

## 2014 TAX COURT NON-ATTORNEY ADMISSION EXAMINATION

### Instructions

Four hours will be allowed to answer all of the questions in the examination. Each question has been allocated a specific number of minutes (see the notation in parenthesis at the beginning of each question). Each question will be weighted according to the time allocated to the question.

Write your answers legibly in ink in the bound answer book/s furnished you for this purpose. Write your examination number on the cover of each answer book that you are given, as well as on your examination. Identify each answer by the same number as the question. Remove no pages from your bound answer book/s; you are being furnished loose sheets of paper for you to use as scratch paper. Do not write your name on any materials or answer books.

This examination is designed to test your overall knowledge of Rules of Practice and Procedure of the United States Tax Court, Federal taxation, the Federal Rules of Evidence, and American Bar Association Model Rules of Professional Conduct. The examination consists of four parts. Each part will be graded separately, and you must show your proficiency with respect to each part of the examination. The first part (60 minutes) deals with the Tax Court Rules of Practice and Procedure; it contains 23 questions and 5 pages. The second part (96 minutes) deals with substantive Federal income, gift, estate, and generation-skipping transfer taxation; it contains 31 questions and 8 pages. The third part (60 minutes) deals with the rules of evidence applicable in the Tax Court; it contains 10 questions and 3 pages. The fourth part (24 minutes) deals with legal ethics rules applicable to practice before the Tax Court; it contains 9 questions and 2 pages. Make sure that your examination is complete; you are responsible for any omissions from the examination.

**ANSWER THE QUESTIONS IN EACH OF THE FOUR PARTS OF THE EXAMINATION IN ANSWER BOOK/S SEPARATE FROM THE ANSWER BOOK/S CONTAINING ANSWERS TO THE OTHER THREE PARTS OF THE EXAMINATION. ONLY WHAT IS WRITTEN IN THE ANSWER BOOK/S WILL BE CONSIDERED WHEN GRADING THE EXAM. NO SCRAP (SCRATCH) PAPER WILL BE CONSIDERED.**

The only reference materials permitted to be with you during the examination (each of which is provided to you) are (1) a copy of the Internal Revenue Code, (2) a copy of the Rules of Practice and Procedure of the Court, and (3) the ABA Model Rules of Professional Conduct. You may refer to and apply these materials in taking the examination. You may also bring with you and use a calculator.

You may not have in your immediate possession, and you may not use, during the examination any device (including, but not limited to, computers, personal digital/data assistants, and telephones) capable of storing, accessing, or transmitting any information.

Clarity and conciseness of expression will be a significant factor in grading your examination. Answer only the questions that are asked.

Do not ask the proctor about any examination question. If you think a question contains an ambiguity, state the ambiguity, resolve the ambiguity by stating a reasonable assumption in your answer, and then answer the question based upon your assumption.

**UNLESS OTHERWISE INDICATED, ASSUME ALL TAXPAYERS USE THE CASH METHOD OF ACCOUNTING AND ARE CALENDAR YEAR TAXPAYERS. ALL STATUTORY REFERENCES ARE TO THE INTERNAL REVENUE CODE. UNLESS OTHERWISE STATED, ASSUME ALL EVENTS OCCUR DURING 2014 AND ANSWER ALL QUESTIONS AS TO THE 2014 TAXABLE YEAR. UNLESS DIRECTED TO THE CONTRARY, ANSWER EACH QUESTION INDEPENDENT OF THE FACTS OF THE OTHER QUESTIONS.**

The proctor will tell you when you may begin the test, and you will be given a warning 5 minutes before the examination is over. When time is called, put your pen down. Absolutely no extension of time is permissible. When the time for completion of your examination has elapsed, turn in to the proctor this examination, your answer books, and the materials furnished to you. If you complete the examination early, you may turn in the materials and leave.

PART ONE  
PRACTICE AND PROCEDURE  
(60 minutes)

**ANSWER THE QUESTIONS IN THIS PART OF THE EXAMINATION IN  
ANSWER BOOK/S SEPARATE FROM THE ANSWER BOOK/S CONTAINING  
ANSWERS TO OTHER PARTS OF THE EXAMINATION**

**In this Part One of the Examination, the taxpayer is referred to as "TP," and the Internal Revenue Service is referred to as "IRS." If TP is married, the spouse of TP is referred to as "Spouse." Unless otherwise directed, answer each Question independently of other Questions.**

Question P-1. (10 minutes total, 1 minute for each subpart) Determine whether the Tax Court has jurisdiction in each of the following situations (assuming that TP, the petitioner, timely files an appropriate Petition with the Tax Court). State YES or NO as to each subpart of the Question.

(a) Following an examination, the IRS determined that individuals who perform services for TP were TP's employees during the years in question. Does the Tax Court have jurisdiction to consider whether the individuals are TP's employees, and, if so, determine the amount of Subtitle C employment taxes owed by TP as a result of that determination?

(b) An IRS revenue agent informed TP, a sole proprietor who employed two individuals, that the agent believed TP underpaid TP's § 3402 withholding taxes. TP petitioned the Tax Court for a review of the asserted underpayment.

(c) TP prepares tax returns for other persons, and TP received from the IRS a notice and demand for penalty pursuant to § 6695(b) for failing to sign the tax returns of some of TP's customers. TP petitioned the Tax Court to challenge the penalty.

(d) The IRS issues to TP a statutory notice with respect to one taxable year. The notice determines an income tax deficiency and also accuracy-related penalties pursuant to § 6662(a) and (b)(2). TP petitions the Tax Court to dispute the deficiency amount and the accuracy-related penalties. Does the Tax Court have jurisdiction as to the accuracy-related penalties?

(e) Does the Tax Court have jurisdiction to determine a deficiency that exceeds the amount of the deficiency determined in the IRS statutory notice of deficiency?

(f) Does the Tax Court have jurisdiction to determine that TP overpaid income tax in the year properly before the Court pursuant to a statutory notice of deficiency and a TP petition?

(g) TP was an officer of a corporation that failed to pay FICA and employee income tax withholdings to the government. The IRS determined that TP was liable for the "trust fund" amounts as a responsible person under §6672, and the IRS initiated a collection action against TP. An IRS appeals office issued a determination notice rejecting TP's settlement offer, which had proposed monthly installment payments by TP. TP filed a Tax Court petition pursuant to §6330(d). Does the Tax Court have jurisdiction with respect to the petition?

(h) TP, who provides tax advice to other persons, received from the IRS a notice and demand for penalty pursuant to §6694(a). TP petitioned the Tax Court to challenge the penalty. Does the Tax Court have jurisdiction?

(i) TP is a substantial contributor to a private foundation and receives a notice of deficiency pursuant to §4941 that claims a tax on self-dealing between TP and the private foundation. TP files a petition with the Tax Court contesting the deficiency.

U) May TP invoke the Court's jurisdiction under §7436 only when the IRS has issued to TP a Letter 3523, Notice of Determination of Worker Classification, with respect to the tax periods in issue, and TP files, a Petition with Tax Court?

Question P-2. (4 minutes) TP is physically present in the United States at all relevant times. On March 3, 2014, the IRS mailed to TP at an address in the United States a notice of deficiency (bearing the date of March 3, 2014) regarding TP's 2012 income tax liability. The notice states that the last day on which a Tax Court petition may be filed is June 3, 2014. TP received the notice on March 7, 2014. What is the last day on which TP timely can file a petition with the Tax Court? The following 2014 calendar may be of use to you:

	Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
March							1
	2	3	4	5	6	7	8
	9	10	11	12	13	14	15
	16	17	18	19	20	21	22
	23	24	25	26	27	28	29
	30	31					
April			1	2	3	4	5
	6	7	8	9	10	11	12
	13	14	15	16	17	18	19
	20	21	22	23	24	25	26
	27	28	29	30			
May					1	2	3
	4	5	6	7	8	9	10
	11	12	13	14	15	16	17
	18	19	20	21	22	23	24
	25	26	27	28	29	30	31
June	1	2	3	4	5	6	7
	8	9	10	11	12	13	14
	15	16	17	18	19	20	21
	22	23	24	25	26	27	28
	29	30					

Question P-3. (3 minutes) The IRS mailed a notice of deficiency to TP's last known address. The 90th day after the IRS mailed the notice was Thursday, July 7, 2011, which was not a legal holiday in the District of Columbia. The Tax Court petition was received by the Court and filed on July 12, 2011. The envelope in which the petition was received bears a Federal Express U.S. Airbill with handwritten entries dated July 7, 2011, as the date the package was received by Federal Express. The delivery service selected on the FedEx Airbill is "Express Saver Third business day".

Discuss whether TP's petition to the Court created jurisdiction for the Tax Court to hear the case.

Question P-4. (6 minutes) Describe the contents of the pleading that must be filed by or on behalf of an individual taxpayer to initiate a Tax Court proceeding in response to a statutory notice of income tax deficiency.

Question P-5. (1 minute) If a Tax Court petition is silent with respect to one or more issues raised in the deficiency notice, what is the effect?

Question P-6. (1 minute) TP receives statutory deficiency notices with respect to proposed income tax deficiencies for more than one taxable year. May TP file one petition with respect to all of the deficiency notices? State YES or NO.

Question P-7. (1 minute) TP and Spouse file a joint return in 2012. TP and Spouse were divorced in 2013. In 2014, the IRS sends a separate notice of deficiency to each of TP and Spouse with regard to the 2012 taxable year. The deficiency notices were mailed to their separate addresses. May TP and Spouse file a joint petition in the Tax Court? State YES or NO.

Question P-8. (2 minutes) Describe how and under what circumstances TP may amend the petition originally filed by TP with the Tax Court.

Question P-9. (1 minute) May the Tax Court grant a partial summary judgment? State YES or NO.

Question P-10. (2 minutes) TP has properly petitioned the Tax Court and is represented by Counsel in the case. TP dies prior to trial of the case. Describe what Counsel should do with respect to the Tax Court case in view of the death of TP.

Question P-11. (2 minutes) Briefly describe the meaning under the Tax Court Rules of "joinder of issue" and explain its significance.

Question P-12. (2 minutes) According to the Tax Court rules, what is the preferred manner of

engaging in pre-trial discovery?

Question P-13. (1 minute) As a general rule, may a party obtain discovery of draft expert witness reports? State YES or NO.

Question P-14. (2 minutes) As applied to Tax Court cases, distinguish the phrase "burden of proof" from the phrase "standard of proof".

Question P-15. (2 minutes) Discuss which party has the burden of proof in a Tax Court proceeding.

Question P-16. (2 minutes) Prior to trial, TP refused to confer informally with the IRS, and the IRS properly submitted to TP a request for admission for the purpose of establishing the identity of X as TP's employer. TP does not respond to the request. What is the effect of this failure to respond?

Question P-17. (2 minutes) As part of pretrial discovery proceedings, counsel for a Tax Court petitioner believes that serving written interrogatories on several nonparty witnesses would generate valuable information. Discuss whether counsel may proceed with the interrogatories assuming that each nonparty witness would not be an expert witness.

Question P-18. (3 minutes) Describe the electronic filing rules with respect to Tax Court cases in which the taxpayer is represented by counsel.

Question P-19. (3 minutes) Certain Tax Court cases qualify for special "small tax case" procedures under the Tax Court Rules. Briefly describe the most fundamental elements of these procedures.

Question P-20. (6 minutes) The Internal Revenue Code prescribes that no levy may be made on any property of any person unless the IRS has notified such person in writing of the right to a hearing before such levy is made. Describe and discuss these hearing rights.

Question P-21. (2 minutes) TP is properly before the Tax Court in a proceeding involving the value of certain property. In TP's petition, TP avers that TP has obtained a written appraisal report, "a copy of which" is attached to the petition. Because TP and the author of the appraisal report are engaged in a fee dispute, the appraiser will not testify in the case. TP seeks to have the appraiser's report admitted into evidence as the appraiser's expert opinion.

Discuss how the Tax Court should rule regarding the admissibility of the written report.

Question P-22. (1 minute) If a Tax Court case opinion is based on legal analysis that subsequently is rejected in a different case by the U.S. Court of Appeals to which an appeal of the Tax Court case would lie, may the Tax Court reconsider the prior opinion? State YES or NO.

Question P-23. (1 minute) In a case before the Tax Court, the Tax Court imposed on the taxpayer a §6673(a)(1) penalty. May the Court, on its own motion, order counsel for the taxpayer to show cause why the counsel should not be required to pay excessive costs to the IRS under §6673(a)(2)? State YES or NO.

PART TWO  
SUBSTANTIVE TAX LAW  
(96 minutes)

**ANSWER THE QUESTIONS IN THIS PART OF THE EXAMINATION IN  
ANSWER BOOK/S SEPARATE FROM THE ANSWER BOOK/S CONTAINING  
ANSWERS TO OTHER PARTS OF THE EXAMINATION**

**In this Part Two of the Examination, the taxpayer is referred to as "TP," and the Internal Revenue Service is referred to as "IRS." If TP is married, the spouse of TP is referred to as "Spouse." For purposes of Part Two, ignore all inflation adjustments prescribed by the Internal Revenue Code as to fixed-dollar amounts. Unless otherwise directed, answer each Question independently of other Questions.**

Question S-1. (4 minutes) X and Y are cash method, calendar year taxpayers. On December 15, Year 1, Y sold and delivered to X goods to be sold in X's business. The terms of the sale provided that payment was due within 30 days of delivery of the goods. The following are alternative situations.

- (a) On December 31, Year 1, X offered to pay Y in cash for the goods, but Y refused and asked that X pay Y in January of Year 2. If X made payment in cash to Y on January 5, Year 2, when should Y report the gross income from the sale of the goods?
- (b) On December 27, Year 1, Y received a payment from X a check made by X that was dated December 24, Year 1. If Y cashed the check on January 3, Year 2, and the check was honored by X's bank, when should Y report the gross income?
- (c) On December 27, Year 1, Y's bookkeeper, a full-time employee of Y, received a payment a check from X that was dated December 24, Year 1, and which was payable to Y. The bookkeeper left on a holiday trip without depositing the check, and the bookkeeper did not return until January 4, Year 2, on which date the bookkeeper delivered the check to Y, who cashed the check at X's bank. When should Y report the gross income?
- (d) On December 31, Year 1, Y received from X a promissory note of X in the amount of X's indebtedness to Y. The note was transferred to Y because X had no cash and was in severe financial difficulty. The note was nonnegotiable, bore no interest, and was due in 180 days. During December, January, February, and March, of Year 2, Y attempted to negotiate the promissory note, but no one would accept the note. On May 1, Year 2, X made full payment on the note. When should Y report the gross income?

Question S-2. (3 minutes) TP is a corporation engaged in a trade or business. To enhance its profitability, TP enters into a management consulting services contract. The contract prescribes that X provide services to TP over the next three years. The contract requires the performance of 40% of the services in year 1, 30% of the services in year 2, and the remaining 30% of the services in year 3. The contract requires TP to pay \$100,000 over the term of the contract: 50% in year 1, 30% in year 2, and 20% in year 3. Discuss when TP will be permitted to deduct amounts paid to TP

in year 1, 30% in year 2, and 20% in year 3. Discuss when TP will be permitted to deduct amounts paid to X if TP uses the accrual method of accounting.

Question S-3. (1 minute) TP has elected the cash method of accounting. Must TP obtain the consent of the IRS to change TP's federal income tax method of accounting to the accrual method of accounting? State YES or NO.

Question S-4. (2 minutes) TP has elected the calendar year and the accrual method of accounting for federal income tax purposes. Over a three-year period, TP is entitled by contract to receive various amounts of gross income from X. If X pays to TP any such amount before the due date, when and how does TP properly report any such payment?

Question S-5. (8 minutes; 2 minutes for each subpart) State the amount that constitutes gross income to TP (without any further explanation) of each of the following items received during 2014 (answer each part below separately).

- (a) \$8,000 payment by TP's employer to car dealership to satisfy TP's debt to the dealership.
- (b) Pursuant to TP's employer's Employee Discount Program, TP purchased property from employer at a discount. The retail price for the property was \$3,000, and TP paid \$1,200. For the relevant period (TP's employer's prior taxable year), employer's sales were \$4,000,000, and employer's cost of goods sold was \$2,000,000.
- (c) \$1,000,000 cash received as the winner of the Nobel Prize in Physics. Immediately upon receipt of the payment, TP transferred the amount to the State of Massachusetts for support public education in Massachusetts.
- (d) \$100,000 lump-sum proceeds of life insurance policy on the life of TP's father. The policy was purchased and owned by TP's father, and the proceeds were payable to TP.
- (e) \$10,000 cash stolen by TP from neighbor's garage, where the neighbor kept cash in a coffee can.
- (f) TP was struck by an all-terrain vehicle which was being negligently operated by the driver. TP suffered (1) physical injury to TP's body and (2) emotional distress associated with the physical injuries. TP takes a court judgment against the driver, and the judgment is paid by the driver on December 15, 2014. The damages paid to TP pursuant to the judgment were as follows: (1) \$100,000 compensatory damages for physical injury to the body of TP, (2) \$300,000 punitive damages for physical injury to the body of TP, and (3) \$20,000 compensatory damages for the emotional distress. State the amount of gross income with respect to the \$100,000 compensatory damages for the physical injury to the body.
- (g) Same facts as in Question S-5(f). State the amount of gross income with respect to the \$300,000 punitive damages for the physical injury to the body.
- (h) Same facts as in Question S-5(f). State the amount of gross income with respect to the \$20,000 compensatory damages for the emotional distress.
- (i) \$10,000 paid to TP at maturity of loan TP made to a business associate (\$9,000 principal repayment and \$1,000 of interest).
- (j) \$8,000 of interest received on a State of North Dakota bond used to finance the construction 2014



- of new public schools.
- (k) \$5,000 gain realized upon sale of State of Iowa bond used to finance the construction of new highways.
  - (l) \$500 of interest received on U.S. Treasury note.
  - (m) Personal property received as a bequest when TP's mother died; fair market value of property as of (1) date of death of mother is \$500,000 and (2) date of receipt of ownership by TP is \$540,000.
  - (n) Free donuts at work on Fridays provided by TP's employer (value per year is \$75).
  - (o) \$10,000 as a partial payment of the proceeds of a life insurance policy in the face amount of \$200,000 on TP's father who died during the year. Pursuant to the terms of the policy, TP (as beneficiary of the policy) elected to receive a \$10,000 payment in each year for TP's life. TP's life expectancy is 25 years when the payments commence in 2014.
  - (p) \$5,000 received from the American Red Cross as a victim of a hurricane to cover TP's unreimbursed medical, temporary housing, and transportation expenses incurred as a result of flooding from the hurricane.

Question S-6. (2 minutes) TP was employed by Employer, who provided equipment to some medical providers who then billed the expenses to the government under Medicare. TP filed a "qui tam" claim under the federal False Claims Act alleging that Employer defrauded the government, and eventually TP received an award. Discuss whether the award received by TP qualifies as a capital gain for federal income tax purposes.

Question S-7. (4 minute/s) Briefly discuss the essential elements of the federal income tax "hobby loss" rules.

Question S-8. (2 minutes) TP owns residential real property that is TP's principal residence for federal income tax purposes. Close to the time TP acquired the real property, TP entered into a loan agreement with TP's mother in respect of the real property. The loan agreement transaction was commemorated in the "Home Equity Loan Agreement" and the "Home Equity Deed of Trust." The Home Equity Loan Agreement provides that TP's interest in the real property is specific security for the payment of the debt. The Home Equity Loan Agreement and the Home Equity Deed of Trust never were recorded in the official records of any jurisdiction. Under applicable state law, an unrecorded mortgage is invalid against third parties who do not have actual notice of it.

TP made payments to TP's mother pursuant to the Home Equity Loan Agreement and claimed a § 163(h)(3) qualified residence interest deduction with respect to the payments. Discuss whether TP is entitled to any deduction for § 163(h)(3) qualified residence interest.

Question S-9. (4 minutes) TP is a full-time employee of Employer as a sales representative for Employer's paper products. TP also owns an apartment building, the apartment units of which TP rents as residences to tenants. During the time TP is not acting as an employee of Employer, TP serves as the manager of the apartment building by being responsible for renting, accounting,

maintenance, repairs, etc. TP does not employ any other person to assist in the management of the apartment building.

Describe how § 469 might apply to TP regarding any loss realized with respect to TP's apartment building.

Question S-10. (4 minutes) TP incurs travel expenses in the context of TP's trade or business. Discuss briefly the requirements that TP must satisfy in order to obtain § 162 deductions for business travel expenses.

Question S-11. (1 minutes) TP owns and operates as a trade or business tractor trailers to haul freight. During the taxable year and as part of TP's trade or business activities, TP was assessed fines for driving in excess of the speed limit. May TP properly deduct as a business expense the fines for driving in excess of the speed limit? State YES or NO.

Question S-12. (3 minutes) TP is a certified public accountant whose accounting practice is limited to federal taxation. TP decides to improve TP's skills in taxation by going to law school at night while continuing full-time employment with an accounting firm. Discuss whether TP's tuition and book costs for attending law school will be deductible for federal income tax purposes.

Question S-13. (2 minutes) TP owns real property (Real Property) that is subject to a first mortgage encumbrance in favor of Bank. TP grants a conservation easement on the Real Property to Charitable Organization. The terms of the easement prohibit TP (and any subsequent owner) from building on, or altering the surface of, the Real Property. The conservation easement recites that TP "warrants that TP owns the Real Property in fee simple and has conveyed it to no other person, and that there are no outstanding mortgages, tax liens, encumbrances, or other interests in the Real Property that have not been expressly subordinated to the Easement," but (contrary to this warranty provision), Bank's mortgage was not then subordinated to the conservation easement.

Discuss whether TP qualifies for a § 170 charitable deduction with respect to the grant of the conservation easement if, subsequent to filing a federal income tax return claiming a § 170 deduction with respect to the conservation easement, TP and Bank execute a subordination agreement under which Bank subordinates its mortgage to the conservation easement. The effect of this subordination agreement is that the conservation easement will remain in force if Bank becomes the owner of the Real Property by foreclosure.

Question S-14. (2 minutes) TP contributed cash and a conservation easement to CO, a charitable organization. Before the contribution, CO at TP's request issued to TP a side letter which promised that, in the event the IRS disallows TP's charitable contribution deductions, CO "will promptly refund your entire cash endowment contribution and join with you to immediately remove the facade conservation easement from the property's title." TP claimed a § 170

charitable contribution deductions for the cash and easement donations to CO.

Discuss whether TP qualifies for a §170 deduction with respect to the value of the conservation easement.

Question S-15. (2 minutes) Explain the meaning of the federal income tax law phrase "refundable credit."

Question S-16. (6 minutes) TP and Spouse were married in 2005. They separated in 2011 and were divorced in early 2012. Pursuant to the terms of the divorce settlement agreement, which the divorce court approved and adopted as its order, TP is required to:

1. Transfer real property to Spouse. TP makes the transfer during 2012 and, on the date of the transfer, the real property has a fair market value of \$700,000 and an adjusted basis to TP of \$850,000.
2. Make the following spousal support payments in cash to Spouse:
  - (1) \$120,000 in 2012
  - (2) \$130,000 in 2013
  - (3) \$90,000 per year after 2013 until the death or remarriage of Spouse.

The divorce settlement agreement and the court order are silent as to the tax consequences of the various payments. TP makes all required payments.

- (a) (2 minutes) Describe the tax consequences in 2012 to TP and Spouse associated with the transfer of the real property.
- (b) (1 minute) State the amount of gross income to Spouse (not TP) in 2012 attributable to the \$20,000 cash payment as spousal support.
- (c) (3 minutes) State the amount of gross income, if any, to TP (not Spouse) in 2014 attributable to the spousal support payments made by TP in 2012-14.

Question S-17. (2 minutes) TP and Spouse divorced in 2014. Pursuant to a divorce decree, TP made "spousal maintenance" payments to Spouse, and TP claimed a §71 alimony deduction on TP's 2014 Federal income tax return. The "spousal maintenance" payments were to terminate when TP's youngest child graduates from high school. Discuss whether the "spousal maintenance" payments are deductible by TP.

Question S-18. (8 minute/s) TP and Spouse filed a joint return, but they did not pay the tax shown as due on the return. Discuss the types of, and requirements for, the relief potentially available to TP pursuant to §6015.

Question S-19. (4 minutes) Discuss the most significant recent developments with respect to the federal tax treatment of same-sex couples.

Question S-20. (4 minutes) In 2009, TP purchased unimproved real property. To acquire the property, TP (1) paid \$300,000 cash at the closing, (2) assumed a preexisting first mortgage debt

secured by the property in the principal amount of \$800,000 (for which TP became personally liable), and (3) executed a second mortgage indebtedness (for which TP was personally liable) to the seller in the principal amount of \$200,000.

In 2014, TP received an offer from Buyer to buy the real property, and TP accepted the offer. Buyer (1) paid \$700,000 cash, (2) took subject to the first mortgage debt in the principal amount of \$500,000 (TP had paid down the principal amount of the debt from \$800,000 to \$500,000), and (3) assumed the second mortgage debt in the principal amount of \$200,000.

- (a) What was TP's adjusted basis in the property at the time of acquisition in 2009?
- (b) Quantify TP's amount realized and any gain or loss realized upon the sale of the property to Buyer in 2014.

Question S-21. (2 minutes) TP previously entered, as lessee, into a ground lease with respect to real property. The lease was nonrenewable and nonextendable with a term of 33 years from the lease commencement date. The ground lease provided that TP would build and operate a motel facility on the property. The ground lease provided that all improvements and appurtenances to, and all personal property placed upon, the property remained the property of the lessee until the expiration or sooner termination of the ground lease. When the leasehold interest had a term of 21 years and 4 months remaining, TP exchanged the leasehold interest for a fee simple interest (outright ownership, not a leasehold interest) in other real property. TP treated the transaction as qualifying for §1031 treatment.

Discuss whether the transaction qualifies for §1031.

Question S-22. (3 minutes) Explain (1) the basis limitation and (2) timing rules applicable to the pass through of a shareholder's pro rata share of a Subchapter S corporation nonseparately computed loss for a taxable year of the Subchapter S corporation.

Question S-23. (5 minutes) Describe the federal income tax consequences to a partner (not the partnership) of a non-liquidating distribution of cash or property by a partnership to its partners.

Question S-24. (3 minutes) At the date of death of TP, who had practiced law during life, a \$90,000,000 malpractice claim was pending in court against TP. The estate of TP claimed a §2053 \$30,000,000 deduction on its estate tax return with respect to the pending lawsuit. Eventually, TP's estate settled the lawsuit for \$250,000. Discuss the amount that TP's estate should be allowed to deduct under §2053.

Question S-25. (3 minutes) Explain the concept of "portability" with respect to the federal estate tax "unified" or "applicable" credit of a married decedent.

Question S-26. (2 minutes) Under what circumstances, if any, may the Tax Court hold TP not liable for a §6651(a)(1) addition to tax for failing to timely file TP's tax return if TP alleges that

TP reasonably relied on the certified public accountant to file an extension request?

Question S-27. (2 minutes) Under what circumstances, if any, may the Tax Court hold TP not liable for §6662 accuracy-related penalties on tax underpayments if TP alleges that TP reasonably relied on the advice of a certified public accountant who prepared TP's income tax returns?

Question S-28. (2 minutes) The IRS issued a notice of deficiency asserting (1) adjustments to income and (2) a §6662(b) and (h) 40% gross valuation misstatement penalty. TP conceded the adjustments to income on grounds other than valuation or basis. TP filed a motion for partial summary judgment that the §6662(b) and (h) 40% gross valuation misstatement penalty does not apply as a matter of law.

Discuss how the Tax Court should rule on the motion for partial summary judgment.

Question S-29. (2 minutes) TP owned real property and made a conservation easement donation with respect to the property and claimed a §170 charitable deduction with respect to the donation. The IRS challenged the §170 charitable deduction on several different grounds, asserting that: (1) the easement had no value, (2) TP failed to obtain a "contemporaneous written acknowledgment" from the donee as required under §170(f)(8), and (3) TP failed to obtain a "qualified appraisal" as required under Regulation §1.170A-13(c). The IRS also asserted a §6662(h) gross valuation misstatement penalty.

Discuss whether the Tax Court is likely to impose the §6662(h) penalty if (1) the §6662(h) numerical threshold for the penalty has been satisfied and (2) TP failed to (a) obtain a "contemporaneous written acknowledgment" from the donee as required under §170(f)(8) and/or (b) to obtain a "qualified appraisal" as required under Regulation §1.170A-13(c).

Question S-30. (2 minutes) TP files a federal income tax return, all the relevant lines of which contain a "0." The IRS receives from third parties with respect to TP a W-2 Wage and Tax Statement and various 1099 forms reporting interest and dividend income. Discuss the statutory authority, if any, under which the IRS may prepare a tax federal income tax return for TP.

Question S-31. (2 minutes) TP participated in an offsetting-option tax shelter designed to generate large paper losses that TP could use to reduce other taxable income. TP purchased from Bank a series of currency-option spreads. Each spread was a package consisting of a long option, which TP purchased from Bank and for which TP paid a premium, and a short option, which TP sold to Bank and for which TP received a premium. Because the premium paid for the long option was largely offset by the premium received for the short option, the net cost of the package to TP was substantially less than the cost of the long option alone. TP contributed the spreads, along with cash, to two partnerships of which TP was a partner, and the partnership used the cash to purchase stock and currency. When calculating TP's basis in the partnership interests, TP included only the long component of the spreads and disregarded the nearly offsetting short component. As a result, when

the partnerships' assets were disposed of for modest gains, TP claimed large losses. Although TP had contributed roughly \$3,200,000 in cash and spreads to the partnerships, TP claimed losses of more than \$45,000,000. The IRS challenged the deduction of the claimed losses and asserted a §6662(h) gross valuation misstatement penalty.

Discuss whether the §6662(h) gross valuation misstatement penalty will apply to TP assuming that (1) the partnerships are disregarded for federal income tax purposes and (2) the deduction of the claimed losses is disallowed.

PART THREE  
FEDERAL RULES OF EVIDENCE  
(60 minutes)

**ANSWER THE QUESTIONS IN THIS PART OF THE EXAMINATION IN  
ANSWER BOOK/S SEPARATE FROM THE ANSWER BOOK/S CONTAINING  
ANSWERS TO OTHER PARTS OF THE EXAMINATION**

Each of the following ten questions is allocated 6 minutes.

Assume the following facts for Questions E1-E10. Taxpayer (TP) has filed a petition with the Tax Court contesting an alleged income tax deficiency and a §6662(b)(1) penalty. The IRS contends that TP failed to report \$100,000 of gross income on TP's 2009 individual tax return, and that a §6662(b)(1) penalty applies with respect to that failure to report the \$100,000.

Whenever a fact pattern states that TP asks a question of a witness, you should assume that the question is being asked by TP's attorney, and not by TP.

Question E-1. In TP's case-in-chief, TP calls Witness (W) to the witness stand. First, TP asks W to state W's name. After W stated W's name, TP then asks W the following question: "And you are employed as the 'Chief Reference Librarian' at the City Local Library, is that correct?" The IRS objects to the form of the question. Explain how the Tax Court should rule.

Question E-2. TP called W to the witness stand with the expectation that W would help establish (1) TP's presence at the City Local Library and (2) TP's good faith attempts to ascertain the Internal Revenue Code requirements regarding gross income. During W's direct examination, however, W testified that W never encountered TP prior to this trial, that W never observed TP in the City Local Library (where W is employed), and that W never assisted TP in any respect in regards to a search within the library for books and materials relevant to Internal Revenue Code gross income reporting requirements. Surprised by W's response, TP then asked W, "Isn't it true that on Monday December 9, 2009 you told your supervisor S that earlier that same day you had just spent several hours with TP helping TP locate books and other materials pertinent to Internal Revenue Code gross income reporting requirements?" IRS objects, arguing that a response to this question calls for hearsay. Explain how the Tax Court should rule.

Question E-3. Assume the same facts as in Question E2. Assume further that the Tax Court overruled the objection, and that W denied having such a conversation with S. In the midst of W's response to TP's question, W added the following: "Moreover, it was impossible for me to have had such a conversation with S as your question suggested, because in 2009 the City Local Library was open Mondays through Saturdays, but it was closed on Sundays. And December 9th fell on a Sunday. I know that because December 9th was my birthday." December 9, 2009,



actually was a Monday, and TP then asks the Court to take judicial notice that December 9, 2009, fell on a Monday. The IRS objects, arguing that TP is required to prove this fact. How should the Tax Court rule?

Question E-4. TP's petition to the Tax Court asserts that no §6662(b)(1) penalty is warranted according to §6664(c)(1) because TP believed TP had reasonable cause for, and acted in good faith with respect to, not reporting the \$100,000 as gross income. TP elects to take the witness stand. TP testifies that, prior to filing TP's 2009 tax return, TP (1) consulted with a tax attorney (who prepared and delivered to TP a written memorandum explaining the tax attorney's conclusions), (2) obtained advice from two online tax preparation programs, and (3) read at the City Local Library several books and materials on federal income taxation. TP further testified that all of these sources either stated directly (or, at the very least, strongly suggested) that the \$100,000 need not be reported as gross income on TP's tax return. On cross-examination, the IRS asks TP, the following: "You testified on direct that your tax attorney prepared and delivered a written memorandum which detailed the attorney's conclusions regarding whether the \$100,000 should be reported on your individual return as gross income. Can you please produce that memorandum for our review?" TP objects, arguing that the memorandum prepared by TP's attorney is privileged matter. How should the Tax Court rule?

Question E-5. On cross-examination of TP, the IRS asks TP whether, in 2007, TP had been convicted of "Bank Fraud." TP denies having been convicted of this offense, but TP had been convicted of this offense in 2007. In the state where TP had been convicted, the crime of "Bank Fraud" is a misdemeanor (a crime punishable by up to one year in prison). The IRS seeks to admit a certified copy of TP's "Bank Fraud" conviction. TP objects, arguing that this is improper impeachment. How should the Tax Court rule?

Question E-6. After TP completed TP's testimony, TP calls W2 to the witness stand. W2 testifies that W2 is a "Records Custodian" at the City Local Library and has been employed in that capacity for the last ten years. W2 further testifies that W2 is familiar with how all records at the library are prepared and maintained. TP then shows W2 a document (Exhibit A) that has the following information written on it: "City Local Library Book Withdrawal Receipt. Book: 'What Constitutes Gross Income for Federal Income Tax Purposes.' Author: John and Jane Doe. Date of Book Withdrawal: December 9, 2009. Return Due Date: December 23, 2009. Identity of Person Making Book Withdrawal: TP" TP asks W2 whether W2 recognizes Exhibit A. W2 testifies that W2 has never seen that particular document before, but that Exhibit A appeared to be a document (a book withdrawal slip) that the City Local Library regularly prepares and maintains, that the information that appears on documents such as Exhibit A are entered contemporaneously with a patron checking out a book from the Library, and that all of the information on Exhibit A is the type of information that W2 would normally expect to see on such a document. TP moves for the admission of Exhibit A. The IRS objects, arguing that TP failed to establish that the document is admissible under an exception to the hearsay rule. How should the Tax Court rule?



Question E-7. Assume that W2 is still on the witness stand and that the same foundation for W2's testimony has been established. On cross-examination, the IRS asks W2 whether W2 received a subpoena directing W2 to search the City Local Library's records to determine whether an individual by the name of "TP" had taken out any other books or materials from the library on any date after Monday December 9, 2009. After W2 affirmatively indicated that W2 had received such a subpoena, the IRS then asked W2 whether W2's research uncovered any other books or materials had been taken out by an individual by the name of "TP". W2 responded that W2's research revealed that no books or materials had been withdrawn by an individual identified as "TP" after Monday December 9, 2009. TP objects to W2's response, arguing that W2's testimony is inadmissible hearsay. How should the Tax Court rule?

Question E-8. TP then calls W3 to the witness stand. W3 testifies that W3 was at home all day on Monday, December 9, 2009, when at 4:45 p.m. W3's phone rang. When W3 answered the phone, W3's friend TP was calling and said to W3, "I'm going to come over your house in about 30 minutes, but before I do so I am going to withdraw this book pertaining to federal income tax gross income rules." The IRS objects to this testimony on hearsay grounds. How should the Tax Court rule?

Question E-9. Assume that W3 is still on the witness stand. On direct examination, W3 testified that W3 was a student at City University. On cross-examination of W3, the IRS asks W3 whether two years ago W3 had been suspended for one academic semester from City University for submitting a plagiarized term paper. TP objects to this question. How should the Tax Court rule?

Question E-10. Assume that W3 is still on the witness stand. Assume further that W3 denies having submitted a plagiarized paper and having been suspended from the university. The IRS then seeks to admit a certified document from City University which is addressed to W3 and informs W3 of W3's suspension from the University for W3's submission of a plagiarized term paper. TP objects, arguing that this type of impeachment is improper. How should the Tax Court rule?

PART FOUR  
LEGAL ETHICS  
(24 minutes)

**ANSWER THE QUESTIONS IN THIS PART OF THE EXAMINATION IN  
ANSWER BOOK/S SEPARATE FROM THE ANSWER BOOK/S CONTAINING  
ANSWERS TO OTHER PARTS OF THE EXAMINATION**

Question LE-1. (3 minutes) Susan Parker has been issued a notice of deficiency with respect to her 2012 federal income tax return on which she claimed an Internal Revenue Code §151 dependency exemption for her best friend, who is unrelated to Susan and has never lived with Susan. Susan would like to engage A to represent her in a Tax Court proceeding with respect to the deficiency. Susan tells A that she wants to challenge the deficiency because she gave her best friend \$10,000 in 2012 to help with rent and food and it would be unfair for Susan not to receive a dependency exemption. Can A file a petition in Tax Court challenging the deficiency on that basis? Briefly explain your answer.

Question LE-2 (3 minutes) B represents Sam Wu, a general partner in a business partnership. Wu has received a notice of deficiency relating to income that the partnership did not report on its return or on his K-1. The IRS has also asserted an understatement penalty. Jim Flynn, another general partner in the partnership, who has received a similar notice of deficiency, has asked B to represent him as well with respect to the deficiency. He tells B that he would contest the penalty because Wu was the partner responsible for filing the partnership returns and the K-1s and that he in good faith relied on Wu to file them correctly. Can B represent Flynn if he continues to represent Wu? Briefly explain your answer.

Question LE-3 (3 minutes) C represents Sabine Dockery in a Tax Court proceeding. C has filed a petition and undertaken discovery. The trial is scheduled to begin in two weeks. C has a signed retainer agreement with Dockery that requires Dockery to pay C's fees on a monthly basis, but Dockery has failed to do so for the previous five months. C sends Dockery a letter informing her that C will no longer represent her in the Tax Court proceeding and that C will not appear at the trial unless C's fees are paid. Has C successfully withdrawn from the representation of Dockery? If not, what other steps, if any, must C undertake?

Question LE-4 (3 minutes) D represents Steve Towery in a Tax Court proceeding in which the issue is whether Towery was entitled to depreciation deductions for a truck, which Towery claims he used solely for business purposes, delivering goods. At the trial, D has Towery testify about his use of the truck in his business. At lunch during a break in the proceedings, Towery says to D: "We really put one over on the court. There is no truck!" Towery reveals to D that he did not own a truck. What action, if any, should D take?

Question LE-5 (3 minutes) Same facts as LE-4 except that, as D is prepping Towery for his testimony, Towery reveals to D that he did not actually purchase a truck and that his receipt for a purchase of a truck was fraudulently prepared by his cousin who works at a car dealer. Towery indicates, however, that he intends to testify that he purchased a truck and used it in his business. If Towery insists on testifying in his own behalf, must D call Towery as a witness? Briefly explain your answer.

Question LE-6 (2 minutes) E is tax counsel for Digital Media, Inc., and in that capacity serves as Secretary of the Board of Directors of the company. The IRS has issued a deficiency notice challenging the tax treatment of certain corporate distributions. The appropriate tax treatment will depend on the timing of the distribution and whether the corporation had accumulated earnings and profits. The timing depends on when the corporation took action by resolution of the Board of Directors. If it will be necessary to call E as a witness with respect to the Board's resolution, can E represent Digital Media in the Tax Court proceeding if the Board of Directors consents on behalf of the corporation? Briefly explain your answer.

Question LE-7 (3 minutes) F, a partner in the Ready, Willing, and Able law firm, regularly provides tax advice to Maria Rodriguez, who runs a successful business. F designed a transaction intended to save federal income taxes. F explained the transaction to Rodriguez who carried it out. F prepared all the documentation for the transaction and prepared Rodriguez's tax returns on which she took deductions with respect to the transaction. The IRS subsequently audited Rodriguez, and asserted that the transaction lacked economic substance. Rodriguez received a notice of deficiency with respect to the transaction. Can F represent Rodriguez in the Tax Court proceeding with respect to the deficiency, assuming that there would be no need to call F as a witness? Briefly explain your answer.

Question LE-8 (2 minutes) G represents Jamal Wright in a Tax Court proceeding involving a deficiency arising out of several deductions he took on his tax return. As part of the pre-trial process, the lawyer representing the IRS offers a settlement. G is surprised by the offer and has never discussed with Wright the possibility of settling the case. G believes the government's offer is quite favorable and should be accepted. Wright is on a sailboat somewhere in the Pacific and cannot be reached. Can G agree to and sign the stipulation of settled issues? Briefly explain your answer.

Question LE-9 (2 minutes) H represents Cynthia Madison, a resident of New York City (which is within the area of the Second Circuit Court of Appeals), in a Tax Court proceeding. After submitting a brief on behalf of Madison, G discovered a decision by the Sixth Circuit Court of Appeals, which is directly adverse to Madison's position. The IRS brief does not mention the case. Must G reveal the Sixth Circuit opinion to the Tax Court? Briefly explain your answer.