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## UWorld Review Questions

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## Regulation CPA Exam Questions

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### **UWorld CPA Exam Sample Questions**

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## Sample CPA Review Questions

### Question 1

#### Question Stem

An individual had the following gains and losses for the year:

Short-term capital loss	\$30,000
Long-term capital gain (unrecaptured Section 1250 at 25%)	18,000
Collectibles gain (28% rate)	20,000
Long-term capital gain (15% rate)	15,000

What will be the net capital gain (loss) reported by the individual and at what applicable tax rate(s)?

Answer Choices	
A)	Short-term ordinary loss of \$3,000, long-term gain of \$15,000 at 15%, Section 1250 gain of \$18,000 at 25%, and collectibles gain of \$20,000 at 28% rate.
B)	Section 1250 gain of \$3,000 at 25% and collectibles gain of \$20,000 at 28% rate.
C)	Section 1250 gain of \$8,000 at 25% and long-term gain of \$15,000 at 15%.
D)	Long-term gain of \$23,000 at the 15% rate.
<b>Correct:</b>	C

## Explanation

Depending on the holding period, a capital gain or loss will be classified as either long-term (LT) (ie, owned more than one year) or short-term (ST). The **gains** and **losses** are netted against each other, generally producing an overall net capital gain or loss. The deduction for a net capital loss is limited to \$3,000 annually for individuals.

Some long-term capital gains (LTCG) may be subject to **special tax rates** (eg, 15%, 25%, 28%) depending on the nature of the gain. For example, gains on collectible assets (eg, artwork, stamps) are taxed at 28%, while Section 1250 unrecaptured gains are taxed at 25%. To ensure that the **LTCG** are **taxed at the lowest preferential rate** possible, an ordering procedure is followed. **Losses** offset the gains in order from the **highest** to the **lowest tax rate**.

Here, the \$30,000 losses offset the gains in the following order, resulting in an \$8,000 unrecaptured Section 1250 gain taxed at 25% and a \$15,000 long-term capital gain taxed at 15%.

	<u>LT gain</u>	<u>Offsetting ST loss</u>	<u>Remaining LT gain</u>
Collectible gain (28%)	\$20,000	(\$20,000)	\$ 0
Unrecaptured Sect. 1250 (25%)	18,000	(10,000)	8,000
Capital gain (15%)	15,000	0	15,000
Net	\$53,000	(\$30,000)	\$23,000

**(Choice A)** A loss of \$3,000, a gain of \$15,000 (15%), an unrecaptured Section 1250 gain of \$18,000 (25%), and a collectibles gain of \$20,000 (28%) neglect to offset the LT gains with ST losses.

**(Choice B)** An unrecaptured Section 1250 gain of \$3,000 and a \$20,000 collectibles gain incorrectly apply losses to gains from the lowest to highest tax rates, rather than from highest to lowest.

**(Choice D)** A gain of \$23,000 taxed at 15% nets the gains and losses but incorrectly applies the 15% rate to all categories of gain.

### Things to remember:

Capital gains and losses are netted against each other, generally resulting in a net capital gain or loss. If the capital gains are taxed at different rates, the losses offset gains in order from the highest to the lowest tax rate.

**Question 2**

**Question Stem**

During the current tax year, a married taxpayer made the following gratuitous transfers:

Funds paid directly to a college to cover a friend's tuition (\$30,000) and room and board (\$19,000) expenses	\$49,000
Cash given to a grandchild (spousal gift-splitting elected)	25,000
Donation to a local political candidate's campaign	18,000
Cash given to spouse	20,000

Assuming that this year's annual gift tax exclusion is \$18,000, what amount of taxable gifts has the taxpayer made this year?

Answer Choices	
A)	\$0
B)	\$1,000
C)	\$3,000
D)	\$10,000
<b>Correct:</b>	<b>B</b>

## Explanation

A direct or indirect transfer to an individual is considered a gift if full consideration (measured in money or money's worth) is not received in return. However, **some transfers** are not subject to gift tax and therefore are deemed **excludable gifts**. This means the transfer is not reportable and not qualified for the annual gift tax exclusion or lifetime unified transfer tax exemption. Gifts subject to tax are first offset by the statutory annual gift tax exclusion per donee (ie, \$18,000 for 2024, or \$36,000 per married couple if spouses are gift-splitting).

Exclusions or deductions permitted from gross gifts include:

- Education exclusion amounts paid directly to an institution for tuition and fees (amounts for room and board are **not** included)
- Political contributions, which are excluded without limit
- Marital gifts of non-terminable (ie, outright) interests, which are deductible without limit
- Statutory annual gift tax exclusion per donee (double if spousal gift-splitting elected)

None of the exclusions or deductions require that a transfer be made to or on behalf of a relative of the donor (**Choices A, C, and D**).

In this scenario, the taxable gift amount is \$2,000, calculated as follows:

Gross gifts (\$49,000 + \$25,000 + \$18,000 + \$20,000)	\$112,000
Less:	
Education exclusion (tuition only)	(30,000)
Political donation	(18,000)
Cash given to spouse	(20,000)
Statutory annual exclusion per donee allowed against \$19,000 room and board	(18,000)
Statutory annual gift tax exclusion per donee for \$25,000* given to grandchild (spousal gift-splitting)	<u>(25,000)</u>
<b>Taxable gifts</b>	<b>\$1,000</b>

*\*Potential \$36,000 exclusion cannot exceed amount of the gift*

### Things to remember:

Some transfers are *not* subject to gift tax (eg, gifts to spouse, tuition paid to educational institutions, political donations) and, therefore, are deemed excludable gifts (ie, not reportable and not qualified for the annual gift tax exclusion). Gifts subject to taxation are entitled to a statutory annual gift tax exclusion.

**Question 3**

**Question Stem**

Monetary sanctions might be imposed against a CPA for disciplinary reasons by which of the following?

Answer Choices	
	<u>AICPA State Board of Accountancy PCAOB</u>
A)	Yes Yes Yes
B)	Yes Yes No
C)	No No Yes
D)	No Yes Yes
<b>Correct:</b>	D



## Explanation

Each **state's board of accountancy enforces** that state's professional conduct code. This enforcement includes the **authority to suspend** or revoke a **CPA's license** for acts discreditable to the profession and **impose monetary damages** when warranted.

The PCAOB is a private sector, nonprofit corporation created by the Sarbanes-Oxley Act of 2002. The **PCAOB** oversees accounting professionals who provide audit reports for publicly traded companies. Its **oversight authority includes** imposing **monetary** and nonmonetary **sanctions** on CPAs who violate PCAOB rules (**Choice C**).

**(Choices A and B)** Membership in the AICPA is voluntary. The organization does not have the authority to revoke or suspend a CPA's license or impose monetary sanctions; however, it can revoke a CPA's membership.

### **Things to remember:**

State boards of public accountancy have the authority to suspend or revoke a CPA's license and impose monetary damages for disciplinary reasons. The PCAOB's oversight authority includes imposing monetary and nonmonetary sanctions on CPAs who violate PCAOB rules. The AICPA does not have the authority to impose sanctions on a CPA.

## Question 4

## Question Stem

A self-employed individual purchased a van for \$30,000 on February 1, Year 1, for business use. The individual elected to take the Section 179 deduction. On January 1, Year 3, the individual sold the van for \$20,000. What amount must the individual report under Section 1245?

Answer Choices	
Header	<i>Enter Choice header here (if any)</i>
A)	\$10,000 ordinary loss.
B)	\$10,000 long-term capital loss.
C)	\$20,000 long-term capital gain.
D)	\$20,000 ordinary income.
<b>Correct:</b>	D

## Explanation

Section 1245 property is tangible or intangible personal property used in a trade or business that is subject to depreciation or amortization. Examples include equipment, furniture, and patents. Depreciation (or amortization) deductions are taken over the life of the asset, reducing *ordinary taxable income*.

In general, when an asset is sold at a gain (ie, sales price exceeds adjusted basis), it has the potential to be treated as a capital gain. However, when a **Section 1245 asset** is sold at a gain, a **portion** of the **gain** is recaptured (ie, reclassified) as **ordinary income**. The reclassification of the character of the gain is required to offset the depreciation deductions taken during the asset's life.

The Section 1245 recapture is the **lesser** of two amounts: the **accumulated depreciation** or the **realized gain**. Any **gain exceeding** the **recapture** amount is the result of the property's appreciation above its original cost and is treated as a Section 1231 gain, which is generally treated as a capital gain.

In this scenario, the individual recognized a total gain of \$20,000 [\$20,000 sales price – (\$30,000 cost basis – \$30,000 Section 179 expense)] (**Choices A and B**). Recapture under Section 1245 is limited to \$20,000 of *ordinary income* because that amount is the *lesser* of the \$20,000 gain and the \$30,000 depreciation (**Choice C**).

*Note: Section 179 expense taken by a taxpayer is, like annual depreciation, subject to recapture.*

### **Things to remember:**

When Section 1245 property is sold at a gain, the *lesser* of the recognized gain *or* the depreciation taken must be recaptured as ordinary income. Any remaining gain exceeding the recaptured amount is a Section 1231 gain treated as a long-term capital gain.

**Question 5****Question Stem**

Which of the following types of evidence is inadmissible as court testimony under the parol evidence rule?

Answer Choices	
A)	Evidence of a subsequent oral modification of the written contract.
B)	Evidence of a prior oral agreement that contradicts the written contract.
C)	Evidence of fraud in the execution of the written contract.
D)	Evidence that clarifies an ambiguous term in the written contract.
<b>Correct:</b>	<b>B</b>

## Explanation

The parol evidence rule (**PER**) bars from court testimony any **prior** or **contemporaneous** (concurrent) **oral** or **written contracts** that **contradict** the final **written contract**. Even if a contract is not required to have written evidence under the statute of frauds, if the parties do choose to make a written contract, the PER applies.

The PER does *not* prevent the use of evidence about:

- *Subsequent* oral or written modifications of the contract (eg, accord and satisfaction) (**Choice A**)
- Fraud in the execution of a written contract (**Choice C**)
- Clarification of ambiguous or missing terms in the written contract (**Choice D**)

The PER exists because courts assume a written, signed contract is the complete and final expression of its parties' agreement. This maintains the integrity of written contracts by preventing parties in a legal dispute from effectively "rewriting" a contract via court testimony. If the parties choose to change the written contract, they must *mutually* agree to those subsequent modifications.

### **Things to remember:**

The parol evidence rule (PER) bars from court testimony any prior or concurrent oral or written contracts that contradict the final written contract. The PER does not bar evidence about subsequent modifications, fraud, and clarifications about ambiguous or missing terms.