

2012 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 books 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 books; 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 the Rules of Practice and Procedure of the United States Tax Court, Federal Taxation, the Federal Rules of Evidence, and the 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 21 questions and 4 pages. The second part (96 minutes) deals with substantive Federal income, gift, estate, and generation-skipping transfer taxation; it contains 27 questions and 7 pages. The third part (60 minutes) deals with the rules of evidence applicable in the Tax Court; it contains 3 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 BOOKS 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 non-programmable 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.

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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 2012 AND ANSWER ALL QUESTIONS AS TO THE 2012 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 BOOKS 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. (11 minutes total, one 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) The Tax Court determined that TP made an overpayment of tax with respect to the relevant taxable year. One hundred days have elapsed since the Tax Court decision became final, but the IRS has not refunded the overpayment. TP seeks a Tax Court order that the IRS refund the overpayment. Does the Tax Court have jurisdiction?
- (b) 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?
- (c) Does the Tax Court have jurisdiction to determine a deficiency that is less than the amount of the deficiency determined in the IRS statutory notice of deficiency?
- (d) The IRS issues to TP a statutory notice with respect to one taxable year. The notice determines an income tax deficiency and also an addition to tax pursuant to §6651. TP petitions the Tax Court to dispute the deficiency amount and the addition to tax. Does the Tax Court have jurisdiction as to the addition to tax?
- (e) TP files a petition with the Tax Court to contest a proposed gift tax deficiency based on the IRS valuation of property transferred by gift by TP. Does the Tax Court have jurisdiction with respect to the proposed gift tax deficiency?
- (f) TP is a tax return preparation professional, and TP 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?

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- (g) TP files a petition with the Tax Court asserting a refund claim against the United States for overpaid income taxes. The IRS has not issued a statutory notice of deficiency to TP with respect to the taxable period as to which the refund claim is asserted. Does the Tax Court have jurisdiction?
- (h) TP receives a statutory notice of deficiency and then timely petitions the Tax Court. Before the Tax Court takes any action with respect to the case, the IRS assesses the tax to which the petition relates, and TP files a motion asking the Tax Court to enjoin the assessment and collection of such tax. Does the Tax Court have jurisdiction to grant such a motion?
- (i) TP litigated a case in the Tax Court, and TP then appealed the adverse decision. On appeal, the decision was reversed in part and remanded to the Tax Court for further proceedings. During these further proceedings in the Tax Court, TP moves to dismiss for lack of jurisdiction because the deficiency notice was not timely. Should the Tax Court grant the motion to dismiss because of lack of jurisdiction?
- (j) A was never appointed executrix over B's estate by a State probate court, but A signed B's estate's Federal estate tax return as executor. The IRS asserted a deficiency in estate tax and issued a notice of deficiency listing A as executor of B's estate. A filed a petition with the Tax Court for redetermination of the estate tax. A thereafter filed a motion to dismiss for lack of jurisdiction, arguing the Tax Court lacked jurisdiction because A was never appointed executrix so that the notice of deficiency had been sent to the wrong person. If the Court determines that A was in possession of the property of B for purposes of §2203, does the Tax Court have jurisdiction?
- (k) The IRS issued to TP a notice of intent to levy and a notice of Federal tax lien filing, both for unpaid income tax assessed with respect to one of TP's previously-filed income tax returns. TP timely requested an administrative hearing under §§6320 and 6330, and TP set forth the grounds for TP's request in an attachment downloaded from the Internet website of an organization known to promote frivolous arguments and activities that delay or impede administration of federal tax laws. The IRS Office of Appeals sent a letter to TP stating that (1) the Office had determined that TP's request for a hearing consisted of §6330(g) frivolous positions and, (2) therefore, the Office was disregarding the request. The Office determination letter stated that the Office was returning TP's request to the IRS collection office and that collection action may proceed as if the hearing request was never submitted. TP timely filed a petition under §6330(d)(1) seeking review of the determination that the IRS collection office could proceed with collection. Does the Tax Court have jurisdiction to review the IRS § 6330(g) determination?

Question P-2. (2 minutes)

Federal tax law distinguishes between (1) an employee and (2) a service provider who is not an employee. Describe the extent to which, if any, the Tax Court has jurisdiction with respect to such distinction.

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Question P-3. (4 minutes)

TP is physically present in the United States at all relevant times. On January 9, 2012, the IRS mailed to TP at an address in the United States a notice of deficiency (bearing the date of January 9, 2012) regarding TP's 2010 income tax liability. The notice states that the last day on which a petition may be filed is April 6, 2012. TP received the notice on January 14, 2012. What is the last day on which TP timely can file a petition with the Tax Court?

Question P-4. (3 minutes)

Describe the methods by which a Tax Court petition may be timely filed.

Question P-5. (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-6. (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 on the Tax Court proceeding?

Question P-7. (1 minute)

Define "joinder of issue" under the Tax Court Rules.

Question P-8. (1 minute)

Explain the significance of "joinder of issue" under the Tax Court Rules.

Question P-9. (1 minute)

Describe how counsel for the petitioner may amend the originally-filed petition.

Question P-10. (1 minute)

Describe the time periods within which discovery may be undertaken with respect to a case in the Tax Court.

Question P-11. (2 minutes)

According to the Tax Court rules, what is the preferred manner of engaging in pre-trial discovery?

Question P-12. (3 minutes)

Under what circumstances will the Court issue a protective order regarding nondisclosure of information that constitutes part of the record of the case?

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Question P-13. (3 minutes)

Describe, compare, and contrast (1) discovery depositions and (2) depositions to perpetuate evidence.

Question P-14. (2 minutes)

Discuss whether, as part of pretrial discovery proceedings, counsel for TP, a Tax Court petitioner, may serve written interrogatories on several nonparty witnesses for the purpose of generating information valuable to TP.

Question P-15. (1 minutes)

Describe the extent to which a stipulation is binding on a party.

Question P-16. (3 minutes)

Briefly describe the burden of proof rules that apply in Tax Court litigation.

Question P-17. (2 minutes)

Under what circumstances, if any, will the Tax Court grant a summary judgment?

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)

IRC §§6320 and 6330 prescribe certain "due process" hearing rights of taxpayers with the IRS Appeals Office. Describe and discuss these hearing rights.

Question P-21. (1 minute)

If the Tax Court has filed its opinion determining the issues in a case, the Court may withhold entry of its decision for the purpose of permitting the parties to submit computations pursuant to the Court's determination of the issues, showing the correct amount to be included in the decision. Under the Tax Court Rules, what is the time period within which the parties must submit such computation?

**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. (3 minutes)

Compare and contrast the federal income tax (1) cash method of accounting and (2) accrual method of accounting.

Question S-2. (6 minutes)

On December 31, year 1, TP owned unencumbered unimproved real property with an adjusted basis of \$100,000 and a fair market value of \$600,000. On December 31, year 1, TP sold the property to Buyer according to the following terms:

1. Buyer paid TP \$200,000 cash at the closing.
2. Buyer executed a promissory note payable to TP in the total principal amount of \$400,000. A principal payment of \$100,000 was due on the anniversary date of the sale in each of the four years following the year of sale. The promissory note required the payment of interest at 4% compounded annually, and the note had a fair market value of \$400,000.

TP received the required \$100,000 payment of principal on the note in year 2, and on January 1, year 3, TP transferred the note (entitled to three additional principal payments of \$100,000 each) to TP's child as a gift. The fair market value of the note on January 1, year 3, was \$300,000.

- (a) (3 minutes) Quantify and discuss the year 1 tax consequences to TP according to §453.
- (b) (2 minutes) Quantify and discuss the year 2 tax consequences to TP according to §453.
- (c) (1 minute) Quantify and discuss the year 3 tax consequences to TP according to §453B.

Question S-3. (8 minutes; 1/2 minute for each subpart)

State the amount that constitutes gross income to TP (without any further explanation) of each of the following items received during 2012 (answer each part below separately).

- (a) \$3,000 payment by TP's employer to TP's bookie in satisfaction of TP's gambling debts to the bookie of \$3,000.
- (b) Pursuant to employer's Employee Discount Program, TP purchased property from employer at a discount. The retail price for the property was \$2,000, and TP paid \$1,200. For the relevant period (employer's prior taxable year), employer's sales were \$3,000,000, and employer's cost of goods sold was \$2,000,000.
- (c) \$1,000,000 cash received as a winner of the State lottery.
- (d) \$300 cost to TP's employer of \$50,000 of life insurance on TP's life, which is provided under a group term policy of the employer.
- (e) \$40,000 lump-sum proceeds of life insurance policy on the life of TP father. The policy was purchased and owned by TP's father, and the proceeds were payable to TP.
- (f) \$4,000 profit from purchases and sales of illegal drugs.
- (g) TP was struck by a construction crane, the operator of which was operating the *crane* recklessly. TP suffered (1) physical injury to TP's body and (2) emotional distress associated with the physical injuries. Because of the emotional distress, TP visited a psychotherapist during 2012 and incurred costs of \$8,000. TP takes a court judgment against the crane operator, and the judgment is paid by the operator on December 1, 2012. The damages paid to TP pursuant to the judgment were as follows: (1) \$200,000 compensatory damages for physical injury to the body of TP, (2) \$130,000 punitive damages for physical injury to the body of TP, and (3) \$15,000 compensatory damages for the emotional distress. State the amount of gross income with respect to the \$200,000 compensatory damages for the physical injury to the body.
- (h) Same facts as in Question S-3(g). State the amount of gross income with respect to the \$130,000 punitive damages for the physical injury to the body.
- (i) Same facts as in Question S-3(g). State the amount of gross income with respect to the \$15,000 compensatory damages for the emotional distress.
- (j) \$100,000 paid to TP at maturity of loan TP made to a business associate (\$96,000 principal repayment and \$4,000 of interest).
- (k) \$12,000 stolen by TP from bank.

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- (l) \$1,000,000 received as winner of the Nobel Prize in literature; TP accepted the prize and used the proceeds to buy a vacation home.
- (m) \$2,000 of interest received on a State of Utah bond used to finance the construction of new highways.
- (n) \$1,000 gain realized upon sale of State of California bond (used to finance the construction of new public schools).
- (o) \$1,000 of interest received on U.S. Treasury note.
- (p) \$2,000 of cash found in the wall of TP's barn; TP spent the cash.

Question S-4. (3 minutes)

In 1999, TP and Spouse purchased for \$200,000 (paid in cash) a residence as TP's and Spouse's principal residence. TP and Spouse own and occupy the property as their principal residence until they sell the property on October 15, 2012, for \$1,500,000. Neither TP nor Spouse ever owned another residence. Quantify and explain the amount of the gain recognized with respect to the sale of the residence in 2012 if TP and Spouse file a joint return for 2012.

Question S-5. (1 minute)

During year 1, TP receives as a gift from a dear friend non-depreciable real property. On the date of the gift, the property has a fair market value of \$100,000 and an adjusted basis to the friend of \$120,000. The friend paid a gift tax of \$1,000 with respect to the transfer to TP. State the amount of gross income to TP in year 1 with respect to the gift of the real property.

Question S-6. (2 minutes)

Same facts as Question S-5.

State the amount of TP's adjusted basis in the real property if TP sells the property in year 4 for \$125,000.

Question S-7. (2 minutes)

TP purchased a principal residence on January 1 of the current year at a cost of \$1,500,000. TP paid \$200,000 down and obtained a purchase money first mortgage loan (secured by the residence) from a bank in the principal amount of \$1,300,000. As of January 1, state the total principal amount of the first mortgage indebtedness as to which interest is deductible, assuming that TP is married, files a joint return with Spouse, and neither TP nor Spouse owns another residence.

Question S-8. (3 minutes)

Same facts as Question S-7.

On June 1 of the current year, TP has reduced the principal amount of the first mortgage debt on the residence to \$900,000. The fair market value of the residence on June 1 is \$1,500,000. On June 1, TP borrows \$400,000 from a bank, and the debt is secured by a second mortgage on the residence. TP expends \$300,000 of the second mortgage loan proceeds to add a game room to the residence, and the other \$100,000 to purchase a boat used for recreation. Discuss the amount, if any, as of June 1, of the principal amount of the second mortgage loan as to which interest is deductible.

Question S-9. (2 minutes)

During the current year, TP realized the following gains and losses: (1) long-term capital losses of \$20,000, (2) short-term capital losses of \$25,000, (3) long-term capital gains of \$5,000, and (4) short-term capital gains of \$23,500. State the total amount of capital losses to be allowed to TP for the current year by §1211.

Question S-10. (2 minutes)

Same facts as Question 9.

State the amount, if any, of:

- (a) the long-term capital loss carryover.
- (b) the short-term capital loss carryover.

Question S-11. (3 minutes)

Will TP, whose abode is in Town, be entitled to a §151(c) dependent exemption-deduction in 2012 for the following persons (each of whom is not disabled as defined in §22(e)(3))?

- (a) A, TP's seventeen year old unmarried child, resides with TP for the entire year in Town. A works full time and has gross income of \$20,000 in 2012. For 2012, A provides 60% of A's support, and TP provides 40% of A's support. State YES or NO.
- (b) B, TP's twenty-one year old unmarried child, is a college student whose permanent residence is University City, not Town. B has 2012 gross income of \$15,000 from summer employment. TP provides 70% of B's support, and B provides 30% of B's support. State YES or NO.
- (c) C, TP's twenty-three year old unmarried child, resides with TP for the three summer months of 2012 but for all other months is temporarily away at college in University City. C has 2012 gross income of \$15,000 from summer employment. TP provides 80% of C's support, and C provides 20% of C's support. State YES or NO.

Question S-12. (2 minutes)

On February 15, 2008, TP purchases for \$300,000 cash a new machine exclusively for use in TP's business activity. The equipment has a §168(i)(1) class life of ten years. TP expects to use the equipment for fifteen years and estimates that the equipment will have a salvage value of \$12,000 at the end of the fifteen-year period of use. State the amount of the §168 deduction allowable in 2012 (ignoring §168(f), (g), (j), (k), (1), (m), (n), and §179 for purposes of this Question).

Question S-13. (1 minute)

Does §213 medical expense deduction provision include as medical care amounts paid for breast pumps and supplies that facilitate lactation? State YES or NO.

Question S-14. (1 minute)

TP1 and TP2 are not married to each other, and they co-own two residences. TP1 and TP2 assert that the §163(h) limitations apply separately to each co-owner TP with respect to up to two residences so that each TP may deduct the interest on up to \$1,000,000 of acquisition indebtedness and up to \$100,000 of home equity indebtedness. The IRS asserts that the §163(h) limitations apply on a per residence basis so that each TP may deduct only a proportionate share of the interest on no more than \$1,100,000. Will the Tax Court apply the §163(h) limitation on a per-residence basis or a per-taxpayer basis? State per-residence or per-taxpayer.

Question S-15. (2 minutes)

TP claimed a §170 charitable contribution deduction for a cash gift to a qualifying organization, a church (Church). Shortly after the gift, TP received a letter from the Church confirming the amount of the gift, but the letter did not contain a statement to the effect that TP received no goods or services in consideration for the contribution. The IRS sent TP a notice of deficiency disallowing TP's §170 deduction for the gift to the Church on the basis of §170(f)(8). TP then sought and received a second letter from the Church that confirmed the amount of the gift, and the letter stated that TP received no goods or services in consideration for the contribution. The issue before the Tax Court is whether the §170 deduction should be allowed. Based on these facts and prior Tax Court precedence, explain how the Tax Court should hold.

Question S-16. (6 minutes)

TP and Spouse separated in 2008 and are divorced in early 2010. 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 publicly traded securities to Spouse. TP makes the transfer during 2010 and, on the date of the transfer, the securities have a fair market value of \$500,000 and an adjusted basis to TP of \$550,000.
2. Make the following spousal support payments in cash to Spouse:
 - (1) \$130,000 in 2010
 - (2) \$140,000 in 2011
 - (3) \$100,000 per year after 2011 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 2010 to TP and Spouse associated with the transfer of the securities.
- (b) (1 minute) State the amount of gross income to Spouse (not TP) in 2010 attributable to the \$130,000 cash payment as spousal support.
- (c) (3 minutes) State the amount of gross income, if any, to TP (not Spouse) in 2012 attributable to the spousal support payments made by TP in 2010-12.

Question S-17. (6 minutes)

In 2008, TP purchased unimproved real property. To acquire the property, TP (1) paid \$100,000 cash at the closing, (2) took the property subject to a preexisting first mortgage debt secured by the property in the principal amount of \$600,000 (for which TP was not personally liable), and (3) executed a second mortgage indebtedness (for which TP was personally liable) to the seller in the principal amount of \$300,000.

In 2012, TP received an offer from Buyer to buy the real property, and TP accepted the offer. Buyer (1) paid \$500,000 cash, (2) took subject to the first mortgage debt in the principal amount of \$400,000 (it had been paid down from \$600,000 to \$400,000), and (3) assumed the second mortgage debt in the principal amount of \$300,000.

- (a) What was TP's adjusted basis in the property at the time of acquisition in 2008?
- (b) Quantify TP's amount realized and any gain or loss realized upon the sale of the property to Buyer in 2012.

Question S-18. (6 minutes)

Describe the federal tax treatment of a limited liability company that is properly formed under state law.

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Question S-19. (11 minutes as allocated below)

On January 1, 2012, A, B, and C organize ABC Corporation (which is not and will not be an "investment company" under §351(e)). The following transfers were made to the corporation:

| <u>Transferor</u> | <u>Property</u> | <u>Fair Market Value</u> | <u>Adjusted Basis to Transferor</u> |
|-------------------|--------------------------|--------------------------|-------------------------------------|
| A | Cash | \$200,000 | \$200,000 |
| B | Equipment | \$300,000 | \$300,000 |
| C | Unimproved real property | \$520,000 | \$100,000 |

B's equipment had been purchased in 2010 for use in B's trade or business at a cost of \$400,000, and because of depreciation, the adjusted basis had been reduced to \$300,000 on January 1, 2012. The unimproved real property had been held by C as an investment since C's acquisition of the property in 2000.

In exchange for the contributions of A, B, and C, the corporation issues its common stock, 200 shares to A, 300 to B, and 500 shares to C. The fair market value of the stock is \$1,000 per share; the common stock is the only class of stock authorized and outstanding. In addition to the 500 shares of stock, C receives from ABC Corporation \$5,000 of cash and a 1-year note of ABC Corporation in the amount of \$15,000 at 6% interest. The ABC note has a fair market value equal to the face amount of the note.

- (a) (4 minutes) Determine C's gain realized, C's gain recognized, and the character of any *gain* recognized by C.
- (b) (3 minutes) Determine C's adjusted basis in the ABC Corporation stock received.
- (c) (2 minutes) Determine the amount of gain recognized ABC Corporation.
- (d) (2 minutes) Determine the adjusted basis of ABC Corporation in the real property received from C.

Question S-20. (7 minutes)

Describe the characterization rules that will or may apply to determine the character of a gain or loss resulting from a partner's sale of the partner's partnership interest.

Question S-21. (2 minutes)

TP incurred non-deductible gambling losses (equaling almost half of TP's reported income) that TP claimed as a deduction on TP's federal income tax return. TP used a commercial software program to prepare TP's tax return for the year of the gambling losses. The IRS disallowed the gambling deductions and asserted a §6662 penalty. Before the Tax Court, TP argued for relief from §6662 on the basis of the §6664(c)(1) exception, which applies if it is shown that there was a reasonable cause and that the taxpayer acted in good faith. TP asserted that TP followed the instructions on the tax preparation software that was "approved by the IRS". TP also asserted that TP was unaware of the provisions of the Internal Revenue Code and that TP did not consult any IRS publications or professional tax advisers before claiming the deductions. TP did not offer into evidence the instructions to the software. Based on these facts and prior Tax Court precedence, explain how the Tax Court should hold.

Question S-22. (2 minutes)

During the year at issue, TP realized gross income, but TP filed a federal tax return, all the lines of which had zero as the amount. The IRS asserted a deficiency in income tax plus an addition to tax under §6651(f) for fraudulently failing to file a return. TP asserted, using arguments that the Tax Court has long deemed frivolous, that the income TP received was not taxable income within the meaning of the federal tax law. Discuss whether TP is liable for the addition to tax under §6651(f) based on Tax Court precedence.

Question S-23. (4 minutes)

Explain the substantial authority exception to the § 6662(b)(2) penalty for substantial understatement of income tax.

Question S-24. (1 minute)

TP files a federal income tax return that reflects an overstatement of the adjusted basis of property sold by TP. Is such an overstatement of basis an omission of gross income for purposes of § 6501(e) (1) (A)? State YES or NO.

Question S-25. (8 minutes)

Discuss the types of, and requirements for, the relief potentially available to a spouse pursuant to §6015.

Question S-26. (1 minute)

TP received an IRS determination letter advising that the IRS would proceed to enforce its lien against property to collect unpaid tax liability of TP. TP petitioned the Tax Court for review of the IRS determination. The Tax Court remanded the matter to the IRS Appeals Office to determine, pursuant to §6330(c)(1), whether the IRS properly sent TP a notice of deficiency. At the hearing on remand, is the IRS settlement officer limited to a consideration of matters considered by the Appeals officer in the original administrative hearing? State YES or NO.

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Question S-27. (1 minute)

TP is admitted to practice before the Tax Court and represents TP in a Tax Court proceeding. Under §7430, can TP receive an award of attorney fees? State YES or NO.

**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**

Assume the following facts for Questions E-1. through E-3.

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, in part, that (1) TP, on TP's 2006 individual federal tax return, improperly claimed charitable deductions and (2) a §6662(b)(1) penalty applies with respect to the improperly claimed charitable deductions. TP submits that the charitable deductions were proper and that no § 6662(b) (1) penalty applies. Trial of the case commenced in June 2012.

Question E-1. There are two parts to Question E-1. Both questions pertain to the testimony of F.

a. (6 minutes)

As part of TP's case-in-chief, TP (through TP's attorney) calls F to the witness stand. After establishing that TP and F had a telephone conversation on April 8, 2007 (less than a week before TP filed TP's 2006 federal tax return), TP asks F whether F recalled TP's last words before their conversation ended. F responded "Yes, I do. TP said 'I'm glad I made several thousand dollars in charitable contributions. They are legitimate deductions.'"

The I.R.S. objects on hearsay grounds. Explain how the Tax Court should rule.

b. (6 minutes)

Assume the Judge in Question E-1.a. above sustains the I.R.S. objection. On cross-examination, the attorney for the I.R.S. decides (for certain strategic reasons) to ask F the same question—whether F recalled TP's last words before F's April 8, 2007, conversation with TP concluded. Once again, F responded, "Yes, I do. TP said 'I'm glad I made several thousand dollars in charitable contributions. They are legitimate deductions.'"

If TP were to object to F's response on hearsay grounds, what is the government's best response, and explain how the Tax Court should rule.

Question E-2. There are three parts to Question E-2. All of the questions pertain to (or stem from) the testimony of A.

a. (6 minutes)

As part of the I.R.S. case, the government calls to the witness stand A. Earlier in the trial, the I.R.S. established that, on January 4, 2007, TP personally contacted A and requested that A contact B. On direct examination, the I.R.S. attorney asks A to describe a telephone conversation between A and B that occurred on January 5, 2007. A testified that A had called B that morning and said to B, "B, there is some big money awaiting us after TP files TP's taxes this year if you can help us out. TP wants to cheat the I.R.S. by claiming some phony charitable deductions. I reviewed TP's charitable deductions and I don't think the I.R.S. will notice the improprieties. But we need your help." TP objects to A's testimony on hearsay grounds.

If the I.R.S. seeks to admit the entirety of the statement for its truth, what is the government's best response, and explain how the Tax Court should rule.

b. (6 minutes)

Assume that A was permitted to testify on direct examination to A's conversation with B as detailed in Question E-2.a. Assume further that it has been established that A is a professional tax return preparer, that A attended a social event on the evening of January 4, 2007, and that A had a conversation during that event with C. Finally assume, for purposes of this Question, that A is on the witness stand and is being cross-examined by TP. On cross-examination, TP asks A, "Is it true that on the night of January 4, 2007, you told C that you found nothing improper when you reviewed TP's tax return?"

If the I.R.S. objects to this question on hearsay grounds, what is TP's best response, and explain how the Tax Court should rule?

c. (6 minutes)

Assume that A was permitted to testify on direct examination to A's conversation with B as detailed in Question E-2.a. Assume further, that it has been established that A is a professional tax return preparer, that A attended a social event on the evening of January 4, 2007, and that A had a conversation during that event with C. Finally assume, for purposes of this Question, that TP (in contrast to the facts presented in Question 2.b.) elected not to cross-examine A. In TP's rebuttal case, TP calls C to the witness stand. TP seeks to have C testify that on the night of January 4, 2007, C was told by A at a social event that A had reviewed TP's tax return and found nothing improper.

If the I.R.S. objects on the basis that the response constitutes hearsay, what is TP's best response, and explain how the Tax Court should rule.

Question E-3. There are five parts to Question E-3. All of the questions pertain to (or stem from) the testimony X.

a. (6 minutes)

During the I.R.S. case, the government calls X as a witness. X testifies that X is a professional tax return preparer and that X and A (the same A identified in Question 2.b.) work together in the same capacity at a local tax return preparation center. X further testifies that, on April 1, 2007, X observed TP walk into the business suite shared by X and A and place TP's tax return (face up) on a table before leaving the area for a few minutes. Shortly after TP's departure, X testified that X walked over to the table and picked up TP's tax return. When TP returned to the area, X testified that "TP looked in my direction and suddenly acted extremely nervous and anxious. He was behaving quite strange. TP started to sweat profusely and was acting as if TP wanted to quickly leave the building."

If TP objects on the basis that the testimony contains improper opinions, what is the best response of the I.R.S., and explain how the Tax Court should rule.

b. (6 minutes)

Assume that X was permitted to testify to the statements at issue in Question E-3.a. During TP's cross-examination of X, TP asks X whether it is true that X was expelled from State University because X cheated on X's "American History" course final examination.

If the I.R.S. objects to this question on the ground that it is improper impeachment, what is TP's best response, and explain how the Tax Court should rule.

c. (6 minutes)

Assume that X was permitted to testify to the statements at issue in Question E-3.a. and that X (on cross-examination by TP) denied both the cheating and expulsion allegations (referenced in Question E-3.b.). As part of TP's rebuttal case, TP calls to the witness stand Dr. Doe, who was the president of State University at the time X was a enrolled there as a student. TP seeks to elicit testimony from Dr. Doe that Dr. Doe expelled X from the university based upon Doe's conclusion that X had cheated on X's "American History" final examination.

If the I.R.S. objects on the grounds that it is improper impeachment, explain how the Tax Court should rule.

d. (6 minutes)

Assume that X was permitted to testify to the statements at issue in Question E-3.a. On cross-examination by TP, X is asked (without objection) whether X was arrested in 2008 for bribery (a misdemeanor for purposes of this Question). X denies having been arrested for that offense. TP then seeks permission of the court to approach the witness in order to show X a copy of a police report reflecting X's 2008 arrest for bribery.

If the I.R.S. objects to the showing of this report, what is TP's best response, and explain how the Tax Court should rule.

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e. (6 minutes)

Assume that X was permitted to testify to the statements at issue in Question E-3.a. During cross-examination of X, TP seeks to admit a properly authenticated 2009 judgment and conviction order reflecting A's conviction for possession with intent to distribute methamphetamine (a felony for purposes of this Question).

If the I.R.S. objects on the grounds that it is improper impeachment, explain how the Tax Court should rule.

**PART FOUR LEGAL
ETHICS
(24 minutes)**

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

Question LE-1. (3 minutes)

A represents Martha Ballard in a Tax Court proceeding. A has filed a petition and undertaken discovery. The trial is scheduled to begin in two weeks. A has a signed agreement with Ballard that requires Ballard to pay A's fees on a monthly basis, but Ballard has failed to do so for the previous four months. A sends Ballard a letter informing her that A will no longer represent her in the Tax Court proceeding and that A will not appear at the trial.

Has A successfully withdrawn from the representation of Ballard? If not, what other steps, if any, must A undertake?

Question LE-2 (2 minutes)

Antonio Gomez has been issued a notice of deficiency with respect to his 2010 federal income tax return on which he claimed a dependency exemption for his neighbor, who is unrelated to Gomez and has never lived with Gomez. Gomez would like to engage B to represent him in a Tax Court proceeding with respect to the deficiency. Gomez tells B that he intends to challenge the deficiency on the ground that he provided \$5000 in 2010 to support the neighbor and it would be unfair for Gomez not to receive a dependency exemption.

Can B file a petition in Tax Court challenging the deficiency on that basis? Briefly explain your answer.

Question LE-3 (2 minutes)

C is tax counsel for Interactive Media, Inc., which was the acquiring corporation in the acquisition of assets from another corporation. In order to be a tax-free reorganization, Interactive needed to acquire substantially all of the assets of the other corporation. C was involved in determining which assets needed to be acquired and opining on their value. The IRS has issued a notice of deficiency challenging the tax-free character of the reorganization, and C has filed a Tax Court petition on behalf of Interactive Media. Assume it is necessary to call C as a witness and that Interactive Media has consented to calling C as a witness.

Can C continue to represent Interactive Media in the Tax Court proceeding? Briefly explain your answer.

Question LE-4 (3 minutes)

D represents Harry, the husband, in a divorce. Harry and Wendy, his former wife, received a notice of deficiency with respect to their 2010 income tax return, which they filed jointly after they separated. Wendy signed the 2010 return but asserts that she had no knowledge about several deductions that Harry took and that are the subject of the notice of deficiency. Harry has asked D to represent both Harry and Wendy in the Tax Court proceeding with respect to the deficiency.

Can D do so? Briefly explain your answer.

Question LE-5 (3 minutes)

E represents Naomi Ludders in a Tax Court proceeding in which the issue is whether Ludders was entitled to depreciation deductions for a computer, which Ludders claims she used solely for business purposes. At the trial, E has Ludders testify about the purchase of the computer and her use of it in her business. The next day Ludders reveals to E that she did not actually purchase a computer and that her receipt for a purchase of a computer was fraudulently prepared by a friend who works at the computer store. Thus, her testimony was false. What action, if any, should E take?

Question LE-6 (3 minutes) Same facts as LE-5 except that, as E is prepping Ludders for her testimony, Ludders reveals to E that she did not actually purchase a computer and that her receipt for a purchase of a computer was fraudulently prepared by a friend who works at the computer store. Ludders indicates that she intends to testify that she purchased the computer.

May E disclose to the court that Ludders did not purchase the computer? Briefly explain your answer.

Question LE-7 (2 minutes)

Same facts as LE-6.

If Ludders insists on testifying in her own behalf, must E call Ludders as a witness?

Briefly explain your answer.

Question LE-8 (3 minutes)

F, a partner in the Ready, Willing, and Able law firm, regularly provides tax advice to Sandra Woo, who runs a successful business. F designed a transaction intended to save federal income taxes. F explained the transaction to Woo who carried it out. F prepared all the documentation for the transaction and prepared Woo's tax returns on which she took the deductions produced by the transaction. The IRS subsequently audited Woo, and she received a notice of deficiency with respect to the transaction.

Can F represent Woo in the Tax Court proceeding with respect to the deficiency assuming that there would be no need to call Woo as a witness? Briefly explain your answer.

2012 Tax Court Non-Attorney Admission Examination

Question LE-9 (3 minutes)

G represents Hakeem Studdard, a resident of New York City, in a Tax Court proceeding. After submitting a brief on behalf of Studdard, G discovered a decision by the Ninth Circuit Court of Appeals, which is directly adverse to Studdard's position. The IRS brief does not mention the case.

Must G reveal the Ninth Circuit opinion to the Tax Court? Briefly explain your answer.