Lally&Co.

CPAs and Business Advisors

The Evergreen

Quarterly Journal for Clients & Friends

Fall 2018 – Volume XXVIII

This Issue:

- **Lally & Co. to Roll Out New and Secure Tax Delivery System**
- **New IRS Guidance on Deductibility of Meals**
- **IRS Releases Guidance for Section 199A Pass-Through Deduction**
- **AICPA: Immediate Guidance Needed on S Corporation Issues**
- **Standard Mileage Rates Increase, While Higher Depreciation Limits Kick In**
- **Can I Still Convert Regular IRAs Into Roth IRAs?**

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 43 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 website for more information.

412.367.8190

Dear Clients and Friends,

We trust that you are enjoying the autumn season thus far. 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/.

Lally & Co. to Roll Out New and Secure Tax Delivery System

Lally & Co. will be rolling out an entirely new and secure tax delivery system this upcoming tax-season.

The new system will be used for most tax returns and will present you with a customer friendly dashboard containing links to your return, our transmittal letter, your e-file authorizations, your payment vouchers for the current year's returns, and your estimate tax coupons and addresses for the upcoming year. With the ease of a mouse click or two, you can review each of the documents, electronically sign your returns/authorizations, print your coupons, and safely save everything to your local hard drive or your cloud storage.

Security features include the latest encryption software, dual authentication, and, when required, individualized knowledge-based authentication (KBA) questions to validate each signer. We believe this new delivery system will enhance our client's experience and allow for quicker and more efficient delivery and receipt of tax returns.

A more detailed description of the new delivery system will be contained in our December 2018 mailing of tax organizers. Similarly, our Winter 2018 – Volume XXIX edition of The Evergreen Newsletter will have an article focused on this system and will be in your email inbox in early January 2019. We look forward to sharing this new system with you and believe it will greatly benefit you, our

(Continued on Page 2)

clients, in being more secure and efficient, as well as assisting us in better serving you.

New IRS Guidance on Deductibility of Meals

On Wednesday, October 3, 2018, the IRS issued guidance clarifying that taxpayers may, in general, continue to deduct 50% of the food and beverage expenses which are related to the operation of their trade or business. This guidance has been issued despite the changes to the meal and entertainment expense deduction under Sec. 274, which was made by the Tax Cuts and Jobs Act (TCJA), P.L. 115-97 (Notice 2018-76). According to the IRS, the amendments specifically deny deductions for expenses for entertainment, amusement, or recreation, but do not expressly address the deductibility of expenses for business meals, which has caused a lot of uncertainty and confusion within the business community. With this interim guidance, the IRS seeks to address this issue temporarily until proposed regulations which clarify the deductibility of meals are formally issued by the IRS.

Under Sec. 274(k), which was not amended by the Tax Cuts and Jobs Act, a deduction for the expense of any food or beverages is not allowed unless (1) the expense is not lavish or extravagant under the circumstances, and (2) the taxpayer (or an employee of the taxpayer) is present when the food or beverages are furnished. Under Sec. 274(n)(1), which was amended by the Tax Cuts and Jobs Act, generally speaking, the amount allowable as a deduction for any food or beverage expense cannot exceed 50% of the amount of the expense that would otherwise be allowable.

Under the IRS' interim guidance, taxpayers are allowed to deduct 50% of an otherwise allowable business meal expense if all of the following rules are met:

- The expense is an ordinary and necessary business expense under Sec. 162(a) paid or incurred during the tax year when carrying on any trade or business;
- The expense is not lavish or extravagant under the circumstances;
- The taxpayer, or an employee of the taxpayer, is present when the food or beverages are furnished;
- The food and beverages are provided to a current or potential business customer, client, consultant, or similar business contact; and
- For food and beverages provided during or at an entertainment activity, they are purchased separately from the entertainment, or the cost of the food and beverages is stated separately from the cost of the entertainment on one or more bills, invoices, or receipts.

It should be noted, as well, that the IRS will not allow the entertainment disallowance rule to be circumvented through inflating the amount charged for food and beverages.

In the notice, the IRS has given three examples as to how they intend to interpret these rules. All three examples are similar, in that they involve attendance of a sporting event with a business client and having food and drink while attending the game. The examples follow the AICPA's recommendation in a letter to the IRS, dated April 2, 2018, that the IRS provide immediate guidance on the change to Sec. 274. In that letter, the AICPA recommended that the IRS confirm that business meals (1) that take place between a business owner or employee and a current or prospective client; (2) that are not lavish or extravagant under the circumstances; and (3) where the taxpayer has a reasonable expectation of deriving income or other specific trade or business benefit from the encounter are deductible.

The IRS is currently requesting that comments on the notice be

(Continued on Page 3)

Firm Promotions & Other News:

John M. Lally, CPA, MBA, CVA has been invited to serve on the Board of Directors of Saint Vincent College in Latrobe, PA, his alma mater.

Todd A. Sacco, JD, CPA/PFS, ABV has been admitted as a Partner in the Firm and will continue to practice in the Tax and Business Valuation area.

Gina A. DeIuliis, CPA has been promoted to Manager in the Tax Department.

Janet L. Nauer, CPA has been promoted to Manager in the Tax Department.

Allen W. Wassel, CPA joined the Firm's Tax Department in September as a Tax Manager

Lisa M. Wiegand, CPA has been promoted to Supervisor in the Tax Department.

Thomas S. Lutz has been promoted to Senior Accountant in the Tax Department.

Patrick Boyer joined the Firm's Tax Department in September as a Tax Associate

Yaonan Zhao, MSA joined the Firm's A&A Department in August as A&A Associate

---

Important Dates

October 15, 2018 – Extended 2017 Individual and C-Corp Tax Returns Due

December 15, 2018 – 2018 4th Quarter Estimated Tax Payments for C Corp's Due

---

received by December 2, 2018 and plans to issue proposed regulations in the coming months. In addition, the IRS is requesting additional comments on the following related topics:

- Whether further guidance is needed to clarify the interaction of Sec. 274(a)(1)(A) entertainment expenses and business meal expenses.
- Whether the definition of entertainment in Regs. Sec. 1.274-2(b)(1)(i) should be retained and, if so, whether it should be revised.
- Whether the objective test in Regs. Sec. 1.274-2(b)(1)(ii) should be retained and, if so, whether it should be revised.
- Whether the IRS should provide more examples in the regulations.

IRS Releases Guidance for Section 199A Pass-Through Deduction

The IRS has released long-awaited guidance on new Code Sec. 199A, commonly known as the "pass-through deduction" or the "qualified business income deduction." Taxpayers can rely on the proposed regulations and a proposed revenue procedure until they are issued as final.

Code Sec. 199A allows business owners to deduct up to 20 percent of their qualified business income (QBI) from sole proprietorships, partnerships, trusts, and S corporations. The deduction is one of the most high-profile pieces of the Tax Cuts and Jobs Act (P.L. 115-97).

In addition to providing general definitions and computational rules, the new guidance helps clarify several concepts that were of special interest to many taxpayers.

Trade or Business

The proposed regulations incorporate the Code Sec. 162 rules for determining what constitutes a trade or business. A taxpayer may have more than one trade or business, but a single trade or business generally cannot be conducted through more than one entity.

Taxpayers cannot use the grouping rules of the passive activity provisions of Code Sec. 469 to group multiple activities into a single business. However, a taxpayer may aggregate trades or businesses if:

- each trade or business is itself a trade or business;
- the same person or group owns a majority interest in each business to be aggregated;
- none of the aggregated trades or businesses can be a specified service trade or business; and

(Continued on Page 4)

- the trades or businesses meet at least two of three factors which demonstrate that they are in fact part of a larger, integrated trade or business.

Specified Service Business

Income from a specified service business generally cannot be QBI, although this exclusion is phased in for lower-income taxpayers.

A new de minimis exception allows some business to escape being designated as a specified service trade or business (SSTB). A business qualifies for this de minimis exception if:

- gross receipts do not exceed $25 million, and less than 10 percent is attributable to services; or
- gross receipts exceed $25 million, and less than five percent is attributable to services.

The regulations largely adopt existing rules for what activities constitute a service. However, a business receives income because of an employee/owner's reputation or skill only when the business is engaged in:

- endorsing products or services;
- licensing the use of an individual's image, name, trademark, etc.; or
- receiving appearance fees.

In addition, the regulations try to limit attempts to spin-off parts of a service business into independent qualified businesses. Thus, a business that provides 80 percent or more of its property or services to a related service business is part of that service business. Similarly, the portion of property or services that a business provides to a related service business is treated as a service business. Businesses are related if they have at least 50-percent common ownership.

Wages/Capital Limit

A higher-income taxpayer's qualified business income may be reduced by the wages/capital limit. This limit is based on the taxpayer's share of the business': (1) W-2 wages that are allocable to QBI; and (2) unadjusted basis in qualified property immediately after acquisition.

The proposed regulations and Notice 2018-64, I.R.B. 2018-34, provide detailed rules for determining the business's W-2 wages. These rules generally follow the rules that applied to the Code Sec. 199 domestic production activities deduction.

The proposed regulations also address unadjusted basis immediately after acquisition (UBIA). The regulations largely adopt the existing capitalization rules for determining unadjusted basis. However, "immediately after acquisition" is the date the business places the property in service. Thus, UBIA is generally the cost of the property as of the date the business places it in service.

Other Rules

The proposed regulations also address several other issues, including:

- definitions;
- basic computations;
- loss carryovers;
- Puerto Rico businesses;
- coordination with other Code Sections;
- penalties;
- special basis rules;
- previously suspended losses and net operating losses;
- other exclusions from qualified business income;
- allocations of items that are not attributable to a single trade or business;
- anti-abuse rules;
- application to trusts and estates; and
- special rules for the related deduction for agricultural cooperatives.

Effective Dates

Taxpayers may generally rely on the proposed regulations and Notice 2018-64 until they are issued as final. The regulations and proposed revenue procedure

(Continued on Page 5)

will be effective for tax years ending after they are published as final. However:

- several proposed anti-abuse rules are proposed to apply to tax years ending after December 22, 2017;
- anti-abuse rules that apply specifically to the use of trusts are proposed to apply to tax years ending after August 9, 2018; and
- if a qualified business's tax year begins before January 1, 2018, and ends after December 31, 2017, the taxpayer's items are treated as having been incurred in the taxpayer's tax year during which business's tax year ends.

AICPA: Immediate Guidance Needed on S Corporation Issues

Being that many of our Lally & Co., LLC clients operate in S corporations, it is imperative that as Taxpayers and practitioners, we are able to obtain clarity on certain S corporation issues by next tax filing season. The American Institute of CPAs (AICPA) has echoed this sentiment. In an August 13th letter sent to the Treasury and the IRS, the AICPA requested immediate guidance on certain S corporation provisions under the Tax Cuts and Jobs Act (TCJA) (P.L. 115-97).

S Corporations

S corporations elect to pass corporate income, losses, deductions, and credits through to shareholders for federal tax purposes. Thus, S corporations are considered a pass-through entity. This election allows S corporations to avoid double taxation on the corporate income, according to the IRS.

"Taxpayers and practitioners need clarity on S corporation issues in order to comply with their 2018 tax obligations and to make informed decisions regarding cash-flow, entity structure, and tax planning issues," Annette Nellen wrote in the letter on behalf of the AICPA. Generally, the letter noted the following three areas for which guidance is needed:

- application of the new laws on loss carryforwards;
- clarification of certain provisions relating to the post-termination transition period (PTTP) and the eligible terminated S corporation period (ETSC Period); and
- treatment of deferred foreign income upon transition to participation exemption system of taxation for S corporation trust shareholders.

Rules and planning related to S corporations can be rather difficult to fully understand. Please feel free to contact us if you have any questions with respect to these complicated matters.

Standard Mileage Rates Increase, While Higher Depreciation Limits Kick In

The IRS has released the 2018 optional standard mileage rates to be used to calculate the qualified deductible costs of operating an automobile. Beginning on January 1, 2018, the standard mileage rates for the use of a car, van, pickup or panel truck will be:

- 54.5 cents per mile for business miles driven (up from 53.5 cents in 2017);
- 18 cents per mile for medical and moving expenses (up from 17 cents in 2017); and
- 14 cents per mile for miles driven for charitable purposes (permanently set by statute at 14 cents).

A taxpayer may not use the business standard mileage rate after using a depreciation method under Code Sec. 168 or after claiming the Code Sec. 179 deduction for that vehicle. A taxpayer may not use the business rate for more than four vehicles at a time. As a result, business owners have a choice for their vehicles: take the standard mileage rate, or "itemize" each part of the

(Continued on Page 6)

expense (gas, tolls, insurance, etc., and depreciation).

New Depreciation Limits Under the Tax Cuts and Jobs Act

The recently passed "Tax Cuts and Jobs Act" raises the cap placed on depreciation write-offs of business-use vehicles. The new caps will be:

- $10,000 for the first year a vehicle is placed in service (up from $3,160);
- $16,000 for the second year (up from $5,100); $9,600 for the third year (up from $3,050); and
- $5,760 for each subsequent year (up from $1,875).

For autos eligible for bonus first-year depreciation, that maximum first-year bonus depreciation allowance remains at $8,000. The new, higher limits only apply to vehicles placed in service after December 31, 2017. For vehicles placed in service in 2018, the preceding caps will apply to all types of vehicles. The IRS figures inflation adjustments differently for (1) trucks/SUVs and vans and (2) regular passenger cars. Beginning in 2019, separate inflation adjusted caps will be provided for (1) trucks/SUVs and vans and for (2) regular passenger cars. Also, the $25,000 section 179 expensing limit on certain heavy SUVs is inflation-adjusted after 2018. The $25,000 limit applies to a sport utility vehicle, a truck with interior cargo bed length less than six feet, or a van that seats fewer than 10 persons behind the driver's seat if the vehicle is exempt from the Code Sec. 280F annual depreciation caps because it has a gross vehicle weight rating in excess of 6,000 pounds or is otherwise exempt.

Can I Still Convert Regular IRAs Into Roth IRAs?

Conversions from regular (traditional) tax-deferred individual retirement accounts (IRAs) to Roth IRAs are still allowed after enactment of the Tax Cuts and Jobs Act. In fact, in some instances, such Roth conversions are more beneficial than they were prior to 2018, since the tax rates on all income, including conversion income, are now lower. However, the rule that allows a contribution to one type of an IRA to be recharacterized as a contribution to another type of IRA will no longer apply to a conversion to a Roth IRA after 2017. Note, however, that recharacterization is still permitted with respect to other contributions. For example, an individual may make a contribution for a year to a Roth IRA and, before the due date for the individual's income tax return for that year, recharacterize it as a contribution to a traditional IRA. The provision is effective for tax years beginning after December 31, 2017.

Earlier versions of the Tax Cut and Jobs Act enacted by both the House and Senate eliminated recharacterization entirely. The provision was narrowed considerably in the reconciled version to target only conversions to Roth IRAs. So, for example, an individual may still make a contribution for a year to a Roth IRA and, before the due date for the individual's income tax return for that year, recharacterize it as a contribution to a traditional IRA. In addition, an individual may still make a contribution to a traditional IRA and convert the traditional IRA to a Roth IRA, but the individual is precluded from later unwinding the conversion through a recharacterization.

This newsletter is furnished for the use of Lally & Co., LLC and its clients and does not constitute the provision of advice to any person. It is not prepared with respect to the specific objectives, situation, or particular needs of any specific person. Use of this newsletter is dependent upon the judgment and analysis applied by duly authorized personnel who consider a client's individual circumstances. Persons reading this report should consult with Lally & Co., LLC regarding the appropriateness of any strategies discussed or recommended in this newsletter.

2018 Lally & Co., LLC. All rights reserved.