EXAMPLIFY PASSWORD:

Advanced Corporate Tax **Spring 2025**
Bogdanski

WRITE YOUR EXAM NUMBER HERE: ________

FINAL EXAMINATION
(Three hours)

INSTRUCTIONS

This examination consists of three essay questions, each of which will be given equal weight in determining grades. Three hours will be permitted for this examination.

The suggested time limit for each question is one hour. Experience has shown that failure to budget one's time according to this limit can result in a drastic lowering of one's overall grade on this examination.

At the end of the three hours, you must turn in this set of questions in the original envelope in which this set came. You must submit your answers using Examplify. No credit will be given for anything written on this set of questions. Only your electronic answer file will be graded.

Pay close attention to the final portion, or "call," of each question. Failure to respond to the matters called for will result in a low score for the question. On the other hand, discussion of matters outside the scope of the call of the question will not receive credit.

Be sure to explain as thoroughly as possible your answers to the questions posed. Your reasoning, discussion, and analysis are often as important as any particular conclusion you reach.

Unless otherwise instructed, assume that:

- all shareholders described in the question are individuals and U.S. citizens;
- all entities described in the questions are organized and operated exclusively in the United States;
- all parties described in the questions use the calendar year as their taxable year for federal income tax purposes; and
- all parties described in the questions report their income using the cash method of accounting for such purposes.

Any references to "the Code" are to the Internal Revenue Code of 1986, as amended.

QUESTION 1
(One hour)

Redco, a C corporation, has two shareholders, each of whom owns 100 shares of Redco's only class of stock. These 200 shares are the only shares outstanding. One of the shareholders of Redco is an individual, Tate; the other shareholder of Redco is an S corporation, Scorp.

The stock of Scorp is owned one half by Tate and the other half by Tate's brother, Bo.

Immediately before the transactions discussed next, Tate's adjusted basis in Tate's Redco stock is $100,000, and the fair market value of Tate's Redco stock is $1,000,000. Redco has earnings and profits well in excess of $1,000,000.

As parts of an integrated plan, (a) Redco redeems 80 shares of Tate's Redco stock, and (b) three weeks later, Tate sells Tate's other 20 shares of Redco stock for cash to an unrelated buyer, Zane.

In the redemption, Redco pays Tate $750,000 cash and transfers to Tate a sculpture out of Redco's art collection, held for investment. The sculpture has a fair market value of $50,000. Immediately before the transfer, Redco's adjusted basis in the sculpture is $80,000.

In the related sale, Zane pays Tate $200,000 cash for 20 shares of Redco stock.

Assuming that Redco never becomes an S corporation, and that Scorp remains an S corporation, what are the federal income tax consequences to Tate, Redco, Scorp, and Bo, of each of the transactions just described, with and without all available elections? Be sure to discuss the amount, timing, and character (capital or ordinary) of any income, gain, loss, or deduction realized or recognized by each party; and each party's basis in the stock or assets that party holds at each stage of the transactions.

Discuss.

(End of Question 1)

QUESTION 2
(One hour)

Hotco is a C corporation, all of the stock of which is owned by Oona. At the start of 2025, Oona's adjusted basis in her Hotco stock is $1,000,000. Hotco has a large amount of accumulated earnings and profits; however, it also has a capital loss carryover from an unsuccessful investment that it sold in a prior year.

On January 1, 2025, Hotco adopts a plan of complete liquidation. On March 1, 2025, Hotco sells all of its assets to an unrelated buyer, a publicly traded corporation, Pyco. The assets, and their adjusted basis to Hotco immediately before the sale, are as follows:

Asset	*Adjusted basis*
Land and buildings	$ 2,000,000
Equipment	50,000
Inventory	150,000
Going concern value	-0-
Total	*$ 2,200,000*

None of the assets were contributed to Hotco by Oona.

In the asset sale agreement by which Pyco buys all of Hotco's assets, Pyco and Hotco agree that Pyco will pay $4,200,000 cash for these assets; in addition, Pyco will pay Oona $200,000 a year for two years in exchange for Oona's covenant not to compete with Pyco in Hotco's region for that two-year period.

The asset sale agreement allocates the consideration to be paid by Pyco for Hotco's assets as follows:

Asset	*Consideration*
Land and buildings	$ 3,500,000
Equipment	300,000
Inventory	200,000
Going concern value	200,000
Total	*$ 4,200,000*

Pyco does not assume any liabilities of Hotco or Oona. None of the assets purchased from Hotco by Pyco are subject to any mortgages or other encumbrances.

At a closing on March 2, 2025, Pyco pays Hotco the $4,200,000 cash purchase price for the assets, and Hotco transfers all of the assets to Pyco.

In 2025 and 2026, the board of directors of Hotco wind up Hotco's affairs and pay all of its debts, including tax liabilities. Hotco makes the following liquidating distributions, in cash, to Oona:

Date	*Distribution*
July 1, 2025	$ 1,500,000
December 15, 2026	500,000
Total	*$ 2,000,000*

The December 2026 distribution is the final distribution by Hotco to Oona.

Oona retires, and does not compete with Pyco. Pyco pays Oona $200,000 on February 28, 2026, and another $200,000 on February 28, 2027, with respect to the covenant not to compete.

Assuming that Hotco never becomes an S corporation, what are the federal income tax consequences to Hotco, Oona, and Pyco of each of the transactions just described, with and without all available elections? Be sure to discuss the amount, timing, and character (capital or ordinary) of any income, gain, loss, or deduction realized or recognized by each party; and each party's basis in the stock or assets that party holds at each stage of the transactions.

Explain.

(End of Question 2)

QUESTION 3
(One hour)

Amy and Bev form a new corporation, Xco, as follows:

On May 1, 2025, after articles of incorporation of Xco are filed with the state, Amy and Bev, individually and as incorporators of Xco, enter into an agreement whereby Amy and Bev will each transfer property with a net fair market value of $1,200,000 to Xco in exchange for one half of Xco's outstanding stock.

Amy's property is ready for immediate transfer to Xco. It consists of (1) equipment with an adjusted basis in Amy's hands of $300,000 and a fair market value of $700,000, and (2) a commercial building, known as The Hub, with an adjusted basis in Amy's hands of $1,000,000 and a fair market value of $700,000. The Hub is encumbered by a mortgage securing a business loan that Amy took out years ago. At the time of the transfer of The Hub to Xco, the outstanding balance on the loan, which is a recourse liability of Amy, is $200,000. Xco assumes the debt, i.e., it promises Amy that Xco will pay it as it comes due. In addition, Xco transfers to Amy 500 shares of Xco's common stock, which is Xco's only class of stock. The exchange takes place on May 2, 2025. The 500 shares have an initial fair market value of $1,200,000.

Bev's property — a patent that Bev purchased some years earlier — is not ready for transfer to Xco on May 2, 2025, because Amy and Bev are unsure of the patent's value. They hire Shannon, an appraiser, to value the patent. On August 28, 2025 Shannon delivers her appraisal, which concludes that the patent has a fair market value of $1,400,000.

On September 2, 2025, Bev transfers the patent to Xco. In exchange for the patent, Xco transfers to Bev 500 shares of Xco's common stock, with a fair market value of $1,200,000, plus Xco's promissory note for $200,000. The note, which is true debt for federal tax purposes, calls for Xco to pay Bev $40,000 a year of principal over five years beginning in 2026; each payment is to include interest at a market rate on the unpaid balance on the note. Immediately before its transfer to Xco, the patent has an adjusted basis in Bev's hands of $400,000.

What are the federal income tax consequences to Amy, Bev, and Xco of each of the transactions just described, with and without all available elections? Be sure to discuss the amount, timing, and character (capital or ordinary) of any income, gain, loss, or deduction realized or recognized by each party; and each party's basis in the stock or assets that party holds at each stage of the transactions.

Discuss.

(End of examination)