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The background of the slide is a collage. The top half shows a close-up of a US one hundred dollar bill, with the portrait of Benjamin Franklin and the serial number 39949756 visible. The bottom half shows wooden blocks spelling out the word 'TAX' in a row. The blocks are light-colored wood with black letters and numbers. The 'T' has a small '1' below it, the 'A' has a small '1' below it, and the 'X' has a small '8' below it. The blocks are resting on a surface that appears to be a US Treasury note, with the text 'THIS NOTE IS LEGAL TENDER FOR ALL DEBTS, PUBLIC AND PRIVATE' visible.

2020 Federal Business Tax Update

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2020 Federal Business Tax Update

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2020 Presidential Candidates Tax Proposals

Ordinary Income Tax Rates

- **Individual Income Tax Rates**

Present Law:

- 37% top marginal rate.

Biden:

- Increase top marginal rate to 39.6% for those with taxable income above \$400,000.
- Those with less than \$400,000 of income would not have a tax increase.

Trump:

- Make TCJA rates permanent – 10%, 12%, 22%, 24%, 32%, 35% and 37%.
- **Cut middle-class taxes by 10%, but no specifics.**

LT Capital Gains & Qualified Dividends

Present law:

- Taxed at 0%, 15% or 20% depending on income.
- 3.8% NIIT on incomes over \$200,000 single and \$250,000 married joint.
- TCJA created Qualified Opportunity Zones (QOZ) which allow for deferral of capital gains.

Biden:

- For taxpayers with income over \$1 million, tax at top ordinary income tax rate of 39.6%.
- Public disclosure of people who receive QOZ tax benefits to show impact on local residents.

Trump:

- Reduce top capital gains tax rate to 15%.
- Index capital gains rates to inflation (i.e., allow for an increase to basis based on inflation).

- **Itemized Deductions**

Present Law:

- The TCJA increase the standard deduction available to all taxpayers. However, it eliminated personal exemptions and further limited or eliminated other itemized deductions.
- Itemized deduction changes under the TCJA sunset after 2025.

Biden:

- **Restores the Pease limitation** on itemized deductions for taxable income above \$400,000.
- **In addition, a cap on itemized deductions at 28% of value.**
- Eliminate **SALT cap**.

Trump: Make TCJA standard deduction and itemized deduction changes permanent.

- **Student Loans and Education**

Biden - **Tax-free forgiveness of all student loans** after 20 years on income-based repayments.

Trump - Tax credit for donations to private school scholarship funds.

Payroll & Self-Employment Taxes

- Payroll Taxes & Self-Employment Taxes

Present Law:

- 6.2% Social Security tax on wages up to \$142,800 (2021 limit) paid by both the employer and employee.
- 1.45% Medicare tax on all wages paid by both the employer and employee.
- 0.9% Medicare tax on wages in excess of \$200,000, \$250,000 if married paid only by employee.
- 12.4% Social Security tax on self-employment earnings up to \$142,800 (2021 limit).
- 2.9% Medicare tax on all self-employment earnings.

Biden:

- Keeps the FICA & Social Security wage cap's existing threshold of \$142,800 (indexed).
- Applies the 6.2% FICA tax on both employer and employee on wages earned above \$400,000.
- Applies the 12.4% tax on all self-employment income over \$400,000.
- The 6.2%/12/4% tax would not apply to wages or self-employment income between \$142,800 and \$400,000.

- **Medicare for All Premium Tax** - Biden currently does not has a public proposal for this.

- **Carried Interest**

Present Law:

- Requires separate holding period tracking for gains allocated to partners who obtain partnership interest in connection with the performance of services.
- Carried interest would need to **be held for a minimum of 3 years in order to receive long-term capital gain** treatment upon sale.

Biden:

- No current public proposal related to this item, but the Obama Administration proposed to change tax treatment of **carried interest from capital to ordinary**.
- Democrats support a change on this item.

- **Qualified Business Income Deduction (QBID) - (Section 199A)**

Present Law - Taxpayers who have domestic (QBID) from a partnership, S corporation, or sole proprietorship. may be entitled to up to a 20% deduction.

Biden:

- **Phases out the QBID for filers with taxable income above \$400,000.**
- **Disallow QBID for real estate investors.**

Trump - Make QBID permanent.

- Like-Kind Exchange - Biden:
 - Repeal of like-kind exchanges of real property for taxpayers with income over \$400,000.
- Retirement Accounts - Biden:
 - Eliminate deduction for retirement contributions and replace with a flat 26% tax credit.
 - Create an automatic 401(k) option for workers whose employer doesn't offer a retirement option.
- Corporate Income Tax Rate - Biden:
 - Increase flat tax rate from 21% to 28%.
 - 15% minimum tax on book income with U.S. – based income of \$100 million or more.
 - 10% offshoring surtax on profits of U.S. companies operating overseas and selling in the U.S.
 - This surtax would raise the effective corporate tax rate to 30.8%.

Tax Credits

- **Renewable Energy Credit - Biden:**
 - Restore electric vehicle tax credit.
 - Expands several renewable-energy-related tax credits, including tax credits for carbon capture, use, and storage as well as credits for residential energy efficiency.
- **Manufacturing Credit - Biden:**
 - Establish an advanceable 10% “Made in America” tax credit for activities that restore production, revitalize existing closed or closing facilities, retool facilities to advance manufacturing employment, or expand manufacturing payroll.
- **First-Time Home Buyers - Biden:**
 - Create **\$15,000 tax credit for first-time home buyers.**
 - Create a refundable **tax credit for renters** aimed at holding rent and utility payments at 30% of income.

Tax Credits

- **Child and Dependent Care Credit, Child Tax Credit & Earned Income Credit - Biden:**
 - Expands from a maximum of \$3,000 in qualified expenses to \$8,000 (\$16,000 for multiple dependents) and Increases maximum credit rate from 35% to 50%.
 - For 2021 and as long as economic conditions require, increases the Child Tax Credit (CTC) from a maximum value of \$2,000 to \$3,000 for children 17 or younger, while providing a \$600 bonus credit for children under 6. The CTC would also be made fully refundable, removing the \$2,500 reimbursement threshold and 15% phase-in rate.
 - Expands the Earned Income Tax Credit (EITC) for childless workers aged 65.

Transfer Tax

- **Gift/Estate/GST Tax Exemption**

Present Law:

- Exemption per donor of \$10 million, with indexing for inflation through 2025, and a return to pre-TCJA levels on January 1, 2026.
- \$11.58 million per donor in 2020.

Biden:

- Return the estate tax to 2009 levels, which would reduce the estate and GST exemption to **\$3.5 million per taxpayer**.
- May imply a lifetime **gift and GST exemption** of **\$1 million per taxpayer**.

- **Estate/Gift/GST Tax Rates**

- **Present Law** –Top rate of **40%**
- **Biden** - A return to 2009 levels may imply a top rate of **45%**.

Transfer Tax

- **Basis Step-Up.**

Present Law:

- Inherited assets receive a basis equal to the fair market value as of the date of death (or alternate valuation date).

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Biden:

- Eliminate step-up in basis and possibly tax unrealized capital gains at death on assets not passing to a surviving spouse or charity.

C Corporations

Reduction in C Corporation Tax Rate

- **Prior Law** - C corporations were subject to graduated tax rates of 15% (for taxable income of \$0 - \$50,000), 25% (for taxable income of \$50,001 - \$75,000), 34% (for taxable income of \$75,001 - \$10,000,000), and 35% (for taxable income over \$10,000,000).
 - Personal service corporations pay tax on their entire taxable income at the rate of 35%.
- **TCJA** - For tax years beginning after December 31, 2017, the corporate tax rate is a **flat 21% rate**, including personal service corporations.
 - The corporate alternative minimum tax **(AMT) is repealed**.
 - **No sunset - permanent**.
 - **Note:** This rate will also apply to the S corporations who have recognized built-in-gains in years beginning after December 31, 2017.

... Should an S Corporation Convert to a C Corporation?

- Since C corporations are now at 21%, does it make sense for S corporations to terminate their S corporation elections?
- Although a detailed analysis should be done, the answer in most cases is probably be no.
- Although at a 21% corporate tax rate, wages paid out are still taxed as ordinary income tax rates (and are not eligible for the 20% QBI deduction).
- Dividends paid out of the after-tax income of the corporation are subject to capital gains rates as the corporation does not receive a deduction for the dividends that income will be subject to double taxation with Federal tax rates approaching 37%.
 - $21\% \text{ Corp Tax} + (79\% \times 23.8\%) \text{ Dividend Tax} = 39.80\% \text{ Total Tax.}$
 - $\text{Top Tax Rate with QBID} (37\% \times 80\%) = 29.60\% \text{ (ignores state tax).}$
 - Even after considering state taxes the difference is still about 10%.

... Should an S Corporation Convert to a C Corporation Under Biden Tax Proposal?

- Dividends paid out of the after-tax income of the corporation are subject to capital gains rates as the corporation does not receive a deduction for the dividends that income will be subject to double taxation with Federal tax rates approaching 39.6%.
 - $28\% \text{ Corp Tax} + (72\% \times 23.8\%) \text{ Dividend Tax} = 45.14\% \text{ Total Tax.}$
 - $\text{Top Tax Rate with QBID } (35\% \times 80\%) = 28.00\% \text{ (ignores state tax).}$
 - $\text{Top Tax Rate without QBID} = 39.60\% \text{ (ignores state tax).}$

Polling Question 1

Paycheck Protection Program

Paycheck Protection Program (PPP)

- The CARES Act established the PPP Loan program.
- PPP loans were made available to businesses and certain non-profit organizations **with 500 employees or less** (including affiliates).
- Applicants have to **certify economic need and uncertainty**.
- Loan amount was determined based on **average monthly “payroll costs”** incurred during a base period (generally incurred in 2019) **multiplied by 2.5**, limited to \$10,000,000.
- **Up to 100% of the PPP loan is forgivable** if certain spending requirements are met during the “covered period.”
- **Covered period is the 8-week or 24-week period** after the loan proceeds were disbursed.

Latest Paycheck Protection Program Statistics

As of August 8, 2020:

- Total PPP loans: **5.212 million loans.**
- Total loan amount: **\$525.0 billion.**
- Average loan size: **\$101,000.**
- **Breakdown of PPP Loan Size:**
 - 68.6% - \$50,000 and under
 - 13.1% - \$50,000 - \$100,000
 - 5.7% - \$100,000 - \$150,000
 - 7.2% - \$150,000 - \$350,000
 - 3.8% - \$350,000 - \$1million
 - 1.0% - \$1 million - \$2 million
 - 0.6% - \$2 million and above
- **Funding:** First round - \$349 million; Second round - \$320 million (closed 8/8/20)
 - Funding remaining - \$134 million.

PPP Loan Borrower Certification Requirements

- An eligible recipient applying for a covered loan **must make a good faith certification** to the lender that:
 - The **uncertainty of current economic conditions makes necessary** the loan request to support the ongoing operations of the eligible recipient.
 - The borrower is taking into account their current business activity and their ability to **access other sources of liquidity** to support their ongoing operations **in a manner that is not significantly detrimental to the business.**
 - The borrower will **use the funds to retain workers** and maintain payroll or **make mortgage, lease, and utility payments.**
 - **Note, there appears to be no tracing rule as to the use of the proceeds.**
 - **Not more than 40% (was 25%)** of the loan proceeds will be **used for non-payroll costs.**

PPP Loan Forgiveness Amount

- An eligible recipient is eligible for forgiveness of indebtedness on a covered loan in an amount equal to the sum of the following **costs incurred** and **payments made** during **the 8-week or 24-week period beginning on the date of the origination of a covered loan but ending not later than December 31, 2020:**
 - **Payroll Costs** - Must be **at least 60%** of loan forgiveness amount.
 - **Non-Payroll Costs** - Must **not exceed 40%** of loan forgiveness amount.
 - **Interest Payments** on indebtedness or a debt instrument incurred in the ordinary course of business that is:
 - A liability of the borrower;
 - Is a **mortgage on real or personal property; and**
 - Was incurred before February 15, 2020.
 - **Rent Payments** made under a lease agreement **dated before February 15, 2020.**
 - Make sure **written related party lease agreements** are in place.
 - **Related party lease payments are limited to mortgage interest owed on the property.**
 - **Utility Payments** related to the distribution of **electricity, gas, water, transportation, telephone or internet access** for which service began before February 15, 2020.

PPP Loan Forgiveness Amount

Payroll Costs Include:

- The sum of payments of any compensation with respect to employees that is a:
 - Salary, wage, commission, or similar compensation;
 - Payment of cash tip or equivalent;
 - Payment for vacation, parental, family, medical or sick leave;
 - Allowance for dismissal or separation;
 - Payment required for the provision of group health care benefits, including insurance premiums, and retirement; or
 - Payment of state or local tax assessed on the compensation of employees.
- Salary (cash compensation) for each employee is limited to an annual salary of \$100,000 prorated based on the Covered Period.

Loan Forgiveness - Covered Period

- When does the covered period (24 weeks or 8 weeks) begin to determine the amount of the forgiveness for the PPP loan?
- The covered period begins on the date the lender makes the first disbursement of the loan.
- Borrowers who received loans prior to June 5, 2020 can elect an 8-week covered period or a 24-week covered period.
- Borrowers who received loans on or after June 5, 2020 will have a 24-week covered period.
- The loan forgiveness application released on May 15, 2020 provides for an “alternative payroll covered period.”
 - Borrowers with a biweekly (or more frequent) payroll schedule may elect to calculate eligible payroll costs using the 24-week (or 8-week if elected) period that begins on the first day of their first pay period following their loan disbursement date.

PPP Loan Forgiveness - Compensation Caps

Non-Owner Employee Compensation Caps

- 8-week Covered Period - \$15,385.
- 24-week Covered Period - \$46,154.

Owner-Employees or Self-Employed Individuals

- 8-week Covered Period - 2.5/12 of 2019 compensation capped at \$15,385.
- 24-week Covered Period - 2.5/12 of 2019 compensation capped at \$20,833.

PPP Loan Forgiveness - Compensation Caps

- **C Corporations:**

- Owner-employee - Any owner who is an employee.
- Cash compensation amount - Payments made or incurred during the Covered Period limited to the above caps.
- Employer state and local payroll taxes, health insurance and retirement contribution payments capped at 2.5/12 of 2019 amounts.
 - These amounts do not count in the \$15,285/\$20,833 caps.

- **S Corporations:**

- Owner-employee - Any owner who is an employee.
- Cash compensation amount - Payments made or incurred during the Covered Period limited to the above caps.
- Employer state and local payroll taxes, health insurance and retirement contribution payments capped at 2.5/12 of 2019 amounts.
 - These amounts do not count in the \$15,285/\$20,833 caps.
- Employer contributions for health insurance for 2% or more owner-employees **are not eligible for forgiveness.**

PPP Loan Forgiveness - Compensation Caps

- **C Schedule C& F Filers:**

- Owner Compensation Replacement - Determined based on 2.5/12 of 2019 net profit on Schedule C and F, capped at above amounts.
- Employer contributions for state or local taxes, health insurance and retirement contributions **for owners are not eligible for forgiveness.**

- **General Partners:**

- Partner Compensation - Determined based payments made during the covered period and limited to 2.5/12 of 2019 Schedule K-1 self-employment earnings multiplied by .9235 and capped at above amounts.
- Employer contributions for state or local taxes, health insurance and retirement contributions **for partners are not eligible for forgiveness.**

Loan Forgiveness Reductions

- The CARES Act specifically requires certain reductions in a borrower's loan forgiveness amount based on:
 - Reductions in FTEs, or
 - Reductions in employee salary and wages during the covered period.
- These reductions are subject to an important statutory exemption for borrowers who have rehired employees and restored salary and wage levels by December 31, 2020 (with limitations).
- FTEs are calculated using either of the following:
 - For each qualifying employee, divide number of hours per week by 40; or
 - Use 0.5 for every employee that works less than 40 hours.

Reduction of Loan Forgiveness - FTEs Reduction

- What effect does a reduction in a borrower's number of FTEs have on the loan forgiveness amount?
 - In general, a reduction in FTE employees during the Covered Period reduces the loan forgiveness amount by the same percentage as the percentage reduction in FTE employees.
 - The borrower must first select a reference period: (i) February 15, 2019 through June 30, 2019; (ii) January 1, 2020 through February 29, 2020.
 - In the case of a seasonal employer, either of the two preceding methods or a consecutive 12-week period between May 1, 2019 and September 15, 2019.
 - If the average number of FTE employees during the Covered Period is less than during the reference period, the total eligible expenses available for forgiveness is reduced proportionally by the percentage reduction in FTE employees.
 - For example, if a borrower had 10.0 FTE employees during the reference period and this declined to 8.0 FTE employees during the covered period, the percentage of FTE employees declined by 20 percent and thus only 80 percent of otherwise eligible expenses are available for forgiveness.

Reduction of Loan Forgiveness - Reduction in Wages

- The amount of loan forgiveness shall also be reduced by the amount of any reduction in total salary (based on average annual salary or hourly wage) of any employee during the period February 15, 2020 and April 26, 2020 that is in excess of 25% of the total salary (based average annual salary or hourly wage) of such employee between January 1, 2020 and March 31, 2020.
 - This reduction rule only applies to employees who did not receive during any single pay period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000.
 - To ensure that borrowers are not doubly penalized, the salary reduction applies only to the portion of the decline in employee salary that is not attributable to the FTE reduction.

Loan Forgiveness Reductions - Salary Restoration

- **Question:** If a borrower restores reductions made to employee salaries and wages by not later than December 31, 2020, can the borrower avoid a reduction in its loan forgiveness amount?
- **Answer:** Yes. If certain employee salaries and wages were reduced between February 15, 2020 and April 26, 2020 but the borrower eliminates those reductions by December 31, 2020 or earlier, the borrower is exempt from any reduction in loan forgiveness amount that would otherwise be required due to reductions in salaries and wages.

Loan Forgiveness Reductions – FTE Safe Harbors

- **Question:** If a borrower restores reductions made to FTE employees by not later than December 31, 2020, can the borrower avoid a reduction in its loan forgiveness amount?
- **Answer:** Yes, if borrower meets one of the following safe harbors:
- **Safe Harbor #1:**
 - If the Borrower reduced its FTE employee levels in the period beginning February 15, 2020, and ending April 26, 2020; and
 - The Borrower then restored its FTE employee levels by not later than December 31, 2020 to its FTE employee levels in the Borrower's pay period that included February 15, 2020.
- **Safe Harbor #2:**
 - Borrower documents an inability to return to the same level of business activity as before February 15, 2020, due to compliance with safety requirements established or guidance issued by the government (HHS, CDC, or OSHA) during the period March 1, 2020 through December 31, 2020 related to COVID-19.

Loan Forgiveness Reductions - Employee Declines

- **Question:** Will a borrower be subject to a reduction to its forgiveness amount due to a reduction in FTE employees during the Covered Period if the borrower offered to rehire one or more laid off employees, **but the employees declined**?
- **Answer:** In calculating its loan forgiveness amount, a borrower may exclude any reduction in FTE employees if the borrower is able to document in good faith the following:
 - An inability to rehire individuals who were employees of the borrower on February 15, 2020 and,
 - An inability to hire similarly qualified individuals for unfilled positions on or before December 31, 2020.
- Borrowers are required to inform the applicable state unemployment insurance office of any employee's rejected rehire offer within 30 days of the employee's rejection of the offer.
- The documents that borrowers should maintain to show compliance with this exemption include the written offer to rehire an individual at the same salary and hours, a written record of the offer's rejection, and a written record of efforts to hire a similarly qualified individual.

... Loan Forgiveness Reductions - Employee Termination, Etc.

- **Question:** Will a borrower's loan forgiveness amount be reduced if an employee is fired for cause, voluntarily resigns, or voluntarily requests a schedule reduction?
- **Answer:** No. In these cases, the borrower may count such employee at the same full-time equivalency level before the FTE reduction event when calculating the FTE employee reduction penalty.

PPP Loan Forgiveness Application

- **SBA Provides Three Different PPP Loan Forgiveness Applications**
 - **Form 3508S** - Only for borrowers that received a PPP loan for 50,000 or less.
 - **Form 3508EZ** - For borrowers that meet one of the following:
 - Borrower is a self-employed individual with no employees;
 - Borrower did not reduce the salaries or wages of any of their employees (making \$100,000 or less in 2019) by more than 25% during the Covered Period compared to the period 1/1/20 - 3/31/20, and did not reduce the number of employees or hours of employees between 1/1/20 and the end of the Covered Period (unless safe harbors apply); or
 - Borrower did not reduce annual salary or hourly wages of any employee (making \$100,000 or less in 2019) by more than 25% during the Covered Period compared to the period 1/1/20 - 3/31/20, and was unable to operate during the Covered Period at the same level of business activity as before 2/15/20, due to compliance requirements established by HHS, CDC or OSHA related to COVID-19.
 - **Form 3508** – For borrowers that aren't allowed to file Form 3508S or 3508EZ.

... Loan Forgiveness Application Documentation Requirements

- An eligible recipient seeking loan forgiveness **shall submit to the lender an application** which shall include the following:
 - **Documentation verifying the number of FTEs** on payroll and pay rates.
 - **Payroll tax filings** reported to the IRS and State income, payroll, and unemployment insurance filings.
 - **Documentation, including cancelled checks, payment receipts**, transcripts of accounts, or other documents verifying payments on covered mortgage obligations, payments on covered lease obligations, and covered utility payments.
 - **Certification from an authorized representative of the eligible recipient that:**
 - The documentation presented is true and correct; and
 - **The amount for which forgiveness is requested was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered rent obligation, or make covered utility payments.**

PPP Loan Necessity Questionnaire

- Applicants (including affiliates) who obtained a **PPP loan of \$2 million or more** must complete one of the following questionnaires when applying for loan forgiveness.
 - **Form 3509 - For-Profit Borrowers.**
 - **Form 3510 - Non-Profit Borrowers.**
- Same or similar questionnaire may be used by SBA for PPP loans under 2 million that are audited.

Loan Forgiveness Approval Process

- Once the loan forgiveness application is submitted to the lender, the lender has **60 days** to review and approve the application and submit their decision to the SBA.
- The SBA then has **90 days** to approve the application.
- **The borrower may submit the loan forgiveness application any time before the maturity date of the loan.**
- However, If the borrower **does not apply for forgiveness within 10 months after the last day of the Covered Period**, payments are no longer deferred and the borrower must begin making payments on the loan.

Unforgiven Portion of PPP Loan Terms

The terms and interest rate of the unforgiven portion of the loan is as follows:

- The interest rate will be 1%.
- The maturity of the loan is 2 years for loans made prior to June 5, 2020 and 5 years for loans made on and after June 5, 2020.
- Loans with a maturity of 2 years can be extended to 5 years with the agreement of the lender.
- Payments are deferred until a determination of the amount of forgiveness is made by the SBA.
- Interest will accrue on the loan beginning with disbursement.

PPP Loan Forgiveness Tax Issues

- CARES Act provides that PPP loan forgiveness amount is excluded from gross income.
 - However, the IRS issued ***IRS Notice 2020-32*** stating that pursuant to ***IRC Section 265***, the expenses paid that are allocable to the loan forgiveness are not deductible up to the amount of the loan forgiveness.
- CARES Act (Section 2301) Employee Retention Tax Credit provision is not available if PPP loan is received.
- CARES Act (Section 2302) Employment Taxes Payment Deferral provision was not originally available if PPP loan is forgiven.
 - The PPP Flexibility Act modified this to now allow for the employment tax deferral even if all or a portion of the PPP loan is forgiven.

CARES ACT: Payroll Tax Provisions

Employee Retention Credit for Employers Subject to Closure Due to COVID-19 *(Act Section 2301)*

- FAQ's on IRS website: <https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act>.
- Provides for a **refundable payroll tax credit for 50% of qualified wages** paid by eligible employers to certain employees during the COVID-19 crisis.
 - **Credit limited to employer paid employment taxes.**
 - IRC Section 3111(a) - old-age, survivors, and disability insurance. **FICA (6.2 %)**.
 - IRC Section 3221(a) - Railroad Retirement Act (RRTA) insurance (6.2%).
 - **Does not apply to Medicare portion (1.45%).**

Employee Retention Credit for Employers Subject to Closure Due to COVID-19 *(Act Section 2301)*

- An **Eligible Employer** is any employer, including non-profits, which is carrying on a trade or business **during calendar year 2020**, with respect to any calendar quarter in which:
 - **Operations are fully or partially suspended** during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to the coronavirus disease 2019 (COVID-19); **or**
 - Where there is a **“significant decline in gross receipts.”**

Employee Retention Credit for Employers Subject to Closure Due to COVID-19 *(Act Section 2301)*

- **Significant decline in gross receipts:**
 - **Beginning with the first calendar quarter** beginning after December 31, 2019, for which gross receipts for the calendar quarter are **less than 50%** of **gross receipts** for the same calendar quarter in the prior year; and
 - **Ending with the calendar quarter** following the first calendar quarter beginning after a calendar quarter described above for which gross receipts of such employer is **greater than 80% of gross receipts** for the same calendar quarter in the prior year.

Employee Retention Credit for Employers Subject to Closure Due to COVID-19 *(Act Section 2301)*

- The term **“qualified wages”** includes health benefits and is capped at the first \$10,000 in wages paid by the employer to an eligible employee.
- **Qualified wages:**
 - For employers who had an average number of full-time employees in 2019 of **100 or fewer**, all employee wages are eligible, **regardless of whether the employee is furloughed.**
 - For employers who had **greater than 100** average number of full-time employees in 2019, only the wages of **employees who are furloughed or face reduced hours** as a result of their employers' closure or reduced gross receipts are eligible for the credit.

Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (*Act Section 2301*)

- Limitations.
 - No credit is available with respect to an employee for any period for which the employer is **allowed a Work Opportunity Credit** (Code Section 21) with respect to the employee.
 - **Not available to employers receiving PPP Loans** under Section 1102 of the Act.
- The credit applies to wages paid after March 12, 2020 and before January 1, 2021.
- The IRS is granted **authority to advance payments** to eligible employers and to waive applicable penalties for employers who do not deposit applicable payroll taxes in anticipation of receiving the credit.
 - **New IRS Form 7200.**

... Delay of Payment of Employer Payroll Taxes (Act Section 2302)

- Allows taxpayers to defer paying the **employer portion** of certain payroll taxes through the end of 2020. Notwithstanding any other provision of law, the payment for "**applicable employment taxes**" for the "**payroll tax deferral period**." Won't be due before the "**applicable date**."
- **Applicable employment taxes:**
 - Social Security Taxes - 6.2% (IRC Section 3111(a)).
 - Railroad Retirement Tax Act - RRTA. (IRC Sections 3211(a) and 3221(a)).
 - Self-employment tax. (IRC Section 1401(a)).
 - **Self-employed individuals** can defer paying 50% of the applicable self-employment taxes due on a quarterly basis and that amount will not be subject to the underpayment penalty.
 - **DOES NOT** include the **employer portion of Medicare taxes**.

... Delay of Payment of Employer Payroll Taxes (Act Section 2302)

- **Payroll tax deferral period:**
 - Period beginning on the date of enactment of the Act (March 27, 2020) and ending before January 1, 2021.
- **Applicable date:**
 - **December 31, 2021**, with respect to **50%** of the amounts to which Act Section 2302(a) (employment taxes) and Act Section 2302(b) (self-employment tax), as the case may apply; **and**
 - **December 31, 2022**, with respect to the **remaining 50%** of those amounts.

... Delay of Payment of Employer Payroll Taxes *(Act Section 2302)*

- *What this means:*
 - **Payment for half of these taxes will not be due until the end of 2021, and the other half will not be due until the end of 2022.**
 - Technically, this interest-free loan is accomplished by providing that, notwithstanding IRC Section 6302 (which authorizes IRS to set deadlines for tax deposits), an employer will be treated as having timely made all deposits of applicable employment taxes deferred by the CARES Act if all such deposits are made no later than the applicable date.

Polling Question 2

Depreciation

Expanded Section 179 Deduction

- The TCJA **permanently** increases the maximum amount a taxpayer may expense under **Section 179**.
- **Increased To \$1,040,000.**
- The phase-out threshold amount increased to \$2,590,000 in 2020.
 - If eligible Section 179 asset acquisitions exceed the phase-out threshold, then the maximum Section 179 deduction amount is reduced dollar-for-dollar by the excess over the threshold.
- The \$1,040,000 and \$2,590,000 amounts, as well as the \$25,900 sport utility vehicle limitation, are indexed for inflation.
- **No sunset provision** for the Section 179 deduction.

Expanded Section 179 Deduction

- The TCJA expands the definition of Section 179 property to include certain depreciable ***tangible personal property used predominantly to furnish lodging*** or in connection with furnishing lodging.
 - Applies to residential rental properties, hotels, etc.
 - Furniture, appliances, etc.
- Under the TCJA, ***qualified real property*** eligible for the Section 179 deduction includes any improvement to the **interior portion** of a **nonresidential building** after the building was placed in service.

Expanded Section 179 Deduction

- ***Qualified real property*** does not include any improvement attributable to the following:
 - The enlargement of the building.
 - Any elevator or escalator.
 - The internal structural framework of the building.
- Under the TCJA, the definition ***qualified real property now*** includes:
 - Roofs.
 - HVAC property.
 - Fire protection and alarm systems.
 - Security systems.

Recovery Period for Real Property Shortened

- The cost recovery periods for most real property are 39 years for non-residential real property and 27.5 years for residential rental property.
- ***Cares Act - Qualified Improvement Property (QIP).***
 - Provides a technical correction to the TCJA, and specifically **designates (QIP) as 15-year property** for depreciation purposes.
 - Prior to this correction, QIP fell into the 39-year recovery period for nonresidential rental property.
 - Effective for property placed in service after December 31, 2017.
 - **Consider amending 2018 or/or 2019 tax returns** which could also create an NOL to carryback to prior years. Due by 10-15-21 (*Rev. Proc. 2020-25*).
 - **Can make an accounting method change** in current year to “catch up” depreciation by filing **Form 3115** (*Rev. Proc. 2020-25*).

100% Bonus Depreciation

- **Prior Law** - An additional first-year depreciation deduction was allowed equal to 50% of the adjusted basis of qualified property placed in service before 2020.
- **TCJA** - Allows 100% expensing for qualified property (generally, depreciable assets other than buildings) that are acquired and **placed in service after September 27, 2017** and before 2023 (before 2024 for “longer production period” property and certain aircraft).
 - ***Sunset Provision*** - A 20% per year phase-down of full expensing will apply for property placed in service after 2022 and before 2027 (2023 – 80%, 2024 – 60%, 2025 – 40%, 2026 – 20%).
 - **The provision now applies to purchases of used, as well as new items.**
 - To prevent abuses, the first-year bonus depreciation deduction applies only to property purchased in an arm’s-length transaction.

Section 179 Deduction & 100% Bonus Depreciation Cautions

- Claiming the Section 179 deduction or the 100% bonus depreciation on **real property** has a **downside**.
 - If the property is later sold for a taxable gain, the gain up to the amount of the Section 179 deduction and/or the bonus depreciation will be treated as depreciation recapture that is taxed at higher ordinary income tax rates (up to 37% plus another 3.8% NIIT, if applicable) .
 - However, if the real property is depreciated under the normal 39- year (commercial) or 27.5-year (residential) periods, then the maximum Federal tax rate attributable to the cumulative depreciation claimed is only 25% (plus the 3.8% NIIT, if applicable).
- Claiming the Section 179 deduction or the 100% bonus depreciation has a **downside** on the **20% QBI Deduction** as well.
 - Since QBI and taxable income is reduced from these accelerated deductions, the 20% QBI Deduction is also reduced.
- **Anticipated future tax rate increases** may also warrant electing out of these accelerated depreciation deductions.

Polling Question 3

Other Business Changes

Net Operating Loss Changes

- **Prior Law** - Generally, with some exceptions, a net operating loss (NOL) could be carried back 2 years and carried over 20 years to offset taxable income in such years.
- **TCJA** - For NOLs arising in tax years ended after December 31, 2017:
 - The 2-year carryback and the special carryback provisions are repealed (except for farming losses and losses of property and casualty insurance companies).
 - For losses arising in tax years beginning after December 31, 2017, the NOL deduction is limited to 80% of taxable income (determined without regard to the deduction).
 - Carryovers to other years are adjusted to take account of this limitation and NOLs can be carried forward indefinitely.
- **CARES Act**
 - **Temporarily removes the 80% taxable income limitation** to allow an NOL to fully offset income.
 - For tax years beginning before 2021, taxpayers can take an NOL deduction equal to 100% of taxable income.
 - For tax years beginning after 2021, taxpayers will be able to take a 100% deduction for NOLs arising in years before 2018 and the 80% taxable income deduction limitation will apply to NOLs arising in tax years after 2017.
 - Provides that NOLs arising in a tax year beginning after December 31, 2018 and before January 1, 2021, can be carried back to each of the five tax years preceding the tax year of such loss.
 - Because of higher tax rates in pre-2018 years, the NOL carryback could be more beneficial than a carryover.

Net Operating Loss Changes

- **CARES Act – When to Make Election to Forgo the Net Operating Loss Carryback Period.**
 - **For an NOL incurred in the 2020 tax year**, by the due date (including extensions) for filing the taxpayer's Federal income tax return for the 2020 tax year.
 - **For an NOL arising in tax years beginning in 2018 or 2019**, by the due date (including extensions) for filing the taxpayer's Federal income tax return for the first tax year ending after March 27, 2020.
 - Therefore, for calendar year taxpayers, the due date could be up to September 15, 2021 for corporations and October 15, 2021 for individuals (assuming an extension was filed).

Excess Business Losses Limitation

- **The TCJA**
 - Provided for rules relating to an “excess business loss” for **tax years beginning after December 31, 2017 and before January 1, 2026.**
 - Provided for a disallowance of “excess business loss” for noncorporate (non-C corporation) taxpayers.
 - Loss limit: \$250,000 single; \$500,000 married joint (adjusted for inflation).
- **CARES Act**
 - Temporarily suspends the loss limitation for noncorporate taxpayers so they can deduct excess business **losses arising in 2018, 2019, and 2020.**
 - Filing an amended return should be considered especially if the increased loss creates an NOL which can be carried back to prior years.

Limitation on Interest Deductions for Businesses

- **Prior Law** - Businesses were allowed to deduct 100 percent of their business interest expense.
- **TCJA** - Interest deductions for businesses with average annual gross receipts over \$26 million for the 3 prior years generally are limited to 30% of the corporation's adjusted taxable income.
 - **Adjusted Taxable Income:** Defined as the taxpayer's taxable income, computed without regard to:
 - Any item of income, gain, deduction or loss that is not properly allocable to a trade or business;
 - Any business interest expense or business interest income;
 - The amount of any net operating loss (NOL) deduction under Code Section 172;
 - The amount of any QBI deduction allowed under Code Section 199A; and
 - For tax years beginning before January 1, 2022, any deduction allowable for depreciation, amortization or depletion.
 - Disallowed interest can be carried forward indefinitely.
 - Special reporting rules apply to partnerships and S corporations.
 - **No sunset provision.**

Limitation on Interest Deductions for Businesses

- **CARES Act Changes.**
 - Temporarily and retroactively increases the taxable income limitation from 30% to 50% for tax years beginning in 2019 and 2020.
 - Amending a 2019 return to reflect an increased interest deduction could result in an NOL in 2019 that could be carried back to prior years.

Tax Shelter Status

- **For entities that pass their losses through to their owners** this can create a major tax hurdle.
- Under the cash method of accounting rules, a tax shelter includes a syndicate.
 - **A syndicate is an entity (other than a C corporation) that allocates more than 35% of its losses during the tax year to limited partners or limited entrepreneurs.**
 - *A limited entrepreneur* is one who has an interest in an enterprise other than as a limited partner and doesn't actively participate in the management of the enterprise.
- **Therefore if the entity allocates more than 35% of its losses in 2020 to owners who don't actively participate in the management of the business (like a passive investor), it will be considered a tax shelter by the IRS.**
- It doesn't mean your business is engaging in tax avoidance activities.
 - It simply means that your business isn't eligible to take advantage of certain small business tax provisions such as the cash basis method of accounting.

Tax Shelter Status

- **Planning Around Tax Shelter Status.**
 - Fortunately, there are a few ways to avoid tax shelter status.
 - **First, if your entity has passive investors, consider granting them some say in the management of the business.**
 - For example, **the investors could serve on the entity's board of managers.** Another option would be to grant the investors voting rights with respect to significant management decisions.
 - **Second, you could amend your LLC's operating agreement to prevent the allocation of losses to passive investors.** You and the other members could agree to allocate tax losses only to owners who actively manage the business. Then, any future income could be first allocated to those owners up to the amount of previously allocated losses.
 - **Finally, the IRS recently released some proposed regulations that allow entities to elect to determine tax shelter status by looking at whether they allocated more than 35% of their losses to limited owners in the prior year.** This allows the entity to know early in the year whether it's a tax shelter. If your business is unable to escape tax shelter classification, we would want to at least postpone that classification for one year by pursuing this election.

... Qualified Disaster Relief Payments Under IRC Section 139

- Any amount received by an individual as a [Section 139](#) **qualified disaster relief payment** is excluded from gross income.
- In the context of the *qualified disaster* that is the COVID-19 crisis, a [Section 139](#) payment is any amount paid to or for the benefit of an individual:
 - To reimburse or pay **reasonable and necessary personal, family, living, or funeral expenses** incurred as a result of the COVID-19 crisis;
 - To reimburse or pay reasonable and necessary expenses incurred for the **repair or rehabilitation of a personal residence, or the repair or replacement of its contents**, to the extent the need for the repair, rehabilitation, or replacement is attributable to the COVID-19 crisis; or
 - By a Federal, state, or local government, or agency or instrumentality thereof, in connection with the COVID-19 crisis to promote the general welfare.

... Qualified Disaster Relief Payments Under IRC Section 139

COVID-19 is a Qualified Disaster.

- The term *qualified disaster* to include the following:
 - Any Federally declared disaster, as specified by [IRC Sec. 165\(i\)\(5\)\(A\)](#). On March 13, 2020, President Trump declared the COVID-19 crisis a national emergency, effective as of March 1, 2020.
 - With respect to assistance payments by a Federal, state, or local government (or agency or instrumentality thereof) to promote the general welfare, a disaster that is determined by an applicable Federal, state, or local authority to warrant such assistance.
 - Any other event that is determined by the IRS to be of a catastrophic nature.

Limitations.

- [Section 139](#) payments don't include payments for **expenses that are compensated by insurance** or otherwise.
- Also, **no Federal income tax deduction or credit is allowed** to the person for whose benefit a tax-free [Section 139](#) payment is made, for an expenditure covered by such payment.

Presumably, tax-free [Section 139](#) payments don't include payments by a governmental agency **for income replacement, such as state unemployment compensation benefits**, because those would be considered payments covered by insurance.

... Qualified Disaster Relief Payments Under IRC Section 139

Can Payments to Employees during the COVID-19 Crisis Qualify as Section 139 Payments?

- Yes, according to the logic espoused in Rev. Rul. 2003-12.
 - In Rev. Rul. 2003-12, the IRS concluded that payments under an employer's program to pay or **reimburse employees for reasonable and necessary unreimbursed medical, temporary housing, or transportation expenses incurred as a result of a flood** met the definition of *tax-free Section 139 payments*.
 - The same logic should apply in the context of the COVID-19 pandemic.
- **For payments to an employee to be tax-free Section 139 payments, they must be for:**
 - The reimbursement or payment of the employee's reasonable and necessary personal, family, living, or funeral expenses incurred as a result of the COVID-19 crisis, or
 - For the repair or rehabilitation of a personal residence (or the repair or replacement of its contents).

... Qualified Disaster Relief Payments Under IRC Section 139

- **Examples of eligible costs include:**
 - Helping to pay utilities or rent;
 - Paying the extra costs for grocery delivery (but not the cost of groceries);
 - Paying for increased commuting expenses (to avoid mass transit);
 - Paying for temporary housing so an employee diagnosed with COVID-19 doesn't infect others;
 - Paying for medical expenses that aren't covered by insurance, over-the-counter medications, and certain medical supplies (including hand sanitizer); and
 - Additional childcare expenses, tutoring expenses, or homeschooling expenses.
- **Limitations**
 - Payments intended to simply replace the employee's income don't qualify.
 - payments to employees for expenses covered by insurance don't qualify.
 - Any nonqualified payments are treated as taxable employee compensation unless some other tax-law provision dictates otherwise.
- **Tax Planning Point:** Employers that want to make tax-free [Section 139](#) payments to employees should consider adopting a written plan outlining when an employee is eligible for the payments and limiting them to reasonable and necessary unreimbursed expenses incurred as a result of the COVID-19 crisis.

Polling Question 4

Meals & Entertainment Expenses

Meals and Entertainment Expenses

- **Prior Law** - Taxpayers could generally deduct 50% of business-related meal and entertainment expenses incurred before January 1, 2018.
 - Taxpayer had to establish that the expenses were directly related to or associated with the business.
- **TCJA - No deduction** will be allowed for expenses of a trade or business related to entertainment, amusement or recreation activities or for membership dues to any club organized for business, pleasure, recreation or other social purposes.
 - Some examples include:
 - Tickets to sporting events.
 - Private boxes or license fees for seating rights at sporting events.
 - Theater tickets.
 - Golf club dues.
 - Golf, hunting, fishing, sailing outings, etc. for customers.
 - Effective for amounts paid or incurred after December 31, 2017.

Meals and Entertainment Expenses

Final Regulations (*TD 9925*)

- The TCJA largely eliminated the deduction for entertainment expenses but left intact certain exceptions.
- Notable changes were made to food and beverage expenses as well.
- The final regulations confirm that 50% deductions for business meals generally remain.
- The final regulations largely follow the proposed regulations issued in February 2020 and *IRS Notice 2018-76*.
- Effective for taxable years that begin on or after October 9, 2020.

Meals and Entertainment Expenses

Entertainment: Listed below are the exceptions to entertainment disallowance: 100% deductible.

- On site food and beverages for employees, including expenses for related facilities.
- Expenses treated as compensation.
- Reimbursed expenses under an accountable plan.
- Expenses for recreational, social, or similar activities primarily for the benefit of employees.
- Expenses directly related to business meetings of employees, stockholders, agents or directors.
- Expenses related to attending business league or chamber meetings.
- Items made available to the general public.
- Entertainment sold to customers.
- Expenses includable in the income of persons who are not employees of the employer.

Meals and Entertainment Expenses

Meals

- The Regs generally limit a deduction for business-related food and beverage expense to 50% of the expenditure. **Taxpayers may deduct 50% of business food and beverages if:**
 - The expense is **ordinary and necessary** under IRC Section 162;
 - The expense is **not lavish or extravagant** under the circumstances;
 - The **taxpayer, or an employee** of the taxpayer, **is present**;
 - The **food or beverage is provided to the taxpayer or a business associate**; which includes clients and employees; and
 - **Food and beverages** are purchased separately or **separately stated** on a receipt if provided **during an entertainment activity**.
- To be an otherwise allowable business meal expense:
 - Business must be conducted immediately before, during, or immediately after the event; and
 - The normal substantiation requirements must be met.

Meals and Entertainment Expenses

Meals

- The Regs provide that the following exceptions under allow for a **full deduction of business-related food and beverages**:
 - Expenses treated as compensation.
 - Reimbursed food or beverage expenses.
 - Expenses for recreational, social, or similar activities primarily for the benefit of employees.
 - Items made available to the general public.
 - Goods or services sold to customers.
 - Expenses includable in the income of persons who are not employees of the taxpayer.

Meals and Entertainment Expenses

De minimis Meals.

- **Prior Law** – Employer could deduct 100% of meal expenses that were excluded from the recipient employee's income as a *de minimis* fringe benefit. Examples include:
 - Meals or meal money provided to employees on an occasional basis.
 - Meals or meal money provided to employees working overtime.
- **TCJA** – De minimis meals are no longer 100% deductible.
 - The new law **still allows a 50% deduction** for de minimis meals.

Meals and Entertainment Expenses

Convenience of Employer Meals and Lodging

- **Prior Law** – Employer could deduct 100% of meal or lodging expenses provided to an employee (including his or her spouse and dependents) for the convenience of the employer and such expenses were excluded from employee's income if the following requirements were met:
 - ***Business Premises.*** The meals or lodging must be furnished on the employer's business premises.
 - ***Convenience of the Employer.*** The meals or lodging must be furnished for the convenience of the employer.
 - ***Condition of Employment.*** In the case of lodging (but not meals), the employee must be required to accept such lodging as a condition of employment.
- **TCJA** – Convenience of employer meals are **now only 50% deductible**.
 - After 2025, no deductions for such meals will be allowable.

Meals and Entertainment Expenses

Employer-Operated Eating Facility

- **Prior Law** – Employer could deduct 100% of the cost (including facility costs) of providing meals to employees at a qualifying employer-operated eating facility (i.e., company cafeteria). To qualify, the facility had to meet the following requirements:
 - Be owned or leased by the employer.
 - Be operated by the employer (can be through a vendor).
 - Be on or near the employer's business premises.
 - Revenue from the facility must equal or exceed the cost of operating the facility.
 - Meals are served during or immediately before or after working hours.
 - The facility is generally available to all employees.
- **TCJA** – Employer-operated eating facility costs are **now only 50% deductible**.
 - After 2025, no deductions for such costs will be allowable.

Meals and Entertainment Expenses

Employee Events

- **Prior Law** – Employer could deduct 100% of food, beverages and entertainment expenses incurred for recreational, social, or similar activities primarily for the benefit of employees. Examples include:
 - Company holiday parties or picnics.
- **TCJA** – Same as prior law - **100% deductible**.
 - Covers applicable entertainment expenses as well.

Meals and Entertainment Expenses

General Public Events

- **Prior Law** – Employer could deduct 100% of food, beverages and entertainment expenses made available to the general public. Examples include:
 - Free snacks at a business showroom.
 - Free food and entertainment at an event open to the public.
- **TCJA** – Same as prior law - **100% deductible**.
 - Covers applicable entertainment expenses as well.

Meals and Entertainment Expenses

Compensation Meals.

- **Prior Law** – Employer could deduct 100% of meal and entertainment expenses that were reported as taxable compensation to recipient employees.
- **TCJA** – Same as prior law - **100% deductible**.
 - Still applies to entertainment expenses as well.

Meals and Entertainment Expenses

Nonemployee Recipients.

- **Prior Law** – Taxpayers could deduct 100% of meals and entertainment expenses that were reported to a nonemployee recipient on a Form 1099. Example includes:
 - Customer or independent contractor wins a trip or entertainment package at a sales event.
- **TCJA** – Same as prior law - **100% deductible**.
 - Covers applicable entertainment expenses as well.

Meals and Entertainment Expenses

Sold to Customers.

- **Prior Law** – Taxpayers could deduct 100% of food, beverages and entertainment expenses sold to customers at full value.
- **TCJA** – Same as prior law - **100% deductible**.
 - Covers applicable entertainment expenses as well.

Meals and Entertainment Expenses

Fundraising Charitable Sporting Events.

- **Prior Law** – Taxpayers could deduct 100% of the cost of tickets to fundraising charitable sporting events if all of the following requirements were met:
 - The event was organized for the benefit of a qualifying charitable organization.
 - 100% of the net proceeds were contributed to the charity.
 - Volunteers did substantially all the work in staging the event.
- **TCJA** – Such expenses are **no longer deductible**.





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