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QUARTERLY CPE EXAM ON THE *Journal of Accountancy*
Second Quarter (April - June), 2019 (Course # 1902)
A Formal CPE Course using the *JoA* as Reference Material
Recommended CPE Credit: 10 Hours (Category: Interactive Self Study)
Subject division: Finance 1; Mgt. 5; Tax 4; (All Technical)

INSTRUCTIONS:

1. Complete but do not submit all the assignments in the **Supplementary Study Guide** with **Course objectives** available at our Web site: www.accounting-education.com
2. Answer the 50 multiple-choice questions by selecting the one **best** answer. **Blacken** the letter; do **not** circle. A score of 70 or better is required.
3. Unless prepaid, please submit a Payment Voucher with your completed Exam.
4. ***Scan/email***, fax or snail mail your answer sheet to AEA for grading by deadline below.
5. For CPE credit, please be sure your name and email address are legible.
6. ***For faster response, please provide your email address below.***

COURSE EVALUATION:

On a scale of A (highest) to F (lowest), please evaluate the following:
____ 1. The course met the objectives described in the promotional material?
____ 2. Any stated prerequisites were necessary or desirable?
____ 3. The course was timely and effective?
____ 4. The course met your professional education needs?
____ 5. The course materials were understandable and helpful?

On my honor as a CPA or CMA, I have neither given nor received assistance on this Exam.

(Signed) ______________________________ (Dated) ___________

Please print your full name: ____

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To which state boards or agencies do you report CPE? ___________________

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We encourage you to scan and email your answer sheet to info@accounting-education.com
****For CPE credit, this exam <u>must</u> be submitted to AEA by 8/15/2021.****

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Date completed: __________________

"Our net worth is ultimately defined not by dollars but rather by how well we serve others."
...Paul Allen – co-founder of Microsoft

This is a formal Interactive self-study CPE course using the ***Journal of Accountancy*** as reference material designed to keep you abreast of the latest changes affecting our profession. Our course consists of a Supplementary Study Packet (available at our Web site: www.accounting-education.com) and this Final Exam; it is divided into sections, each corresponding to selected articles appearing in the JoA. This series of quarterly formal self-study programs can be completed in your home or office without the inconvenience and high costs associated with many CPE courses. New courses normally appear on our Web site around the beginning of each quarter.

LEARNING OBJECTIVES:
The specific learning objectives are stated in the individual sections of the **Supplementary Study Guide** associated with this Quarterly CPE Exam available at www.accounting-education.com

PREREQUISITES: None.

LEVEL: Basic.

COURSE NUMBER: The course number we assign to each Quarterly CPE Exam is derived from the Year and Quarter, YYQQ.

COURSE SPONSOR:
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RECOMMENDED CPE CREDIT:
We recommend CPE credit of ten (10) hours in accordance with the standards of NASBA, CPE credits have been granted based on a 50-minute hour for Interactive Self-Study CPE courses. The estimated completion time of 10 hours is based on pilot tests of our Study Packet, reference material readings and final exam and are likely to vary from quarter to quarter. A few state boards still use the old standard of awarding CPE credit of only 50% of the estimated completion time. For further guidance, please check with your own state board or agency.

SUBJECT DIVISIONS OF CPE CREDIT:
The recommended subject division is shown on the Final Exam answer sheet, applies to this quarter only and is likely to vary from quarter to quarter.

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The price of a **Quarterly CPE Exam** is $49, with lower prices when an order involves four or more courses:

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Price per course for orders of 4 to 7 courses:	$46
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Firm (If part of address) ____________________________
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I am submitting _____ completed Exam(s) on the ***JofA*** that I've downloaded from www.accounting-education.com

Quantity Year
_____ First Quarter (January - March), 20___
_____ Second Quarter (April - June), 20___
_____ Third Quarter (July - September), 20___
_____ Fourth Quarter (October - December), 20___

_____ First Quarter (January - March), 20___
_____ Second Quarter (April - June), 20___
_____ Third Quarter (July - September), 20___
_____ Fourth Quarter (October - December), 20___

_____ Total Quantity times Unit price of $ _____ = $ _______ Total charge

Unit price depends on total number of Exams:

1 – 3 Exams: $49	8 – 23 Exams: $43
4 – 7 Exams: $46	24 and over: $40

Payment options:

______ By check that I'm mailing today.
(Take a dollar off each exam you pay by check.)

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Optional: Please estimate your course completion time. _____

Thank you for your business and referrals.

The learning objectives of this course are in the Study Guide at www.accounting-education.com.

Sections I–V and Exam Questions 1–30 Relate to the *Journal of Accountancy* of April/May, 2019.

Section I. Providing Services to Cannabis Clients (Page 16)

1. Federally-insured banks cannot accept deposits from activities illegal under federal law. Therefore, cannabis enterprises primarily:
   a. Use PayPal.
   b. Use cryptocurrency, such as bitcoin.
   c. Deal in cash.
   d. Use off-shore banks.
   e. Use virtual banks.

2. In addition to banking challenges, what other issues can arise from differing legal treatment of cannabis between federal and state laws?
   a. Possible limited access to the US judicial system.
   b. Possible limited access to the bankruptcy process.
   c. Limited ability to restructure or discharge debt.
   d. No access to state courts.
   e. a, b and c.

3. When considering a cannabis business engagement, the author recommends that you:
   a. Meet with the prospect's banker to understand the cash flow.
   b. Conduct credit and criminal background checks on the owners, management and those charged with governance.
   c. Consult the local Better Business Bureau for complaints and resolutions.
   d. Contact the prior CPA to get copies of the three prior years' tax returns.
   e. Have an underage third party attempt a purchase from the prospect.

4. What advice does the author recommend regarding cannabis client billing?
   a. Always collect in cash; cannabis clients are more likely to issue bad checks.
   b. To reduce risk of theft and to keep a distance from illegal activities, never accept cash.
   c. Require a retainer and maintain a positive balance.
   d. b and c.
   e. None of the above.

5. How do IRS rules under Sec. 280E treat cannabis business expenses differently from those in a federally-legal business?
   a. Cost of goods sold are <u>not</u> deductible.
   b. Cost of goods sold <u>are</u> deductible, but not other business expenses.
   c. Cost of goods sold are <u>not</u> deductible because the cannabis product is illegal, but other business expenses such as rent and payroll <u>are</u> deductible.
   d. No expenses are deductible because the business is illegal.
   e. No expenses are deductible. Cannabis revenue is subject a federal excise tax only.

Section II. Business Development Tips to Boost a Firm's Reach (Page 34)

6. What type of online marketing did a suburban Chicago area CPA firm (DHJJ) employ to compete in the greater Chicago area market and beyond?
   a. Content marketing.
   b. Paid online advertising.
   c. Targeted email blasts.
   d. Search algorithm manipulation.
   e. Data analytics.

7. What did DHJJ do to develop or acquire expertise in state and local tax (SALT) knowledge in order to form a niche in that area?
   a. Recruit talent from a larger firm.
   b. Identify interested staff and focus their CPE hours on SALT topics.
   c. Hire experienced employees from state and local taxing agencies.
   d. Nothing, they formed a practice group with existing employees who already had the skills.
   e. Purchased an area firm that already had a SALT niche.

8. How does DHJJ attract attention to its SALT practice group?
   a. Direct mail announcements.
   b. Blog posts.
   c. Host webinars.
   d. All of the above.
   e. b and c only.

9. Salim Omar, founder of CPA Marketing Genius, suggests using networking events as an opportunity to:
   a. Showcase expertise by leading the event.
   b. Showcase expertise by appearing as a guest speaker.
   c. Hand out business cards.
   d. a and b.
   e. a, b and c.

10. A Dubuque, Iowa CPA developed a client patronage app to encourage employees to shop at client businesses. The app also:
    a. Attracted new clients who want exposure to the firm's 500 employee shoppers.
    b. Helped retain existing clients who see the value in referrals.
    c. Induced clients to offer discounts to the employee shoppers.
    d. a, b and c.
    e. a and b.

Section III. How the "Sandwich Generation" Affects Retirement (Page 44)

11. Multigenerational households include:
    a. The "sandwich generation."
    b. The "boomerang generation."
    c. The "baby boomer generation."
    d. a and b.
    e. b and c.

12. Which of the following descriptions are accurate?
    a. The "sandwich generation" involves adults who care for parents while supporting their children.
    b. The "sandwich generation" involves young adults who return home to live with their parents.
    c. The "sandwich generation" involves grandparents taking care of grandchildren.
    d. The "boomerang generation" involves adults caring for their parents.
    e. The "boomerang generation" involves older siblings taking care of younger siblings.

13. In multigenerational households student loan debt is often an issue. The author notes that many of the people who are over the age of 60 and behind on their student loan payments:
    a. Attended expensive private schools and incurred substantial student loan debt.
    b. Received a degree in subject matter that did not lead to a high-paying job.
    c. Did not finish college.
    d. Co-signed their children's student loans.
    e. Filed for bankruptcy.

14. What advice does the author offer about adding children's names to the parent's bank accounts?
    a. Do it. It will make access to funds easier in an emergency.
    b. Avoid it. The accounts will be at risk for the child's creditor claims.
    c. Not a bad idea. It may help avoid any gift or estate tax.
    d. Not a bad idea. It could help raise the child's credit score.
    e. Avoid it. It could decrease the child's ACA premium credit.

15. Whether parents move in with their children or into assisted living, discussion of some financial issues can be emotional but needs to happen in advance. Topics include:
    a. Parent's available resources, including pensions and social security.
    b. Parent's home.
    c. Immediate and long-term care needs.
    d. a and b.
    e. a, b and c.

Section IV. Avoid Tax Traps with a Timely Appraisal (Page 48)

16. The Tax Cuts and Jobs Act left in place what some call the biggest loophole in the code, basis "step-up," which
    a. Allows a person to gift property to a direct descendant at market value as of the date of the gift.
    b. Allows a taxpayer to donate stock to a charity and deduct the original cost basis.
    c. Allows the recipient of gifted property to "step-up" their tax basis to current market value.
    d. Allows the inheritor to "step-up" the tax basis of the inherited property to the value at the date of death.
    e. Allows the IRS to "step-up" the tax basis of gifts to market value, thus using more of the gift tax exclusion.

17. Gifting strategies to maximize basis step-up include:
    a. Avoid gifting highly appreciated property (so inheritors get the basis step-up at death).
    b. Consider gifting assets with a high tax basis.
    c. Consider gifting assets that are slower to appreciate in value.
    d. a and b.
    e. a, b and c.

18. Irrevocable grantor trusts can help establish basis step-up using "substitution powers." How would a grantor use this technique effectively?
    a. Transfer low-basis assets to the trust.
    b. Have the trust donate high-basis assets to charity.
    c. Transfer high-basis assets to the trust in exchange for low-basis assets.
    d. Direct the trust to sell high-basis assets and hold the cash in a money market fund.
    e. Direct the grantor trust to transfer low-basis assets to a spousal trust.

19. With the increased estate and gift tax exemption, what does the author recommend regarding existing credit shelter trusts?
    a. Consider modifying the credit shelter trust to allow assets to enter the estate so the surviving spouse can get the basis step-up.
    b. Consider modifying the credit shelter trust to retain the assets so the surviving spouse gets the basis step-up.
    c. Consider transferring low-basis assets from the credit shelter trust to an irrevocable grantor trust.
    d. Consider modifying the credit shelter trust to donate high-basis assets to charity.
    e. Fund the credit shelter trust using a life insurance trust.

20. With the increased gift and estate tax exemptions, the author recommends reviewing and modifying existing irrevocable trusts for negative tax consequences. As part of this review, what are some potential nontax advantages you may want to preserve?
    a. Basis step-up.
    b. Protection from creditors.
    c. Preservation of assets in case of divorce.
    d. a and b.
    e. b and c.

21. In 2015, the Surface Transportation and Veterans Health Care Choice Improvement Act made "basis consistency" a statutory requirement. What is "basis consistency?"
    a. The selling price of inherited property must equal the appraised value.
    b. The selling price of inherited property must equal the the value listed on the estate tax form.
    c. The value used for estate tax reporting must match the basis claimed by the beneficiary.
    d. Values used for estate tax reporting must be supported by an independent appraisal.
    e. Values claimed by the beneficiary must be supported by an independent appraisal.

22. What can help the IRS monitor "basis consistency?"

    a. New Form 8971 (sent to the IRS) and Schedule A (sent to the beneficiary) show asset valuations reported by the estate.
    b. Old Form 8971 has been replaced with Schedule A (sent to the IRS) which shows asset values.
    c. The IRS reviews copies of all appraisal reports which all estates are required to provide.
    d. Estate executors are now required to send new Form 8971 to all beneficiaries.
    e. There is a new 65% accuracy-related penalty.

23. You are asked to prepare a 2019 individual income tax return that includes the sale of an inherited home. The taxpayer claims an extraordinarily high cost-basis and provides no substantiation. How do you proceed?

    a. Prepare the return. The taxpayer alone is responsible for any inaccurate information.
    b. Prepare the return. Inform the taxpayer that they are subject to a valuation misstatement penalty only.
    c. Tax preparers are subject to the <u>Sec. 6694 penalty</u> if they knew or should have known of a valuation misstatement. Either get suitable substantiation or consider declining the engagement.
    d. The tax preparer is subject to the <u>Sec. 6662(e) 20% accuracy-related penalty</u>. Proceed with caution.
    e. Provide the taxpayer a value you consider reasonable and proceed.

24. The owner of a business dies. After a substantial period of time, an appraiser is asked to value the business. Since death, business revenue has collapsed due to an event that as of the date of death was not known or knowable. How will this subsequent event affect the appraised value?
    a. The business has no value beyond the current liquidation value of the assets.
    b. The appraiser must consider this subsequent event, but must also consider the likelihood that future events will improve the revenue stream.
    c. The appraiser must consider the event but also discount the negative effects.
    d. The appraiser has discretion whether to consider subsequent events but must not mention them in disclosures.
    e. The appraiser ignores the subsequent event but may disclose for informational purposes only.

25. On your most recently filed income tax return you report the sale of property you inherited six years ago. The IRS informs you that the entire proceeds of the sale are taxable because you have zero cost-basis. In addition to the tax, you owe various penalties. How did this happen?
    a. The executor of the estate failed to get a timely appraisal.
    b. The estate was taxable, so an estate tax return was required to be filed.
    c. The executor did not file an estate tax return.
    d. The IRS asked for substantiation of your cost basis which you "ballparked" with no support.
    e. All of the above.

Section V. Optimizing Residential Real Estate Deductions (Page 56)

26. A comprehensive remodeling would be considered:
    a. A betterment or restoration and expensed in the year incurred.
    b. A betterment or restoration and capitalized.
    c. A maintenance item because the structure is not enlarged.
    d. A maintenance item expensed under the *de minimis* rules.
    e. A betterment capitalized and deducted under Sec. 179.

27. If an expenditure is determined <u>not</u> to be a betterment, restoration or adaptation, the next step is to determine whether it can be expensed under:
    a. Sec. 179.
    b. *De minimis* rules or small taxpayer election.
    c. Routine maintenance safe harbor.
    d. a, b and c.
    e. b and c only.

28. A taxpayer spent $2,500 to improve a residential rental property, which you determine to be a "betterment" and normally capitalized. Which tax treatment would you advise?
    a. Capitalize and expense under Sec. 179.
    b. Capitalize and depreciate under MACRS using a 7-year life.
    c. Expense and attach the following statement to the tax return: "Section 1.2636(a)-1(f) *de minimis* safe harbor election."
    d. Expense and attach the following statement to the tax return: "Routine maintenance safe harbor election."
    e. File the annual election "Section 1.263(a)-3(h) Safe Harbor Election for Small Taxpayers."

29. If a taxpayer cannot meet the safe-harbor requirements of IRS Notice 2019-07, they may still qualify as a trade or business under the rules of Section 162. However, specifically excluded from the safe harbor rules are residences leased:
    a. For one year or less.
    b. To relatives.
    c. Under a "rent to own" arrangement.
    d. Where the tenant pays all of the cost of ownership, known as "triple-net" leases.
    e. Where the tenant pays utilities but the owner pays property taxes and insurance.

30. To determine if rental property activities rise to the level of "trade or business" rather than investment activity, courts have held that certain activities will qualify as a trade or business. These include:
    a. Taxpayer is involved in high level decisions only.
    b. Taxpayer has occasional involvement.
    c. Taxpayer has profit motive but no involvement in the activities.
    d. Taxpayer has regular and continuous involvement and a profit motive.
    e. Taxpayer shows a profit two out of every five years.

Sections VI–IX and Exam Questions 31–50 Relate to the *Journal of Accountancy* of June, 2019.

Section VI. How We Successfully Implemented AI in Audit (Page 26)

31. The profiled CPA firm used AI software in their audit practice to:
    a. Prepare financial statements.
    b. Total the number of transactions for the year by module (sales, payables, payroll, etc.).
    c. Monitor staff efficiency during the audit engagement.
    d. Analyze general ledger transactions and sort by risk level.
    e. Calculate various ratios for financial performance.

32. "Machine learning" is:
    a. The process of writing computer audit code.
    b. The process of entering data samples.
    c. The process where the machine uses built-in algorithms that help it learn based on transactions fed.
    d. The process of using "fixes" to speed machine performance.
    e. The process where a computer generates audit program steps.

33. In the example of a client using cloud-based software, the profiled CPA firm was able to:
    a. Access the client information through cloud-based AI and create risk-based audit samples.
    b. Perform the entire audit while working remotely.
    c. Document client internal control procedures.
    d. Identify evidence of malware attacks.
    e. Automatically generate adjusting journal entries.

34. In addition to audit sample selection and transaction risk assessment, the profiled CPA firm has used the same AI technology to:
    a. Help assess and improve staff proficiency.
    b. Recruit and retain staff.
    c. Assess potential clients for risk and help estimate fees accordingly.
    d. Improve processes in their tax preparation practice.
    e. Assess other CPA firms for possible merger.

35. In addition to use as an audit tool by CPA firms, who else does the author envision might make use of AI software?
    a. The Internal Revenue Service.
    b. Internal auditors.
    c. Controllers.
    d. a and b.
    e. b and c.

Section VII. What's Your Fraud IQ? (Page 34)

36. Why are small organizations more susceptible to fraud?
    a. Limited resources result in limited segregation of duties and fewer anti-fraud controls.
    b. The owners are too involved in the accounting function.
    c. They are more likely to use outdated software.
    d. The financial impact of fraud in small organizations is so small that spending for detection and prevention would exceed potential savings.
    e. Tools and techniques to prevent or detect fraud are unaffordable to small organizations.

37. Regardless of the size of the organization, the most common fraud detection method is:
    a. Segregation of duties.
    b. Reporting by tip.
    c. Owner review of bank statements.
    d. Owner distribution of payroll checks.
    e. Reconciling petty cash.

38. In small organizations, employees who commit fraud are more likely to:
    a. Have been employed one to five years.
    b. Be age 41 to 45.
    c. Work in the accounting department.
    d. a and b.
    e. a, b and c.

39. The author discusses two identity-theft schemes. In one, a fraudster uses the company's employer identification number to report fraudulent income and withholding in order to file and receive a refund. In the other, a fraudster registers an existing company in another state in order to conduct fraudulent business in the company's name. What advice did the author offer to help prevent or detect these two types of identity theft?
    a. Review online reports of new business registrations with similar or identical names.
    b. Be aware of employees appearing to have an unexplained expensive lifestyle.
    c. Have all mail from taxing authorities delivered unopened to the owner.
    d. The author offers <u>no</u> advice.
    e. Occasionally perform internet search of the company name.

40. The author describes two types of billing schemes and concludes that many billing schemes could be detected with:
    a. Use of online banking software.
    b. Proper management oversight and review of the accounts payable and payment disbursement processes.
    c. Proper employee oversight and training.
    d. Segregation of duties.
    e. Proper management oversight and review of the accounts receivable and receipt collection processes.

Section VIII. Accounting Firm Data Breaches: One State's Records. (Page 40)

41. Several states publish information about data breaches online. Where else can you learn about data breaches in your state that combines data from government sources and media reports?
    a. aicpa.org.
    b. irs.gov.
    c. Your state CPA licensing board web site.
    d. Private web sites such as: privacyrights.org.
    e. lifelock.com.

42. The authors examined a sample of accounting firm data breaches reported in Maryland. Included among the three most common <u>types</u> of breaches were:
    a. Unknown.
    b. Hacking.
    c. General unauthorized access.
    d. a and b.
    e. a, b and c.

43. IRS Publication 4557, *Safeguarding Taxpayer Data* suggests the following action(s) to help secure data:
    a. Firewalls.
    b. Data encryption.
    c. Limit internet connectivity.
    d. a and b.
    e. a, b and c.

44. A small accounting firm considering breach insurance:
    a. May find it useful to help identify lacking security measures. These will need to be implemented to comply with policy requirements).
    b. Can worry less about data breaches because the insurance will cover all breach-related costs.
    c. Can expect high premium costs.
    d. Will find it difficult to collect for data breach claims.
    e. Will be required to carry breach insurance if serving clients in multiple states.

45. In addition to the costs (direct and indirect) related to a data breach, CPA's also have to consider:
    a. Potential fines from the Internal Revenue Service.
    b. Whether they have violated the *AICPA Code of Professional Conduct* rules regarding confidential client information.
    c. Whether they have violated the *AICPA Code of Professional Conduct* rules engaging in "acts discreditable" to the profession.
    d. Potential fines and censure from their state licensing board.
    e. Rebranding because of damage to the firm's reputation.

Section IX. The At-Risk Rules for Partnerships. (Page 50)

46. The at-risk rules of Sec. 465 were intended to prevent taxpayers from using aggressive tax shelters to manipulate income. Prior to the enactment of the at-risk rules, <u>how was taxable income manipulated</u>? Hint: the author doesn't state explicitly, but alludes to it in the section titled "Operational Rules."
    a. Taxpayers were able to exchange stock for tax shelters, tax free.
    b. Tax shelters invested in tax-exempt bonds only.
    c. Tax shelters were based in foreign countries and so were "sheltered" from US income tax.
    d. Tax shelters allocated deductible <u>net losses</u> to investors that exceeded their at-risk basis.
    e. Tax shelters allocated taxable <u>net income</u> to investors that exceeded their at-risk basis.

47. To calculate the at-risk basis at the end of the tax year, you adjust the <u>initial</u> at risk amount for the following:
    a. Net income or loss..
    b. Net increase in accounts receivable.
    c. Contributions or distributions.
    d. a and b.
    e. a and c.

48. Which of the following are included in the calculation of at-risk basis?
    a. Tax exempt income and nondeductible expenses.
    b. AMT depreciation adjustments.
    c. Foreign tax credit allocated.
    d. a and b.
    e. a, b and c.

49. Which of the following will increase at-risk basis?
    a. Personal property loans of the partnership for which the taxpayer is not liable.
    b. Nondeductible expenses.
    c. Qualified nonrecourse debt secured by real property.
    d. The appraised value of real property.
    e. Partner distributions.

50. Using the following facts, calculate the at-risk basis for Partner A for year one of the partnership:

Cash invested	$20,000
Share of qualified recourse real estate loan	$100,000
Partnership distribution	$5,000
Net loss for the year	$7,000

    a. $13,000.
    b. $15,000.
    c. $20,000.
    d. $108,000.
    e. $120,000.

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Please email, fax or mail your answer sheet to AEA. **Our email address: *info@accounting-education.com***

Thank you for your business and referrals.