss on involuntary conversion?

A. $520,000

B. $530,000

C. $550,000

D. $560,000

Correct Answer: B

Choice "b" is correct. $530,000 basis of involuntary converted building.

Building carrying amount	$520,000
Removal and clean up cost	10,000
Basis of involuntary conversion	$530,000
Insurance proceeds	(500,000)
Loss on involuntary conversion	$ 30,000

QUESTION 2

Among which of the following related parties are losses from sales and exchanges not recognized for tax purposes?

A. Father-in-law and son-in-law.

B. Brother-in-law and sister-in-law.

C. Grandfather and granddaughter.

D. Ancestors, lineal descendants, and all in-laws.

Correct Answer: C

Choice "c" is correct. Losses from sales and exchanges are not recognized for tax purposes between grandfather and granddaughter. Rule: Losses are disallowed on sales between related parties. "Related" includes brothers and sisters, husband-wife, lineal descendants (father, son, grandfather), and entities that are more than 50% owned by individuals, corporations, trusts and/or partnerships.

Choices "a", "b", and "d" are incorrect, because losses from sales and exchanges are recognized for all "in-laws."

QUESTION 3

During 1993 Kay received interest income as follows:

On U.S. Treasury certificates $4,000 On refund of 1991 federal income tax 500

The total amount of interest subject to tax in Kay\\'s 1993 tax return is:

A. $4,500

B. $4,000

C. $500

D. $0

Correct Answer: A

Choice "a" is correct. Interest income from U.S. obligations is generally taxable. Interest income on a federal tax refund is taxable, even though the refund itself is not taxed.

Choice "b" is incorrect. Interest income on a federal tax refund is taxable, even though the refund itself is not taxed.

Choice "c" is incorrect. Interest income from U.S. obligations is generally taxable.

Choice "d" is incorrect. Interest income from U.S. obligations is generally taxable. Interest income on a federal tax refund is taxable, even though the refund itself is not taxed.

QUESTION 4

Which one of the following statements is correct with regard to an individual taxpayer who has elected to amortize the premium on a bond that yields taxable interest?

A. The amortization is treated as an itemized deduction.

B. The amortization is not treated as a reduction of taxable income.

C. The bond\\'s basis is reduced by the amortization.

D. The bond\\'s basis is increased by the amortization.

Correct Answer: C

Choice "c" is correct. The bond\\'s basis is reduced by the amortization of the premium.

Choice "a" is incorrect. For bonds acquired after 12/31/87, the amortization of the premium is an offset to

interest income on the bond rather than a separate interest deduction.

Choice "b" is incorrect. The amortization of the premium will reduce taxable income.

Choice "d" is incorrect. The bond\\'s basis will be decreased by the amortization.

QUESTION 5

Capital assets include:

A. A corporation\\'s accounts receivable from the sale of its inventory.

B. Seven-year MACRS property used in a corporation\\'s trade or business.

C. A manufacturing company\\'s investment in U.S. Treasury bonds.

D. A corporate real estate developer\\'s unimproved land that is to be subdivided to build homes, which will be sold to customers.

Correct Answer: C

Choice "c" is correct. Investment assets of a taxpayer that are not inventory are capital assets. The manufacturing company would have capital assets including an investment in U.S. Treasury bonds. Choice "a" is incorrect. Accounts receivable generated from the sale of inventory are excluded from the statutory definition of capital assets. Choice "b" is incorrect. Depreciable property used in a trade or business is excluded from the statutory definition of capital assets. Choice "d" is incorrect. Land is usually a capital asset, but when it is effectively inventory, as when it is used by a developer to be subdivided, it is excluded from the statutory definition of capital assets.