

Exam No. _____

Law School of Harvard University / 2013-2014

Federal Income Taxation

**Professor Abrams
Wednesday, April 30
2:00pm - 5:00pm**

This exam is 11 pages long. Please check to see that you have all 11 pages.

This examination consists of three essay questions and 20 multiple-choice questions. You should allow approximately 2 hours for the essay questions and an hour for the multiple-choice questions. Each essay question will be weighted in proportion to the recommended time (120 points total for the essay questions), and each multiple-choice question will be worth 3 points (60 points total for the multiple-choice questions). **You have three hours in which to complete the examination.** You must turn in your answers and the examination itself to receive credit for the class. Please answer the multiple-choice questions directly on the examination.

The exam mode is OPEN. You will not be able to cut and paste text from any document on your hard drive or the Internet into your exam answer.

Assume that the law in effect for taxable years beginning January 1, 2014, always has been in effect. *Unless otherwise indicated, assume that all persons use the calendar year as their taxable year and that they keep their books and records using the cash receipts and disbursements method of accounting.*

If any facts are not given which you believe you need, please state the facts and explain their relevance. Citation to relevant authority is expected, and "relevant authority" includes cases, code sections, and regulations. You may assume that all regulations, proposed regulations, and temporary regulations not overruled by any court are valid. If you believe that the correct answer to any multiple-choice question is not provided or that the facts of any multiple-choice question are not adequate to determine the correct answer, briefly indicate the problem with the question at the end of your essay answers.

You may have with you any material you desire *other than* commercially prepared secondary material not required for the course. No material may be shared by any students during the examination. You may use a calculator if you desire. You may not access the Internet.

Exam4 will automatically put your Anonymous ID on the exam copy.

Good luck!

DO NOT TURN TO PAGE TWO UNTIL THE PROCTOR TELLS YOU TO BEGIN.

Essay Question 1 (Suggested Time = 40 Minutes)

Several years ago, T inherited unimproved real estate (that is, dirt, called Blackacre), then worth \$40,000. On January 1, 2014, Blackacre is worth \$200,000, and T borrows \$50,000 from the First National Bank. This loan is nonrecourse and is secured only by Blackacre. The terms of the loan provide that no principle is due for twelve years but that fair market interest of 10% (\$5,000) must be paid each year.

On December 31, 2014, T transfers Blackacre (subject to the debt) to his daughter, D, out of detached and disinterested generosity. D makes the \$5,000 interest payment due the following day and then contributes the property (still subject to the debt) to Harvard University. Assume that donors of property to Harvard University may deduct their contributions pursuant to §170. Assume that Blackacre is still worth \$200,000 when it is transferred to D and to Harvard University and that at all times it remains unimproved.

Questions: (1) What are the tax consequences to T and to D of the transfer of Blackacre on December 31, 2014? (2) Can D deduct the interest payment made on January 1, 2015? (3) What are the tax consequences to D of the contribution of Blackacre to Harvard?

Essay Question 2 (Suggested Time = 40 Minutes)

Victim brought suit against Driver for injuries sustained by Victim from an automobile accident caused by Driver's negligence. At the time of the accident, Driver was making deliveries as part of Driver's normal course of business. At trial, the jury awarded Victim \$1,000,000 in compensatory damages for partial loss of sight (the eyesight award) and \$250,000 in compensatory damages for loss of hearing (the hearing award). Because Driver's insurance did not cover the hearing award, Victim agreed to accept \$100,000 from Driver in full satisfaction of the hearing award, thereby discharging the remaining \$150,000 of that obligation.

Driver appealed the eyesight award but did not appeal the hearing award. In need of money pending appeal, Victim assigned all amounts ultimately received under the eyesight award to Buyer in exchange for an immediate payment of \$600,000. Ultimately, the eyesight award was affirmed, and Driver's insurance company paid the full \$1,000,000 to Driver who endorsed the check to Buyer.

Question: Discuss the tax consequences of these events to Victim ("V"), to Driver ("D"), and to Buyer ("B").

Essay Question 3 (Suggested Time = 40 Minutes)

On March 15, 2014, National Savings and Loan (“National”) purchased all of the assets, subject to all of the liabilities, of Local Savings & Loan (“Local”). The assets of Local consisted entirely of cash on hand plus outstanding loans made by Local. The liabilities of Local consisted entirely of savings accounts deposited with Local by individuals in the community. Assume the following: (a) the purchase price was \$10,000,000; (b) all loans made by Local were made at fair market interest; (c) all outstanding loans made by Local require interest payments on the first of each month; (d) Local must pay market interest on all savings accounts on the first of each month; (e) both Local and National are cash-basis taxpayers; (f) the OID rules do not apply to any of the assets or liabilities of Local; and (g) Local's adjusted basis in its assets (treating cash as having an adjusted basis equal to face value) is \$8,000,000.

Question: Discuss the tax consequences of the acquisition by National of the assets and liabilities of Local including (1) the amount of gain recognized by Local, (2) National's basis in the assets acquired from Local, (3) the tax treatment to National when it pays interest on April 1, 2014, on the acquired savings accounts; and (4) any other tax issues to Local.