

CERTIFIED FINANCIAL PLANNER (CFP) TAX PLANNING PRACTICE EXAM (SAMPLE)

STUDY GUIDE



Prepare with structure. Pass with confidence



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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 – 45 minutes). Review a handful of questions, reflect on the explanations.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning. Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly, adapt the tips above to fit your pace and learning style. You've got this!

Questions

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- 1. What amount of installment sale income must a seller recognize in the current year if they sold an antique automobile?**
 - A. \$7,667
 - B. \$23,000
 - C. \$7,334
 - D. \$15,333

- 2. What are the tax implications of a 1031 exchange?**
 - A. Immediate payment of capital gains tax
 - B. Allows deferral of capital gains tax on sales
 - C. Permanent loss of tax benefits
 - D. No tax implications whatsoever

- 3. If Karl gifts appreciated stock valued at \$70,000 to Ohio State University, what is the maximum charitable deduction he can claim?**
 - A. \$21,000
 - B. \$50,000
 - C. \$18,000
 - D. \$30,000

- 4. What is the primary function of a tax deduction?**
 - A. To eliminate tax liability completely
 - B. To increase the taxpayer's refund significantly
 - C. To lower taxable income and potentially reduce overall tax owed
 - D. To convert a tax credit into a deduction

- 5. What determines the validity of a premarital agreement with claims of duress?**
 - A. It is automatically void.
 - B. It can still be binding under certain conditions.
 - C. It is always enforceable regardless of duress.
 - D. Health issues negate the agreement.

- 6. Amy's adjusted basis for her print shop, after adding a new wing, is what amount?**
- A. \$80,000, less the actual cost of construction of the new addition
 - B. \$78,000, less the actual cost of construction of the new addition
 - C. \$80,000
 - D. \$78,000
- 7. Which tax benefit is associated with tax-deferred growth investments?**
- A. Taxes are paid at the time of investment
 - B. Taxes are paid when funds are withdrawn
 - C. No taxes are paid ever
 - D. Taxes are paid annually
- 8. For tax purposes, how is Joy's basis in the life insurance policy transferred to Jack?**
- A. It's reset to fair market value at transfer
 - B. It's zeroed out
 - C. Jack receives Joy's basis at transfer
 - D. It's based on cash value at transfer
- 9. What is a requirement for claiming the Home Office Deduction?**
- A. The space must be a separate building from the residence
 - B. The space must be used exclusively and regularly for business purposes
 - C. Home offices must be over 300 square feet in size
 - D. The business must be registered with the state
- 10. Which statement is CORRECT with respect to active participation in rental real estate?**
- A. The interest may be held through a limited partnership
 - B. A deduction-equivalent tax credit of up to \$25,000 is available
 - C. The taxpayer must hold a 10% or greater ownership interest
 - D. The taxpayer must participate in management in a bona fide sense

Answers

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1. D
2. B
3. C
4. C
5. B
6. D
7. B
8. C
9. B
10. C

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Explanations

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1. What amount of installment sale income must a seller recognize in the current year if they sold an antique automobile?

- A. \$7,667
- B. \$23,000
- C. \$7,334
- D. \$15,333**

When determining the amount of installment sale income a seller must recognize in the current year, it's important to understand the basics of the installment sale method. This approach allows the seller to recognize income as payments are received rather than all at once at the time of sale. The key components to consider when calculating the recognized income are the gross profit, the total contract price, and the payments received during the tax year. The formula used is: $\text{Recognized Income} = (\text{Payments Received in Current Year}) \times (\text{Gross Profit Percentage})$. To arrive at the correct amount, one would typically have calculated the total gain from the sale, including the total selling price and the seller's basis in the asset. The gross profit percentage is calculated by dividing the total gain by the total contract price. Once you have this percentage, you apply it to the payments received during the year to determine how much income should be recognized for tax purposes in that year. In this scenario, if the recognized amount is \$15,333, it is likely that this figure represents the calculated portion of the payments received that corresponds with the seller's gross profit on the sale of the antique automobile for that current tax year. This means the seller is only taxed on the portion of the gain that corresponds

2. What are the tax implications of a 1031 exchange?

- A. Immediate payment of capital gains tax
- B. Allows deferral of capital gains tax on sales**
- C. Permanent loss of tax benefits
- D. No tax implications whatsoever

A 1031 exchange, also known as a like-kind exchange, allows an investor to defer paying capital gains taxes on an investment property when it is sold, as long as a similar property is purchased with the profit gained by the sale. This is a significant tax benefit that encourages more frequent reinvestment in real estate. The ability to defer capital gains tax means that the investor can maintain greater liquidity and use the proceeds from the sale to further grow their investment portfolio without the immediate tax burden. This deferral can be particularly advantageous in wealth accumulation strategies, as it allows for compound growth without the reduction of capital from tax liabilities. While there are strict requirements and timelines that must be adhered to in a 1031 exchange, it fundamentally provides a mechanism for investors to postpone their tax obligations rather than facing an immediate payment of capital gains tax, which could hinder their investment strategy. Thus, the choice that highlights the deferral of capital gains tax accurately captures the essence of a 1031 exchange's tax implications.

3. If Karl gifts appreciated stock valued at \$70,000 to Ohio State University, what is the maximum charitable deduction he can claim?

- A. \$21,000
- B. \$50,000
- C. \$18,000**
- D. \$30,000

When a taxpayer gives appreciated stock to a qualified charitable organization, such as Ohio State University, they are generally able to claim a charitable deduction for the fair market value of the stock at the time of the gift. In this case, the appreciated stock is valued at \$70,000. However, the maximum charitable deduction that Karl can claim for this gift will depend on several factors, including the type of gain that would have been taxed if he sold the stock and his adjusted gross income (AGI). For donations of appreciated stock to public charities, the deduction is usually equal to the fair market value of the stock, subject to certain limitations based on the taxpayer's AGI. For individuals, contributions of appreciated capital gains property to public charities are typically limited to 30% of AGI if the stock is held for more than one year. If Karl's AGI were, for example, \$100,000, he could take a deduction up to \$30,000 (which is 30% of \$100,000) for the stock contribution. In this context, the deduction of \$18,000 does not align with the 30% of AGI guideline, and \$21,000, \$50,000, and \$30,

4. What is the primary function of a tax deduction?

- A. To eliminate tax liability completely
- B. To increase the taxpayer's refund significantly
- C. To lower taxable income and potentially reduce overall tax owed**
- D. To convert a tax credit into a deduction

The primary function of a tax deduction is to lower taxable income and potentially reduce overall tax owed. When taxpayers claim a deduction, they decrease their total income subject to taxation, which can lead to a lower overall tax liability. For example, if an individual has a taxable income of \$50,000 and qualifies for a deduction of \$10,000, their new taxable income would be \$40,000. This lower income could place them in a reduced tax bracket or simply lessen the amount of tax owed, effectively making deductions a useful tool for tax planning. Deductions can take various forms, including those for mortgage interest, medical expenses, and charitable contributions, and their benefits depend on the taxpayer's circumstances and marginal tax rate. It's important to understand that while deductions reduce taxable income, they do not provide a direct dollar-for-dollar reduction of tax liability like credits do. Therefore, the focus of deductions is on improving tax efficiency rather than eliminating tax responsibility entirely or directly increasing refunds.

5. What determines the validity of a premarital agreement with claims of duress?

- A. It is automatically void.
- B. It can still be binding under certain conditions.**
- C. It is always enforceable regardless of duress.
- D. Health issues negate the agreement.

The validity of a premarital agreement with claims of duress is determined by the understanding that such agreements can still be binding under certain conditions. For a premarital agreement to be considered valid, it must be executed voluntarily and without coercion. If a party claims that they were under duress when entering into the agreement, the courts will assess the circumstances surrounding the signing of the agreement. In legal terms, duress is a situation where one party is forced or pressured to sign an agreement against their free will. However, if one can demonstrate that the agreement was entered into despite claims of duress—meaning there were no undue pressures or threats that compromised the signing party's ability to consent—the court may still enforce the agreement. Factors that courts often examine include the nature of the pressure applied, the timing of the agreement, and whether the aggrieved party had access to independent legal advice. This nuanced understanding allows for the possibility of enforcing premarital agreements despite allegations of duress, highlighting that their binding nature is contingent upon specific circumstances in a given case. Thus, the correct answer reflects that the validity of a premarital agreement in such situations is not a blanket determination but rather a considered legal analysis of the evidence surrounding the claim of

6. Amy's adjusted basis for her print shop, after adding a new wing, is what amount?

- A. \$80,000, less the actual cost of construction of the new addition
- B. \$78,000, less the actual cost of construction of the new addition
- C. \$80,000
- D. \$78,000**

To determine the adjusted basis for Amy's print shop after adding a new wing, it is important to understand how adjustments to basis are calculated. The adjusted basis generally includes the original cost of the property plus the costs of any improvements made, less any depreciation taken. In this case, assuming the original basis is \$78,000 and that Amy added a new wing, if the cost of that addition is not specified but we know that the adjustments typically increase the basis, the adjusted basis would likely be the original basis (prior to the addition) if the addition doesn't affect this specific example. If \$78,000 is indeed the basis given and there are no other costs provided that would add to this amount for the new wing's construction, then the correct adjusted basis would remain at \$78,000. Hence, the chosen answer accurately reflects that situation, indicating that the construction of the addition might not be an additional factor to change this specific adjusted basis in the context provided.

7. Which tax benefit is associated with tax-deferred growth investments?

- A. Taxes are paid at the time of investment
- B. Taxes are paid when funds are withdrawn**
- C. No taxes are paid ever
- D. Taxes are paid annually

The tax benefit associated with tax-deferred growth investments is that taxes are paid when funds are withdrawn. This means that the investment can grow without being subject to annual taxation on the earnings, allowing for potentially greater growth over time due to the compounding effect. This feature is especially beneficial in retirement accounts, such as traditional IRAs and 401(k) plans, where individuals can defer taxes until they reach withdrawal age, typically during retirement when they may be in a lower tax bracket. This structure enables investors to reinvest the full amount of their earnings without deductions for tax payments, which can significantly enhance the growth potential of the investment. Once the funds are eventually withdrawn, they are taxed as ordinary income, reflecting the individual's tax rate at that time. In contrast, the other options do not accurately describe tax-deferred accounts. Some require taxes to be paid upfront, some suggest no tax liability ever, and others imply annual tax obligations, which do not capture the essence of tax-deferred growth investments.

8. For tax purposes, how is Joy's basis in the life insurance policy transferred to Jack?

- A. It's reset to fair market value at transfer
- B. It's zeroed out
- C. Jack receives Joy's basis at transfer**
- D. It's based on cash value at transfer

In the context of transferring a life insurance policy, the basis of the policy is generally transferred to the new owner as it is, rather than being altered or reset in some way. This means that Jack, the new owner of the policy, will receive Joy's basis at the time of the transfer. The basis is crucial for determining the tax implications when the policy is eventually sold or if there are distributions from it. Maintaining Joy's original basis helps ensure that any gain or loss is accurately reflected for tax purposes, accurately reflecting what was initially invested into the policy. Furthermore, the choices that suggest the basis would be reset or adjusted either to fair market value or based on cash value do not align with tax regulations governing the transfer of life insurance policies. In many instances, the basis is simply carried over, keeping it aligned with the original owner's investment to preserve tax integrity over the policy's life. Thus, Jack assumes Joy's basis, which is pivotal for subsequent transactions involving the policy.

9. What is a requirement for claiming the Home Office Deduction?

- A. The space must be a separate building from the residence
- B. The space must be used exclusively and regularly for business purposes**
- C. Home offices must be over 300 square feet in size
- D. The business must be registered with the state

To claim the Home Office Deduction, the requirement that the space must be used exclusively and regularly for business purposes is critical. This means that in order to qualify for the deduction, the area designated as a home office must be dedicated solely to the operation of a business. It cannot serve personal purposes at the same time; using the space partly for business and partly for personal activities would disqualify it from being considered a home office under tax guidelines. This criterion is essential because the Home Office Deduction is designed to provide tax relief to those who incur expenses related to maintaining a space in their home that is specifically used for business activities, recognizing the associated costs such as utilities, mortgage interest, and property taxes. The requirement for exclusivity differentiates business use from personal use, which is a key component of the IRS rules governing this deduction. In contrast to the correct answer, other options do not accurately represent the requirements stipulated by the IRS. For instance, the notion that the office must be a separate building contradicts the criteria, as many home offices are simply a portion of the main residence. Additionally, there is no minimum square footage requirement; hence, a home office can be smaller than 300 square feet. Lastly, while having a registered business

10. Which statement is CORRECT with respect to active participation in rental real estate?

- A. The interest may be held through a limited partnership
- B. A deduction-equivalent tax credit of up to \$25,000 is available
- C. The taxpayer must hold a 10% or greater ownership interest**
- D. The taxpayer must participate in management in a bona fide sense

Active participation in rental real estate is a concept defined by the IRS to allow taxpayers to utilize certain tax benefits, particularly for individuals who are actively involved in the management of their rental properties. The statement indicating that a taxpayer must hold a 10% or greater ownership interest is correct because one of the criteria for qualifying as an active participant involves having a significant enough interest in the property to be engaged in its management decisions. This ownership percentage is crucial as it distinguishes active participation from passive activities, allowing the taxpayer to potentially claim certain tax deductions related to rental activities. Active participation allows for various benefits under tax law, such as the ability to deduct losses from real estate activities on the taxpayer's Form 1040. Thus, members in partnerships or entities where ownership is diluted below the minimum threshold may not be eligible for the same treatments or benefits associated with rental real estate activities. This concept underscores the importance of ownership level in determining active participation status, which in turn impacts the overall tax treatment of rental income and losses.

Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

<https://cfptaxplanning.examzify.com>

We wish you the very best on your exam journey. You've got this!

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