

# 2010 “S” CORPORATION QUIZ

1. T F Subchapter “S” provides a means to avoid double taxation of regular “C” corporation.
2. T F Profits and Losses of an S corporation are taxed at the corporate level.
3. T F Income once reported on the tax returns of the S corporation shareholders can be distributed by the S corporation without being taxed a second time.
4. T F In most respects, an S corporation has all the legal attributes and is subject to all the rules, regulations, benefits, and burdens of corporate form.
5. T F Some states may impose franchise or excise tax on S corporations.
6. Which of the following is NOT a reason to chose S corporation form of doing business:
  - a. Limited liability
  - b. No separate tax on corporate income
  - c. Individual shareholders can deduct share of net operating loss.
  - d. Fringe benefits received by 2% shareholders are not excludable from shareholder’s income
7. Which of the following IS a reason to chose S status?
  - a. Shareholders are subject to FICA tax and other payroll taxes on required reasonable salary
  - b. S corporation must use a calendar year
  - c. No accumulated earnings or alternative minimum tax at corporate level
  - d. Some states do not recognize S corporations for state tax purposes
8. T F Capital gains are generally not taxed at S corporation level
9. T F Family members may more easily split income among family members with S status.
10. T F Shareholders, like partners, are subject to FICA (Self employment) tax on the corporation net income pass through amount.
11. T F Passive S corporation shareholders can offset passive losses from other activities with their S corporation earnings.
12. T F Interest expense incurred by the S corporation shareholder to acquire the stock of the company are deductible only as “investment interest”.
13. T F Employee stock ownership plans are not available to S corporations
14. T F Shareholders of S corporation who hold more than 5% of stock can not borrow from the company pension plan.
15. T F An S corporation with more than 35% of losses allocated to shareholders who do not actively participate in management of the corporation is required to use accrual method of accounting.

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16. T F If shareholders take out distributions of profits, they must take out reasonable salary.
17. T F Jeff is a shareholder in an S corporation. His father Jim is NOT a member of the S corporation. Jim has expertise in the type of business that son Jeff is in and agrees to provide consulting services at no cost to the corporation. IRS may make adjustments to reflect the value of such services
18. T F A domestic corporation is a corporation that is organized in the home State of the business operations only.
19. T F Corporations that take Puerto Rico and possessions tax credits may not be S corporations.
20. T F Insurance companies are not eligible to be S corporations.
21. T F An S corporation may not have more than 100 shareholders.
22. T F Spouses are treated as separate shareholders for the # of shareholders limitation.
23. T F If spouse dies, the estate and the surviving spouse are treated as one shareholder for the 100 shareholder test.
24. T F A minor child is counted as a separate shareholder
25. T F When stock is held by a nominee, guardian or custodian, the person who holds the stock (nominee guardian custodian) is treated as the shareholder.
26. T F An S corporation may not be a partner in a partnership
27. Which of the following may NOT be a shareholder in an S corporation?
- a. Individual
  - b. Estate
  - c. Certain trusts
  - d. Certain qualified non profit organizations
  - e. Certain pension, profit sharing and stock bonus plans
  - f. Self directed IRA
28. T F A resident alien may be a shareholder of an S corporation
29. T F To qualify as an “Electing Small Business Trust” acquisition can not be acquired by purchase.
30. T F A trust must ELECT to be an Electing Small Business Trust.
31. T F EACH beneficiary of an ESBT is counted as a shareholder in the 100 shareholder limitations.
32. T F Income from an S corporation is taxed to an Electing Small Business Trust at the lowest applicable rate for trusts

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33. T F Common stock that differs only with respect to voting rights is treated as one class of stock for the “one class of stock” eligibility requirement.
34. T F Nonvoting shares may be given to children and other family members in connection with estate planning without causing a second class of stock.
35. T F For the “one class of stock” requirements all “authorized” shares are considered.
36. T F Outstanding stock does not include treasury stock
37. T F Disproportionate payment of dividends will be deemed to have created a second class of stock.
38. T F Loans to the corporation may be treated as a second class of stock in some cases.
39. T F Stock appreciation right plans (deferred compensation plans) do not constitute a second class of stock if certain rules are met.
40. T F If a “resident” alien gives up US residence, the S election will be terminated on the date the shareholder gives up US residence.
41. T F A non resident alien shareholder who moves to a foreign country may continue his or her US resident status in some cases.
42. T F Shares of an S corporation issued to a non resident alien as custodial for a resident minor will disqualify S corporation status.
43. T F If shareholder is a US citizen or resident and the shares are NOT community property, it does not matter that the spouse is a nonresident alien.
44. T F If shares are held as community property, they are deemed to be owned by both spouses and the nonresident alien spouse is ineligible to be an S corporation shareholder.
45. T F “Permitted tax year” must always be December 31.
46. T F An S corporation may now own a subsidiary C corporation but can not file a consolidated tax return.
47. T F If shareholder transfers unencumbered property to S corporation in exchange for stock ONLY and such shareholder is part of a group that controls more than 80% of the corporation, no gain or loss is recognized on the transfer
48. T F If shareholder transfers property to an S corporation in exchange for stock and shareholder is NOT part of a group that controls 80% or more of the corporation, gain or loss will be recognized on the transfer.
49. T F If shareholder receives anything **other than stock** in transfer of property to S corporation, the shareholder must recognize gain to extent of amount of money received plus fair market value of “other” property received but **no loss is recognized.**

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50. T F Regardless of “control interest” the corporation does NOT recognize gain or loss on receipt of property in exchange for stock.
51. T F When shareholder transfers property to S corporation in exchange for stock, the shareholder’s basis for the stock is FMV of the stock
52. T F In general, the **corporation** basis in the asset received in exchange for stock is the same as the basis in the asset in the hands of the transferor, increased by any gain recognized to the transferor on the transfer.
53. When an S corporation issues stock in exchange for performance of services:
- a. Shareholder recognizes income in amount equal to value of the stock
  - b. Corporation receives a deduction for value of stock given up
  - c. In some states, restrictions on such transactions may disqualify S status
  - d. - “a” and “b” only
  - e. - “a’ , “b” and “c” are all correct.
54. T F To qualify for 1244 stock treatment, the corporation must be a domestic corporation **and** a small business corporation.
55. T F To qualify for section 1244 stock loss treatment, the designation as 1244 stock must be made by application to IRS
56. T F The benefit of section 1244 stock is that, in the event of a loss, the loss is treated by the individual as an **ordinary** loss instead of a capital loss.
57. T F It is not necessary for minor shareholders to sign consent form 2553.
58. T F An election form 2553 that is made after the 15<sup>th</sup> day of the third month but before the end of the tax year is treated as made for the next year.
59. T F Timely filing of form 2553 does **not** automatically mean that S corporation status has been accepted.
60. T F If corporation is an existing “C” corporation, an election to become an S corporation may be made at any time during the year to be effective for the NEXT year.
61. T F For election to be effective for **current** year, the election must be made on or before the 15<sup>th</sup> day of the third month of the **calendar** year.
62. For a newly formed corporation, the “beginning of the first taxable year” is when the first of the following events occurs:
- a. Corporation first had shareholders
  - b. Corporation first acquired assets
  - c. Corporation began doing business
  - d. Form 2553 is accepted by IRS
  - e. All of the above EXCEPT “d”

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63. T F If a new corporation fails to meet the deadline for filing the election, the earliest possible effective date is the first day of the NEXT taxable year.
64. T F In the case of a newly formed corporation (except personal service corporation) which fails to make the election timely, the “next taxable year” may be a short fiscal year.
65. T F If an election is mailed on the last day but is not postmarked until the next day, it is invalid.
66. T F Gus and the other shareholders in a newly formed corporation completed all of the formation requirements at the attorney’s office six months before the beginning of business and they all signed the form 2553 at that time. The attorney went on an extended vacation and instructed his secretary to mail the form in. She did not do so. Generally, the election can not be salvaged.
67. T F A late or nonexistent S election may now be treated as made timely if IRS determines that there was reasonable cause for failure to file on time.
68. T F IRS determination that there was reasonable cause generally requires a request for a private letter ruling and payment of a user fee.
69. T F It is possible to avoid the user fee if corporation fails to qualify solely because form 2553 was not filed timely and the due date for the first tax return for the first year has not passed.
70. T F Automatic relief for late S elections can be granted if certain conditions are met.
71. T F If form 2553 indicates more shares are issued and outstanding than the shareholder consent forms indicate - the election will be invalid.
72. T F Clerical errors on form 2553 MAY result in loss of S status.
73. T F When an election is made within the first two and one half month period and the election is to be retroactive, persons who are no longer shareholders on the date of the election but were shareholders at any time during the taxable year must also consent.
74. T F If stock is held as community property, only one spouse must consent.
75. T F If stock is held by tenants in common, joint tenants, or tenants by entirety, all such parties must sign the consent form.
76. T F If a shareholder can not be located, timely filed election may be made and request for extension of time to file the missing consent only - but election is not valid without consent of all shareholders.
77. T F New shareholders (except qualified Subchapter S trusts) are not required to file a consent in order for corporation to maintain S status.
78. T F Any new shareholder may refuse to consent to S election, thereby terminating the election.
79. T F Net income or loss from rental real estate activities, as well as other rental activities, must be separately stated on Schedule K and K1

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80. Portfolio income or loss must be separately stated on K and K1. Portfolio income DOES NOT include
- a. Interest income
  - b. Dividend income
  - c. Royalty income
  - d. Short term capital gain or loss
  - e. Long term capital gain or loss
  - f. Section 1231 net gains or losses
81. T F Charitable contributions made by S corporation must be separately shown on K and K1
82. T F Section 179 expense elected by S corporation must be separately stated on K and K1
83. T F Tax preference and adjustment items needed to figure shareholders alternative minimum tax must be shown separately on schedule K and K1
84. T F If an S corporation borrows funds **and distributes the money to the shareholders**, the interest paid on the loan is deductible as a business operation expense by the corporation and is not required to be separately stated on K and K1
85. T F Shareholder wages are added back to income to determine taxable income limitation for the section 179 expense election.
86. T F Section 179 expense passed through to a shareholder reduces the shareholder's **stock basis** even if the shareholder is unable to deduct the 179 expense.
87. T F If a shareholder has over the maximum in total section 179 expenses because of amounts allocated to him from the S corporation and from other trades or businesses, the excess over maximum can be carried over by the shareholder to next year.
88. T F If a corporation was a “C” corporation in one year and sustained a net operating loss, then became an S corporation in the 2<sup>nd</sup> year, the net operating loss can be carried over to the S corporation year.
89. T F If an S corporation election does not terminate before the 15-20 year carryover period for NOL of a former C corporation, the NOL may not be used. (Each year that the corporation is an S corporation counts as one of the carryover years for C corporation loss)
90. T F Losses realized on sales or exchanges of property between related parties generally may not be deducted and , if later resold at a gain, gain is recognized only up to the amount that is more than the disallowed loss.
91. T F For related party rules, an individual and a corporation are “related” if more than 80% of the value of the outstanding stock is owned by the individual.
92. T F An accrual method S corporation must use CASH method to deduct business expenses and interest owed to cash method related parties.

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93. Which of the following items, if paid on behalf of a 2% or more shareholder, is NOT deductible by the S corporation?
- a. Medical expenses under section 105(b)
  - b. Accident and Health Insurance premiums
  - c. Cost of \$50,000 group term life insurance
  - d. Cost of meals or lodging furnished for convenience of employer
  - e. Moving expenses
94. T F Items that are paid on behalf of a 2% shareholder and are NOT deductible by the S corporation are treated as a distribution to the 2% shareholder.
95. T F Certain items are deductible by the S corporation but paid on behalf of a 2% shareholder must be included in gross income of the 2% shareholder
96. T F If accident and health insurance premiums are paid by the corporation on behalf of the 2% shareholder employees, it must be included in wages on the form W2 and is subject to FICA and medicare tax.
97. T F A shareholder who disposes of stock or dies is treated as the shareholder for the day of disposition or death.
98. T F S corporations may establish retirement plans
99. T F Stockholders can use pass through income from S corporation for purposes of making contributions to a SEP or Keogh plan
100. T F Stockholders can only use W2 income received from S corporations for purposes of making a contribution to an IRA
101. T F An S corporation shareholder may deduct all losses passed through
102. T F Shareholder loss is limited to stock basis only.
103. T F Tax exempt income of the S corporation does NOT increase basis for shareholders
104. T F Non deductible expenses do not decrease shareholder basis
105. T F Discharge of indebtedness income that is excluded from insolvent S corporation's income does not increase shareholder basis.
106. T F Taxpayer (shareholder) is allowed basis in the corporation for wages owed to him but unpaid.
107. T F In adjustment to shareholder's basis, for loss limitations - distributions to the shareholder are deducted from basis before losses and deductions.
108. T F Subchapter S shareholder's basis can never be reduced below zero.
109. T F Excess losses are suspended and carried forward indefinitely until basis is restored.

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110. T F Shareholder’s basis can be increased by direct loans to the S corporation.
111. T F Debts owed by the corporation to third parties, if personally guaranteed by the shareholder, can be added to shareholder’s adjusted basis.
112. T F Suspended losses are attributed only to the shareholder who owned the stock when the loss occurred.
113. T F Ability to deduct a suspended loss ends when the S corporation election is terminated.
114. T F Ability to deduct a suspended loss ends when shareholder dies.
115. T F Increase in **stock** basis is made only after any basis in **loans** that have previously been reduced is restored.
116. T F Restoration of debt basis only applies to debt held on the **first** day of the year and is generally restored on the **last** day of the year.
117. T F If loans are paid back in full that were previously reduced for debt basis, before restoration, the repayment is income to the shareholder.
118. T F **Distributions** never reduce **debt basis**
119. T F Shareholders recognize income to extent distributions exceed **stock basis ONLY**
120. T F A stepped up basis is available for surviving shareholders in a cash basis S corporation
121. T F Even though shareholders have basis, losses are still only deductible if shareholder is at risk for those amounts.
122. T F If S corporation stock is sold with a zero basis, the gain is equal to the net proceeds.
123. T F Suspended losses are **not used** to reduce gain on disposition of stock.
124. T F Suspended losses are not deductible in year of disposition. They simply go away.
125. T F It is not possible to be passive with regard to one or more activities of an S corporation and non passive with regard to other activities of the same S corporation
126. T F When an S corporation passes through a passive loss which is disallowed to a shareholder under Passive Activity Loss rules, the amount of the shareholder’s pro rata share of the loss still reduces basis of stock.
127. T F When a C corporation makes an S election, any previously suspended passive losses are locked in the corporation only to be used if the corporation terminates its S election.
128. T F Net passive income tax will never apply to a corporation which has always been an S corporation.
129. T F Automatic termination of the S election occurs if the corporation has excess net passive income for three consecutive years and has pre-S corporation earnings at the end of each year.

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130. T F The tax on built in gains applies at the S corporation level if **appreciated** property that was held at the time of conversion is sold or distributed within ten years of the date of the S election.
131. T F Built in gains tax does not apply to corporations which made the S election prior to 1987 or which formed after 1986 but have always been S corporations.
132. T F Built in Gains tax applies to all appreciation of property held at time of conversion if sold within ten years of election.
133. T F Unused “C” corporation credit carryforwards and NOL or capital loss carryovers can reduce the built in gains tax.
134. T F Built in Gains tax is 39%
135. T F The built in gains tax that is paid by the corporation is passed through to the shareholder, as a deductible loss, at the character of the gain that gave rise to the BIG tax.
136. T F Installment sales made after 3-26-90 which occur either before or during the ten year recognition period are subject to the BIG tax even though the payments may be received outside the 10 year recognition period.
137. T F For tax on certain capital gains to apply, part or all of the gain must result from sale of substituted basis property.
138. T F Tax on certain capital gains applies only if S election was made prior to 1987 (or during 1987 and 1988 under transitional rules)
139. T F If tax is due from re-computing a prior year investment credit, it is payable at corporate level.
140. T F If taxes are due at S corporation level, the S corporation is required to pay estimated tax if liability is \$500 or more.
141. T F Distributions can reduce the AAA account below zero.
142. T F Distributions are tax free to shareholder to extent of shareholder’s **stock** basis and any excess is capital gain income
143. T F The AAA account belongs to the shareholders.
144. T F AAA account is reduced by all S corporation losses even if losses are suspended at the shareholder level.
145. T F An S corporation that was formerly a C corporation may have earnings and profits which were not distributed prior to S corporation. Distributions from this account are taxable to shareholders as capital gains.
146. T F Distributions from the “Other Adjustments Account” are tax free to shareholders.
147. T F Under new Small Business Job Protection Act, adjustments to AAA and to Shareholder Basis accounts are the same.

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148. T F To revoke an S election, consent of all shareholders is required.
149. T F If a nonresident alien acquires stock in the S corporation, the S election is immediately terminated.
150. T F If more than 25% of a corporation’s gross receipts constitute passive investment income for each of three consecutive tax years and the corporation has always been an S corporation, the S election will automatically terminate.
151. T F If a corporation is disqualified and believes termination was inadvertent, the corporation may request permission from IRS to continue to be treated as an S corporation for a specified period if the corporation takes the steps needed to perfect the election
152. T F Any shareholder can cause the S election to be terminated by transferring one of his or her shares to a disqualified shareholder.
153. T F When termination occurs in mid year, two tax returns must be filed for that “termination year”
154. T F After termination of S election there is generally a five year waiting period before S election can be made again.
155. T F The small business job protection Act of 1996 - for purposes of the 5 year waiting period, any termination in a tax year beginning before 1997 is not taken into account.
156. T F A short taxable year can count toward the five year waiting period.

**TRANSFER YOUR ANSWERS TO ANSWER PAGE(S)**

**EMAIL OR FAX OR MAIL ANSWER PAGE(S) ONLY**

Voice or FAX: 1-866-755-2853  
Voice only: 1-541-915-4915  
Email: [tax-ed@tax-educators.com](mailto:tax-ed@tax-educators.com)  
Website: <http://www.tax-educators.com>

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