

**TAX STRATEGY PROBLEM**

- C3-62 Mike Barton owns Barton Products, Inc. The corporation has 30 employees. Barton Corporation expects \$500,000 of net income before taxes in 2004. Mike is married and files a joint return with his wife, Elaine, who has no earnings of her own. They have one dependent son, Robert, who is 16 years old. Mike and Elaine have no other income and do not itemize. Mike's salary is \$200,000 per year (already deducted in computing Barton Corporation's \$500,000 net income).
- Should Mike increase his salary from Barton to reduce the overall tax burden to himself and Barton Products? If so, by how much?
  - Should Barton employ Mike's wife for \$50,000 rather than increase Mike's salary? Take into consideration employment taxes as well as federal income taxes.
  - How much would be saved in overall taxes if Barton employs Robert part-time for \$20,000 per year? Assume the corporation and Robert each would incur a 7.65% payroll tax with the corporate portion being deductible.

**TAX FORM/RETURN PREPARATION PROBLEM**

- C3-63 Packer Corporation, incorporated on January 3, 1994, is a calendar year taxpayer that uses the accrual method of accounting. Its employer identification number is 74-1234567. Its address is 1010 West Avenue, San Antonio, Texas 78213. Packer operates a bookstore. Bob Parks (social security number 000-45-3000) owns 100% of the single class of stock. Bob resides at 25 Ancient Bend, San Antonio, TX 78248. He receives \$65,000 in salary from Packer in the current year. During the current year, Packer reports the following income and expense items:

|                                                            |           |
|------------------------------------------------------------|-----------|
| Gross receipts                                             | \$595,000 |
| Purchases                                                  | 300,000   |
| Salaries: Officers                                         | 65,000    |
| Other employees                                            | 50,000    |
| Rent payments                                              | 48,000    |
| Taxes: Payroll                                             | 9,000     |
| Franchise                                                  | 250       |
| Interest payments                                          | 250       |
| Charitable contributions (cash)                            | 8,000     |
| Depreciation (see schedule below)                          | 38,820    |
| Advertising                                                | 15,000    |
| Telephone                                                  | 500       |
| Utilities                                                  | 17,080    |
| Officer's life insurance premium (firm is the beneficiary) | 1,500     |

Depreciation Schedule

| <u>Asset</u> | <u>Cost</u>      | <u>Prior<br/>Depreciation</u> | <u>Method</u> | <u>Current Year<br/>Depreciation</u> |
|--------------|------------------|-------------------------------|---------------|--------------------------------------|
| Light truck  | \$ 20,000        | \$10,400                      | MACRS         | \$ 3,840                             |
| Fixtures     | 200,000          | 77,560                        | MACRS         | 34,980                               |
| Total        | <u>\$220,000</u> | <u>\$87,960</u>               |               | <u>\$38,820</u>                      |

On May 10, Packer sold for \$3,500 a truck purchased seven years earlier for \$8,000. The corporation has fully depreciated the truck using the regular MACRS tables. Packer uses the same depreciation method for tax and book purposes. The corporation made estimated tax payments on April 13, June 14, September 11, and December 13 of the current year of \$2,000 each (total of \$8,000). Its prior year tax liability was \$8,000. Packer's balance sheet at the beginning and end of the current year is as follows:

| <u>Assets</u>                   | <u>January 1</u> | <u>December 31</u> |
|---------------------------------|------------------|--------------------|
| Cash                            | \$ 34,000        | \$ 32,420          |
| Other current assets            | —0—              | 48,075             |
| Depreciable assets              | 228,000          | 220,000            |
| Minus: Accumulated depreciation | (95,960)         | (126,780)          |
| Inventory                       | 125,000          | 145,000            |
| Total assets                    | <u>\$291,040</u> | <u>\$318,715</u>   |

Form 1120  
pp 1-5  
Form 4797  
Form 4562

Liabilities and Stockholders' Equity

|                                    |                  |                  |
|------------------------------------|------------------|------------------|
| Accounts payable                   | \$ 68,900        | \$ 39,475        |
| Common stock                       | 60,000           | 60,000           |
| Retained earnings (unappropriated) | 162,140          | 219,240          |
| Total liabilities and equity       | <u>\$291,040</u> | <u>\$318,715</u> |

Packer Corporation uses the first-in, first-out inventory method. The corporation does not claim any deduction for expenses connected with entertainment facilities, living accommodations, or employees attending foreign conventions. The corporation does not own any stock in any other corporation and has no interest in or authority over any foreign bank account or other foreign assets. The corporation did not pay any dividends in the current year. The other current assets amount at year-end consists entirely of marketable securities. No NOL carryovers are available from prior tax years. In computing the year-end retained earnings balance, Packer expensed \$8,000 of federal income taxes (i.e., the amount paid in estimated taxes during the year). Prepare Form 1120 for Packer Corporation for the current year.

### CASE STUDY PROBLEMS

C3-64

Marquette Corporation, a tax client since its creation three years ago, has requested that you prepare a memorandum explaining its estimated tax requirements for 2005. The corporation is in the fabricated steel business. Its earnings have been growing each year. Marquette's taxable income for the last three tax years has been \$500,000, \$1.5 million, and \$2.5 million, respectively. The Chief Financial Officer expects its taxable income in 2005 to be approximately \$3 million.

*Required:* Prepare a one-page client memorandum explaining Marquette's estimated tax requirements for 2005, providing the necessary supporting authorities.

C3-65

Susan Smith accepted a new corporate client, Winter Park Corporation. One of Susan's tax managers conducted a review of Winter Park's prior year tax returns. The review revealed that an NOL for a prior tax year was incorrectly computed, resulting in an overstatement of NOL carrybacks and carryovers to prior tax years.

- Assume the incorrect NOL calculation does not affect the current year's tax liability. What recommendations (if any) should be made to the new client?
- Assume the IRS is currently auditing a prior year. What are Susan's responsibilities in this situation?
- Assume that the NOL carryover is being carried to the current year and that Winter Park Corporation does not want to file amended tax returns to correct the error? What should Susan do in this case?

C3-66

The Chief Executive Officer of a client of your public accounting firm saw the following advertisement in *The Wall Street Journal*:

**DONATIONS WANTED**

The Center for Restoration of Waters

A Nonprofit Research and Educational Organization

Needs Donations—Autos, Boats, Real Estate, Etc.

**ALL DONATIONS ARE TAX-DEDUCTIBLE**

Prepare a memorandum to your client Phil Nickelson explaining how the federal income tax laws regarding donations of cash, automobiles, boats, and real estate apply to corporate taxpayers.

### TAX RESEARCH PROBLEMS

Wicker Corporation makes estimated tax payments of \$6,000 in 2003. On March 15, 2004, it files its 2003 tax return, showing a tax liability of \$20,000, and it pays the balance of \$14,000. On April 15, 2004, it discovers an error and files an amended return for 2003 showing a reduced tax liability of \$8,000. Prepare a memorandum for your tax manager explaining whether Wicker Corporation can base its estimated tax payments for 2004 on the \$8,000 tax liability for 2003, or must it use the \$20,000 tax liability reported on its original return. Your manager has suggested that, at a minimum, you consult the following resources: