

SOLUTIONS MANUAL

SOUTH-WESTERN
FEDERAL TAXATION



CORPORATIONS,
PARTNERSHIPS,
ESTATES & TRUSTS

2013

Hoffman
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CHAPTER 2
WORKING WITH THE TAX LAW
SOLUTIONS TO PROBLEM MATERIALS

<u>Question/ Problem</u>	<u>Learning Objective</u>	<u>Topic</u>	<u>Status: Present Edition</u>	<u>Q/P in Prior Edition</u>
1	LO 1	Codifications of the Code	New	
2	LO 1	Changes in the Code	New	
3	LO 1	Origination of the tax laws	New	
4	LO 1	Joint Conference Committee	New	
5	LO 1	Missing Code section numbers	New	
6	LO 2, 5	Treaties	Unchanged	6
7	LO 1, 2	Regulation citation	Unchanged	7
8	LO 1, 2	Regulations	Unchanged	8
9	LO 1, 4	Types of Regulations	Unchanged	9
10	LO 1	Revenue Ruling citation	New	
11	LO 1, 4	Authority	Unchanged	11
12	LO 1	Citations	New	
13	LO 1	Using the judicial system	Modified	13
14	LO 1	Small Cases Division	Unchanged	14
15	LO 1	U.S. District Court	Unchanged	15
16	LO 1, 5	Judicial alternatives: trial courts	Modified	16
17	LO 1	U.S. Tax Court	Unchanged	17
18	LO 1	Judicial system	Unchanged	18
19	LO 1	Respondent	New	
20	LO 1	Appellate court and fact-finding determination	Unchanged	20
21	LO 1	Circuit Court of Appeals	New	
22	LO 1	Circuit Court of Appeals	Unchanged	22
23	LO 1, 4	Court decision validity	Unchanged	23
24	LO 2	Appeal to U.S. Supreme Court	Unchanged	24
25	LO 2	Citations	New	
26	LO 1, 2	Abbreviations	Unchanged	26
27	LO 2	Commerce Clearing House citations	Unchanged	27
28	LO 2	Location of decision of U.S. Court of Federal Claims	Unchanged	28
29	LO 1, 2	Cumulative Bulletin	Unchanged	29

<u>Question/ Problem</u>	<u>Learning Objective</u>	<u>Topic</u>	<u>Status: Present Edition</u>	<u>Q/P in Prior Edition</u>
30	LO 3	Tax research	Unchanged	30
31	LO 6	Tax avoidance versus tax evasion	Unchanged	31
32	LO 1	Subchapters	Unchanged	32
33	LO 1	Location of Revenue Rulings	Modified	33
34	LO 1, 4	Reliability	Unchanged	34
35	LO 1, 2	Publishers' citations	New	
36	LO 6	Tax avoidance versus tax evasion	Modified	36

<u>Research Problem</u>	<u>Topic</u>	<u>Status: Present Edition</u>	<u>Q/P in Prior Edition</u>
1	Citations	New	
2	Reliability	New	2
3	Internet activity	Unchanged	3

DISCUSSION QUESTIONS

1. The statement is not true. Neither the 1939 nor the 1954 Code substantially changed the tax laws existing on the date of enactment. The major change was the reorganization and renumbering of the tax provisions. So a judicial decision may still be valid. p. 2-1
2. This statement is true because statutory amendments to the tax law are integrated directly into the Code. p. 2-2
3. This statement is generally correct because Federal tax legislation generally starts in the House of Representatives. A tax bill can originate in the Senate when it is attached as a rider to another legislative proposal. p. 2-2
4. When the Senate version of the bill differs from that passed by the House, the Joint Conference Committee, which includes members of both the House Ways and Means Committee and the Senate Finance Committee, is called upon to resolve the differences. The deliberations of the Joint Conference Committee usually produce a compromise between the two versions, which is then voted on by both the House and the Senate. If both bodies accept the bill, it is referred to the President for approval or veto. p. 2-3
5. Not all Code Section numbers are used. When the 1954 Code was drafted, some Section numbers were intentionally omitted so that later changes could be incorporated into the Code without disrupting its organization. When Congress does not leave enough space, subsequent Code Sections are given A, B, C, etc., designations. A good example is the treatment of §§ 280A through 280H. p. 2-4
6. Hoffman, Maloney, Raabe, and Young, CPAs
5191 Natorp Boulevard
Mason, OH 45040

March 22, 2012

Mr. Butch Bishop

Tile, Inc.

100 International Drive

Tampa, Florida 33620

Dear Mr. Bishop:

This letter is in response to your request about information concerning a conflict between a U.S. treaty with France and a section of the Internal Revenue Code. The major reason for treaties between the U.S. and certain foreign countries is to eliminate double taxation and to render mutual assistance in tax enforcement.

Section 7852(d) provides that if a U.S. treaty is in conflict with a provision in the Code, neither will take general precedence. Rather, the more recent of the two will have precedence. In your case, the French treaty takes precedence over the Code section.

A taxpayer must disclose on the tax return any positions where a treaty overrides a tax law. There is a \$1,000 penalty per failure to disclose for individuals and a \$10,000 penalty per failure for corporations.

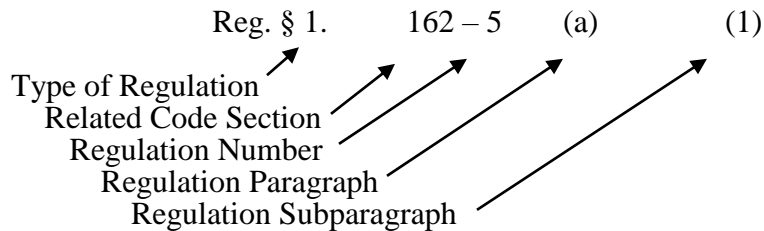
Should you need more information, feel free to contact me.

Sincerely,

Alice Hanks, CPA
Tax Partner

p. 2-18

7. Income tax



p. 2-6

8. Since Regulations interpret the Code, they are arranged in the same sequence as the Code. Regulations are prefixed by a number that designates the type of tax or administrative, procedural, or definitional matter to which they relate. These Regulations would be cited as follows with subparts added for further identification. The subparts have no correlation with the subsections in the Code.

- a. Reg. § 1.351.
- b. Prop. Reg. § 1.2036.
- c. Temp. Reg. § 1.482.
- d. Reg. § 1.1504.

p. 2-6

9. In many Code sections, Congress has given to the “Secretary or his delegate” the authority to prescribe Regulations to carry out the details of administration or otherwise to complete the prevailing administrative rules. Under such circumstances, it almost could be said that Congress is delegating its legislative powers to the Treasury Department. Regulations that are issued pursuant to this type of authority truly possess the force and effect of law and often are called “legislative” Regulations. Examples of “legislative” Regulations include those that address consolidated returns issued under §§ 1501 through 1505 and those that addressed the debt/equity question issued under § 385 (withdrawn).

Legislative Regulations are to be distinguished from “interpretive” Regulations, which purport to rephrase and elaborate on the meaning (i.e., intent of Congress) of a particular Code Section. An example of interpretive Regulations are those issued under § 1031 for like-kind exchanges.

Procedural Regulations are “housekeeping-type” instructions indicating information that taxpayers should provide to the IRS as well as information about the management and conduct of the IRS itself.

The need to distinguish between these three types of Regulations relates to their validity as a tax law source.

pp. 2-26 and 2-27

10. Rev. Rul. 63-144 is the 144th revenue ruling issued during 1963, and it appears on page 129 of Volume 2 of the Cumulative Bulletin in 1963. p. 2-8
11. The items would probably be ranked as follows (from lowest to highest):
 - (1) Letter ruling (valid only to the taxpayer to whom issued).
 - (2) Proposed Regulation (most courts ignore Proposed Regs.).
 - (3) Revenue Ruling.
 - (4) Interpretive Regulation.
 - (5) Legislative Regulation.
 - (6) Internal Revenue Code.

pp. 2-5 to 2-9, 2-26 to 2-27, and Exhibit 2.1

12. a. A Temporary Regulation, with 1 referring to the type of Regulation (i.e., income tax), 444 is the related Code section number, 2 is the subsection number, and T refers to temporary.
- b. Revenue Procedure number 23, appearing on page 609 of Volume 1 of the Cumulative Bulletin issued in 1994.
- c. Letter Ruling 48, issued in the 3rd week of 2001.

pp. 2-6 to 2-9

13. Dwain must consider several factors in deciding whether to take the dispute to the judicial system:
 - How expensive will it be?
 - How much time will be consumed?
 - Does he have the temperament to engage in the battle?
 - What is the probability of winning?

Once a decision is made to litigate the issue, the appropriate judicial forum must be selected.

- Tax Court judges have more expertise in tax matters.
- The tax deficiency need not be paid to litigate in the Tax Court. However, if Dwain loses, interest must be paid on any unpaid deficiency.
- If a trial by jury is preferred, the U.S. Tax Court is the appropriate forum.

- The tax deficiency must be paid before litigating in the District Court or the Court of Federal Claims.
- If an appeal to the Federal Circuit is important, Dwain should select the Court of Federal Claims.

A survey of the decisions involving the issues in dispute is appropriate. If a particular court has taken an unfavorable position, that court should be avoided.

pp. 2-10 to 2-15

- 14.
- a. No. There is no appeal from the Small Cases Division.
 - b. No. Deficiency cannot exceed \$50,000.
 - c. Yes.
 - d. No. However, decisions are now published on the Tax Court's website.
 - e. Yes.
 - f. Yes.

pp. 2-10 and 2-11

15. The major advantage of a U.S. District Court is the availability of a trial by a jury. One disadvantage of a U.S. District Court is that the tentative tax deficiency first must be paid before the Court will hear and decide the controversy. In the U.S. Tax Court, the tax need not be paid prior to litigating the controversy (although interest will be due on an unpaid deficiency). Concept Summary 2.1
16. Hoffman, Maloney, Raabe, and Young, CPAs
5191 Natorp Boulevard
Mason, OH 45040

July 8, 2012

Mr. Eddy Wall
200 Mesa Drive
Tucson, AZ 85714

Dear Mr. Wall:

You have three alternatives should you decide to pursue your \$323,000 deficiency in the court system. One alternative is the U.S. Tax Court, the most popular forum. Some people believe that the Tax Court judges have more expertise in tax matters. The main advantage is that the U.S. Tax Court is the only trial court where the tax need not be paid prior to litigating the controversy. However, interest will be due on an unpaid deficiency. The interest rate varies from one quarter to the next as announced by the IRS.

One disadvantage of the U.S. Tax Court is the possible delay that might result before a case is decided. The length of delay depends on the Court calendar, which includes a schedule of locations where cases will be tried. Another disadvantage is being unable to have the case heard before a jury.

The major advantage of another alternative, the U.S. District Court, is the availability of a trial by jury. One disadvantage of a U.S. District Court is that the tentative tax deficiency first must be paid before the Court will hear and decide the controversy.

The Court of Federal Claims, the third alternative, is a trial court that usually meets in Washington, D.C. It has jurisdiction for any claim against the United States that is based on the Constitution, any Act of Congress, or any regulation of an executive department. The main advantage of the U.S. Court of Federal Claims occurs when a taxpayer's applicable Circuit Court previously has rendered an adverse decision. Such a taxpayer may select the Court of Federal Claims, since any appeal instead will be to the Federal Circuit. One disadvantage of the Court of Federal Claims is that the tentative deficiency first must be paid before the Court will hear and decide the controversy.

I hope this information is helpful, and should you need more help, please contact me.

Sincerely,

Agnes Reynolds, CPA
Tax Partner

pp. 2-11, 2-12, Figure 2.3, and Concept Summary 2.1

17. The U.S. Tax Court hears only tax cases and is the most popular forum for tax cases. Some people suggest that the Tax Court has more expertise in tax matters. A taxpayer does not have to pay the tax deficiency assessed by the IRS before trial, but a taxpayer may deposit a cash bond to stop the running of interest. Appeals from a Tax Court are to the appropriate U.S. Court of Appeals. A taxpayer may not obtain a jury trial in the U.S. Tax Court. pp. 2-12 and 2-13
18. See Figure 2.3 and Concept Summary 2.1.
 - a. There is no appeal by either the taxpayer or the IRS from a decision of the Small Cases Division of the U.S. Tax Court. p. 2-10
 - b. The first appeal would be to the Sixth Circuit Court of Appeals. Further appeal would be to the U.S. Supreme Court. p. 2-12 and Figures 2.3 and 2.4
 - c. Same as b. above. p. 2-12 and Figures 2.3 and 2.4
 - d. The appeal would be to the Federal Circuit Court of Appeals and then to the U.S. Supreme Court. p. 2-12 and Figures 2.3 and 2.4
19. The term "respondent" is a synonym for defendant, who is the party against whom a suit is brought. p. 2-11
20. Both the Code and the Supreme Court indicate that the Federal appellate courts are bound by findings of facts unless they are clearly erroneous. Thus, the *role* of appellate courts is limited to a review of the record of trial compiled by the trial courts. Thus, the appellate process usually involves a determination of whether the trial court applied the proper law in arriving at its decision. Rarely will an appellate court disturb a lower court's fact-finding determination. p. 2-13

- 21. a. 9th.
- b. 5th.
- c. 10th.
- d. 8th.
- e. 11th.

Figure 2.4

- 22. The appropriate Circuit Court of Appeals for an appeal depends on where the litigation originated. For example, an appeal from Texas would go to the Fifth Circuit Court of Appeals, or an appeal from Colorado would go to the Tenth Circuit Court of Appeals. p. 2-14 and Figure 2.4
- 23. a. If the taxpayer chooses a U.S. District Court as the trial court for litigation, the U.S. District Court of Wyoming would be the forum to hear the case. Unless the prior decision has been reversed on appeal, one would expect the same court to follow its earlier holding. pp. 2-10 and 2-27
- b. If the taxpayer chooses the U.S. Court of Federal Claims as the trial court for litigation, the decision that previously was rendered by this Court should have a direct bearing on the outcome. If the taxpayer selects a different trial court (i.e., the appropriate U.S. District Court or the U.S. Tax Court), the decision that was rendered by the U.S. Court of Federal Claims would be persuasive, but not controlling. It is, of course, assumed that the result that was reached by the U.S. Court of Federal Claims was not reversed on appeal. pp. 2-10, 2-14, and 2-27
- c. The decision of a U.S. Circuit Court of Appeals will carry more weight than will one that was rendered by a trial court. Since the taxpayer lives in California, however, any appeal from a U.S. District Court or the U.S. Tax Court would go to the Ninth Circuit Court of Appeals (see Figure 2.2). Although the Ninth Circuit Court of Appeals might be influenced by what the Second Circuit Court of Appeals has decided, it is not compelled to follow such holding. pp. 2-10, 2-14, 2-27, and Figure 2.4
- d. Because the U.S. Supreme Court is the highest appellate court, one can place complete reliance upon its decisions. Nevertheless, one should investigate any decision to see whether the Code has been modified with respect to the result that was reached. There also exists the rare possibility that the Court may have changed its position in a later decision. pp. 2-10, 2-15, 2-27, and Figure 2.3
- e. When the IRS acquiesces to a decision of the U.S. Tax Court, it agrees with the result that was reached. As long as such acquiescence remains in effect, taxpayers can be assured that this represents the position of the IRS on the issue that was involved. Keep in mind, however, that the IRS can change its mind and can, at any time, withdraw the acquiescence and substitute a nonacquiescence. p. 2-16
- f. The issuance of a nonacquiescence usually reflects that the IRS does not agree with the result that was reached by the U.S. Tax Court. Consequently, taxpayers are placed on notice that the IRS will continue to challenge the issue that was involved. p. 2-16

24. There is no automatic right of appeal to the U.S. Supreme Court. Appeal is by *writ of certiorari*. If the Court agrees to hear the dispute, it will grant the *writ* (*Cert. granted*). Most often, the highest court will deny jurisdiction (*Cert. denied*). p. 2-15
25. a. This citation is to a regular decision of the U.S. Tax Court that was issued in 1950. The decision can be found in Volume 14, page 74, of the Tax Court of the United States Report, published by the U. S. Government Printing Office. pp. 2-15 to 2-18 and Concept Summary 2.2
- b. This citation is for a decision of the U. S. Fifth Circuit Court of Appeals that was rendered in 1979. The decision can be found in Volume 592, page 1251, of the Federal Reporter, Second Series (F. 2d), published by West Publishing Company. pp. 2-15 to 2-17 and Concept Summary 2.2
- c. This citation is for a decision of the U.S. Sixth Circuit Court of Appeals that was rendered in 1995. The decision can be found in Volume 1 for 1995, paragraph 50,104 of U.S. Tax Cases, published by Commerce Clearing House. pp. 2-15 to 2-17 and Concept Summary 2.2
- d. This citation is for a decision of the U.S. Sixth Circuit Court of Appeals that was rendered in 1995. The decision can be found in Volume 75, page 110, of the Second Series of American Federal Tax Reports, published by RIA. pp. 2-15 to 2-17 and Concept Summary 2.2
- e. This citation is for a decision of the U.S. District Court of Texas that was rendered in 1963. The decision can be found in Volume 223, page 663, of the Federal Supplement Series, published by West Publishing Company. pp. 2-15 to 2-17 and Concept Summary 2.2
26. a. CA-2. An abbreviation that designates the U.S. Second Circuit Court of Appeals. pp. 2-15 to 2-17
- b. Fed.Cl. An abbreviation for the Federal Claims Reporter published by West Publishing Company. It includes the decisions of the U.S. Court of Federal Claims and begins with Volume 27. pp. 2-15 to 2-17
- c. aff'd. An abbreviation for "affirmed," which indicates that a lower court decision was affirmed (approved of) on appeal. p. 2-13
- d. rev'd. An abbreviation for was "reversed," which indicates that a lower court decision was reversed (disapproved of) on appeal. p. 2-13
- e. rem'd. An abbreviation for "remanded," which indicates that a lower court decision is being sent back by a higher court for further consideration. p. 2-13
- f. Cert. denied. The Writ of Certiorari has been denied by the U.S. Supreme Court. This writ means that the Court will not accept an appeal from a lower court and, therefore, will not consider the case further. p. 2-15
- g. Acq. An abbreviation for "acquiescence" (agreement). The IRS follows a policy of either acquiescing or nonacquiescing to certain decisions. p. 2-16
- h. B.T.A. An abbreviation for the Board of Tax Appeals. From 1924 to 1942, the U.S. Tax Court was designated as the Board of Tax Appeals. p. 2-16

- i. USTC. U.S. District Court, U.S. Circuit Court of Appeals, U.S. Court of Federal Claims, and U.S. Supreme Court decisions that address Federal tax matters are reported in the Commerce Clearing House U.S. Tax Cases (USTC) and the RIA (formerly P-H) American Federal Tax Reports (AFTR) series. pp. 2-16, 2-17, and Concept Summary 2.2
 - j. AFTR. See the solution to i. above. pp. 2-16, 2-17, and Concept Summary 2.2
 - k. F.3d. All of the decisions (both tax and nontax) of the U.S. Claims Court (before October 1982) and the U.S. Circuit Court of Appeals are published by West Publishing Company in a reporter that is designated as the Federal Reporter, Second Series (F.2d). Volume 999, published in 1993, is the last volume of the Federal Second Series. It is followed by the Federal Third Series (F.3d). p. 2-17 and Concept Summary 2.2
 - l. F.Supp. Most Federal District Court decisions, dealing with both tax and nontax issues, are published by West Publishing Company in their Federal Supplement Series (F.Supp.). p. 2-16 and Concept Summary 2.2
 - m. USSC. An abbreviation for the U.S. Supreme Court. p. 2-17
 - n. S.Ct. West Publishing Company publishes all of the U.S. Supreme Court decisions in its Supreme Court Reporter (S.Ct.). p. 2-17 and Concept Summary 2.2
 - o. D.Ct. An abbreviation for a U.S. District Court decision. p. 2-17
27. a. None.
- b. USTC.
- c. USTC.
- d. USTC.
- e. TCM.
- pp. 2-16, 2-17, and Concept Summary 2.2
28. Decisions of the U.S. Court of Federal Claims (formerly named the Claims Court) are published in the USTCs, AFTRs, and the West Publishing Co. reporter called the Federal Reporter, Second Series (F.2d) (before October 1982) and Claims Court Reporter (beginning October 1982 through October 30, 1992). The name of the U.S. Court of Federal Claims was changed from the Claims Court effective October 30, 1992. Currently, this court's decision are published in the Federal Claims Reporter. pp. 2-16, 2-17, and Concept Summary 2.2
29. a. Yes. Exhibit 2.1
- b. No. Not published there. Concept Summary 2.2
- c. No. Published by private publishers. pp. 2-8, 2-9, and Exhibit 2.1
- d. Yes. p. 2-8 and Exhibit 2.1
- e. Yes. p. 2-7 and Exhibit 2.1

- f. No. pp. 2-16, 2-17, and Concept Summary 2.2
 - g. Yes, when major tax legislation has been enacted by Congress. Footnote 10
 - h. Yes. p. 2-16
 - i. No. Concept Summary 2.2
30. After understanding the relevant facts:
- Yvonne may begin with the index volumes of the available tax services: RIA, CCH, BNA Portfolios, etc.
 - A key word search on an online service could be helpful—WESTLAW, LEXIS, CCH, and RIA Checkpoint.
 - Yvonne may employ a key word search of a CD-ROM and browse through a tax service, IRS publications, etc. West Publishing, CCH, Kleinrock, and RIA offer CD-ROM products.
 - Yvonne could consult CCH's Federal Tax Articles to locate current appropriate articles written about alimony payments. RIA's Tax Service also has a topical "Index to Tax Articles" section that is organized using the RIA paragraph index system.
 - Yvonne may consult The Accounting & Tax Index which is available in three quarterly issues and a cumulative year-end volume covering all four quarters.
 - Up-to-date information may be found on the World Wide Web feature of the Internet. Various legal, accounting, and financial gateways can be found by clicking on highlighted words or phrases.
- pp. 2-19 to 2-30
31. Denis Healy says "the difference between tax avoidance and tax evasion is the thickness of a prison wall." A fine line exists between legal tax planning and illegal tax planning—tax avoidance versus tax evasion. Tax avoidance is merely tax minimization through legal techniques. In this sense, tax avoidance is the proper objective of all tax planning. Tax evasion, while also aimed at the elimination or reduction of taxes, connotes the use of subterfuge and fraud as a means to an end. p. 2-33

PROBLEMS

- 32. d. p. 2-4
- 33. d. Exhibit 2.1
- 34. a. Code section.
- b. Legislative Regulation.
- c. Recent Temporary Regulation.
- d. Interpretive Regulation.

- e. Revenue Ruling.
- f. Letter Ruling.
- g. Proposed Regulation.

pp. 2-26, 2-27, and Exhibit 2.1

- 35.
- a. U.S.
 - b. CCH.
 - c. W.
 - d. RIA.
 - e. CCH.
 - f. RIA.
 - g. U.S.
 - h. U.S.
 - i. W.
 - j. U.S.

pp. 2-15 to 2-17 and Concept Summary 2.2

- 36.
- a. E.
 - b. E.
 - c. A.
 - d. A.
 - e. A.

pp. 2-30 to 2-34

Proposed solutions to the **Research Problems** and the **Appendix E Tax Return Problems** are found at the Instructor Companion Site for the textbook (www.cengage.com/taxation/swft). Previously, these items were a part of the Instructor's Guide for the text, but now they are available online at this site as free-standing documents, as well as on the Instructor's Resource CD.