

FINAL EXAMINATION
FEDERAL INCOME TAXATION
PROFESSOR G. FLINT

ESSAY
PLEASE READ CAREFULLY

ALL ANSWERS ARE TO BE WRITTEN ON THE BLUE BOOKS PROVIDED WITH THIS EXAM. BE SURE TO NUMBER EACH RESPONSE.

There are three questions (time and percent indicated). The Time for completing the examination is three hours.

1. This examination is "open book". You may use your casebook, statutory supplement, and class notes. Use of calculators and cleansed laptops is permitted.
2. **Be sure to answer the specific question that is asked. No question asks for a general recitation about a topic from you notes.** Information supplied relating to general material from your notes or some unasked question will not increase your score and consumes you time needed to answer the asked questions.
3. If additional facts are necessary to resolve an issue, specify what additional facts you believe to be necessary and why they are significant. You may not make an assumption that changes or contradicts the stated facts.
4. Quality, not quantity, is desired. Think through and briefly outline your answer before you begin to write.
5. Write legibly. Be sure to formulate your answers in complete sentences and paragraphs with proper grammar. Failure to do so will result in an appropriately lower score.
6. Do not seek an interpretation of language in the question from anyone. If you sense ambiguity or typographical error, correct the shortcoming by shaping the question in a reasonable way and by recording your editorial correction in your answer.

Under the Honor Code, when you turn in this examination, you affirm that you have neither given, received, nor obtained aid in connection with this examination, nor have you known of any one so doing. If you cannot make this affirmation, you shall note such fact on your examination and must immediately advise the Dean of the reason therefore.

NOTE FOR ALL QUESTIONS--For purposes of those items that are adjusted annually by the Treasury Department to reflect inflation, use the numbers on the 2004 tax return provided with the syllabus. Also use the tax rates contained in the version of the Internal Revenue Code contained in the Supplement. Assume a federal rate of 10 %.

I. (50 %--1 ½ hours)

Ezekiel Solomon has decided to invest in a real estate partnership with several of his co-workers to purchase rent houses. Ezekiel Solomon's ownership percentage in the partnership will be 30 %. Another partner, Isidore Peltier, will handle all the repairs and the tenants so that the partnership work will not impinge on Ezekiel Solomon's job as a cook at a fancy restaurant. All Ezekiel Solomon need do is pay \$10,000 to the partnership. The partnership this year intends to purchase a duplex for \$100,000, putting down \$33,000 and borrowing the remaining \$67,000 at 10 % per annum. The partnership hopes to charge rents of \$800 per month and expects repairs and upkeep to run only \$100 per month and local taxes to be only \$400 per month.

Ezekiel Solomon's cooking job provides him with an annual salary of \$40,000. The restaurant also allows Ezekiel Solomon to eat "free" at the restaurant. Ezekiel Solomon has noticed that the amounts credited back to his account for these meals runs about \$300 per month. The restaurant also provides him with medical coverage worth \$250 per month of which he pays \$100. Ezekiel Solomon is single.

Ezekiel Solomon has entered your associate's office at Silk Stocking Law Firm, P.C. Ezekiel Solomon is concerned that the partnership investment might not provide him sufficient deduction to reduce his tax burden. Compute his taxable income. What is your response to Ezekiel Solomon's problem? Be sure to provide support, including Code sections.

II. (25%--3/4 hour)

Angeline Rogers operates a sole-proprietor, genealogical book publishing business. She has three employees that she pays monthly salaries of \$1500 each. Last year she purchased all new printing and binding equipment for \$10,000. Paper, ink, and bindings cost annually around \$20,000. Utilities run about \$300 per month. Rent costs the business \$500 per month. Last year Angeline Rogers's business produced 10,000 volumes of which she was able to sell 7,000 at \$30 each. Angeline Rogers has raised the price per volume for this year to \$35 each. Angeline Rogers expects this year's expenses to run 10 % more than last year. Angeline Rogers also expects to produce 20,000 volumes and sell 15,000.

Angeline Rogers is considering adopting a profit-sharing plan for her business. She wants to contribute \$35,000 this year to the profit-sharing plan. Angeline Rogers also wants to make a contribution to the Public Broadcasting station in San Antonio in the amount of \$20,000. Angeline Rogers is single.

Angeline Rogers has entered your associate's office at Blue Blood Law Firm, P.C. Angeline Rogers is concerned that the profit-sharing plan will significantly reduce her take-home pay from the book publishing business for the current year. Compute her taxable income. What is your response to Angeline Rogers's problem? Be sure to provide support, including Code sections.

III. (25 %--3/4 hour)

Alice Burpee spends her time as an investor in the securities markets. The last two years she made the following securities transactions:

Date	Shares	Security	Price Bought/Sold	Commission
4/30/03	10,000	Exxon	bought at \$30 per share	\$15.00 total
1/26/04	8,000	Texas Utilities	sold short at \$60 per share	\$16.00 total
4/1/04	\$10,000 face	Exxon Bond	\$6700	\$25.00 total
5/28/04	9,000	Exxon	sold at \$45 per share	\$16.00 total
6/4/04	10,000	Texas Utilities	bought at \$40 per share	\$15.00 total
11/1/04	\$10,000 face	Exxon Bond	\$8800	\$25.00 total

For the short sale, Alice Burpee had to borrow funds for which she paid \$99.00 in interest. She also received \$1.38 per share dividend on the Exxon stock during 2004 and had to pay \$.45 per share dividend on the short sale of Texas Utilities. The Bond paid \$1500 in interest on 9/1/04, and had accrued interest of \$250 on 4/1/04 and accrued interest of \$500 on 11/1/04.

Alice Burpee subscribes to the Investors Daily, which costs \$30 per month. Alice Burpee also went to Houston to attend the annual shareholder meeting of Exxon. The airfare was \$150, the hotel stay for 3 nights was \$600, food at Galleria area restaurants was \$200, the rental car was \$60, and the admission ticket to the art museum was \$10. Alice Burpee stayed over to shop at in the Galleria and bought \$800 in dresses.

Alice Burpee has entered your associate's office at Bribem and Stickem, P.C. Alice Burpee is not sure how to account for all these transactions on her 2004 tax return. Compute her taxable income. What is your response to Alice Burpee's inquiry? Be sure to provide support, including Code sections.