



Lally & Co.

CPAs and Business Advisors

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The Evergreen. Always Growing.

Like the evergreen oak tree, Lally & Co. is always growing. With the support and loyalty of our clients and friends we have grown into a firm of 42 individuals serving clients in many diverse fields. Our growth gives us the ability to better serve our clients and provide effective solutions to their needs. If you have questions about your business or personal tax situation, please contact us. We welcome your call and are always looking for ways to better serve you.

Contact our office or visit our new website for more information.

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Dear Clients and Friends,

We trust that you are enjoying your summer. We understand that tax and accounting concerns might be the farthest thing from your mind. It is our goal to keep you up to date with timely and informative news happening in our world.

As you read through *The Evergreen*, please do not hesitate to contact us if you have questions regarding an article or regarding your business or personal tax situation. We would be happy to hear from you! This and past issues of *The Evergreen* are available on our website at <http://lallycpas.com/newsletters/>.

Okay, So When Can We Expect Tax Reform?

We have been promised reduced tax rates and a “simplified” tax code for many, many years. What’s the hold up? That’s not a simple question to answer. In fact, as complicated as the tax code is, purportedly some 70,000 pages long, congressional rules are no slouches.

The first question might be, why not pass tax reform within the annual budget approval process? Well, first a budget needs to pass in both the Senate and House and by simple majority in each. Then, the two bills go through a budget reconciliation process. As you would guess, rarely will opposing party lines vote together and, in today’s world, you cannot even count all party members as being on the same

side. In reality, passing a budget is no easy task and then linking tax reform to it is too heavy a weight to carry. So, you first pass a budget and then head to “reconciliation”.

The rules of reconciliation, in many ways, works against making significant changes to the tax code. One rule states that any changes made through the reconciliation process cannot increase a passed budget’s deficit in the ensuing 10 years, i.e. the reconciliation changes need to be revenue and expense neutral.

Who makes that assessment? Enter: the Joint Committee on Taxation and the Congressional Budget Office. By definition, these groups are to be nonpartisan and, among other things, are tasked with assessing

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the impact of reconciliation changes over the 10-year window. If the tax rates are dropped too much, the deficits would grow and the tax reform being considered would need to be re-worked again and again until a neutral effect is achieved.

You might ask “How does the JCT and CBO make that determination?” The answer is based on many assumptions and this is where the proverbial *devil is in the details*. The impact is measured over a 10-year period, but why 10 years? What would happen if they considered a 15- or 20-year period, would the outcome be different? Probably. But how accurate are 10-year projections let alone 15- and 20-year projections? Not very.

“What assumptions are being used for the US economy?” For the past two presidential administrations, growth has been an anemic 2.1%. Is that reasonable going forward? What would be the outcome if JCT and CBO used 3.0%? If you increase the growth of the US economy, you would have a commensurate growth in tax revenues that would support a greater tax rate reduction today.

Which brings us to how temporary tax breaks are treated by JCT and CBO. Are they assumed to expire as written or do they assume they will be reauthorized? If assumed they

would expire, it would make room for more permanent tax cuts now. But in reality, they are usually reauthorized in a subsequent budget or reconciliation so shouldn't they be treated as more permanent than temporary?

Next, they need to decide what deductions stay and which ones go. A frequent bone of contention is the deductibility of state and local taxes on Schedule A (Itemized Deduction) of an individual's tax return. States, such as New York and California, have high real estate and income taxes and strongly support keeping this deduction. States like Texas and Florida that have no income taxes see less value in this deduction. Can you see red state vs. blue states on this one?

The process is long and it is complicated; a mere newsletter article does no justice to the work, analysis, lobbying, and horse trading that needs to be done to make tax reform happen. So, when you hear someone propose a 15% corporate tax rate or a cut in deductions, remember that talk is cheap and politics is a contact sport. The general consensus is that a tax cut will spur the economy and get everyone's attention. However, rarely can you get more than half of 535 individuals in Washington DC to agree on anything.

Debate Over Health Care and Taxes Moves to Senate

The future of the Affordable Care Act and its associated taxes has moved to the Senate following passage of the American Health Care Act (AHCA) in the House in April. Traditionally, legislation moves more slowly in the Senate than in the House, which means that any ACA repeal and replacement bill may be weeks if not months away.

At the time this article was prepared, few details have emerged about discussions in the Senate on the ACA's taxes. Some senators have predicted that the Senate will write its own ACA repeal and replacement bill. A Congressional Budget Office (CBO) report, issued in late May, scored the House-passed AHCA as eventually causing 23 million fewer individuals to be covered, a number that may prompt the Senate to move further away from the House bill. It is also unclear if a Senate bill would repeal all or some of the ACA's taxes. A Senate bill could also make other changes to the ACA, such as changes to the individual and employer shared responsibility requirements and the Code Sec. 36B premium assistance tax credit.

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Firm Announcements

Zachary S. Bussard, CPA joined the firm as a Senior Associate in our A&A Department in August 2017

Zachary E. Miles, CPA has been promoted within the firm's Tax Department to Supervisor

Kari M. Miller became a first-time mother to baby boy, Derrick James Miller, born August 12, 2017

Susan Sciacca joined the firm as an Administrative Assistant in our A&A Department in June 2017

Michael J. Teitel joined the firm as an Associate in our A&A Department in September 2017

Important Dates

October 2, 2017 – Extended 2016 Trust Tax Returns Due

October 16, 2017 – Extended 2016 Individual and C-Corp Tax Returns Due

Health care taxes

As approved by the House, the AHCA repeals nearly all of the ACA's taxes and delays the ones it does not repeal immediately. The House-passed version of the AHCA repeals the net investment income (NII) tax, the excise tax on medical devices, and the health insurance provider fee, among others, retroactively to the start of 2017. Further, the House-passed version of the AHCA delays the ACA's excise tax on high-dollar health plans.

Whether the Senate will go along with repealing all or some of the ACA's taxes is unclear. Some GOP members of the Senate Finance Committee had previously called for immediate repeal of the additional Medicare tax. Other Republican senators called for immediate repeal of the medical device excise tax.

Code Sec. 36B credit

Individuals who obtain health insurance through the ACA Marketplace may qualify for a tax credit to help offset the cost of coverage. The House-passed version of the AHCA also revises the Code Sec. 36B premium assistance tax credit. The amount of the credit would vary depending on the taxpayer's age, among other modifications. Again, it is unclear if the Senate will adopt

these changes to the credit or make its own revisions.

Other provisions

An ACA repeal and replacement bill in the Senate also is expected to address, among other things:

- Individual and employer shared responsibility requirements;
- Health savings accounts;
- Code Sec. 45R small employer health insurance credit;
- Branded prescription drug fee;
- Medical expense deduction;
- Minimum essential health benefits; and
- Other health care bills.

Just before Congress' Memorial Day recess, the House Ways and Means Committee approved several bills related to the House version of the AHCA. One bill would allow individuals with certain types of COBRA coverage to claim the revised Code Sec. 36B credit. Another bill would disallow advance payments of the credit unless the recipient is a citizen or national or an alien lawfully present in the U.S.

Administrative actions

The U.S. Department of Health and Human Services (HHS), the

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Department of Labor (DOL) and the IRS administer different parts of the ACA. In May, HHS announced changes to the direct enrollment process for the ACA Marketplace. HHS announced that online enrollment for the Small Business Health Options Program (SHOP) would be through an agent or broker.

Business Meals and Entertainment: How to Maximize Tax Deductions

Many businesses consider the occasional wining and dining of customers and clients just to stay in touch with them to be a necessary cost of doing business. The same goes for taking business associates or even employees out to lunch once in a while after an especially tough assignment has been completed successfully. It's easy to think of these costs as deductible business expenses, but they may not be. As a general rule, meals and entertainment are deductible as business expenses only if specific conditions are met. The deduction for either type of expense is generally limited to 50 percent of the cost.

Meals and entertainment directly connected to business

To be considered directly connected to business, the meal or entertainment event must meet three conditions:

1. It must have been scheduled with more than a general expectation of deriving future income or a specific business benefit from the event. In other words, a meal or dinner date arranged for general goodwill purposes does not qualify.
2. A business meeting, negotiation, or transaction must actually occur during the meal or entertainment, or immediately preceding and following it. In other words, business actually must be discussed.
3. The main character of the event, considering the facts and circumstances, is the active conduct of your company's trade or business. For example, an executive employee who treats a client to a golf game in order to discuss the general parameters of a business deal in an informal atmosphere is engaged in entertainment that is directly connected to business. So is a manager who discusses sensitive business plans with a subordinate over lunch at an off-premises restaurant.

Applicable limitations

In general, only 50 percent of expenses incurred for entertainment and meal expenses is deductible. A

limited exception applies to entertainment or on-premise meals provided to employees.

Expenses with respect to entertainment facilities generally are not deductible at all. A facility includes any item of personal or real property owned, rented, or used by a taxpayer if it is used during the tax year for or in connection with entertainment. They include yachts, hunting lodges, fishing camps, swimming pools, tennis courts, bowling alleys, automobiles, airplanes, apartments, hotel suites and homes in vacation resorts.

Country club dues are not deductible (although the meals purchased with business clients at the club are, up to the 50 percent limit). Deductions for skyboxes or other private luxury boxes at sporting events are limited to the face value of a nonluxury box seat ticket multiplied by the number of seats in the box.

Fully deductible meals and entertainment expenses

There are certain situations in which 100 percent of meals and entertainment can be written off. If the expenses in question are provided for the benefit of your employees, 100 percent of the costs may be expensed accordingly. Some common examples of expenses that can

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be written off at 100 percent are as follows:

- Meals and entertainment expenses for company picnics or holiday parties;
- Free coffee, bottled water, soft drinks, and donuts provided to employees at the place of business;
- Free food or beverages provided to the public for promotional purposes;
- Meals provided at the place of business to more than half of the employees as an enticement for working after-hours, weekends, or holidays; and
- The cost of meals that are included on employee W-2 forms as taxable compensation.

Record-keeping requirements

Even if a meal or entertainment expense qualifies as a business expense, none of the cost is deductible unless strict and detailed substantiation and recordkeeping requirements are met to the letter.

What are Passive Losses?

Individuals, trusts, estates, personal service corporations and closely held C-corps may only deduct passive activities losses from passive activity income. The rules do not apply to S corporations and partnerships but do apply to

their respective shareholders and partners. In general, limited partners are not deemed to materially participate in partnership activities. Thus, a limited partner's share of partnership income is passive income. However, general partners or acting general partners may hold limited partnership interests and materially participate in the partnership.

Closely held C corporations and personal service corporations are treated as materially participating in an activity if shareholders owning 50 percent or more by value of the outstanding stock materially participate in the activity. Closely held C corporations can also satisfy the material participation standard under an alternative rule based on the participation of full-time employees in the activity.

A passive activity is trade or business activity in which the taxpayer does not materially participate. A passive activity is any activity that involves the conduct of a trade or business in which the taxpayer does not materially participate. Passive activities generally include rental activities, regardless of whether the taxpayer materially participates in the activity. A taxpayer's rental real estate activity is not a passive activity, however, if the taxpayer (1) materially participates in the activity, and (2) performs

qualifying services in real property trades or businesses. A facts and circumstances test applies in determining whether other activities are combined or treated as separate for purposes of the passive loss rules.

Individuals who own and actively participate in the management of rental real estate may offset up to \$25,000 of passive activity loss from rental real estate against active income in any tax year. The offset amount is reduced by 50 percent of the amount by which the taxpayer's adjusted gross income exceeds \$100,000, phasing out completely at \$150,000 of adjusted gross income. More liberal rules apply to the offset of rehabilitation and low-income housing credits.

Deductions and credits that are disallowed under passive activity rules may be carried forward and used as passive activity deductions and credits in succeeding years. Remaining passive activity deductions are deductible against nonpassive income when taxpayer disposes of the passive activity. Passive activity credits may only be applied to taxes on passive income.

A major exception to the definition of a passive activity is a working interest in any oil and gas property that the

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taxpayer holds directly or through an entity that does not limit the taxpayer's liability for the interest, regardless of whether the taxpayer materially participates in the activity.

A taxpayer's passive activity loss for the tax year is disallowed and is carried forward until the taxpayer has available passive activity income. Passive activity loss is the amount by which passive activity deductions from all passive activities exceed passive activity gross income from all passive activities for the tax year.

Lawmakers Continue Tax Reform Debate and Discussions

Lawmakers from both parties spent much of June debating and discussing tax reform, but without giving many details of what a comprehensive tax reform package could look like before year-end. At the same time, several bipartisan tax bills have been introduced in Congress, which could see their way to passage.

Tax reform

House Speaker Paul Ryan, R-Wisc., predicted that tax reform would be accomplished in 2017. "Transformational tax reform can be done, and we are moving forward," Ryan said in June.

We need to get this done in 2017. We cannot let this once-in-a-generation moment slip by." Last year, House Republicans unveiled their "Better Way Blueprint," which sets for principles for tax reform, including lower individual tax rates, a reduced corporate tax rate, and a border adjustment tax, among other measures.

"Republicans have been afraid to expose their Blueprint to scrutiny," Rep. Lloyd Doggett, D-Texas, a senior member of the House Ways and Means Committee, said. "The Republican Blueprint is both the wrong way for tax policy and the wrong way to legislate tax reform," Doggett said.

In the Senate, the chair of the Senate Finance Committee (SFC), Orrin Hatch, R-Utah, asked stakeholders for input on tax reform. Hatch requested recommendations on individual, business and international tax reform. "After years of committee hearings, public statements, working groups, and conceptual exercises, Congress is poised to make significant steps toward comprehensive tax reform," Hatch said. "As we work to achieve those goals, it is essential that Congress has the best possible advice and insight from experts and stakeholders," he added.

Sen. Ron Wyden, D-Oregon, is ranking member of the SFC and

urged lawmakers to take a bipartisan approach to tax reform. "The only way to pass lasting, job-creating tax reform that's more than an economic sugar-high is for it to be bipartisan," Wyden said. "Tax reform takes a lot of careful consideration to write a bipartisan tax reform bill, and I know because I've written two of them."

Small business

The Senate Small Business Committee explored tax reform at a hearing in June. "Tax compliance costs are 67 percent higher for small businesses," Committee Chair James Risch, R-Idaho, said. Ranking member Jeanne Shaheen, D-N.H., said that "small businesses spend 2.5-billion hours complying with IRS rules."

Mark Mazur, former Treasury assistant secretary for tax policy, was one of the experts who testified before the committee. Mazur said that small businesses generally have a larger per-unit cost of tax compliance than larger businesses. "One particular area that adds to the complexity of complying with the tax code is accrual accounting," he said.

Other tax legislation

In June, the House passed HR

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1551, a bipartisan bill. The legislation generally modifies the tax credit for advanced nuclear power facilities. Several bipartisan stand-alone tax bills have been introduced in Congress recently, including:

- The Invent and Manufacture in America Bill, a bipartisan bill that would enhance the research tax credit. Generally, the bill would increase the value of the credit by up to 25 percent for qualified research activities.

- The Graduate Student Savings Bill, introduced by a group of Senate Democrats and Republicans. The bill would generally allow funds from a graduate student's stipend or fellowship to be deposited into an individual retirement account (IRA).
- The Adoption Tax Credit Refundability Act is another bipartisan bill. The measure generally would enhance the adoption tax credit.

- Another bipartisan proposal would treat bicycle sharing systems as mass transit facilities for purposes of qualified transportation fringe benefits.

Additionally, a group of House Democrats and Republicans wrote to Treasury Secretary Mnuchin in June. The bipartisan group asked him to preserve the state & local sales tax deduction in any tax reform plan.



On Tuesday, September 19th, the employees of Lally & Co. were treated to an afternoon at The Pittsburgh Glass Center located at 5472 Penn Avenue in Pittsburgh. While there, they were shown a demonstration on the glass-blowing process, followed by one-on-one assistance in creating the impressive works of art that you see to the left. Fun was had by all who attended and we look forward to our next firm outing... anyone up for skydiving?

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