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Federal Income Tax Law: Final Examination (January 1966)

William & Mary Law School

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[See instructions at the end of the problem]

Taxpayer is 67 years old, his spouse 62 and blind, his son is 30 and fully dependent on taxpayer. During calendar year 1965 Taxpayer had the following receipts:

\$1524 Social Security benefits

\$5000 gift from his employer upon his retirement on 1/1/65. The employer was under no legal duty to make this payment.

A gift of a silver service set, valued at \$1000, from a firm to whom he referred customers. He had no expectation of any gifts from this firm, nor has it been the custom of this firm to make such gifts.

A motor boat, valued at \$1500, from his brother. Taxpayer likes to fish, and his brother felt that now that he has retired he should do more fishing.

A \$250 award from a civic organization in recognition of a patriotic composition written by taxpayer. He did not enter this competition in a contest, but merely read it at a rally.

A \$5000 bequest from his father: the testator appointed him executor and made this gift to him for acting as such.

Taxpayer owns an apartment building. He received rents of \$8000, of which \$7000 was for current rents and \$1000 for rents due in 1970, which by the terms of the lease one tenant had to pay in advance. He also received \$2000 for agreeing to cancel one tenant's lease that had 3 more years to run. He constructed the building in 1950 for \$50000; it has an estimated life of 50 years, no salvage value.

Taxpayer collected the following annuities:

\$1000 on an annuity that cost him \$8000 and is payable at the rate of \$1000 per year for 10 years.

\$1000 on a group annuity the premiums for which were paid by the employer and not included in the income of taxpayer.

\$1000 on a group annuity to which taxpayer contributed by payroll withholdings a total of \$2200. In 1963 and 1964 he collected a total of \$2000 on this annuity.

An endowment policy matured in 1965 in the amount of \$10000.

Gross premiums paid by taxpayer amounted to \$8000. During the premium paying period \$1000 dividends on this policy were paid to taxpayer by this mutual life insurance company.

Taxpayer's brother has an interest in a partnership. In order to reduce his own (i. e., brother's) income taxes he assigned (without consideration) all his income therefrom to taxpayer. Brother's distributive income for 1965 was \$5000. The whole \$5000 was paid directly to taxpayer.

To show his appreciation for the above transfer, taxpayer clipped bond coupons in the amount of \$1000 and donated them before maturity to his brother's favorite charity (a church) advising the charity that this donation is in honor of brother.

Taxpayer set up a 12 year trust (reversionary interest in him after 12 yrs.) income from which to be used for support of his 30 year old dependent son. He had no control at all over the trust. Income of trust in 1965 was \$2000, all of which was spent on maintenance of the son including \$500 for hospital expenses.

Taxpayer had an automobile/during the year. He received property damages of \$500 (it cost \$400 to repair the damage) and punitive damages of \$5000 and personal injury damages of \$1000. Medical expenses were \$600. During the year 1965 taxpayer entered into the following transactions: He sold his residence for \$27000 and purchased a new one for \$18000 within one year after the sale. Selling expenses were \$1500, fixing-up expenses \$500. Cost of residence sold \$18000, purchased in 1950, lived in continuously since then.

Bonds he bought on 2/1/65 for \$1000 became worthless on 4/3/65.

A personal loan of \$250 he made (i. e., he lent the money) in 1957 became worthless on 5/1/65.

On 9/1/65 he sold furniture he had used in his rental building:

Sales price \$1550, cost on 1/1/55 \$3300, depreciation through 1964 \$2700 (\$300/annum)

He had a casualty loss on his summer cottage which he owned since 1960 in amount of \$350.

On his rental apartment he had the following expenses:

Taxes - property \$500, Insurance \$200, interest \$200, repairs \$100. He replaced the roof in December of 1965 at a cost of \$5000. A leak in a gutter caused rain water to drip on the sidewalk. This was a violation of a city ordinance and he had to pay a fine of \$100. A neighbor claimed that the fence on the right side of this property was encroaching on neighbor's property. Taxpayer brought suit to clear the title and his legal fees and costs amounted to \$1000.

During 1965 he made the following personal expenditures:

Life insurance premiums \$500, health insurance \$200, insurance on his auto \$200, state income taxes \$500, federal income taxes \$5000, state sales taxes \$200, federal excise taxes \$50, property taxes on his residence \$200, personal property taxes \$100, hospital and doctor bills for himself (exclusive of accident medical bills) \$800, doctor bills for his wife \$500, medicines for himself \$100, medicines for his wife \$80, doctors for his son (exclusive of trust payments) \$300, medicines for his son \$314.50, \$9000 contributions to qualified organizations (exclusive of bond coupons), \$800 wages to a maid, \$56 social security thereon, \$200 for termite treatment on his residence, \$500 tuition for art lessons, \$5 for fishing license, \$10 cigarette taxes, \$1000 funeral expenses for his father, \$100 contribution to Democratic Party.

You are to determine the taxable income of taxpayer. Discuss the reasons for including or excluding each item of receipt or disbursement. If §1231 is involved explain why you finally did what you did.