

Tax School Practice Test (Sample)

Study Guide



Everything you need from our exam experts!

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SAMPLE

Questions

SAMPLE

- 1. What is implied about David's tax liability in California based on his income?**
 - A. Both David's parents were alive at the end of the year, so the Kiddie Tax is owed**
 - B. The Kiddie Tax is owed because David is a student under the age of 24**
 - C. David had investment income less than \$2,200 so there is no tax obligation**
 - D. David had earned income and must pay California taxes on all income**
- 2. What is the standard deduction?**
 - A. An optional deduction for self-employed individuals**
 - B. A fixed dollar amount that reduces the income subject to tax**
 - C. A percentage of total income deducted from taxes**
 - D. A deduction that varies by state**
- 3. Under California law, after how many days absent from the state under an employment-related contract will an individual not be treated as a resident for taxation purposes?**
 - A. 500 days**
 - B. 546 days**
 - C. 600 days**
 - D. 650 days**
- 4. How do you determine the basis of an asset?**
 - A. By evaluating its market value**
 - B. By considering the purchase price plus associated costs or improvements**
 - C. By applying a standard depreciation rate**
 - D. By dividing the asset value by its lifespan**
- 5. What amount must Tricia include for the discharge of indebtedness on her Schedule CA after a short sale of her principal residence?**
 - A. A. \$0**
 - B. B. \$25,000**
 - C. C. \$50,000**
 - D. D. \$100,000**

- 6. Which of the following best defines a sole proprietorship?**
- A. A business owned by multiple partners**
 - B. A corporation with shareholders**
 - C. A business owned and operated by one individual**
 - D. A non-profit organization**
- 7. How many days after the billing notice do other penalties need to be paid to avoid additional interest charges?**
- A. A. 10 days**
 - B. B. 14 days**
 - C. C. 15 days**
 - D. D. 20 days**
- 8. What is the primary purpose of filing a tax return?**
- A. To report income and claim social security benefits**
 - B. To report income, calculate tax liability, and determine any refund or amount owed**
 - C. To provide the government with personal information**
 - D. To apply for government grants**
- 9. What obligation does Paula have concerning California use tax for her television purchase from an out-of-state retailer?**
- A. She must use the Use Tax Worksheet to calculate the tax due**
 - B. She is not responsible for the use tax**
 - C. Only liable if the business has representatives in California**
 - D. Only liable if the business installs the merchandise**
- 10. Which method for paying state income taxes may be deducted for Federal purposes but not for California?**
- A. Withholding**
 - B. Estimated taxes**
 - C. Prior year balance dues paid in the current year**
 - D. All of the above**

Answers

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

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Explanations

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1. What is implied about David's tax liability in California based on his income?
- A. Both David's parents were alive at the end of the year, so the Kiddie Tax is owed
 - B. The Kiddie Tax is owed because David is a student under the age of 24
 - C. David had investment income less than \$2,200 so there is no tax obligation
 - D. David had earned income and must pay California taxes on all income**

David's situation implies that he had earned income, which is subject to taxation in California. California imposes taxes on all income earned by residents, regardless of the source, including wages, salaries, tips, and even self-employment income. This means that any earned income David received must be reported and taxed according to California's tax laws. In addition, if David is a resident of California, his tax liability would not only be based on his earned income but also on any other forms of income he might have, such as investment income, unless it falls below the thresholds for taxation. While the options related to the Kiddie Tax or investment income thresholds provide context about specific tax rules that might apply to minors or dependents, they don't directly address the broader obligation of all earned income being taxable in the state. Thus, David's tax liability would encompass all income he earned, which leads to the conclusion that he must pay California taxes on it.

2. What is the standard deduction?
- A. An optional deduction for self-employed individuals
 - B. A fixed dollar amount that reduces the income subject to tax**
 - C. A percentage of total income deducted from taxes
 - D. A deduction that varies by state

The standard deduction is a fixed dollar amount that reduces the income subject to tax, making option B the correct choice. It is a predetermined amount that taxpayers can claim to lower their taxable income instead of itemizing their deductions. This deduction varies based on the taxpayer's filing status, age, and in some cases, disability status. The significance of the standard deduction lies in its simplicity, as it allows individuals to automatically reduce their taxable income without the need to detail or document specific expenses that qualify for itemized deductions. This can make tax preparation more straightforward, especially for those with uncomplicated tax situations. In contrast, the other options do not accurately describe the standard deduction. The notion of it being an optional deduction for self-employed individuals doesn't align with its purpose, as the standard deduction is available to most taxpayers, regardless of their employment status. Suggesting that it is a percentage of total income misrepresents how it works, as it is a set dollar amount instead of a variable percentage. Lastly, the idea that it varies by state is incorrect because the standard deduction is a federal tax provision, while individual state deductions may exist but are separate from the federal standard deduction.

3. Under California law, after how many days absent from the state under an employment-related contract will an individual not be treated as a resident for taxation purposes?

- A. 500 days**
- B. 546 days**
- C. 600 days**
- D. 650 days**

Under California law, an individual may not be treated as a resident for taxation purposes if they are absent from the state for more than 546 days under an employment-related contract. This provision is designed to address situations where individuals may work outside of California for extended periods, allowing them to avoid being classified as a resident for tax purposes, which generally requires that a person be physically present in the state for more than half the year. Choosing 600 days may seem close, but it exceeds the threshold set forth in the legislation. The key to understanding this rule lies in recognizing the specific duration stipulated by California tax law, which is clearly stated as 546 days. This means that if someone is absent from the state for any employment-related contract for a period greater than this, they are no longer liable for California state income taxes as a resident. This rule serves as an important guideline for individuals who frequently travel for work and need to understand their tax obligations concerning residency status. It's essential to accurately track days spent within and outside of California to ensure compliance with the state's tax regulations.

4. How do you determine the basis of an asset?

- A. By evaluating its market value**
- B. By considering the purchase price plus associated costs or improvements**
- C. By applying a standard depreciation rate**
- D. By dividing the asset value by its lifespan**

To determine the basis of an asset, the correct approach involves considering the purchase price along with any associated costs or improvements. This comprehensive calculation accounts for not just the initial expense but also any modifications or additional costs incurred that enhance the value or usability of the asset. The basis is critical because it establishes the value used for calculating gain or loss upon sale or transfer of the asset. For example, if an individual buys equipment for \$10,000 but also spends an additional \$1,000 on installation, the basis would be \$11,000. This complete picture of costs ensures that when the asset is sold in the future, the gain or loss reflects the true investment made. Utilizing market value, applying a standard depreciation rate, or simply dividing the asset's value by its lifespan does not provide an accurate basis as they do not fully represent all costs associated with acquiring and preparing the asset for its intended use. These methods might overlook significant expenditures or fail to provide a realistic calculation necessary for tax implications when the asset is disposed of or assessed for depreciation. Thus, calculating the basis accurately is crucial for proper tax reporting and financial management.

5. What amount must Tricia include for the discharge of indebtedness on her Schedule CA after a short sale of her principal residence?

A. A. \$0

B. B. \$25,000

C. C. \$50,000

D. D. \$100,000

In the context of the discharge of indebtedness during a short sale of a principal residence, Tricia is typically able to exclude the amount of any forgiven debt from her taxable income. This is primarily due to provisions under the Mortgage Forgiveness Debt Relief Act, which allows taxpayers to exclude from income any discharge of debt that occurs when a principal residence is sold in a short sale. Since a short sale results in the lender forgiving a portion of the mortgage debt, this forgiven debt would normally be considered income. However, because of the specified tax relief provisions, if the transaction meets certain conditions, zero income recognition is required for Tricia. Thus, she would report "\$0" for the discharge of indebtedness on her Schedule CA, as the act protects homeowners from income tax liability for such forgiven amounts. This exclusion is specifically applicable to the debt associated with the principal residence, which typically allows homeowners relief and avoids additional financial burden during a challenging financial situation.

6. Which of the following best defines a sole proprietorship?

A. A business owned by multiple partners

B. A corporation with shareholders

C. A business owned and operated by one individual

D. A non-profit organization

A sole proprietorship is best defined as a business owned and operated by one individual. This form of business structure is characterized by its simplicity and direct control, as the owner has full rights to the income generated by the business while also bearing complete responsibility for its debts and obligations. This direct relationship between the owner and the business is what sets sole proprietorships apart from other business entities, such as partnerships or corporations. In a sole proprietorship, there's no legal distinction between the owner and the business, which means that income is reported on the owner's personal tax return and any losses incurred in the business can be deducted from the owner's personal income. This structure allows for minimal regulatory requirements and is often easier and less expensive to establish compared to other business forms. As a result, it is a popular choice for individual entrepreneurs and small business owners.

7. How many days after the billing notice do other penalties need to be paid to avoid additional interest charges?

- A. A. 10 days**
- B. B. 14 days**
- C. C. 15 days**
- D. D. 20 days**

The correct response indicates that penalties need to be addressed within 15 days following the issuance of a billing notice to avoid incurring additional interest charges. Understanding this timeframe is essential for taxpayers to manage their obligations effectively. If payments or actions are not taken within this 15-day period, the consequences can include additional interest accruing on the outstanding amounts, which can significantly increase the total liability. In the context of tax penalties, it is critical for taxpayers to be aware of deadlines, as timely responses can lead to avoidance of further financial repercussions. This proactive management of tax obligations aids in minimizing costs associated with late payments or lingering debts. Being informed about how many days remain after receiving a billing notice empowers individuals to plan their payment strategies accordingly in order to fulfill their obligations and potentially ease the burden of interest charges.

8. What is the primary purpose of filing a tax return?

- A. To report income and claim social security benefits**
- B. To report income, calculate tax liability, and determine any refund or amount owed**
- C. To provide the government with personal information**
- D. To apply for government grants**

Filing a tax return serves multiple important functions, but its primary purpose revolves around reporting income, calculating tax liability, and determining whether there are any taxes owed or whether a refund is due. When individuals or businesses file their tax returns, they provide the Internal Revenue Service (IRS) with comprehensive information about their earnings and other financial activities over the year. This allows the IRS to assess how much tax should have been paid based on that income. Tax returns also play a crucial role in ensuring compliance with tax laws. When individuals accurately report their income and expenses, it helps the government ensure that everyone contributes their fair share towards public projects and services. In situations where too much tax has been paid throughout the year, individuals can receive a refund, providing a financial benefit. Conversely, if insufficient taxes were paid, the tax return helps calculate the amount owed, ensuring that taxpayers can fulfill their obligations. This process promotes transparency and accountability in the tax system, reinforcing the relationship between taxpayers and the government. The other options, while they contain some elements related to tax returns, do not fully encompass the comprehensive rationale behind why a tax return is primarily filed. Reporting income for social security benefits and providing government with personal information are secondary outcomes, and applying for government grants is unrelated.

9. What obligation does Paula have concerning California use tax for her television purchase from an out-of-state retailer?

- A. She must use the Use Tax Worksheet to calculate the tax due**
- B. She is not responsible for the use tax**
- C. Only liable if the business has representatives in California**
- D. Only liable if the business installs the merchandise**

Paula has an obligation regarding California use tax for her television purchase from an out-of-state retailer because use tax is levied on goods purchased from outside California for use within the state. This tax is applicable when sales tax has not been paid at the time of purchase. When an individual purchases an item like a television from an out-of-state retailer who does not charge California sales tax, the buyer is responsible for reporting and paying the appropriate use tax to ensure compliance with state tax laws. Utilizing the Use Tax Worksheet is an effective method provided by California's tax authority to assist taxpayers in calculating the amount of use tax owed. This process involves identifying the purchase price and applying the local tax rate to ensure accurate reporting of the tax due. Therefore, Paula must indeed use the Use Tax Worksheet to determine her specific tax obligation. The other options inaccurately represent the obligations related to use tax. For instance, the notion that she is not responsible for use tax ignores the law that establishes liability in this scenario. Similarly, the claims about being liable only if the business has representatives in California or if installation occurs are also misleading, as the obligation to pay use tax exists independently of these factors.

10. Which method for paying state income taxes may be deducted for Federal purposes but not for California?

- A. Withholding**
- B. Estimated taxes**
- C. Prior year balance dues paid in the current year**
- D. All of the above**

The correct choice suggests that all the provided methods for paying state income taxes can be deducted for federal purposes but not for California. In general, the federal tax code allows taxpayers to deduct certain state and local taxes (SALT), including income taxes, as an itemized deduction. However, California has its own specific rules about these deductions. Withholding involves the amounts deducted from wages to pay state taxes and is typically deductible on federal returns. Estimated taxes refer to payments made toward anticipated state tax liabilities, which are also usually deductible federally. Prior year balance dues paid in the current year can be seen as fulfilling an obligation from the previous year, these amounts generally consider deductible for federal reporting. However, California limits the deduction for state income taxes significantly through its own tax rules, including the SALT cap. This means that while these payments may reduce taxable income on the federal return, California does not allow the same deductions or provides different treatment for these tax payments. Thus, it's accurate that these methods of paying state income taxes may be deductible for federal purposes but not for California specifically due to the state's unique rules and regulations regarding tax deductions.