2023 WICPA BUSINESS & INDUSTRY FALL CONFERENCE

YOUR SOURCE FOR KEY UPDATES & INSIGHTS ON TIMELY ISSUES

HIGHLIGHTED TOPICS:

HOW TO COMBAT THE BIGGEST RISKS TO YOUR RETIREMENT

Learn how to get the most out of Social Security, lower your lifetime taxes, get more interest on your cash and avoid the big mistakes most investors make

ECONOMIC & FINANCIAL MARKET OUTLOOK

Learn about key economic and financial variables that are affecting businesses and get the short- and long-run outlook for 2023-2028

LEADERSHIP ETHICS

Develop leadership skills while understanding and upholding ethics and professional conduct

MONDAY, SEPT. 18 | BROOKFIELD CONFERENCE CENTER & WICPA CPE LIVESTREAM

MATERIALS AT A GLANCE

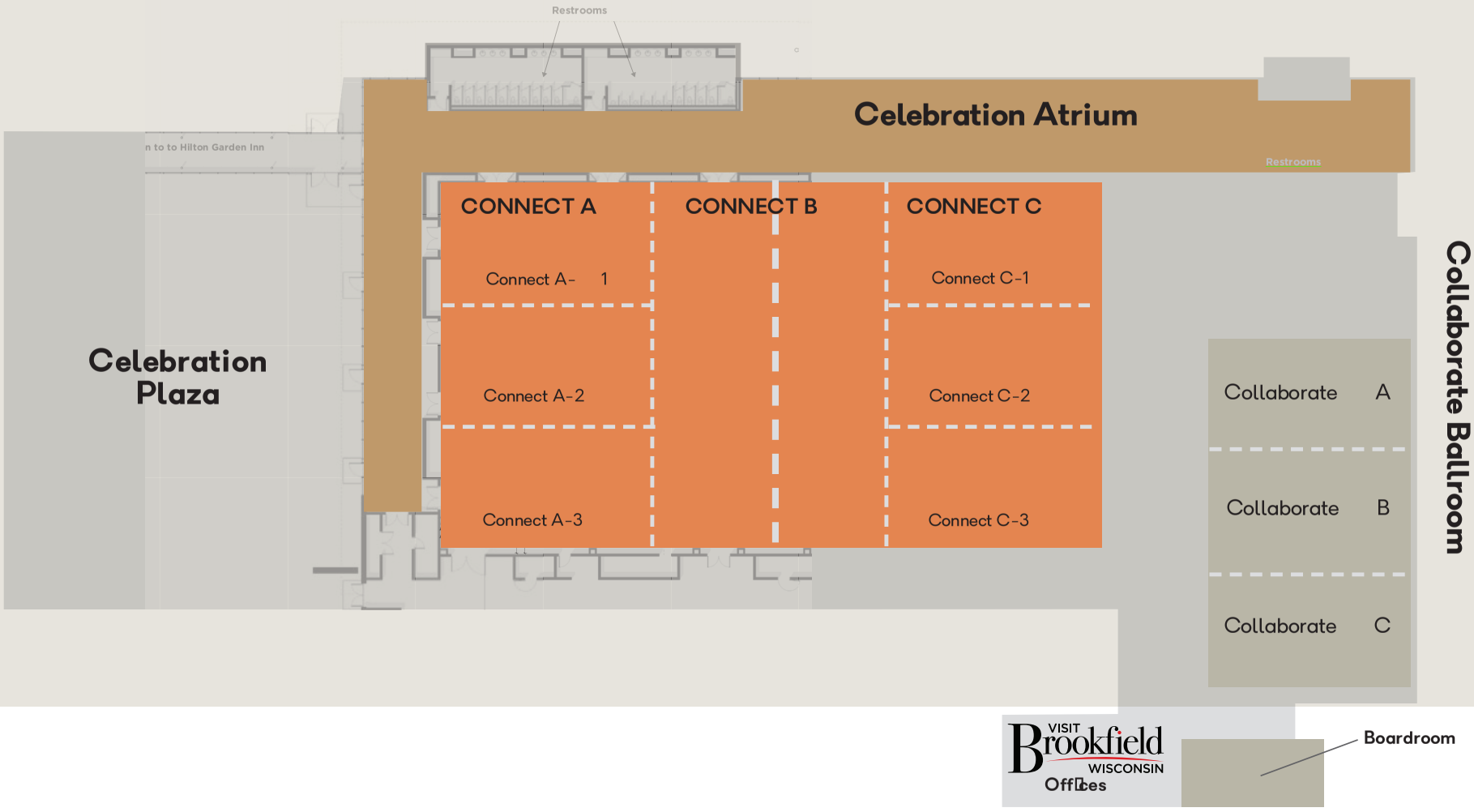
The following materials are from the morning sessions of the 2023 WICPA Business & Industry Fall Conference held on Monday, Sept. 18, including:

- Economic & Financial Market Outlook: 2023-2028
- Accounting & Tax Update
- Cyber Liability Insurance

VIEW THOUSANDS OF ADDITIONAL IN-PERSON AND ONLINE CPE OPPORTUNITIES AT WICPA.ORG/CPECATALOG

BROOKFIELD CONFERENCE CENTER

FLOOR PLANS AND CAPACITY CHARTS



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* Fidelity. "2023 Plan Sponsor Attitudes Survey." 13 July 2023.

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	Jerry Pennington	Jerry.Pennington@TSTTLLC.com
	Annette Gioia	Annette.Gioia@TSTTLLC.com

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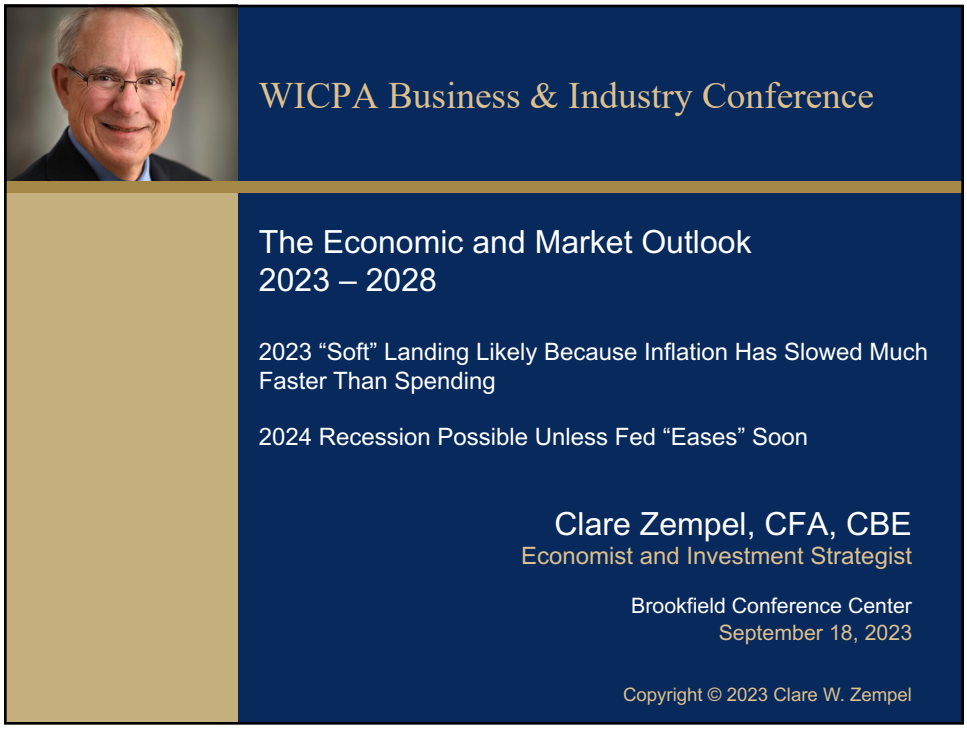
Recipients will be announced in January and honored at the Member Recognition Banquet & Annual Business Meeting on May 9, 2024.

8:15 – 9:15 a.m.

Economic & Financial Market Outlook: 2023-2028

Clare Zempel, CFA, CBE, *Principal, Zempel Strategic*


WICPA Business & Industry Conference
The Economic and Market Outlook
2023 – 2028
2023 “Soft” Landing Likely Because Inflation Has Slowed Much Faster Than Spending
2024 Recession Possible Unless Fed “Eases” Soon
Clare Zempel, CFA, CBE
Economist and Investment Strategist
Brookfield Conference Center
September 18, 2023
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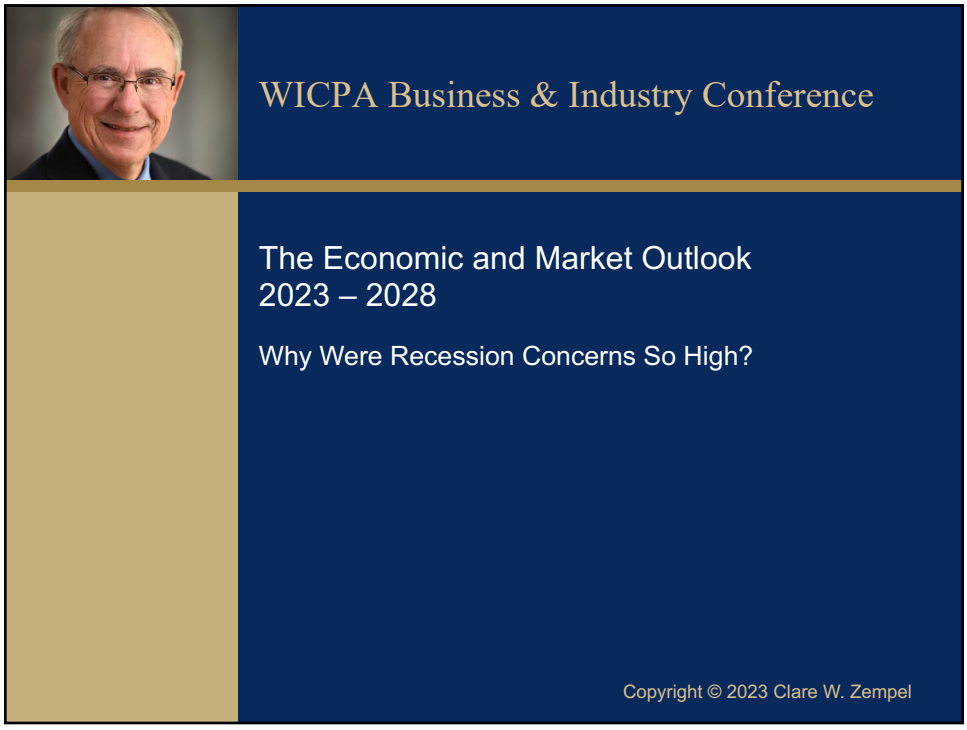
1


WICPA Business & Industry Conference
The Economic and Market Outlook
2023 – 2028
Why Were Recession Concerns So High?
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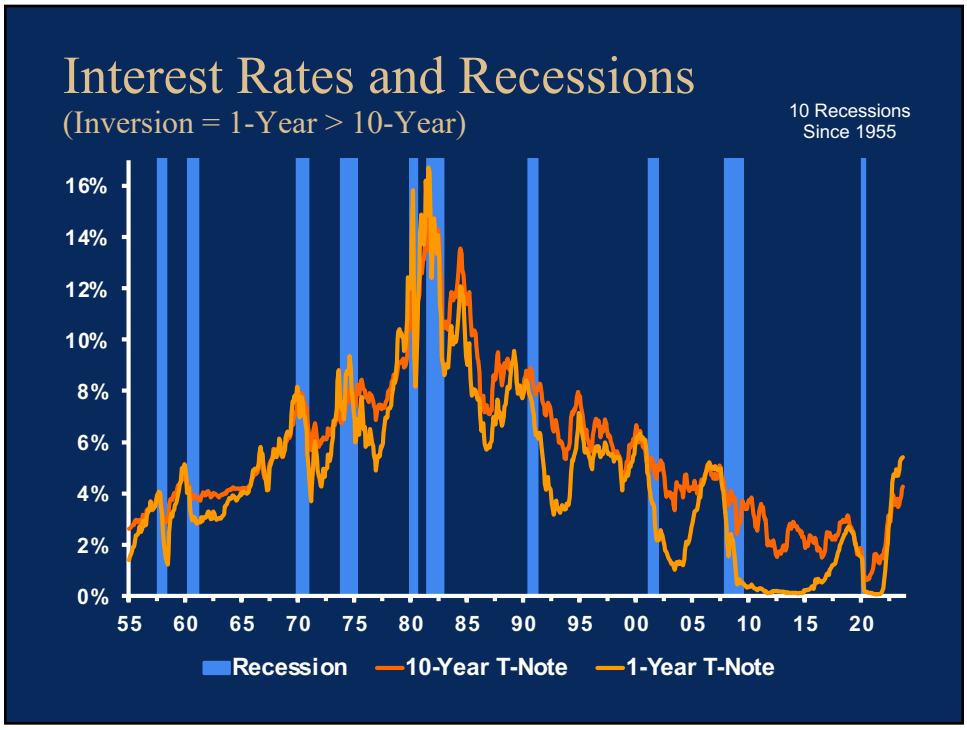
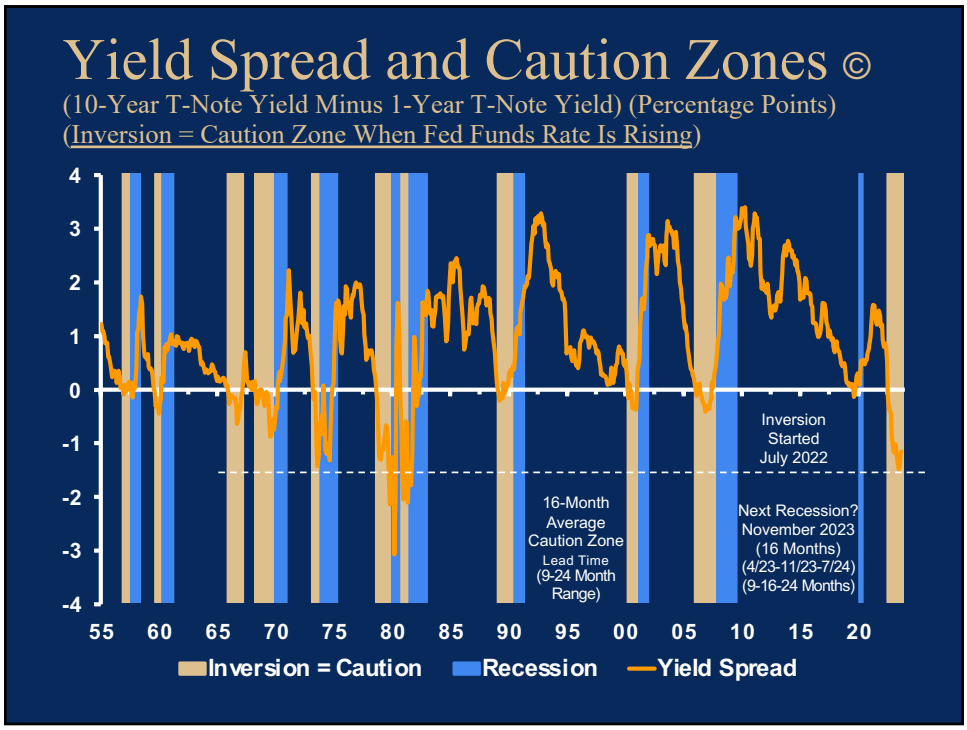
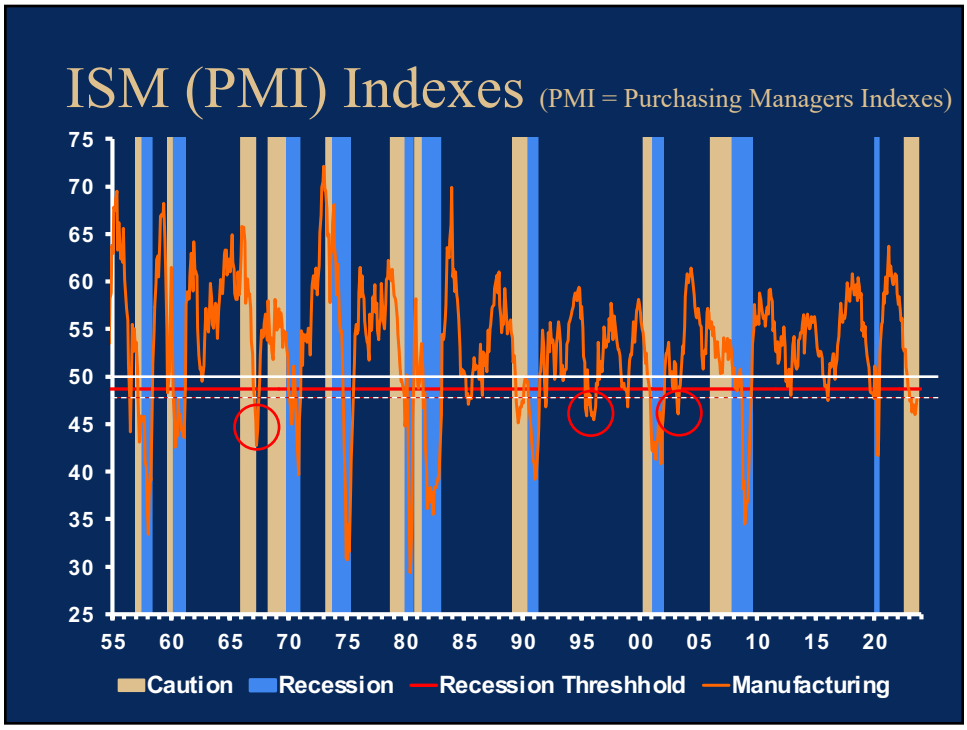
2


Interest Rates and Recessions
(Inversion = 1-Year > 10-Year)
10 Recessions
Since 1955
16%
14%
12%
10%
8%
6%
4%
2%
0%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
10-Year T-Note
1-Year T-Note

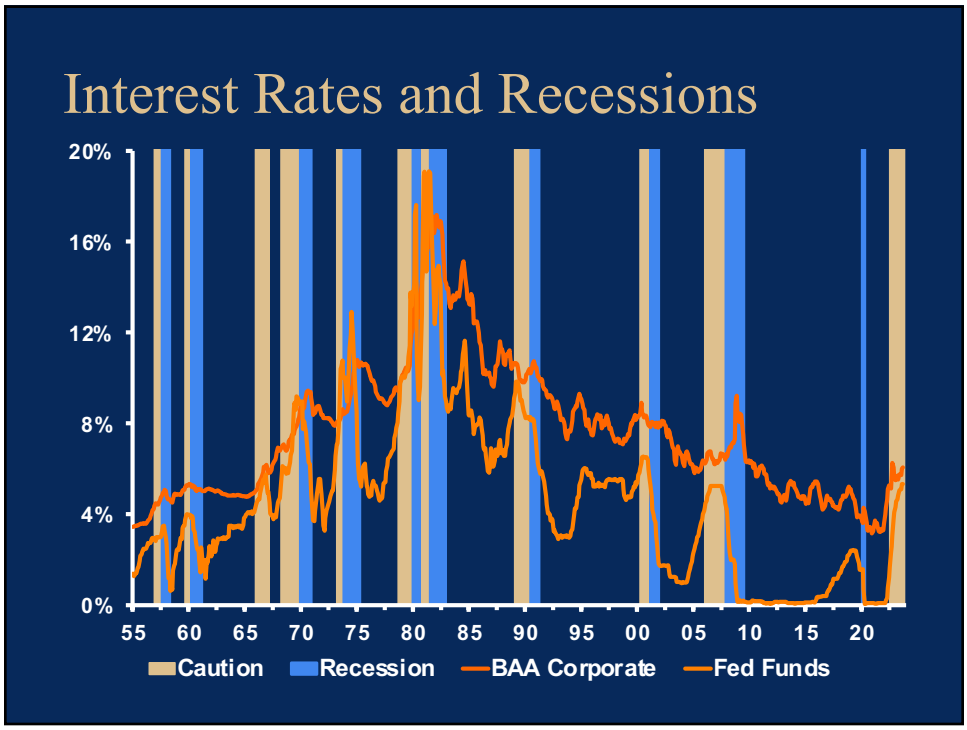
3


Yield Spread and Caution Zones ©
(10-Year T-Note Yield Minus 1-Year T-Note Yield) (Percentage Points)
(Inversion = Caution Zone When Fed Funds Rate Is Rising)
4
3
2
1
0
-1
-2
-3
-4
Inversion
Started
July 2022
16-Month
Average
Caution Zone
Lead Time
(9-24 Month
Range)
Next Recession?
November 2023
(16 Months)
(4/23-11/23-7/24)
(9-16-24 Months)
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Inversion = Caution
Recession
Yield Spread

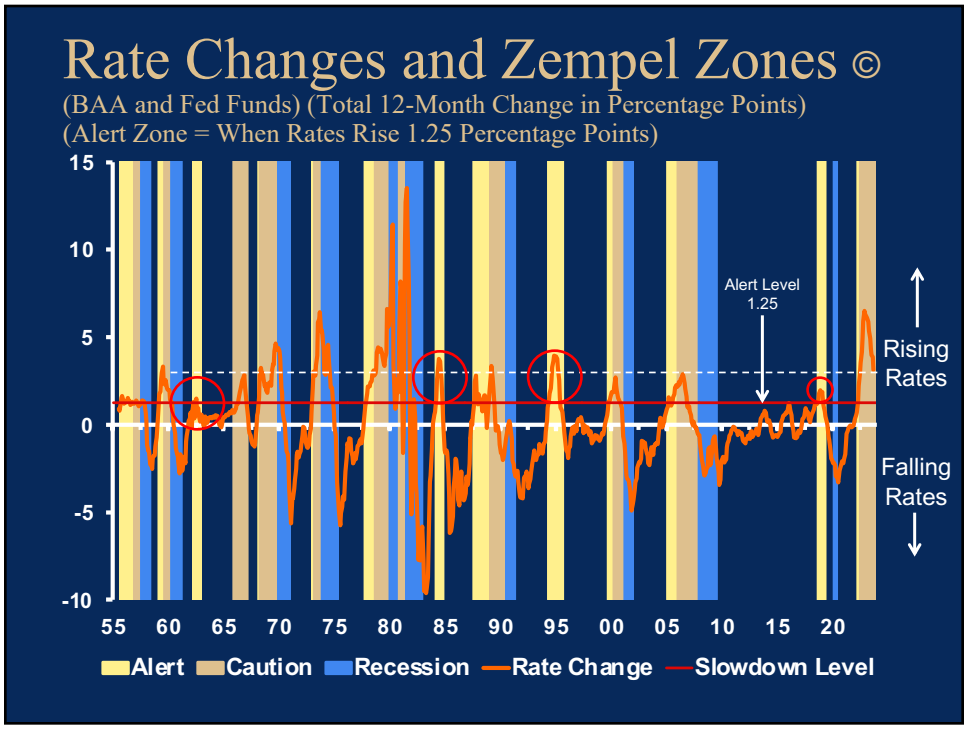
4


ISM (PMI) Indexes
(PMI = Purchasing Managers Indexes)
75
70
65
60
55
50
45
40
35
30
25
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Caution
Recession
Recession Threshhold
Manufacturing

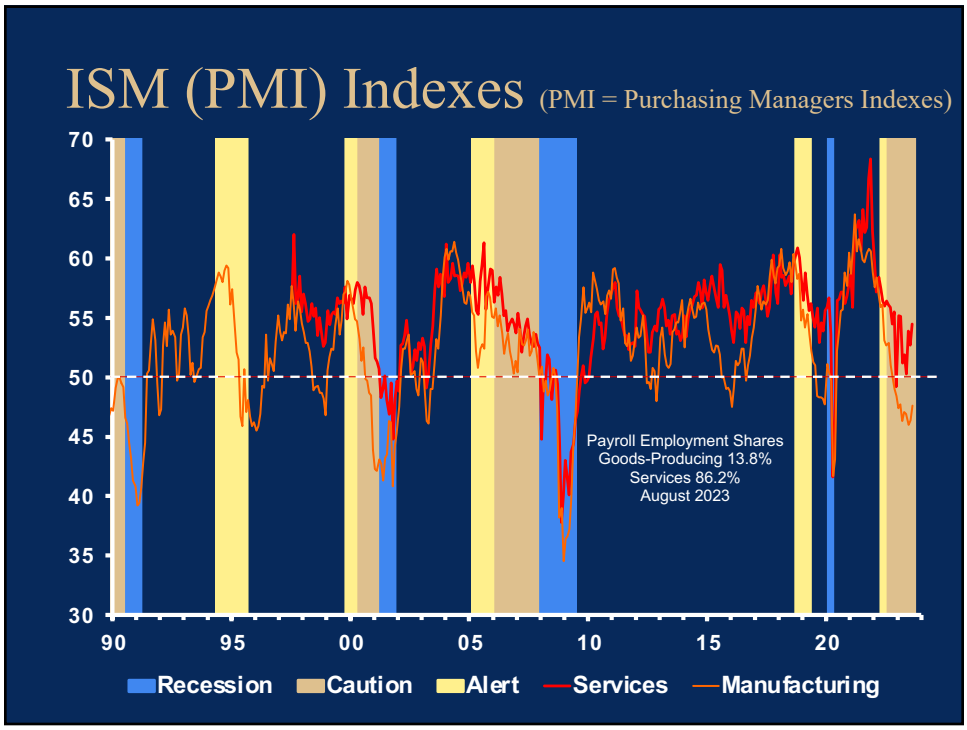
5


Interest Rates and Recessions
20%
16%
12%
8%
4%
0%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Caution
Recession
BAA Corporate
Fed Funds

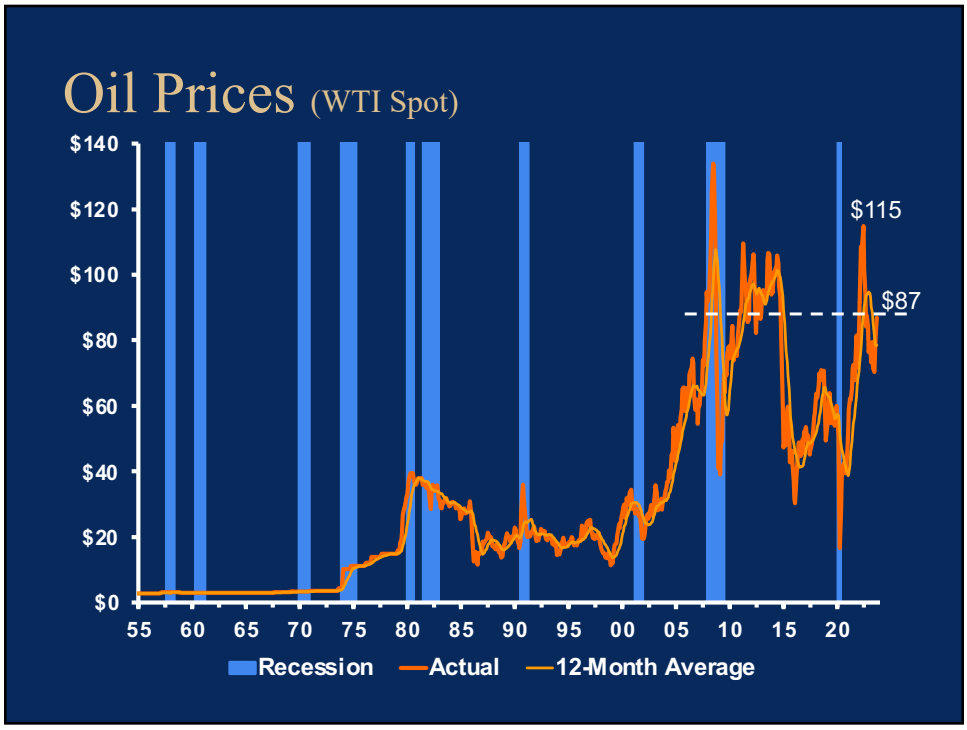
6


Rate Changes and Zempel Zones ©
(BAA and Fed Funds) (Total 12-Month Change in Percentage Points)
(Alert Zone = When Rates Rise 1.25 Percentage Points)
15
10
5
0
-5
-10
Alert Level
1.25
Rising
Rates
Falling
Rates
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Alert
Caution
Recession
Rate Change
Slowdown Level

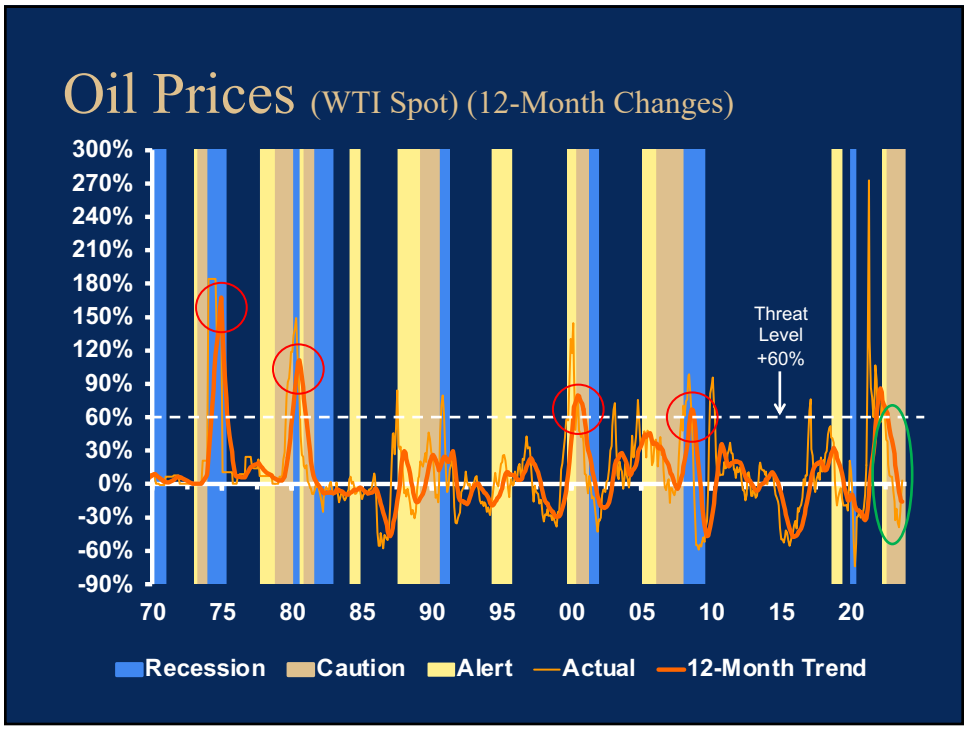
7


ISM (PMI) Indexes (PMI = Purchasing Managers Indexes)
70
65
60
55
50
45
40
35
30
Payroll Employment Shares
Goods-Producing 13.8%
Services 86.2%
August 2023
90 95 00 05 10 15 20
Recession
Caution
Alert
Services
Manufacturing

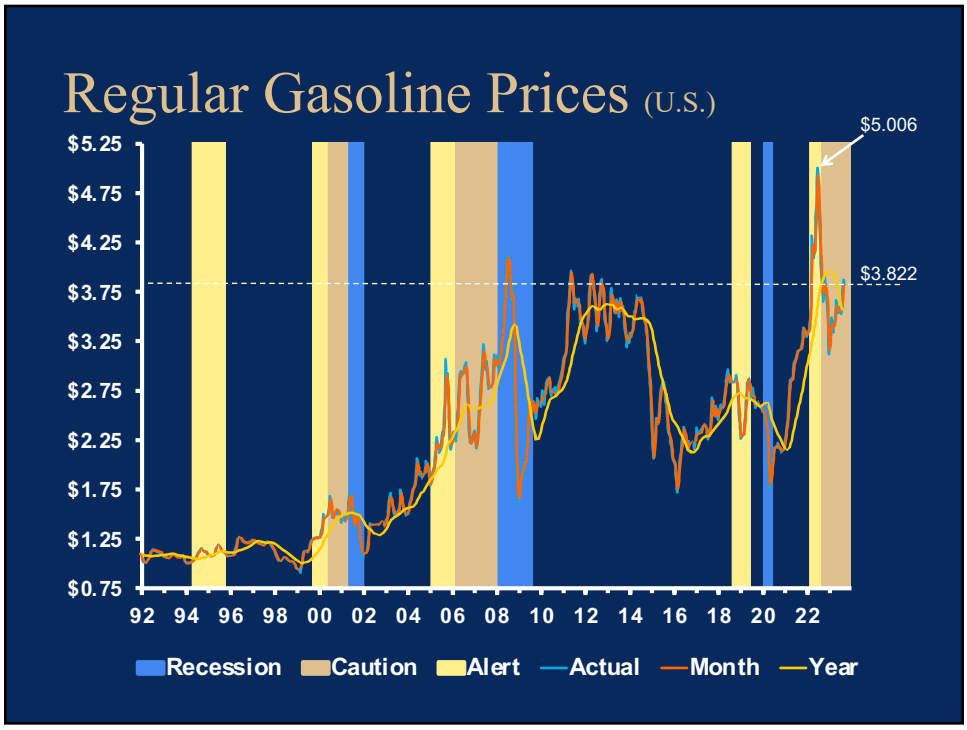
8


Oil Prices (WTI Spot)
$140
$120
$100
$80
$60
$40
$20
$0
$115
$87
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
Actual
12-Month Average

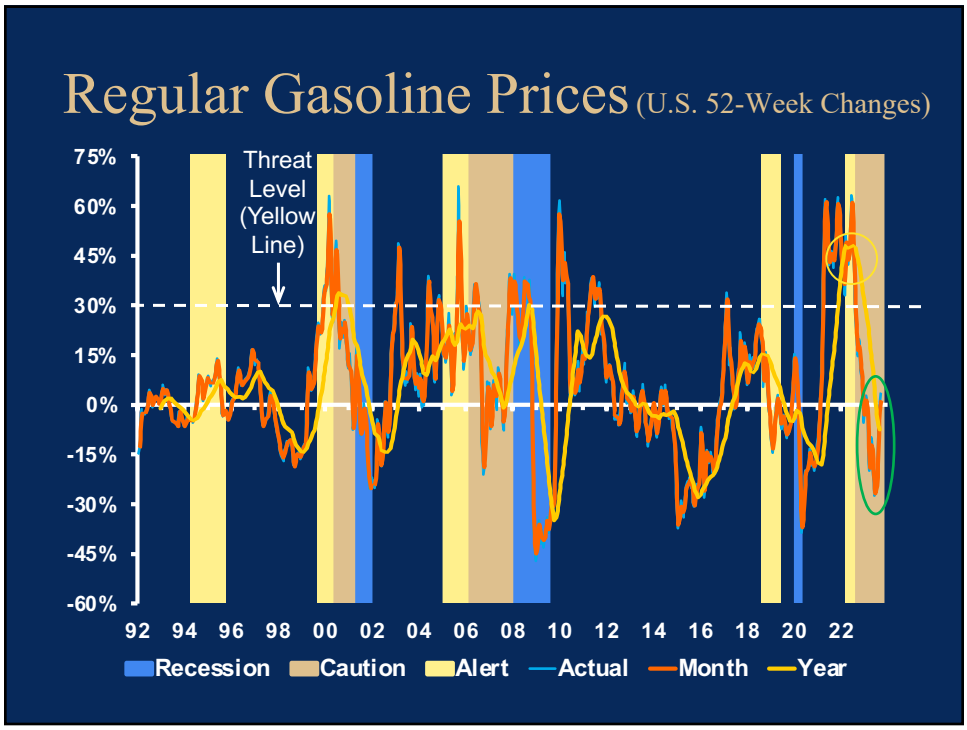
9


Oil Prices (WTI Spot) (12-Month Changes)
300%
270%
240%
210%
180%
150%
120%
90%
60%
30%
0%
-30%
-60%
-90%
Threat Level +60%
70 75 80 85 90 95 00 05 10 15 20
Recession
Caution
Alert
Actual
12-Month Trend

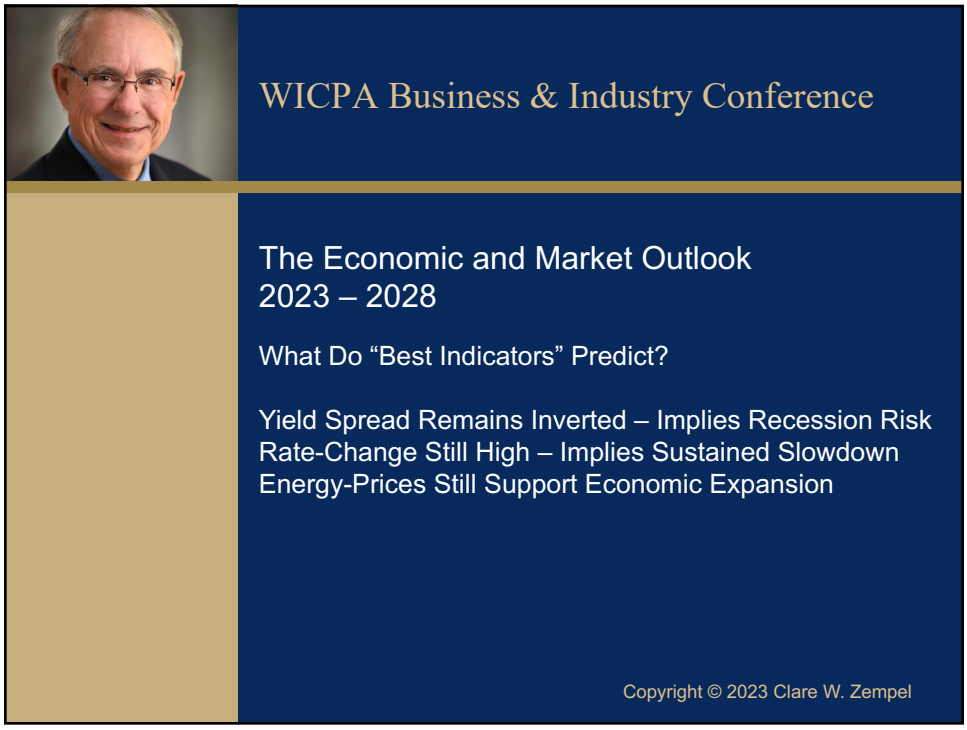
10


Regular Gasoline Prices (U.S.)
$5.006
$3.822
$5.25
$4.75
$4.25
$3.75
$3.25
$2.75
$2.25
$1.75
$1.25
$0.75
92 94 96 98 00 02 04 06 08 10 12 14 16 18 20 22
Recession
Caution
Alert
Actual
Month
Year

11


Regular Gasoline Prices (U.S. 52-Week Changes)
Threat Level (Yellow Line)
75%
60%
45%
30%
15%
0%
-15%
-30%
-45%
-60%
92 94 96 98 00 02 04 06 08 10 12 14 16 18 20 22
Recession
Caution
Alert
Actual
Month
Year

12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The Economic and Market Outlook
2023 – 2028
What Do “Best Indicators” Predict?
Yield Spread Remains Inverted – Implies Recession Risk
Rate-Change Still High – Implies Sustained Slowdown
Energy-Prices Still Support Economic Expansion
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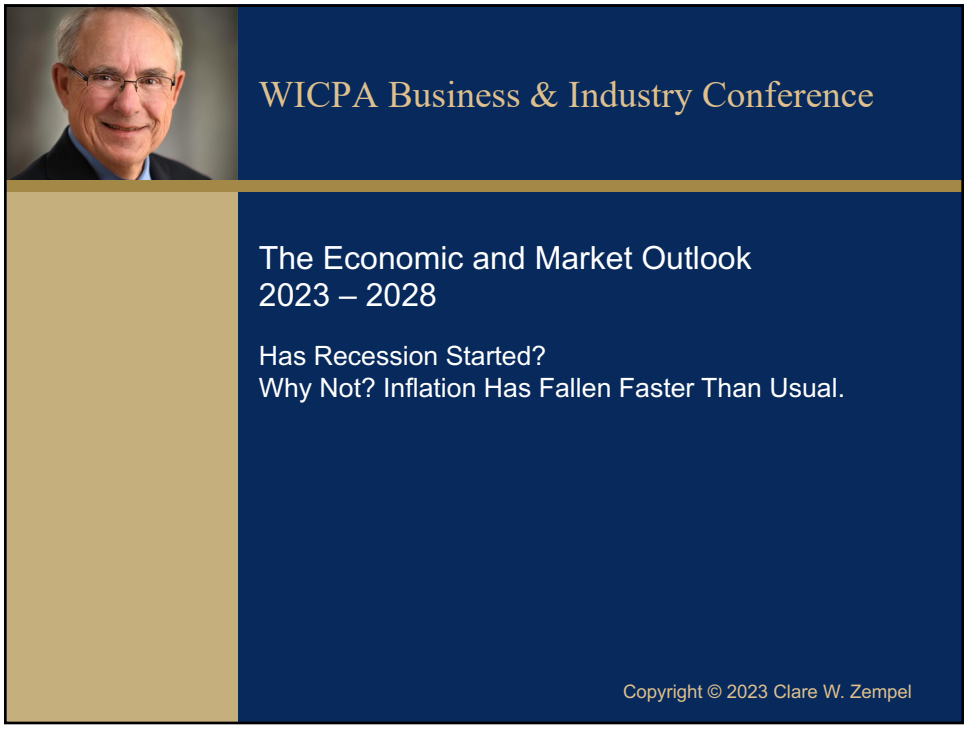
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The Economic and Market Outlook
2023 – 2028
Has Recession Started?
Why Not? Inflation Has Fallen Faster Than Usual.
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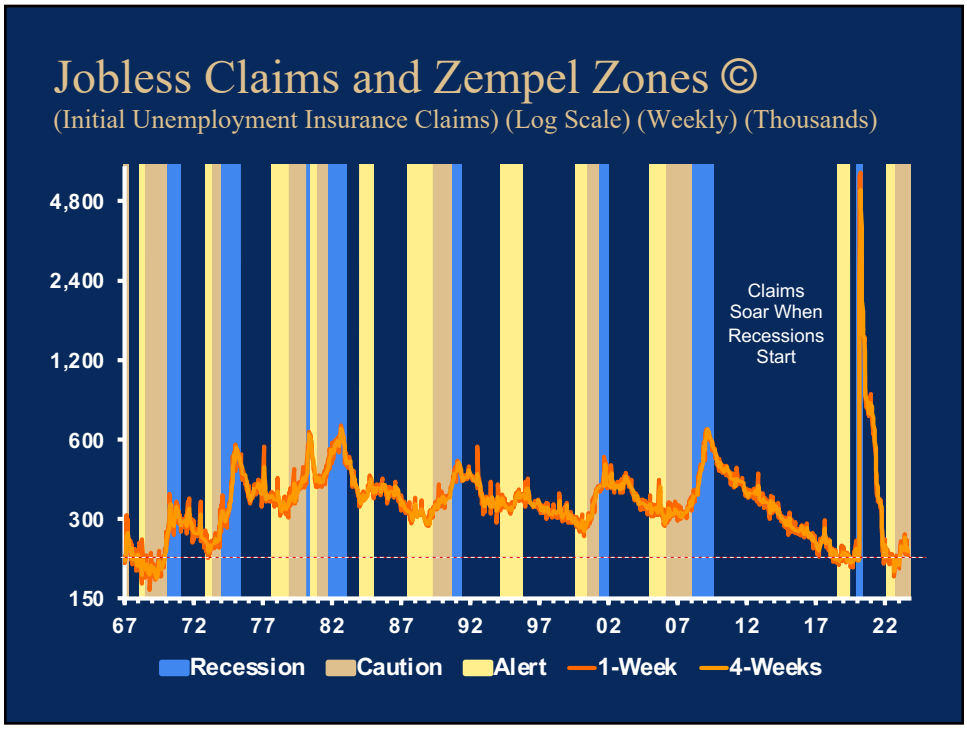
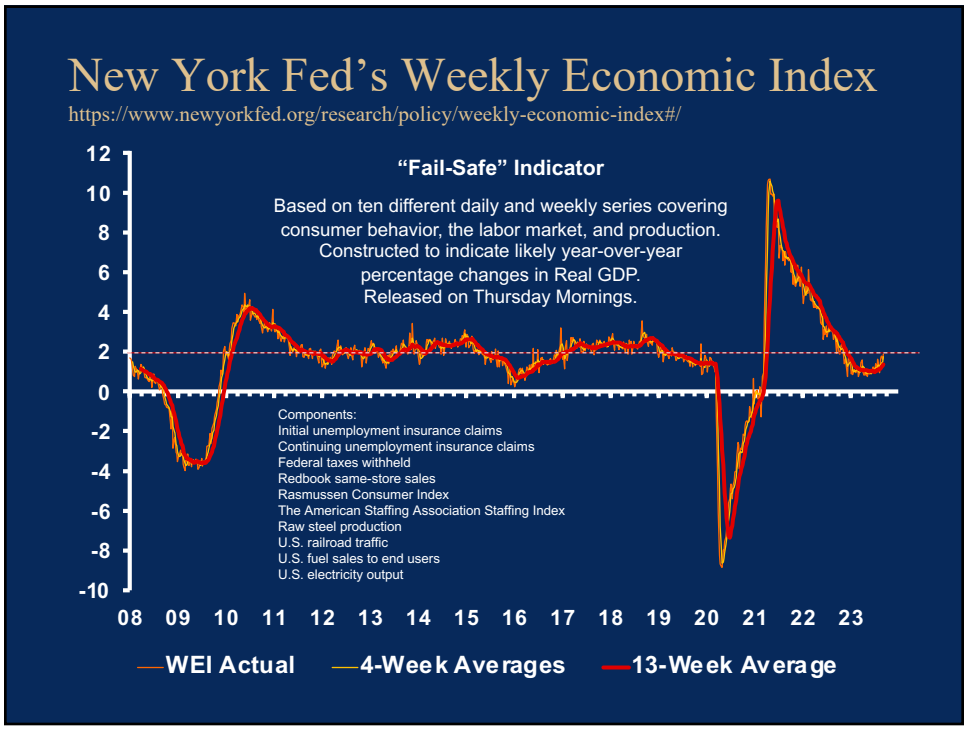
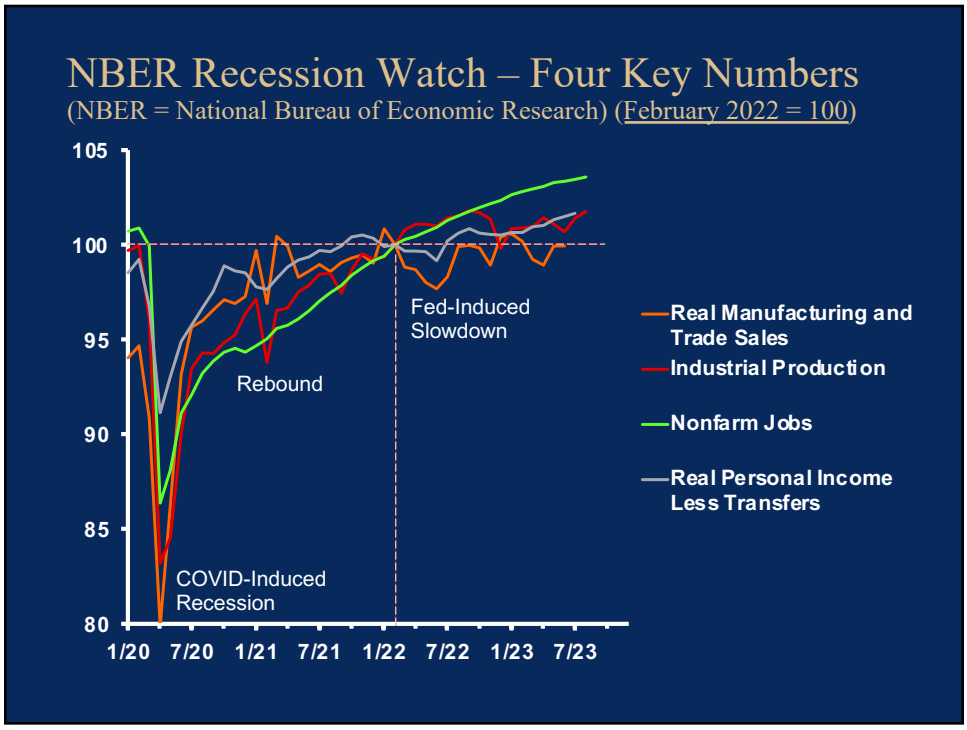

Jobless Claims and Zempel Zones ©
(Initial Unemployment Insurance Claims) (Log Scale) (Weekly) (Thousands)
4,800
2,400
1,200
600
300
150
67 72 77 82 87 92 97 02 07 12 17 22
Claims Soar When Recessions Start
Recession
Caution
Alert
1-Week
4-Weeks

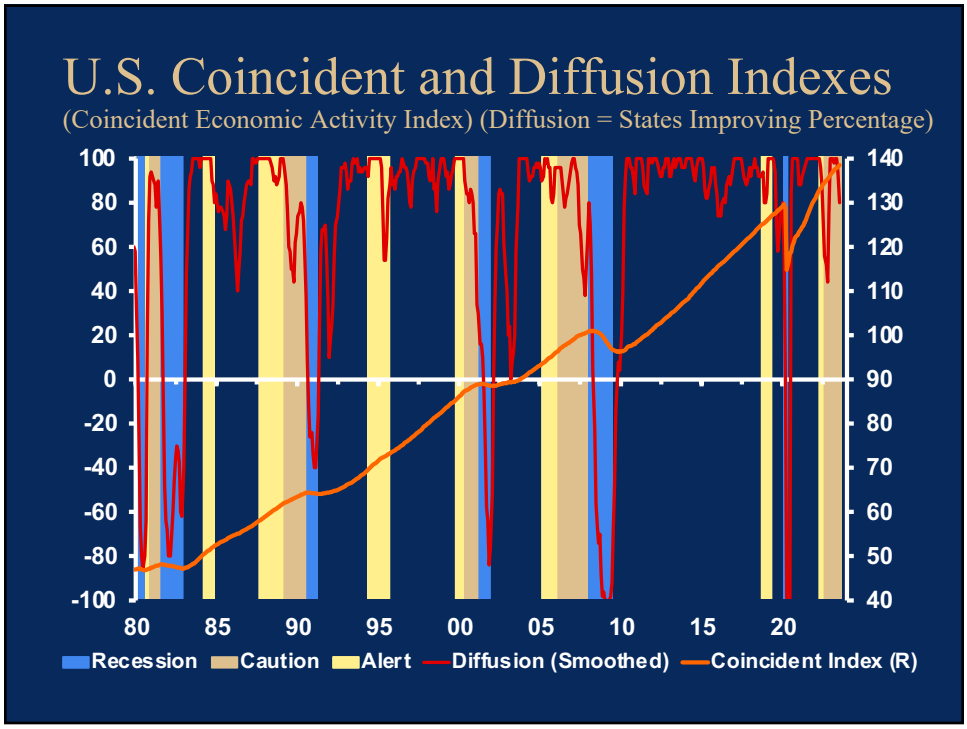
15


New York Fed's Weekly Economic Index
https://www.newyorkfed.org/research/policy/weekly-economic-index#/
"Fail-Safe" Indicator
Based on ten different daily and weekly series covering consumer behavior, the labor market, and production. Constructed to indicate likely year-over-year percentage changes in Real GDP. Released on Thursday Mornings.
Components:
Initial unemployment insurance claims
Continuing unemployment insurance claims
Federal taxes withheld
Redbook same-store sales
Rasmussen Consumer Index
The American Staffing Association Staffing Index
Raw steel production
U.S. railroad traffic
U.S. fuel sales to end users
U.S. electricity output
12
10
8
6
4
2
0
-2
-4
-6
-8
-10
08 09 10 11 12 13 14 15 16 17 18 19 20 21 22 23
WEI Actual
4-Week Averages
13-Week Average

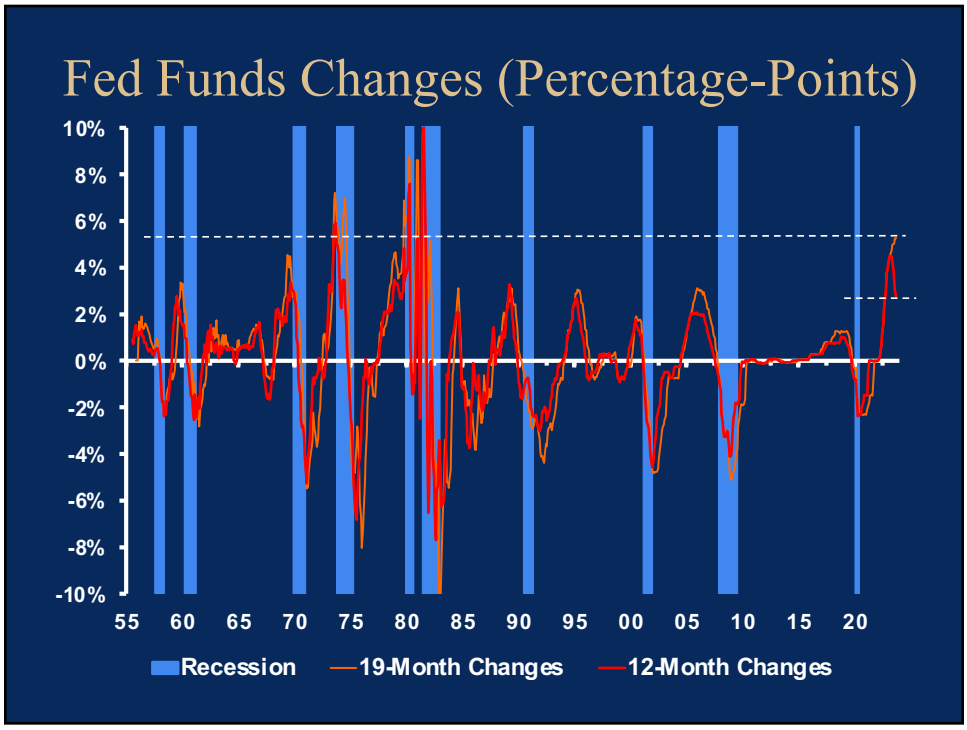
16


NBER Recession Watch – Four Key Numbers
(NBER = National Bureau of Economic Research) (February 2022 = 100)
105
100
95
90
85
80
1/20
7/20
1/21
7/21
1/22
7/22
1/23
7/23
COVID-Induced Recession
Rebound
Fed-Induced Slowdown
Real Manufacturing and Trade Sales
Industrial Production
Nonfarm Jobs
Real Personal Income Less Transfers

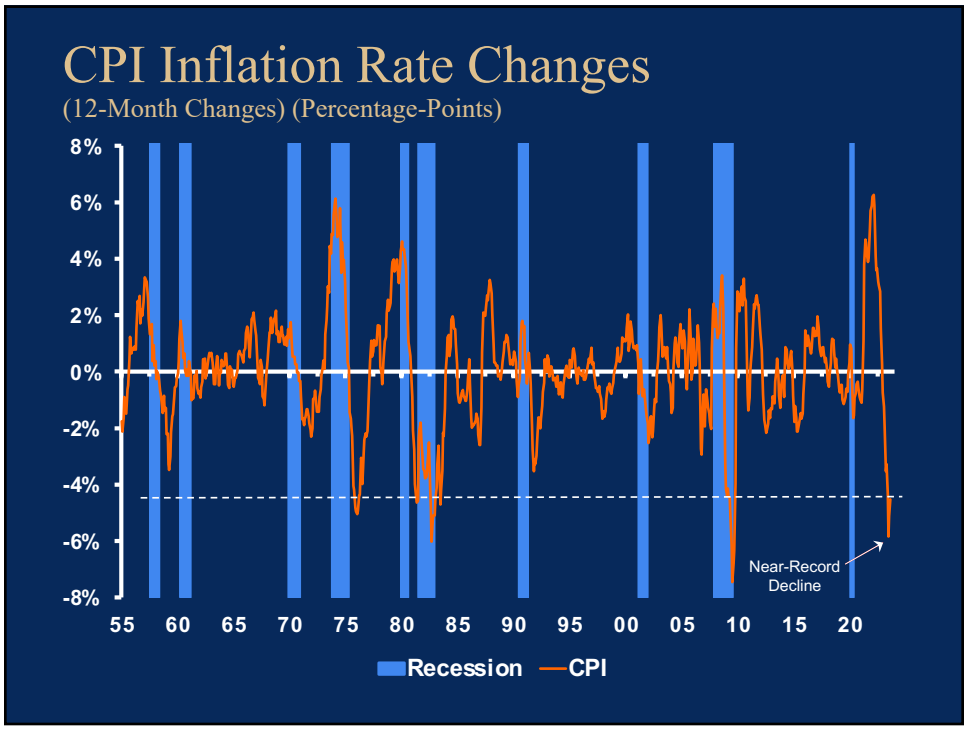
17


U.S. Coincident and Diffusion Indexes
(Coincident Economic Activity Index) (Diffusion = States Improving Percentage)
100
80
60
40
20
0
-20
-40
-60
-80
-100
140
130
120
110
100
90
80
70
60
50
40
80
85
90
95
00
05
10
15
20
Recession
Caution
Alert
Diffusion (Smoothed)
Coincident Index (R)

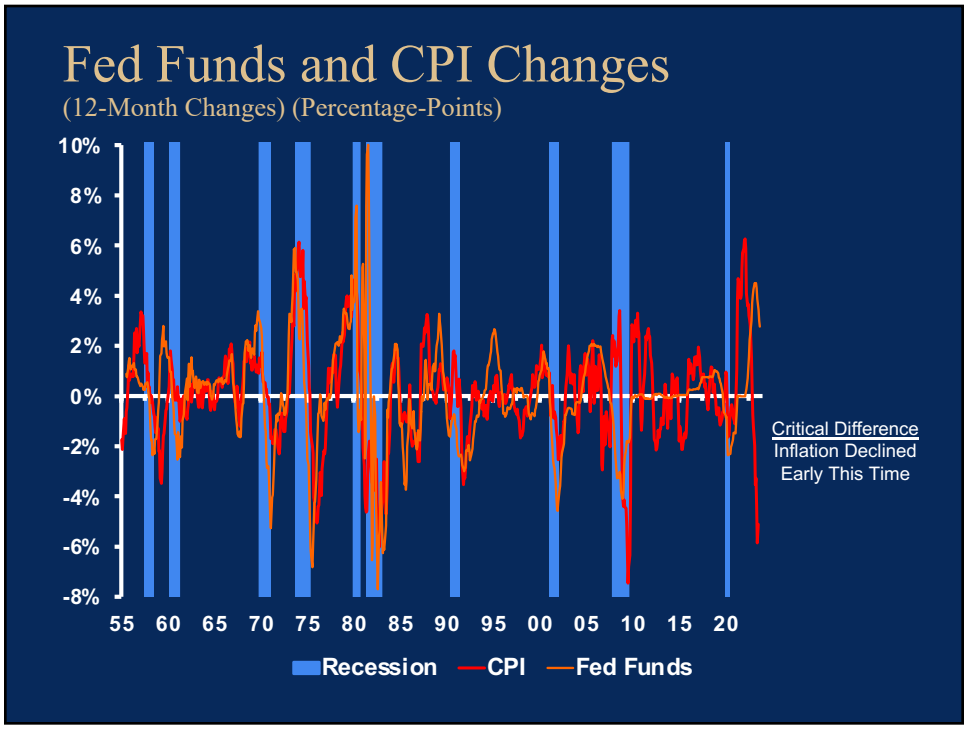
18


Fed Funds Changes (Percentage-Points)
10%
8%
6%
4%
2%
0%
-2%
-4%
-6%
-8%
-10%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
19-Month Changes
12-Month Changes

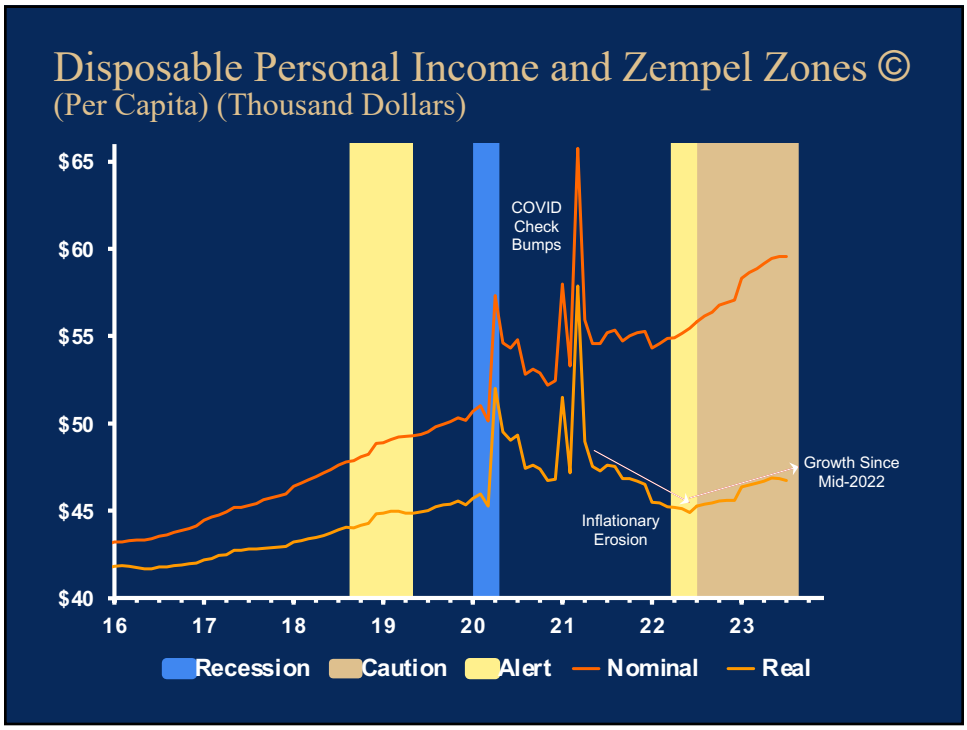
19


CPI Inflation Rate Changes
(12-Month Changes) (Percentage-Points)
8%
6%
4%
2%
0%
-2%
-4%
-6%
-8%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Near-Record Decline
Recession
CPI

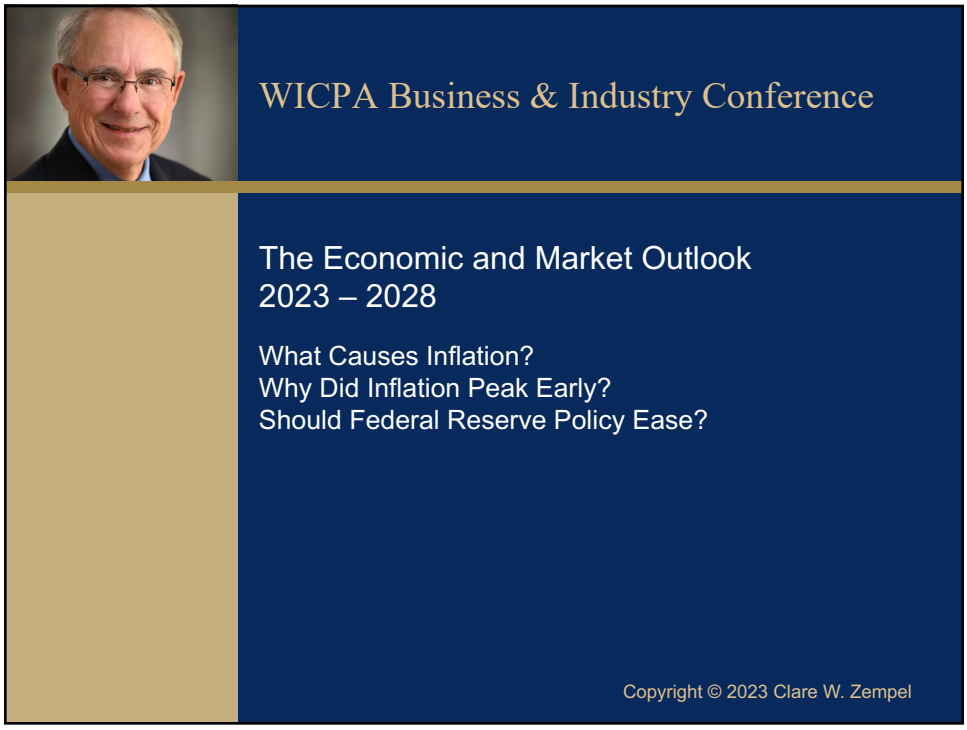
20


Fed Funds and CPI Changes
(12-Month Changes) (Percentage-Points)
10%
8%
6%
4%
2%
0%
-2%
-4%
-6%
-8%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
CPI
Fed Funds
Critical Difference
Inflation Declined
Early This Time

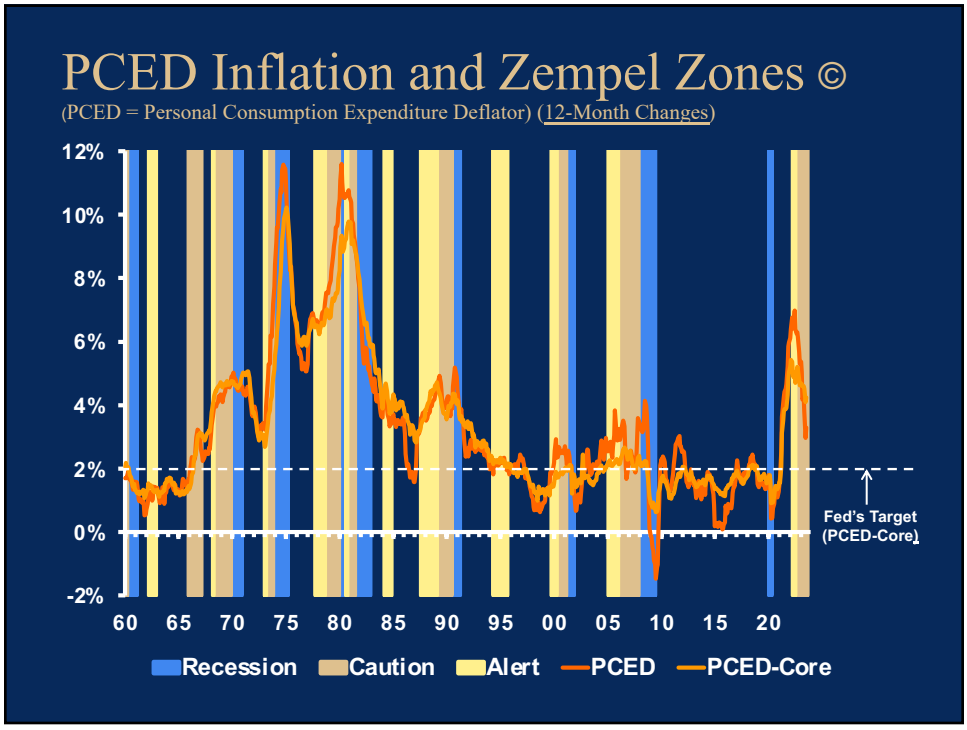
21


Disposable Personal Income and Zempel Zones ©
(Per Capita) (Thousand Dollars)
$65
$60
$55
$50
$45
$40
16 17 18 19 20 21 22 23
COVID
Check
Bumps
Inflationary
Erosion
Growth Since
Mid-2022
Recession
Caution
Alert
Nominal
Real

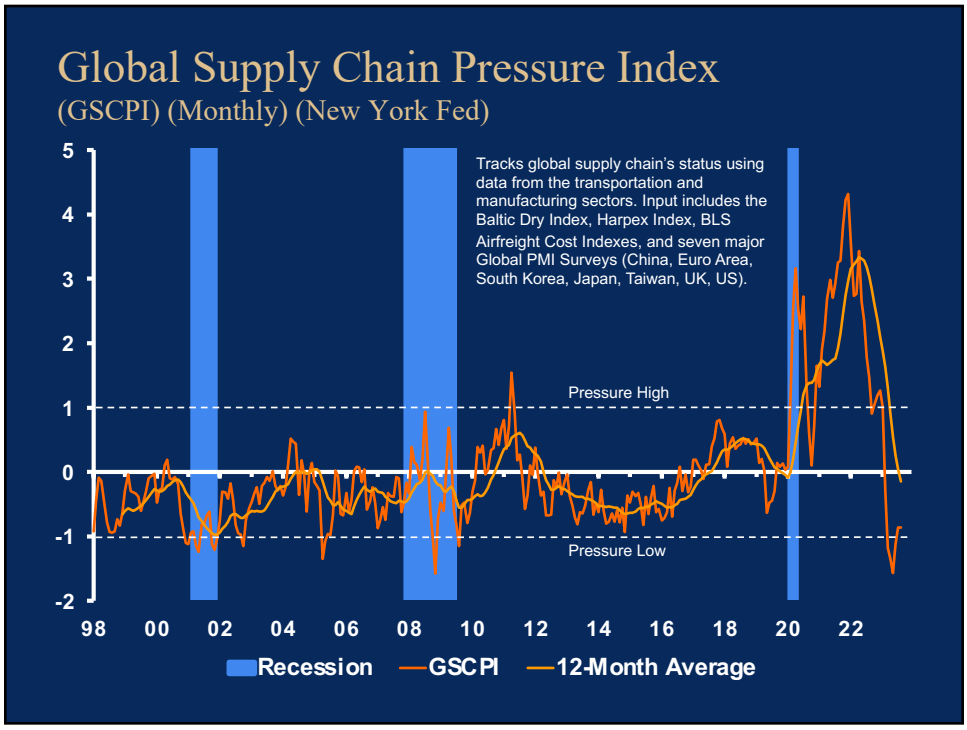
22


WICPA Business & Industry Conference
The Economic and Market Outlook
2023 – 2028
What Causes Inflation?
Why Did Inflation Peak Early?
Should Federal Reserve Policy Ease?
Copyright © 2023 Clare W. Zempel

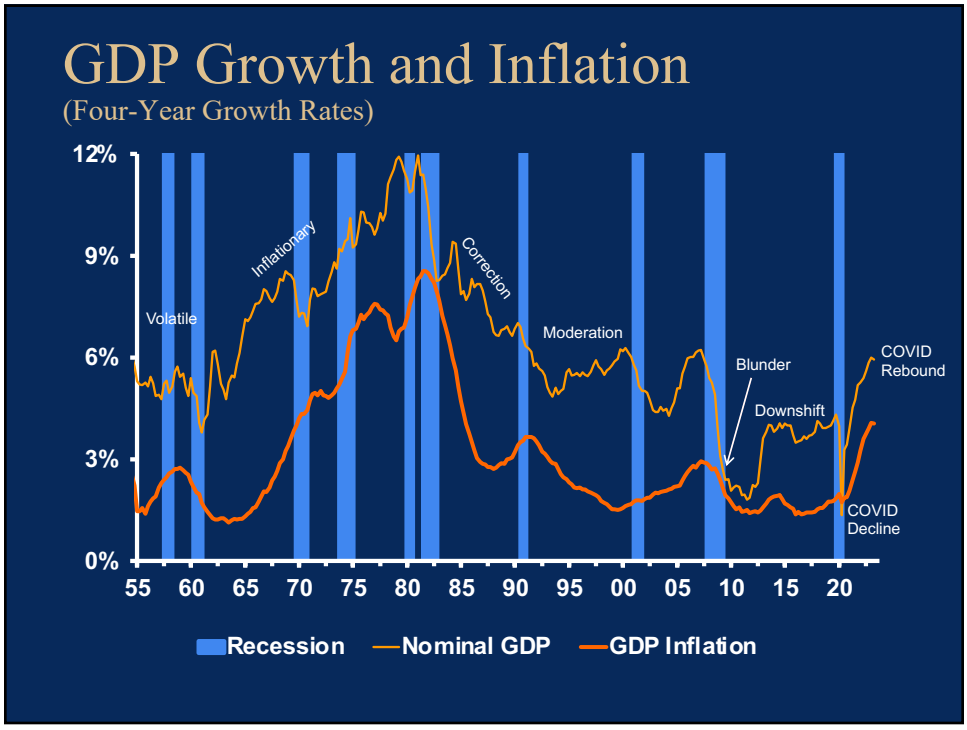
23


PCED Inflation and Zempel Zones ©
(PCED = Personal Consumption Expenditure Deflator) (12-Month Changes)
12%
10%
8%
6%
4%
2%
0%
-2%
60 65 70 75 80 85 90 95 00 05 10 15 20
Fed's Target
(PCED-Core)
Recession
Caution
Alert
PCED
PCED-Core

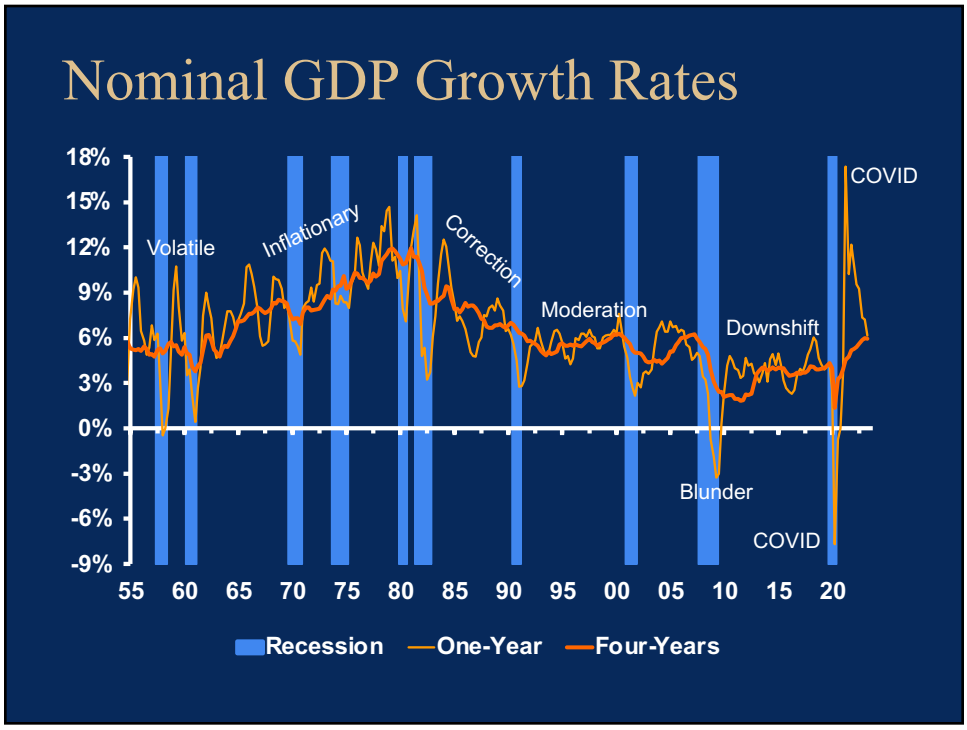
24


Global Supply Chain Pressure Index
(GSCPI) (Monthly) (New York Fed)
Tracks global supply chain's status using data from the transportation and manufacturing sectors. Input includes the Baltic Dry Index, Harpex Index, BLS Airfreight Cost Indexes, and seven major Global PMI Surveys (China, Euro Area, South Korea, Japan, Taiwan, UK, US).
Pressure High
Pressure Low
5
4
3
2
1
0
-1
-2
98 00 02 04 06 08 10 12 14 16 18 20 22
Recession
GSCPI
12-Month Average

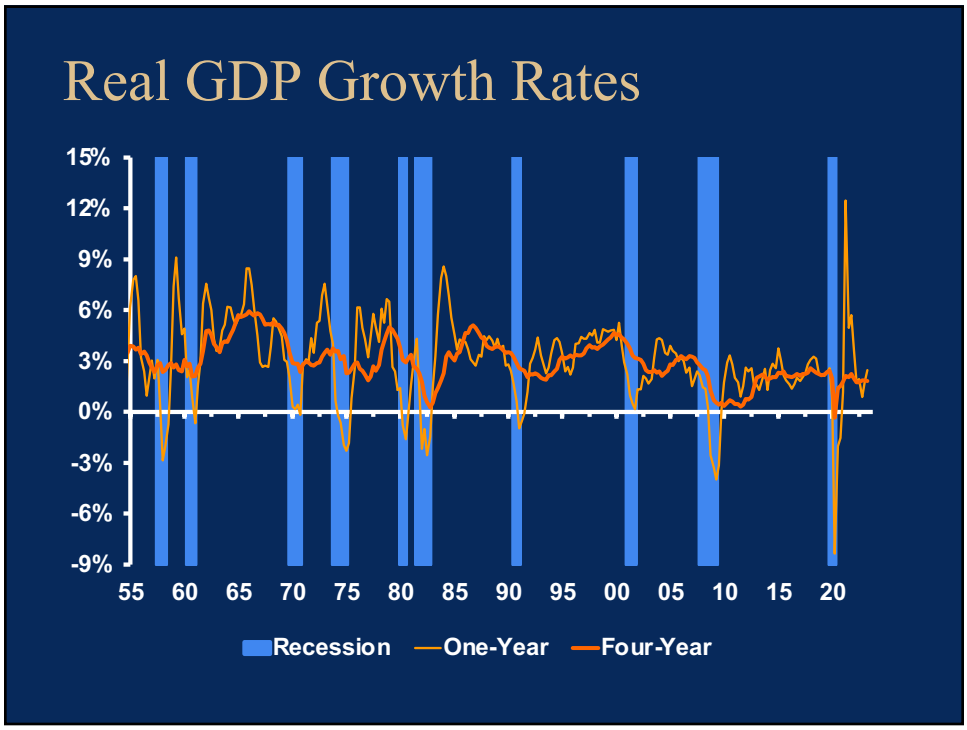
25


GDP Growth and Inflation
(Four-Year Growth Rates)
12%
9%
6%
3%
0%
Volatile
Inflationary
Correction
Moderation
Blunder
Downshift
COVID Rebound
COVID Decline
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
Nominal GDP
GDP Inflation

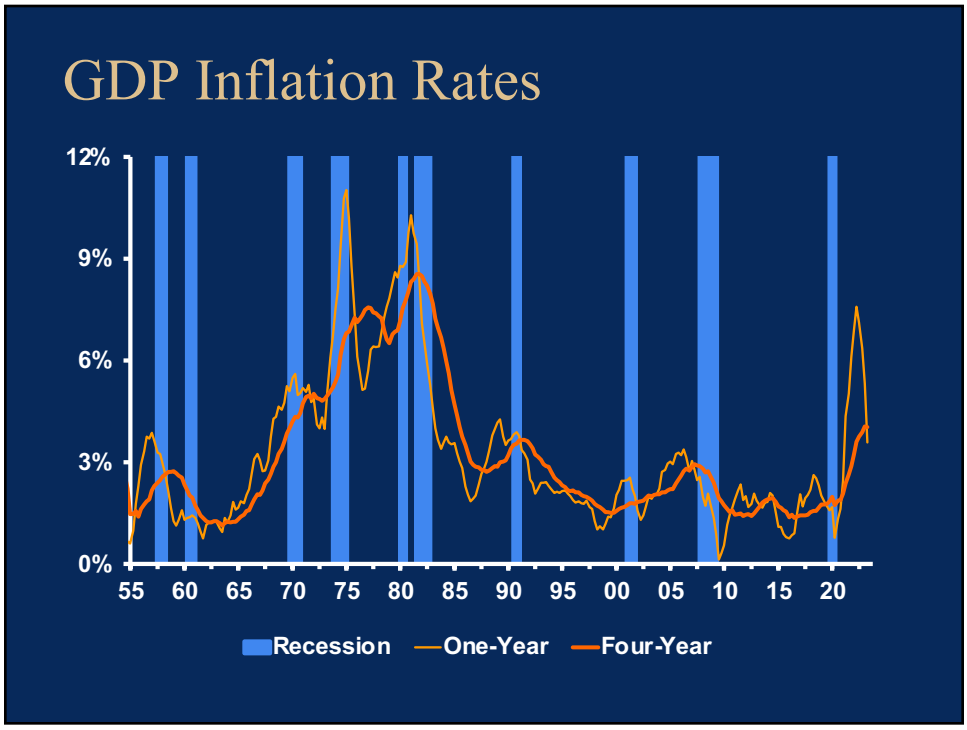
26


Nominal GDP Growth Rates
18%
15%
12%
9%
6%
3%
0%
-3%
-6%
-9%
Volatile
Inflationary
Correction
Moderation
Downshift
Blunder
COVID
COVID
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
One-Year
Four-Years

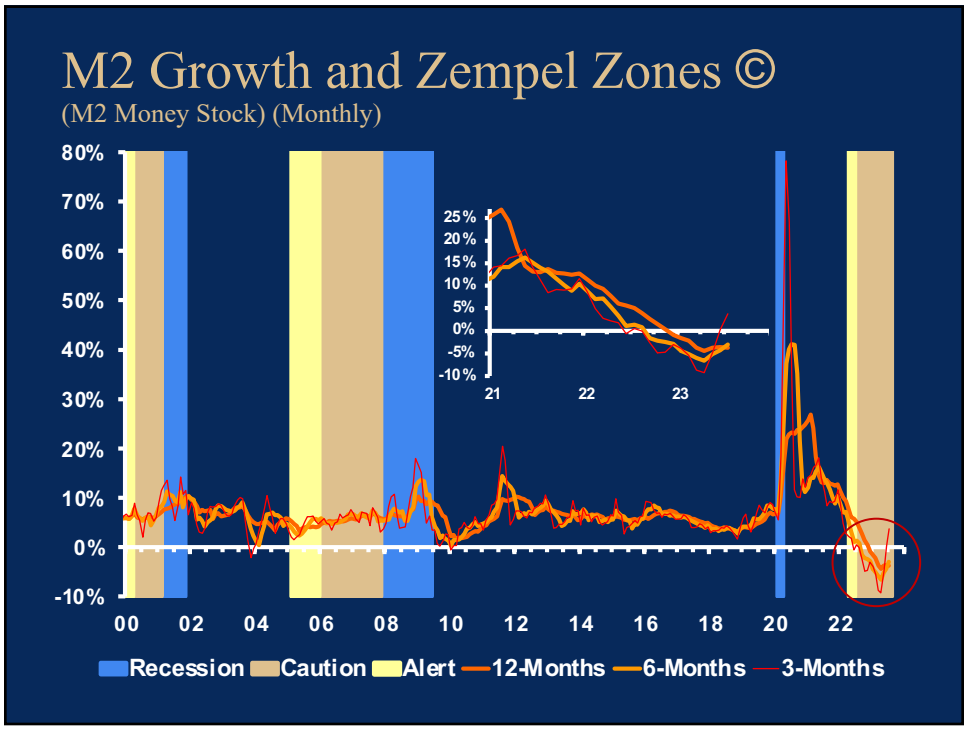
27


Real GDP Growth Rates
15%
12%
9%
6%
3%
0%
-3%
-6%
-9%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
One-Year
Four-Year

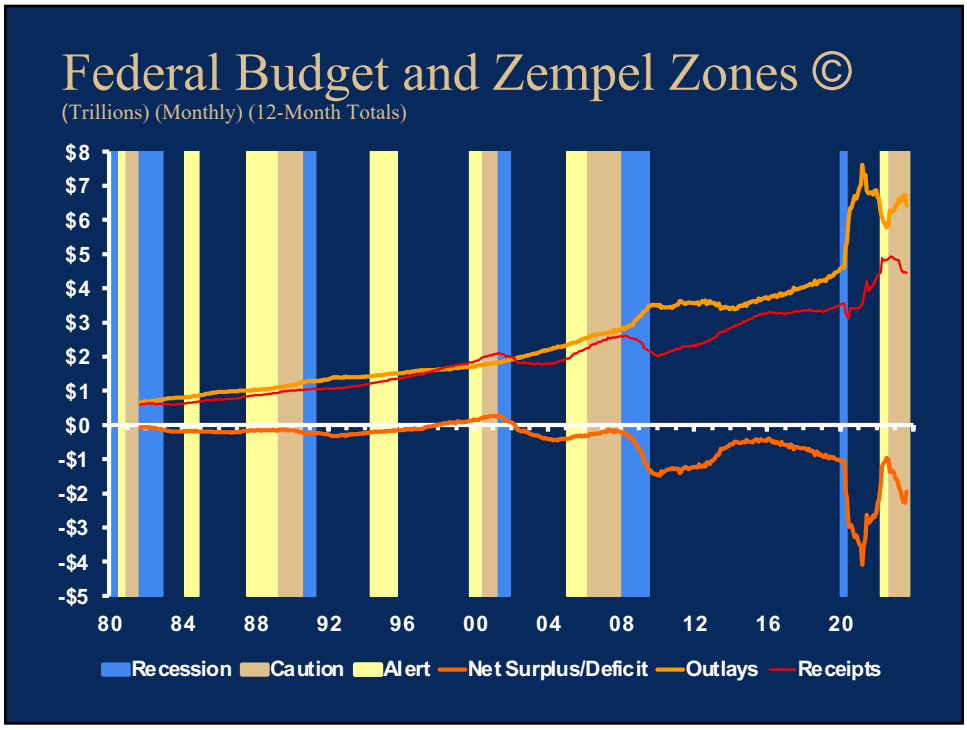
28


GDP Inflation Rates
12%
9%
6%
3%
0%
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
One-Year
Four-Year

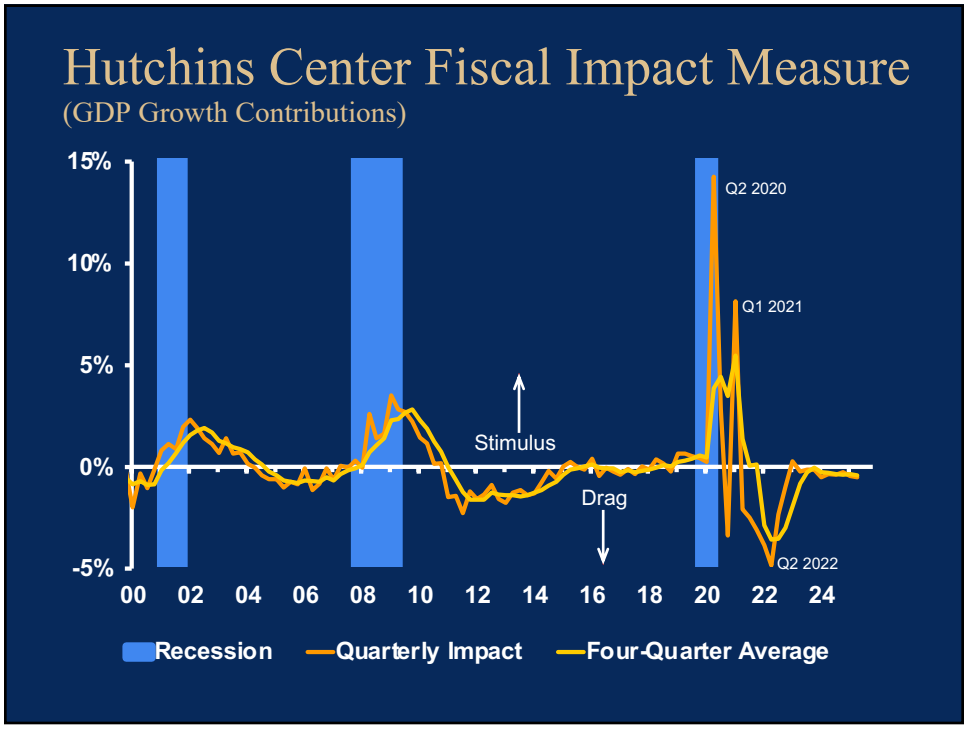
29


M2 Growth and Zempel Zones ©
(M2 Money Stock) (Monthly)
80%
70%
60%
50%
40%
30%
20%
10%
0%
-10%
00 02 04 06 08 10 12 14 16 18 20 22
25%
20%
15%
10%
5%
0%
-5%
-10%
21 22 23
Recession
Caution
Alert
12-Months
6-Months
3-Months

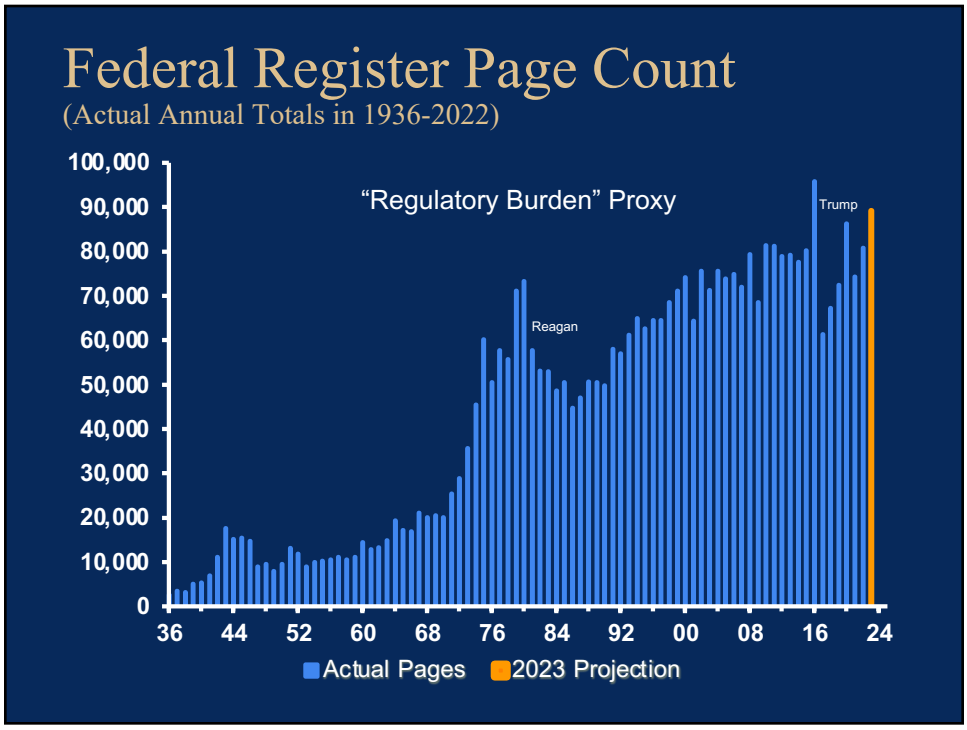
30


Federal Budget and Zempel Zones ©
(Trillions) (Monthly) (12-Month Totals)
$8
$7
$6
$5
$4
$3
$2
$1
$0
-$1
-$2
-$3
-$4
-$5
80
84
88
92
96
00
04
08
12
16
20
Recession
Caution
Alert
Net Surplus/Deficit
Outlays
Receipts

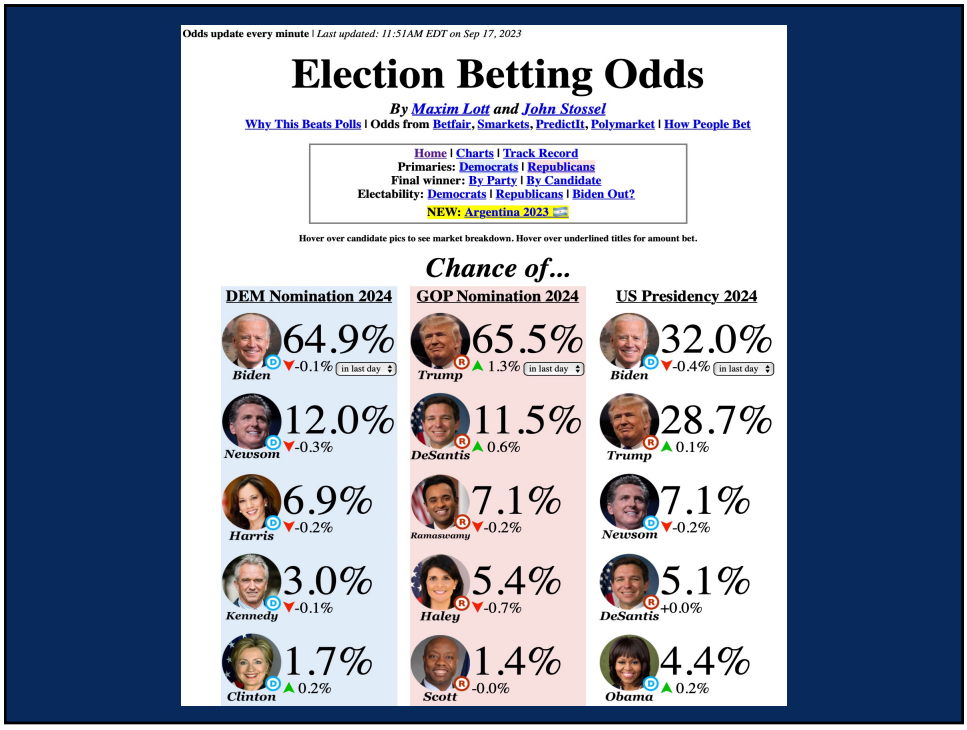
31


Hutchins Center Fiscal Impact Measure
(GDP Growth Contributions)
15%
10%
5%
0%
-5%
Q2 2020
Q1 2021
Stimulus
Drag
Q2 2022
00
02
04
06
08
10
12
14
16
18
20
22
24
Recession
Quarterly Impact
Four-Quarter Average

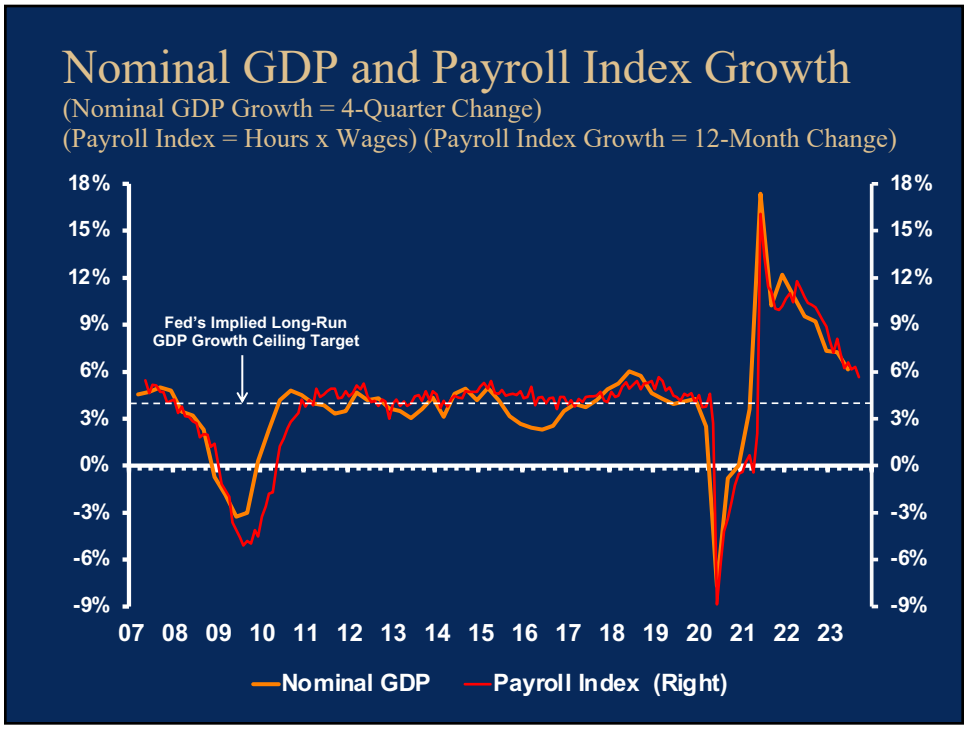
32


Federal Register Page Count
(Actual Annual Totals in 1936-2022)
"Regulatory Burden" Proxy
Reagan
Trump
100,000
90,000
80,000
70,000
60,000
50,000
40,000
30,000
20,000
10,000
0
36 44 52 60 68 76 84 92 00 08 16 24
Actual Pages
2023 Projection

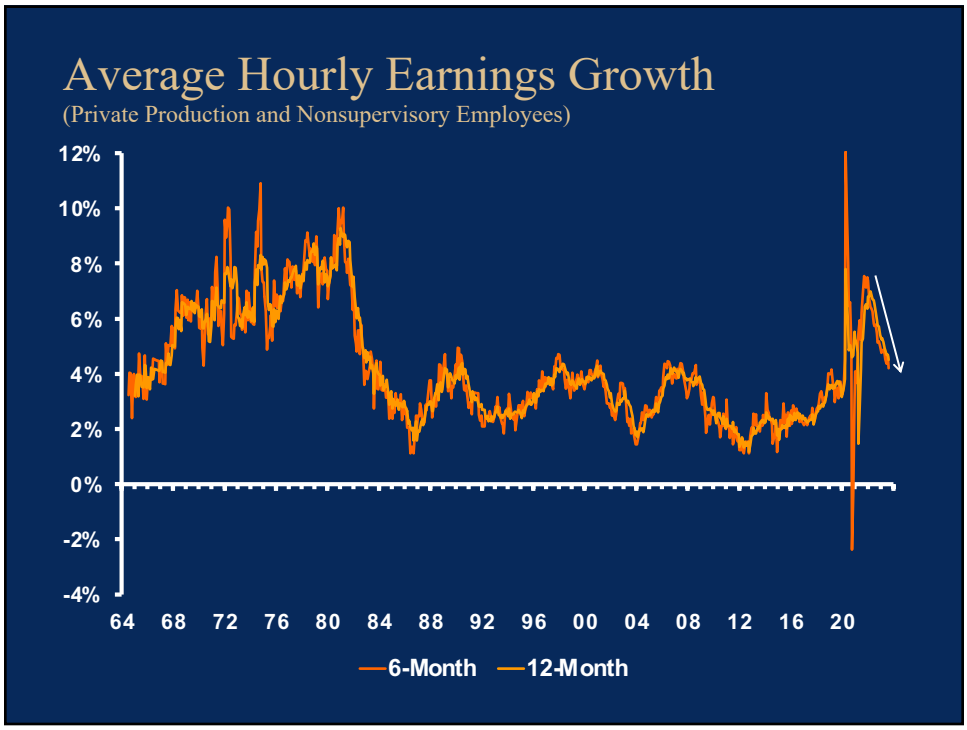
33


Odds update every minute | Last updated: 11:51AM EDT on Sep 17, 2023
Election Betting Odds
By Maxim Lott and John Stossel
Why This Beats Polls | Odds from Betfair, Smarkets, PredictIt, Polymarket | How People Bet
Home | Charts | Track Record
Primaries: Democrats | Republicans
Final winner: By Party | By Candidate
Electability: Democrats | Republicans | Biden Out?
NEW: Argentina 2023
Hover over candidate pics to see market breakdown. Hover over underlined titles for amount bet.
Chance of...
DEM Nomination 2024
Biden 64.9% -0.1% in last day
Newsom 12.0% -0.3%
Harris 6.9% -0.2%
Kennedy 3.0% -0.1%
Clinton 1.7% 0.2%
GOP Nomination 2024
Trump 65.5% 1.3% in last day
DeSantis 11.5% 0.6%
Ramaswamy 7.1% -0.2%
Haley 5.4% -0.7%
Scott 1.4% -0.0%
US Presidency 2024
Biden 32.0% -0.4% in last day
Trump 28.7% 0.1%
Newsom 7.1% -0.2%
DeSantis 5.1% +0.0%
Obama 4.4% 0.2%

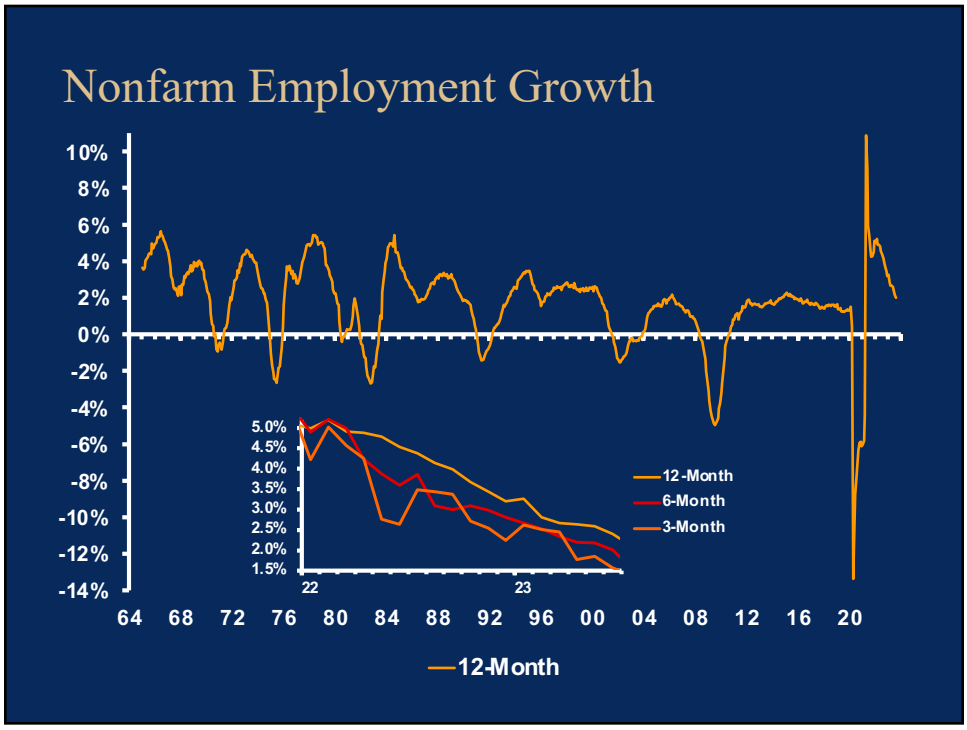
34


Nominal GDP and Payroll Index Growth
(Nominal GDP Growth = 4-Quarter Change)
(Payroll Index = Hours x Wages) (Payroll Index Growth = 12-Month Change)
18%
15%
12%
9%
6%
3%
0%
-3%
-6%
-9%
Fed's Implied Long-Run
GDP Growth Ceiling Target
07 08 09 10 11 12 13 14 15 16 17 18 19 20 21 22 23
Nominal GDP
Payroll Index (Right)

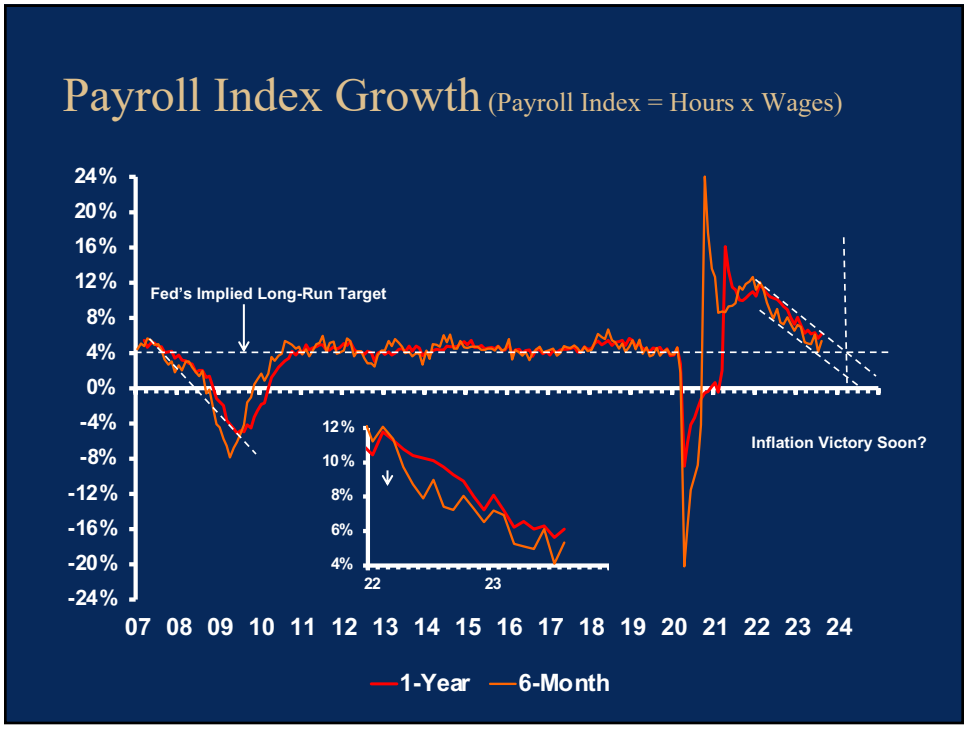
35


Average Hourly Earnings Growth
(Private Production and Nonsupervisory Employees)
12%
10%
8%
6%
4%
2%
0%
-2%
-4%
64 68 72 76 80 84 88 92 96 00 04 08 12 16 20
6-Month
12-Month

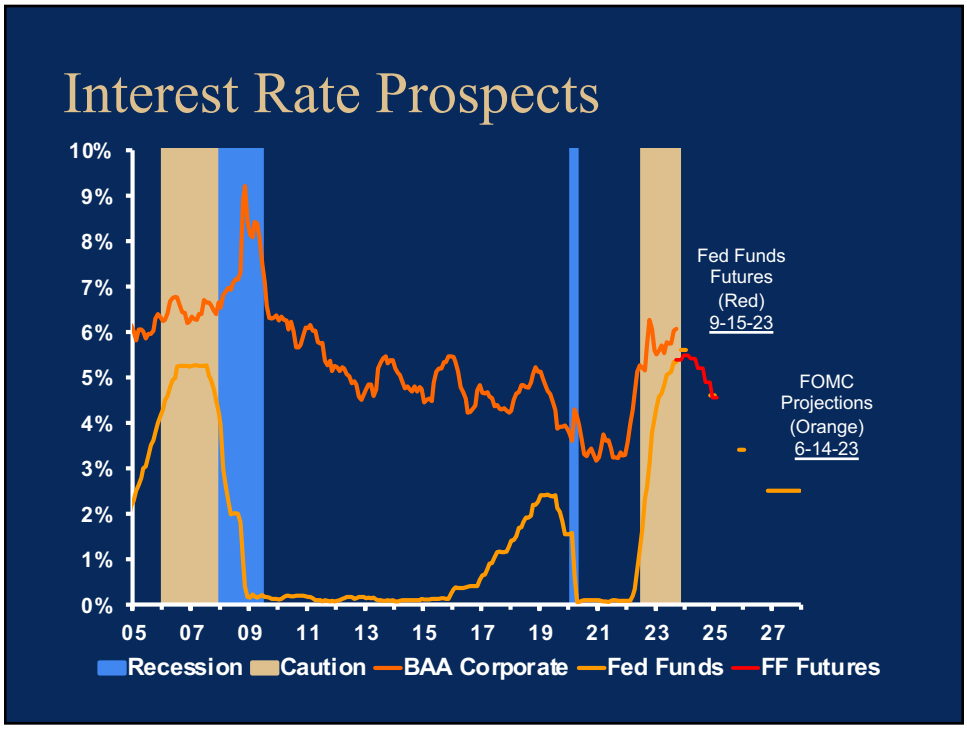
36


Nonfarm Employment Growth
10%
8%
6%
4%
2%
0%
-2%
-4%
-6%
-8%
-10%
-12%
-14%
64 68 72 76 80 84 88 92 96 00 04 08 12 16 20
12-Month
5.0%
4.5%
4.0%
3.5%
3.0%
2.5%
2.0%
1.5%
22 23
12-Month
6-Month
3-Month

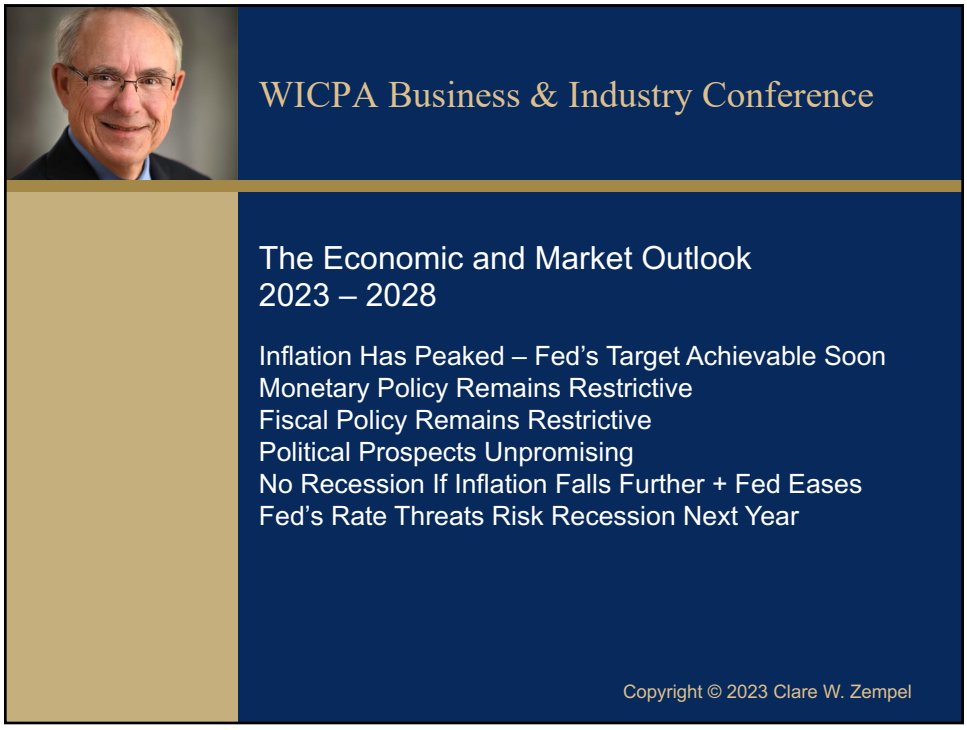
37


Payroll Index Growth (Payroll Index = Hours x Wages)
24%
20%
16%
12%
8%
4%
0%
-4%
-8%
-12%
-16%
-20%
-24%
Fed's Implied Long-Run Target
Inflation Victory Soon?
07 08 09 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24
12%
10%
8%
6%
4%
22 23
1-Year
6-Month

38


Interest Rate Prospects
10%
9%
8%
7%
6%
5%
4%
3%
2%
1%
0%
05 07 09 11 13 15 17 19 21 23 25 27
Fed Funds Futures (Red) 9-15-23
FOMC Projections (Orange) 6-14-23
Recession
Caution
BAA Corporate
Fed Funds
FF Futures

39


WICPA Business & Industry Conference
The Economic and Market Outlook
2023 – 2028
Inflation Has Peaked – Fed's Target Achievable Soon
Monetary Policy Remains Restrictive
Fiscal Policy Remains Restrictive
Political Prospects Unpromising
No Recession If Inflation Falls Further + Fed Eases
Fed's Rate Threats Risk Recession Next Year
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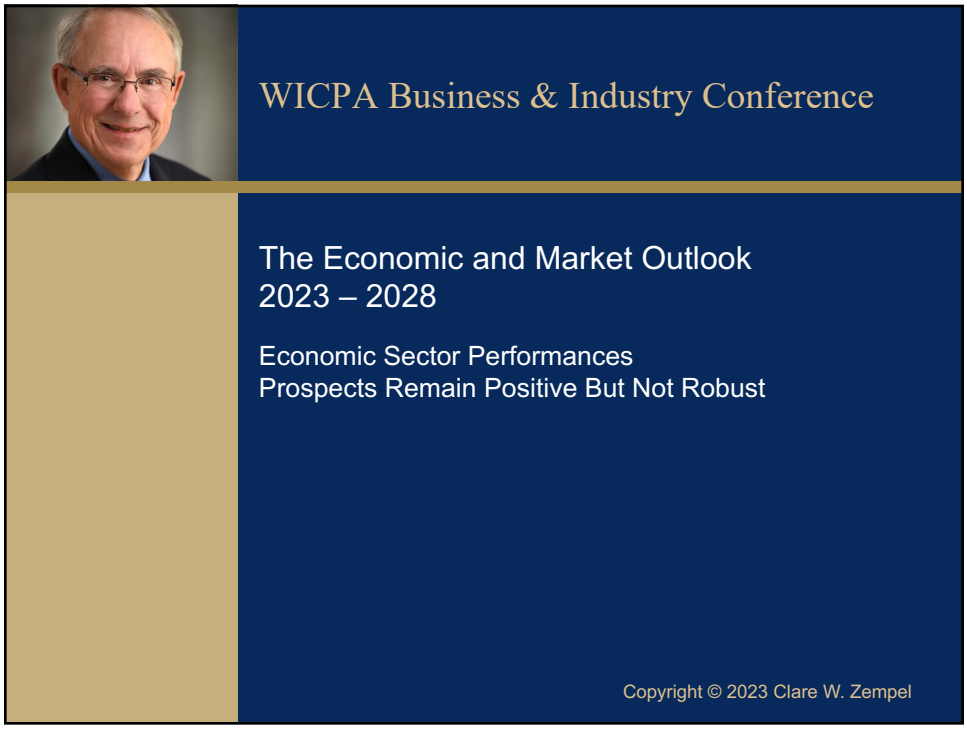
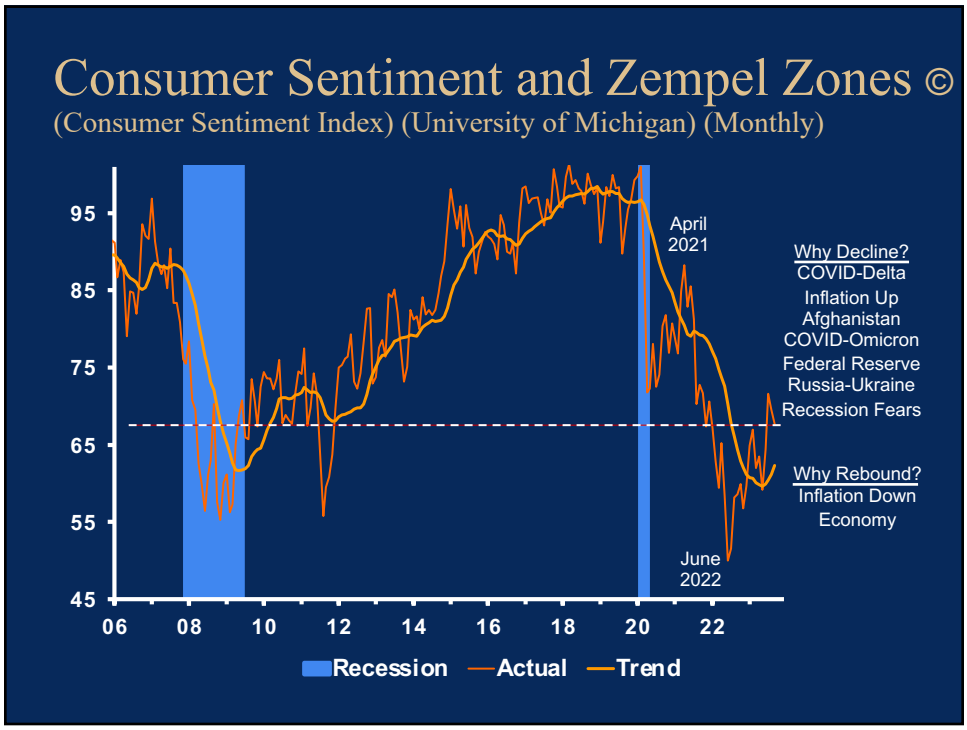
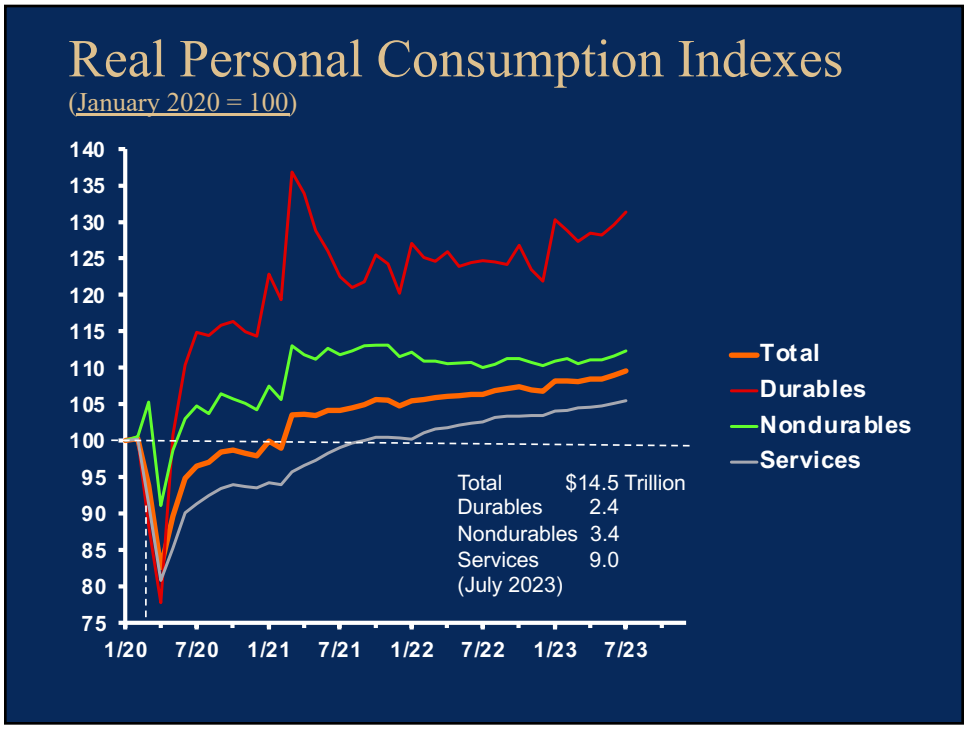
40


WICPA Business & Industry Conference
The Economic and Market Outlook
2023 – 2028
Economic Sector Performances
Prospects Remain Positive But Not Robust
Copyright © 2023 Clare W. Zempel

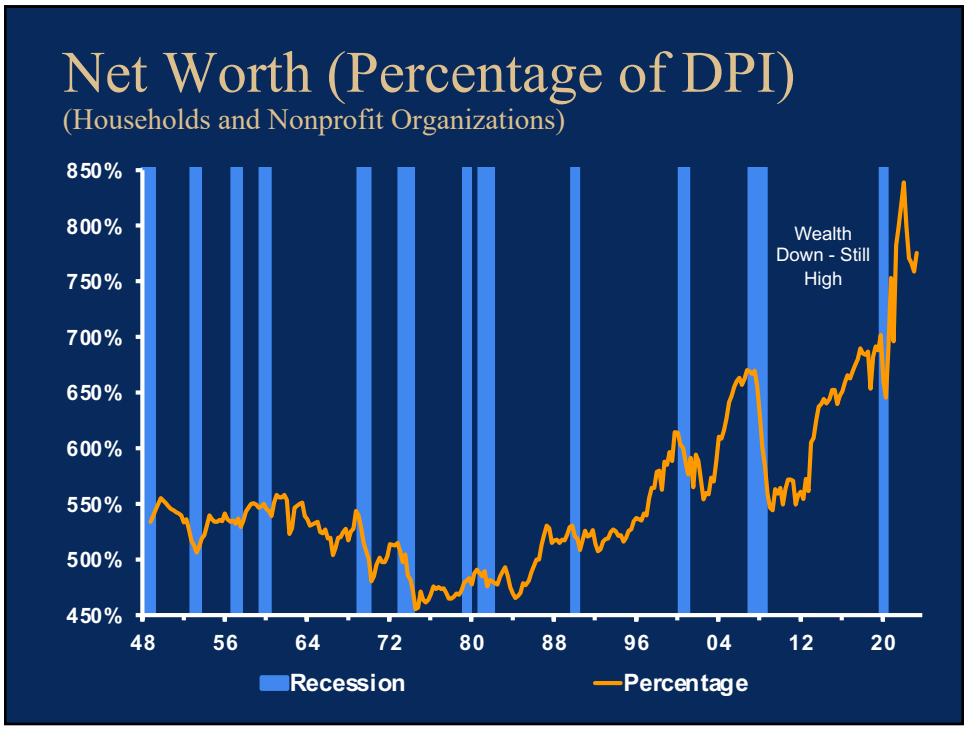
41


Consumer Sentiment and Zempel Zones ©
(Consumer Sentiment Index) (University of Michigan) (Monthly)
95
85
75
65
55
45
06
08
10
12
14
16
18
20
22
April
2021
June
2022
Why Decline?
COVID-Delta
Inflation Up
Afghanistan
COVID-Omicron
Federal Reserve
Russia-Ukraine
Recession Fears
Why Rebound?
Inflation Down
Economy
Recession
Actual
Trend

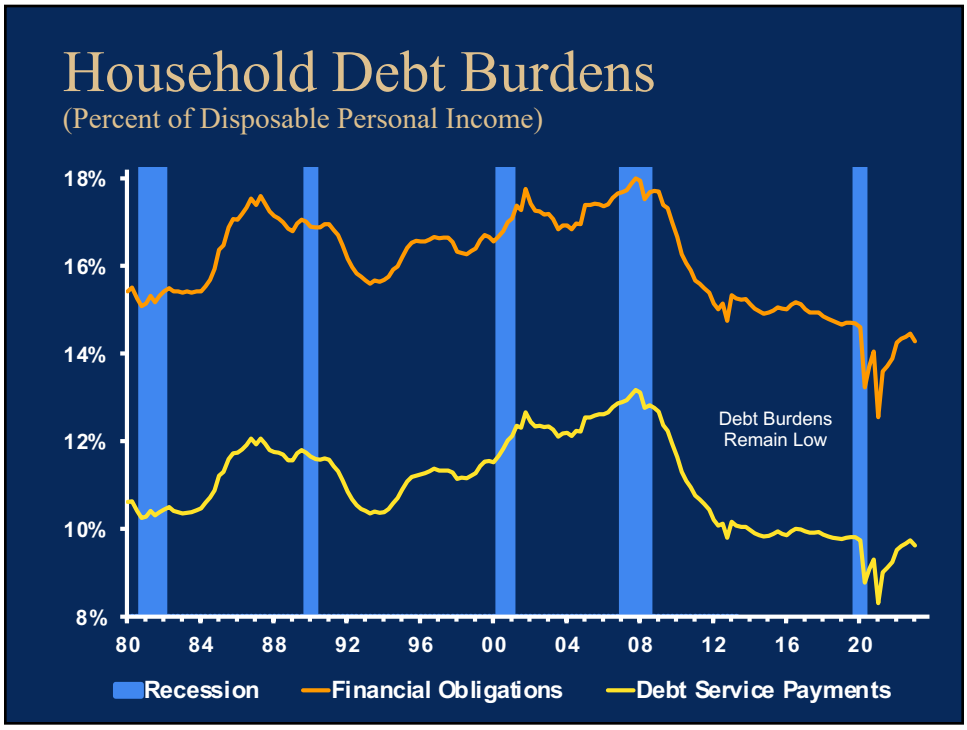
42


Real Personal Consumption Indexes
(January 2020 = 100)
140
135
130
125
120
115
110
105
100
95
90
85
80
75
1/20
7/20
1/21
7/21
1/22
7/22
1/23
7/23
Total
Durables
Nondurables
Services
Total $14.5 Trillion
Durables 2.4
Nondurables 3.4
Services 9.0
(July 2023)

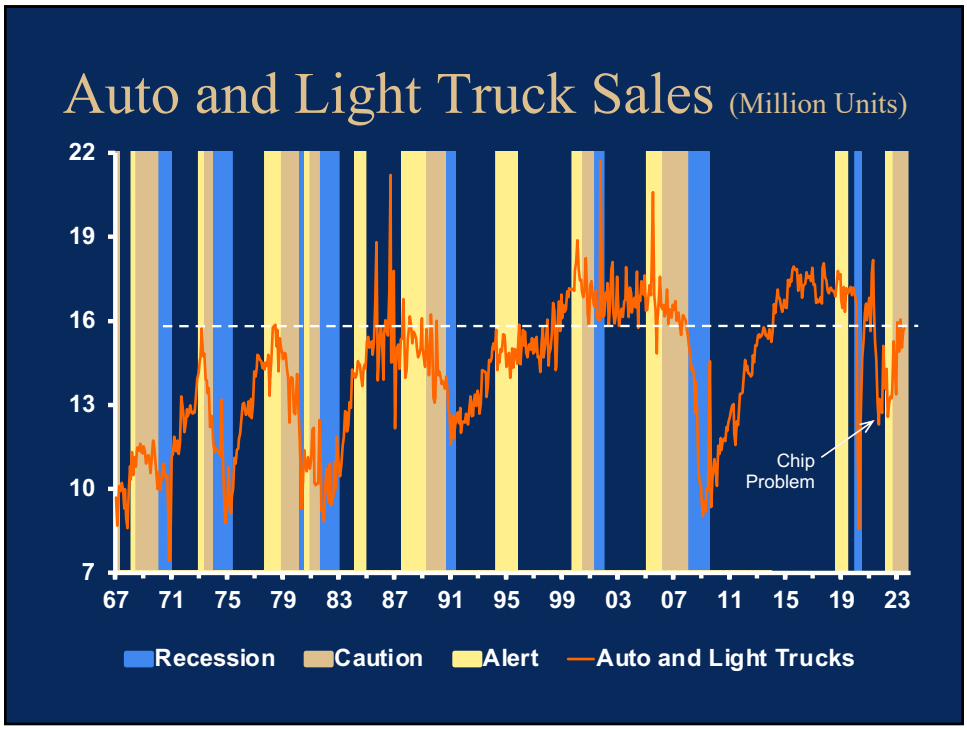
43


Net Worth (Percentage of DPI)
(Households and Nonprofit Organizations)
850%
800%
750%
700%
650%
600%
550%
500%
450%
48
56
64
72
80
88
96
04
12
20
Wealth
Down - Still
High
Recession
Percentage

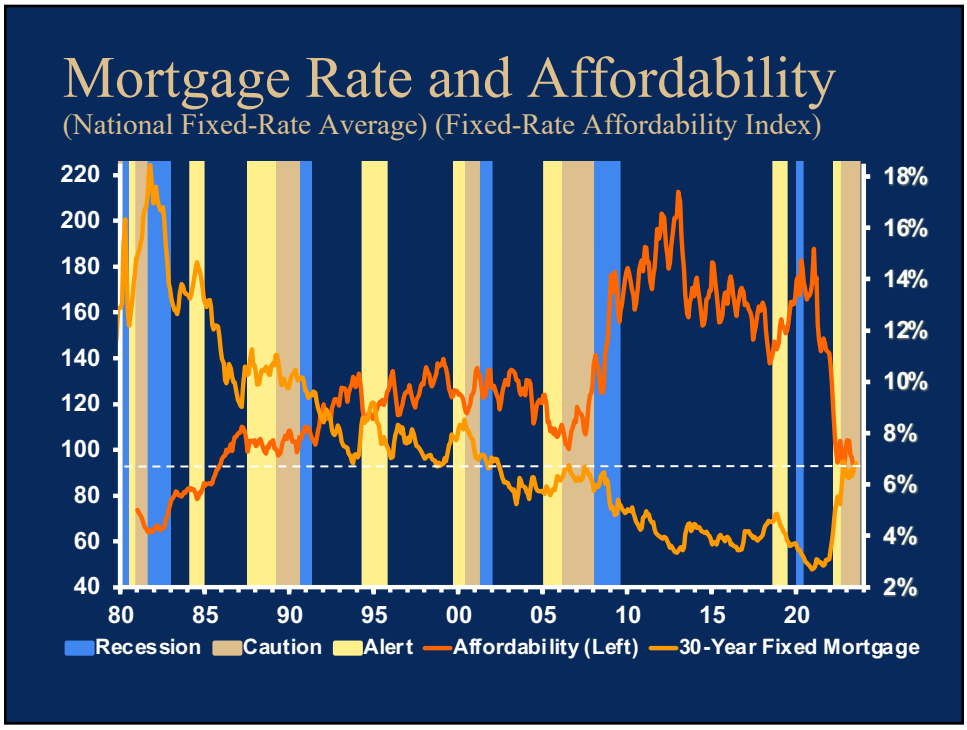
44


Household Debt Burdens
(Percent of Disposable Personal Income)
18%
16%
14%
12%
10%
8%
80
84
88
92
96
00
04
08
12
16
20
Debt Burdens
Remain Low
Recession
Financial Obligations
Debt Service Payments

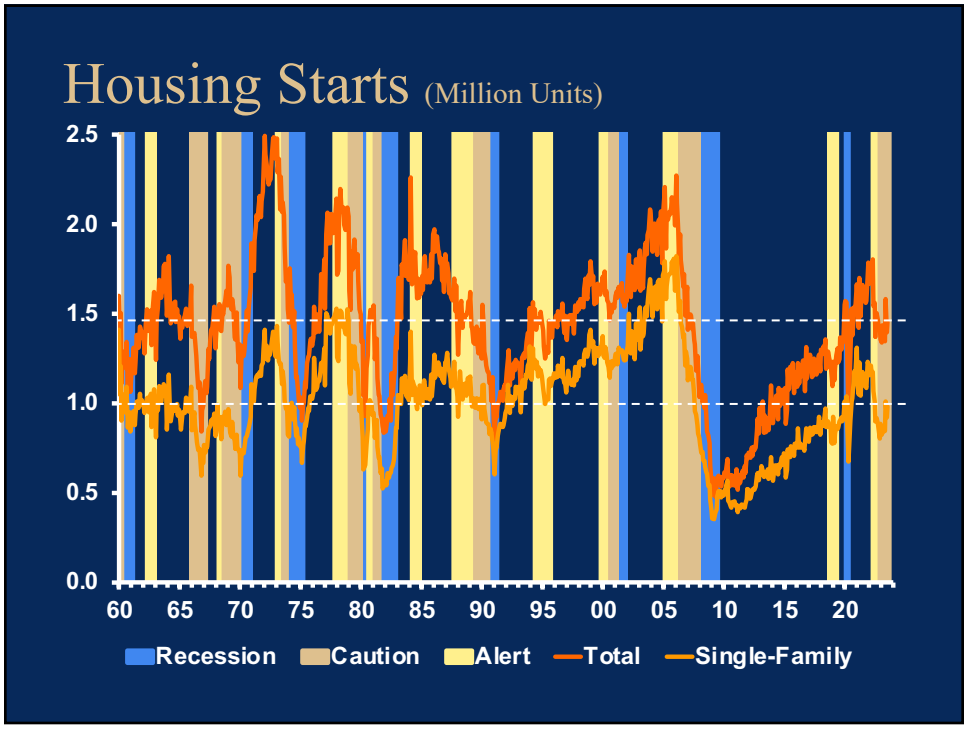
45


Auto and Light Truck Sales (Million Units)
22
19
16
13
10
7
67
71
75
79
83
87
91
95
99
03
07
11
15
19
23
Chip
Problem
Recession
Caution
Alert
Auto and Light Trucks

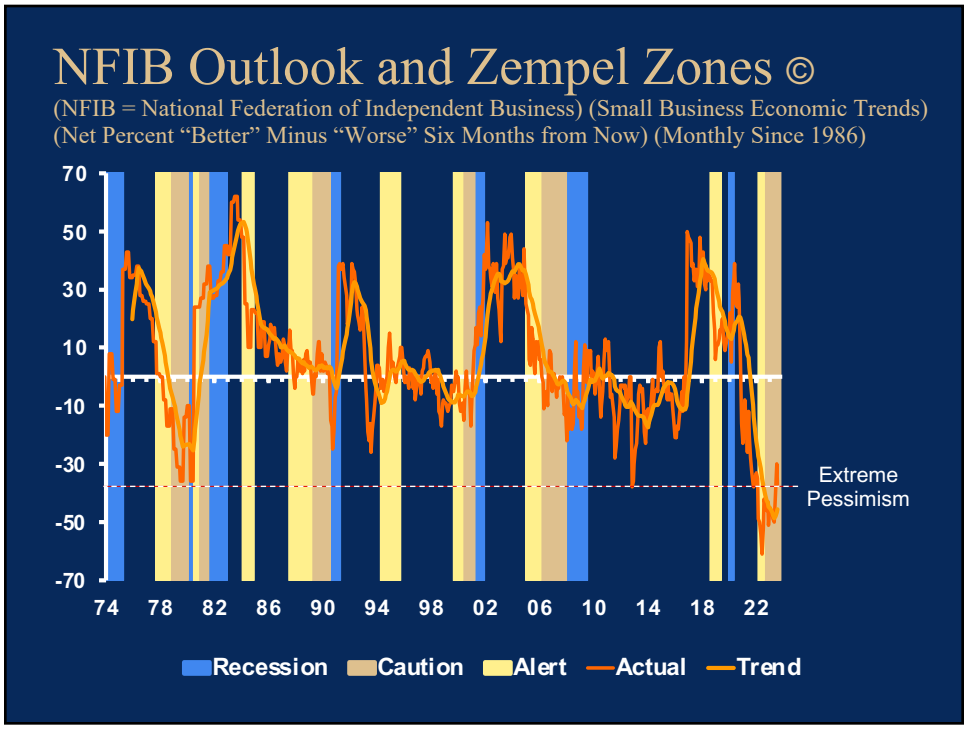
46


Mortgage Rate and Affordability
(National Fixed-Rate Average) (Fixed-Rate Affordability Index)
220
200
180
160
140
120
100
80
60
40
18%
16%
14%
12%
10%
8%
6%
4%
2%
80 85 90 95 00 05 10 15 20
Recession Caution Alert Affordability (Left) 30-Year Fixed Mortgage

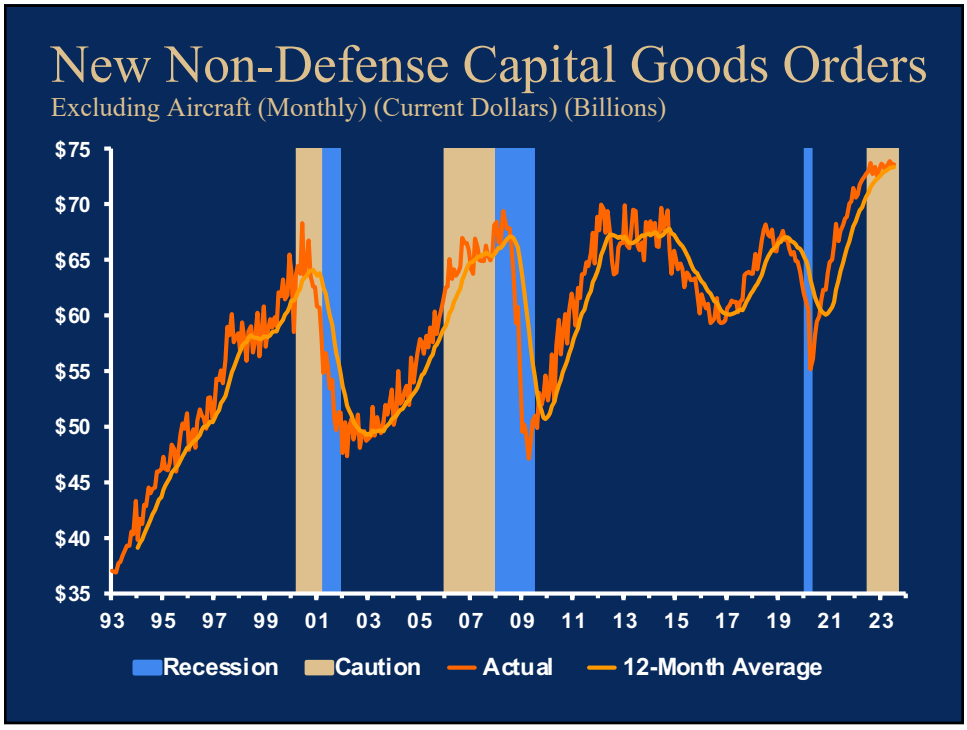
47


Housing Starts (Million Units)
2.5
2.0
1.5
1.0
0.5
0.0
60 65 70 75 80 85 90 95 00 05 10 15 20
Recession Caution Alert Total Single-Family

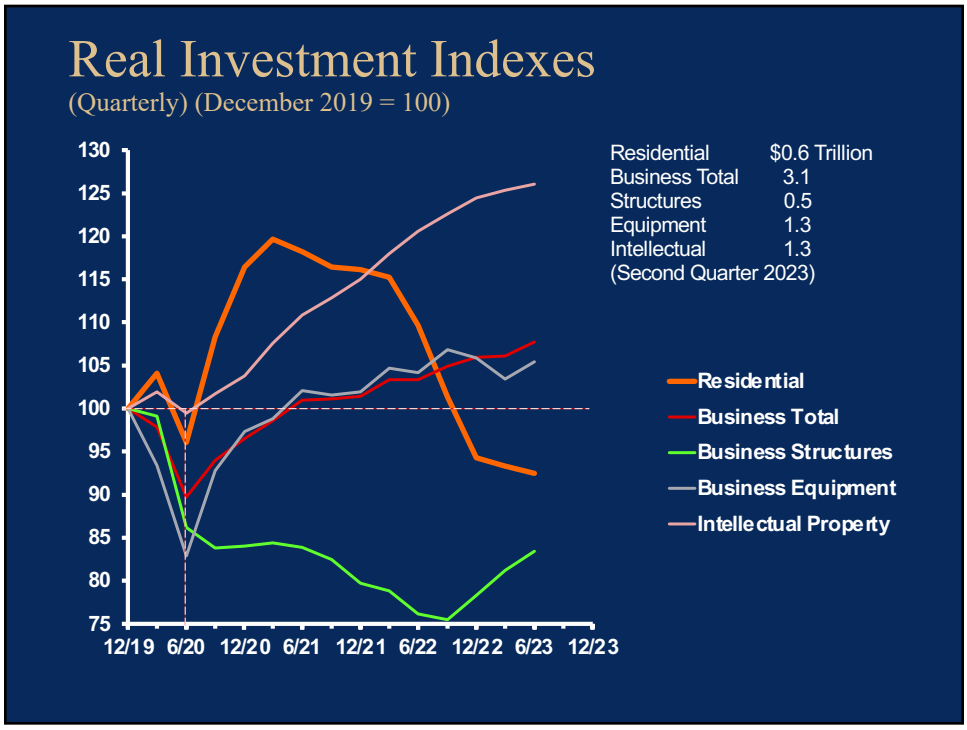
48


NFIB Outlook and Zempel Zones ©
(NFIB = National Federation of Independent Business) (Small Business Economic Trends)
(Net Percent "Better" Minus "Worse" Six Months from Now) (Monthly Since 1986)
70
50
30
10
-10
-30
-50
-70
74 78 82 86 90 94 98 02 06 10 14 18 22
Extreme Pessimism
Recession Caution Alert Actual Trend

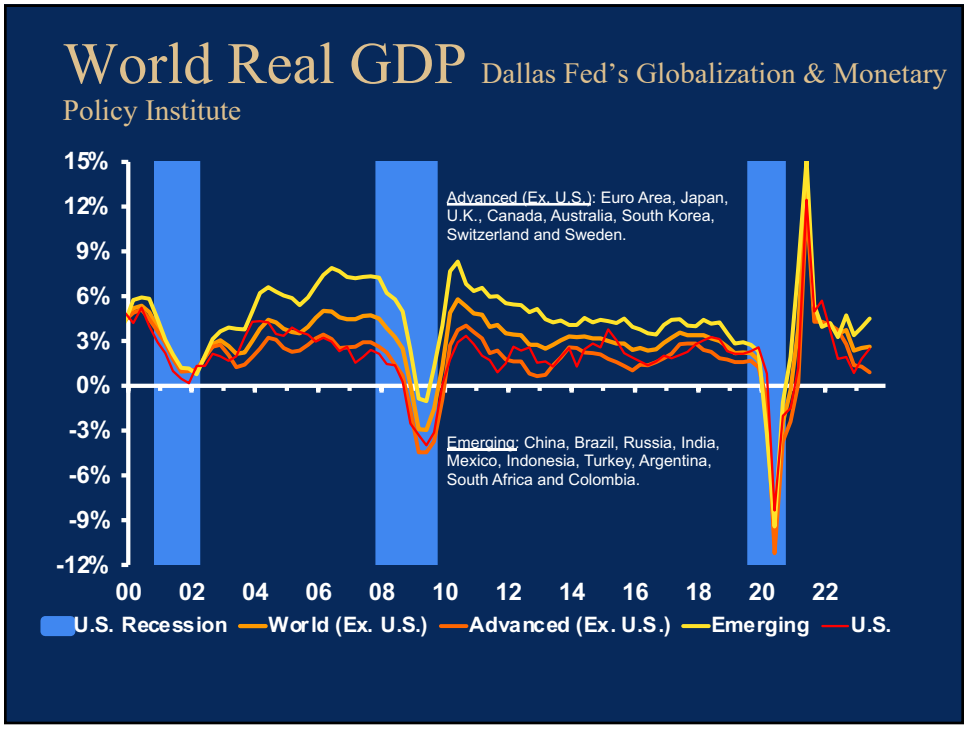
49


New Non-Defense Capital Goods Orders
Excluding Aircraft (Monthly) (Current Dollars) (Billions)
$75
$70
$65
$60
$55
$50
$45
$40
$35
93 95 97 99 01 03 05 07 09 11 13 15 17 19 21 23
Recession Caution Actual 12-Month Average

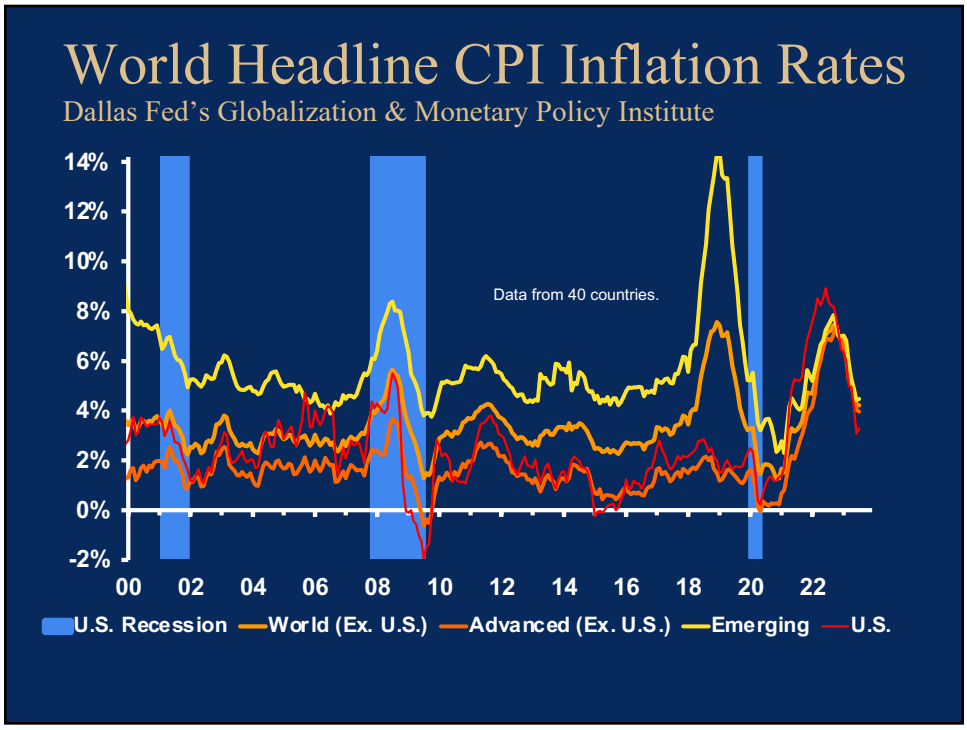
50


Real Investment Indexes
(Quarterly) (December 2019 = 100)
130
125
120
115
110
105
100
95
90
85
80
75
12/19 6/20 12/20 6/21 12/21 6/22 12/22 6/23 12/23
Residential $0.6 Trillion
Business Total 3.1
Structures 0.5
Equipment 1.3
Intellectual 1.3
(Second Quarter 2023)
Residential
Business Total
Business Structures
Business Equipment
Intellectual Property

51


World Real GDP Dallas Fed's Globalization & Monetary Policy Institute
15%
12%
9%
6%
3%
0%
-3%
-6%
-9%
-12%
00 02 04 06 08 10 12 14 16 18 20 22
Advanced (Ex. U.S.): Euro Area, Japan, U.K., Canada, Australia, South Korea, Switzerland and Sweden.
Emerging: China, Brazil, Russia, India, Mexico, Indonesia, Turkey, Argentina, South Africa and Colombia.
U.S. Recession
World (Ex. U.S.)
Advanced (Ex. U.S.)
Emerging
U.S.

52


World Headline CPI Inflation Rates
Dallas Fed's Globalization & Monetary Policy Institute
14%
12%
10%
8%
6%
4%
2%
0%
-2%
Data from 40 countries.
00 02 04 06 08 10 12 14 16 18 20 22
U.S. Recession
World (Ex. U.S.)
Advanced (Ex. U.S.)
Emerging
U.S.

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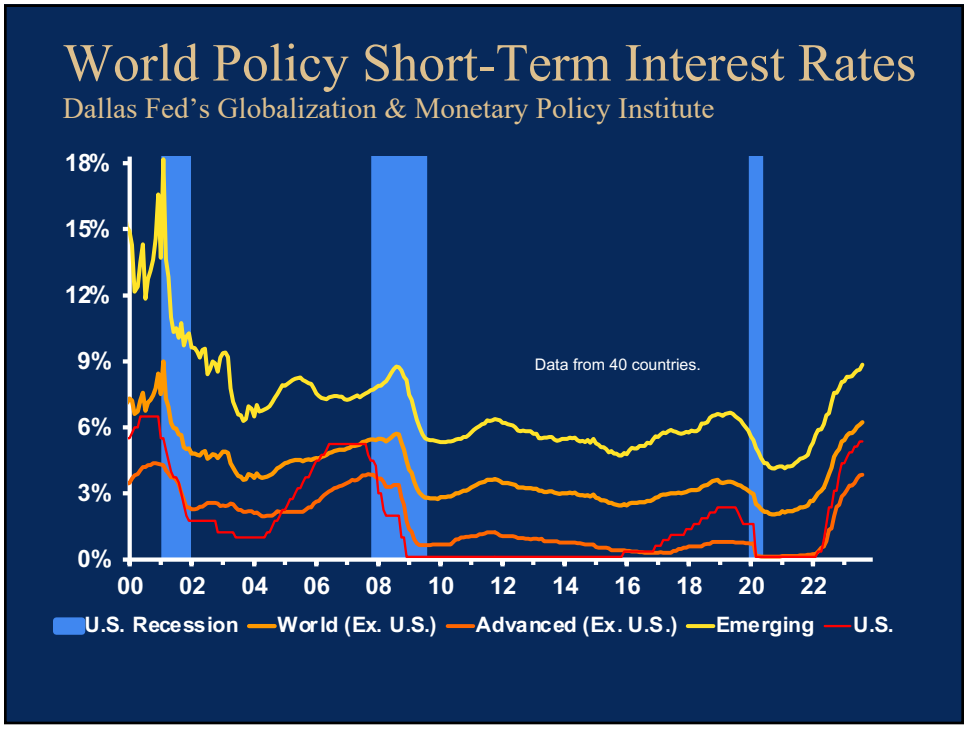
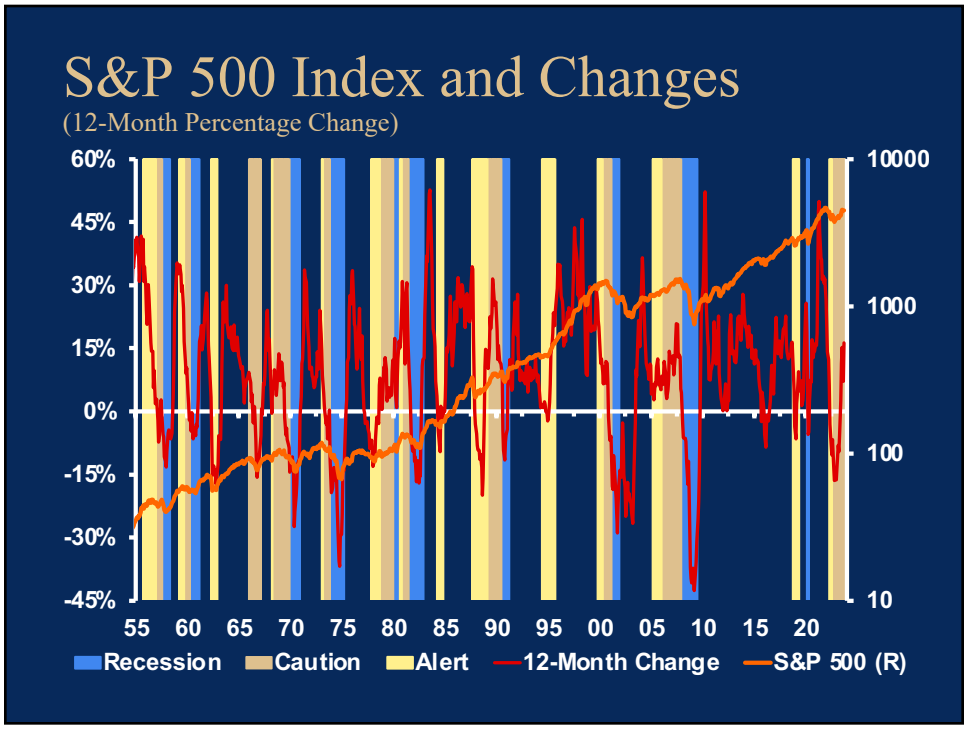

World Policy Short-Term Interest Rates
Dallas Fed's Globalization & Monetary Policy Institute
18%
15%
12%
9%
6%
3%
0%
Data from 40 countries.
00 02 04 06 08 10 12 14 16 18 20 22
U.S. Recession
World (Ex. U.S.)
Advanced (Ex. U.S.)
Emerging
U.S.

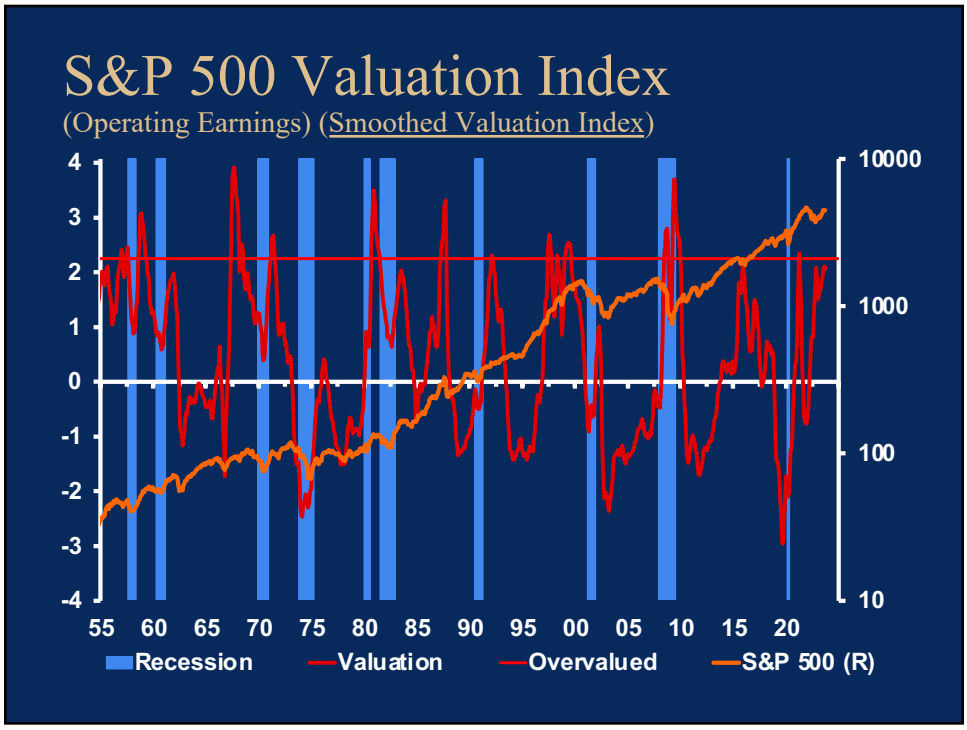
54


S&P 500 Index and Changes
(12-Month Percentage Change)
60%
45%
30%
15%
0%
-15%
-30%
-45%
10000
1000
100
10
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
Caution
Alert
12-Month Change
S&P 500 (R)

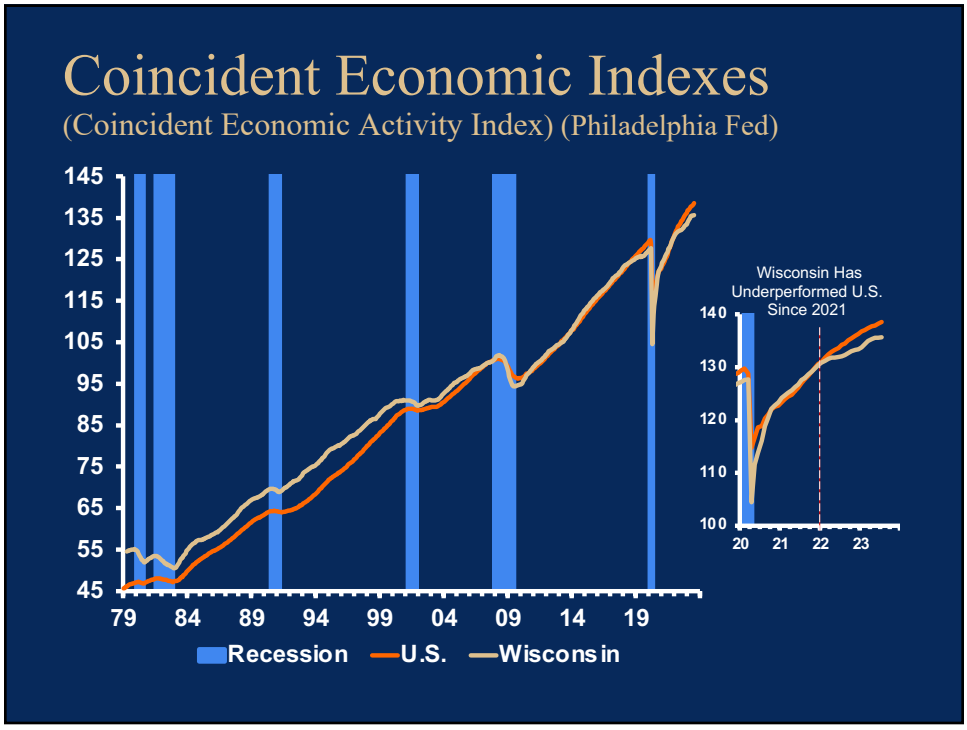
55

WICPA Business & Industry Conference
Stock Market Model Components
Momentum
Interest-Rate Changes
Valuation
Stock Market Valuation Index Concepts
Ratio = Bond Yield / Earnings Yield
Earnings Yield = E/P
Valuation Index = Normalized Ratio
Bond Yield = Moody's BAA Corporate Bond Yield
E = Trailing Year Operating Earnings
P = S&P 500 Index
Normalization = (Actual – Mean) / Standard Deviation

56


S&P 500 Valuation Index
(Operating Earnings) (Smoothed Valuation Index)
4
3
2
1
0
-1
-2
-3
-4
10000
1000
100
10
55 60 65 70 75 80 85 90 95 00 05 10 15 20
Recession
Valuation
Overvalued
S&P 500 (R)

57


Coincident Economic Indexes
(Coincident Economic Activity Index) (Philadelphia Fed)
145
135
125
115
105
95
85
75
65
55
45
79 84 89 94 99 04 09 14 19
Recession
U.S.
Wisconsin
Wisconsin Has Underperformed U.S. Since 2021
140
130
120
110
100
20 21 22 23

58

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The Economic and Market Outlook
2023 – 2028
Has Recession Started? No
What Do "Best Indicators" Predict? Slowdown + Recession
Can Recession Be Averted? Or Downside Limited? Yes
Best Case? Inflation Slows Further + Fed Tempers Hawkishness
How Would Sectors Perform Then? Moderate Expansion
Worst Case? Fed's Hawkishness Triggers 2024 Downturn
What to do now depends on sensitivity to economic slowdowns.
"Alert Zone" means temper optimism.
"Caution Zone" now means plan for recession.
Delay implementation until jobless claims soar or own orders drop.
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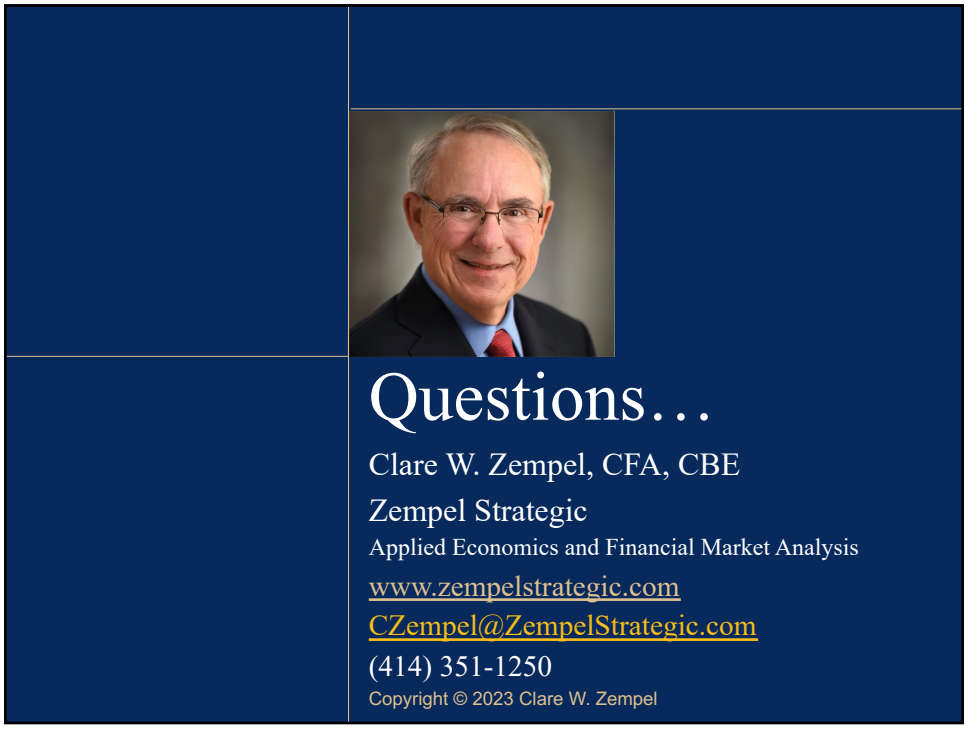
Questions…
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9:35 – 10:35 a.m.

Accounting & Tax Update

Jim Brandenburg, CPA, MST, *Tax Partner, Sikich LLP*

Brad Hermes, CPA, *Partner, Sikich LLP*

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ACCOUNTING TECHNOLOGY ADVISORY

WICPA Fall Conference – Brookfield, WI

2023 TAX UPDATES

JIM BRANDENBURG, CPA, MST – SIKICH, LLP

SIKICH.COM

MONDAY, SEPTEMBER 18, 2023

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THE AGENDA

- 2022 TAX LEGISLATION – "SECURE 2.0"
- 2023 TAX LEGISLATION
- EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

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2022 TAX LEGISLATION

SECURE 2.0

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"OMNIBUS SPENDING BILL" (CONSOLIDATED APPROPRIATIONS ACT, 2023)

- **Passed Congress December 23, 2022**
- **Signed into law December 29, 2022**
- **Included "SECURE 2.0" Retirement Package**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 "SECURE 2.0" RETIREMENT BILL

- RETIREMENT LEGISLATION WITH MANY FAVORABLE PROVISIONS FOR EMPLOYEES, PARTICIPANTS, AND RETIREES.
- COMMONLY REFERRED TO AS "SECURE 2.0."
- BILL PASSED HOUSE BY WIDE MARGIN ON MARCH 29, 2022.
- SIMILAR BILL, "EARN," PASSED BY SENATE FINANCE COMMITTEE IN JUNE, 2022. *"ENHANCING AMERICAN RETIREMENT NOW" (EARN).*
- BI-PARTISAN SUPPORT.
- FOLLOWS UP ON MANY RETIREMENT PROVISIONS IN **"SECURE 1.0"** ENACTED IN 2019.

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RECAP OF "SECURE ACT OF 2019" ("SECURE 1.0")

"SECURE 1.0" ENACTED DECEMBER 20, 2019 – SELECTED PROVISIONS:

- MANDATES MOST NON-SPOUSES INHERITING IRAS FULLY DISTRIBUTE THE ACCOUNT WITHIN TEN YEARS.
- PROVIDES MODIFICATIONS TO RETIREMENT PLANS TO ALLOW SMALL BUSINESSES TO SET PLANS UP EASIER AND WITH LESS ADMIN COSTS. ALLOWS PART-TIME EMPLOYEES TO PARTICIPATE.
- REQUIRED MINIMUM DISTRIBUTIONS (RMDS) STARTING AGE MOVED FROM 70½ TO 72.
- ALLOWS THE USE OF SECTION 529 ACCOUNTS FOR QUALIFIED STUDENT LOAN REPAYMENTS UP TO $10,000 ANNUALLY.
- PERMITS PENALTY-FREE WITHDRAWALS OF $5,000 FROM 401(K) ACCOUNTS FOR BIRTH OR ADOPTION OF A CHILD.

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RECAP OF "SECURE ACT OF 2019" ("SECURE 1.0")

"SECURE 1.0" ENACTED DECEMBER 20, 2019 – SELECTED PROVISIONS:

- MANDATES MOST NON-SPOUSES INHERITING IRAS FULLY DISTRIBUTE THE ACCOUNT WITHIN TEN YEARS.
- INITIAL INTERPRETATION: DISTRIBUTE FUNDS AT ANY TIME DURING THE 10-YEAR PAYOUT WINDOW, INCLUDING WAITING UNTIL THE 10TH YEAR BEFORE TAKING ANY DISTRIBUTIONS
- GUIDANCE IN PROPOSED REGULATIONS ISSUED FEBRUARY 23, 2022: WHEN DEATH OCCURS ON OR AFTER THE ACCOUNT HOLDER'S REQUIRED BEGINNING DATE, RMDS ARE REQUIRED IN YEAR ONE THROUGH YEAR NINE, WITH THE REMAINING BALANCE REQUIRED TO BE WITHDRAWN IN YEAR TEN.

➢Does not apply for a ROTH IRA, but watch potential five-year rule applicability.

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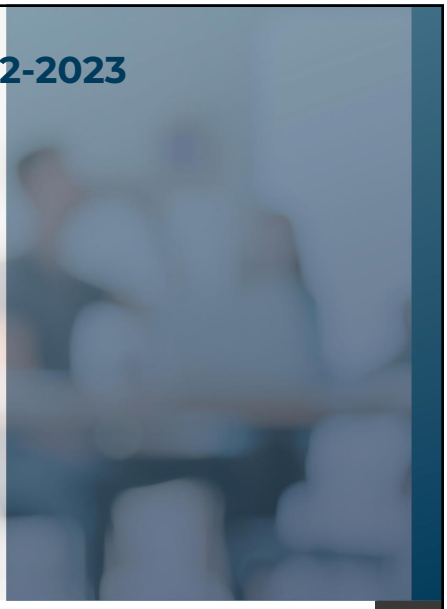
FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL



- BILL MOVED TO FULL SENATE WHERE IT ALSO HAD BI-PARTISAN SUPPORT.
- WHILE SECURE 2.0 HAD STRONG BI-PARTISAN BACKING IN BOTH THE HOUSE AND SENATE, DIFFERENCES NEEDED TO BE RECONCILED.
- FINAL PASSAGE OF SECURE 2.0 OCCURRED LATE IN 2022 AS PART OF OMNIBUS SPENDING BILL ("CONSOLIDATED APPROPRIATIONS ACT, 2023"), IN "LAME DUCK SESSION" OF CONGRESS FOLLOWING NOVEMBER, 2022 ELECTIONS.
- RELATIVELY MINOR DIFFERENCES IN HOUSE AND SENATE VERSIONS OF THEIR RETIREMENT BILLS RESOLVED BY SENATE AND HOUSE TAX COMMITTEE LEADERS.
- **WATCH CLOSELY THE EFFECTIVE DATES OF SECURE 2.0 PROVISIONS.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- EXPANDING AUTOMATIC ENROLLMENT IN RETIREMENT PLANS **(ACT §101)**.
- PROVISION REQUIRES 401(K) AND 403(B) PLANS TO AUTOMATICALLY ENROLL PARTICIPANTS IN PLANS UPON BECOMING ELIGIBLE.
- EMPLOYEES MAY OPT OUT OF COVERAGE.
- INITIAL AUTOMATIC ENROLLMENT AMOUNT IS ≥ 3% BUT < 10%.
- INCREASES 1% PER YEAR UNTIL REACHES ≥ 10%, BUT ≤ 15%.
  - Exception for small businesses with ≤ 10 employees; new businesses (in business for < 3 years); church plans; and governmental plans.
- **EFFECTIVE FOR PLAN YEARS AFTER 2024.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- MODIFICATION OF CREDIT FOR SMALL EMPLOYER PENSION PLAN STARTUP COSTS **(ACT §102)**.
- THE THREE-YEAR SMALL BUSINESS START-UP CREDIT IS CURRENTLY 50% OF ADMINISTRATIVE COSTS, UP TO ANNUAL CAP OF $5,000.
- BILL INCREASES START-UP CREDIT FROM 50% TO 100% FOR EMPLOYERS WITH UP TO 50 EMPLOYEES.
- CREDIT PHASED OUT FOR EMPLOYERS WITH 51-100 EMPLOYEES.
- IN ADDITION, BILL PROVIDES ADDITIONAL CREDIT, EXCEPT FOR DEFINED BENEFIT PLANS.
- **EFFECTIVE FOR TAX YEARS AFTER 2022.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- INCREASE IN AGE FOR REQUIRED BEGINNING DATE FOR MANDATORY DISTRIBUTIONS (RMD). (**ACT §107**).
- UNDER CURRENT LAW, PARTICIPANTS ARE GENERALLY REQUIRED TO BEGIN TAKING DISTRIBUTIONS AT AGE 72.
- SECURE 2.0 INCREASES RMD AGE TO **AGE 73 STARTING ON 1/1/2023.**
- SECURE 2.0 INCREASES RMD **AGE 75 STARTING ON 1/1/2033**.

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- MATCHING PAYMENTS FOR ELECTIVE DEFERRAL AND IRA CONTRIBUTIONS BY CERTAIN INDIVIDUALS. "SAVER'S MATCH." **(ACT §103).**
- PROVISION WOULD MODIFY CREDIT FOR IRAS AND RETIREMENT CONTRIBUTIONS BY CHANGING IT FROM A CREDIT PAID IN CASH, TO A "GOVERNMENT MATCHING CONTRIBUTION" THAT MUST BE DEPOSITED INTO THE PARTICIPANT'S IRA OR RETIREMENT ACCOUNT.
- CREDIT WOULD BE 50% OF CONTRIBUTION TO IRA OR RETIREMENT ACCOUNT, WITH A MAXIMUM OF $2,000.
- CREDIT WOULD BE SUBJECT TO A PHASE-OUT BETWEEN $41,000 TO $71,000 OF AGI.
- **PROVISION TAKES EFFECT IN 2027.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- HIGHER CATCH-UP LIMIT TO APPLY AT AGES 60, 61, 62, AND 63. **(ACT §109)**.
- UNDER CURRENT LAW, EMPLOYEES WHO HAVE ATTAINED AGE 50 ARE PERMITTED TO MAKE "CATCH-UP CONTRIBUTIONS" UNDER A RETIREMENT PLAN IN EXCESS OF APPLICABLE LIMITS. GENERAL LIMIT ON CATCH-UP CONTRIBUTIONS FOR 2021 IS $6,500.
- SECURE 2.0 INCREASES THESE "CATCH-UP" LIMITS TO GREATER OF:
  1. $10,000;
  2. 50% more than regular catch-up amount in 2025,
- Applies for individuals aged 60, 61, 62, and 63.
- AMOUNTS INDEXED FOR INFLATION AFTER 2025.
- **EFFECTIVE FOR TAXABLE YEARS BEGINNING AFTER 2024.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- TREATMENT OF STUDENT LOAN PAYMENTS AS ELECTIVE DEFERRALS FOR PURPOSES OF MATCHING CONTRIBUTIONS. **(ACT §110)**.
- PROVISION INTENDED TO ASSIST EMPLOYEES WHO MAY NOT BE ABLE TO SAVE FOR RETIREMENT DUE TO THEIR STUDENT DEBT LOAD, AND THUS MISS OUT ON AVAILABLE MATCHING EMPLOYER CONTRIBUTIONS.
- BILL ALLOWS SUCH EMPLOYEES TO RECEIVE THOSE MATCHING CONTRIBUTIONS BY REASON OF REPAYING THEIR STUDENT LOANS.
- QUALIFIED STUDENT LOAN PAYMENT BROADLY DEFINED "AS ANY DEBT INCURRED BY EMPLOYEE SOLELY TO PAY QUALIFIED HIGHER EDUCATION EXPENSES OF THE EMPLOYEE."
- **EFFECTIVE FOR CONTRIBUTIONS MADE FOR PLAN YEARS AFTER 2023.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- DEFERRAL OF TAX FOR CERTAIN SALES OF EMPLOYER STOCK TO EMPLOYEE STOCK OWNERSHIP PLAN (ESOP) SPONSORED BY S CORPORATION. **(ACT §114).**
- SECTION 1042 PERMITS AN INDIVIDUAL OWNER OF STOCK IN A NON-PUBLICLY TRADED C CORPORATION WITH AN ESOP MAY ELECT TO DEFER GAIN RECOGNITION FROM STOCK SALE TO ESOP IF SELLER REINVESTS THE SALES PROCEEDS INTO QUALIFIED REPLACEMENT PROPERTY, PUBLICLY TRADED STOCKS/SECURITIES. AFTER SALE, ESOP MUST OWN ≥ 30% OF THE EMPLOYER'S STOCK.
- NEW LAW EXPANDS SECTION 1042 GAIN DEFERRAL PROVISIONS WITH A 10% LIMIT ON THE DEFERRAL TO SALES OF EMPLOYER STOCK TO S CORPORATION ESOPS.
- **EFFECTIVE FOR SALES MADE AFTER DECEMBER 31, 2027.**

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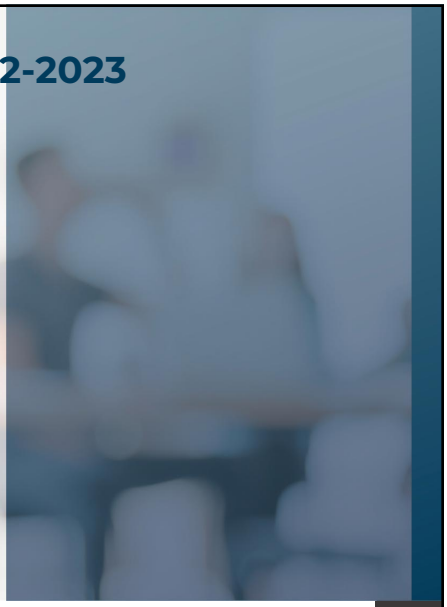
FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- BY REDUCTION IN EXCISE TAX ON CERTAIN ACCUMULATIONS IN QUALIFIED RETIREMENT PLANS **(ACT §302)**.
- THE BILL REDUCES PENALTY FOR FAILURE TO TAKE RMDS FROM 50% TO 25%.
- FURTHER, IF A FAILURE TO TAKE A RMD FROM AN IRA IS CORRECTED IN A TIMELY MANNER (WITHIN TWO TAX YEARS AFTER YEAR RMD SHOULD HAVE BEEN MADE), THE EXCISE TAX ON THE FAILURE IS FURTHER REDUCED FROM 25% TO 10%.
- EFFECTIVE FOR TAXABLE YEARS BEGINNING AFTER DATE OF ENACTMENT. BILL WAS ENACTED IN DECEMBER, 2022, THUS, **EFFECTIVE FOR TAX YEARS BEGINNING IN 2023**.



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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- ONE-TIME ELECTION FOR QUALIFIED CHARITABLE DISTRIBUTION TO SPLIT-INTEREST ENTITY; INCREASE IN QUALIFIED CHARITABLE DISTRIBUTION LIMITATION (ACT §307).
- THE BILL EXPANDS IRA CHARITABLE DISTRIBUTION PROVISION TO ALLOW FOR A ONE-TIME, $50,000 DISTRIBUTION TO CHARITIES THROUGH CHARITABLE GIFT ANNUITIES; CHARITABLE REMAINDER UNITRUSTS (CRUT); AND CHARITABLE REMAINDER ANNUITY TRUSTS (CRAT).
- EFFECTIVE FOR DISTRIBUTIONS MADE IN TAXABLE YEARS BEGINNING AFTER THE DATE OF ENACTMENT (2023 IN THIS CASE).
- THE BILL ALSO INDEXES FOR INFLATION, THE ANNUAL $100,000 IRA CHARITABLE DISTRIBUTION LIMITATION.
- EFFECTIVE FOR TAXABLE YEARS ENDING AFTER THE DATE OF ENACTMENT (2022).

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- EMPLOYER MAY RELY ON EMPLOYEE CERTIFYING THAT HARDSHIP DISTRIBUTION CONDITIONS ARE MET. (ACT §312).
- THE BILL PROVIDES THAT, UNDER CERTAIN CIRCUMSTANCES, EMPLOYEES WILL BE PERMITTED TO SELF-CERTIFY THAT THEY HAVE HAD AN EVENT THAT CONSTITUTES A HARDSHIP FOR PURPOSES OF TAKING A HARDSHIP WITHDRAWAL.
- EFFECTIVE FOR TAX YEARS AFTER 2022.

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- AMENDMENTS TO INCREASE BENEFIT ACCRUALS UNDER PLAN FOR PREVIOUS PLAN YEAR ALLOWED UNTIL EMPLOYER TAX RETURN DUE DATE. **(ACT §316)**.
- CURRENT LAW, HOWEVER, PROVIDES THAT PLAN AMENDMENTS TO AN EXISTING PLAN MUST GENERALLY BE ADOPTED BY THE LAST DAY OF THE PLAN YEAR IN WHICH THE AMENDMENT IS EFFECTIVE.
- THE BILL AMENDS THESE PROVISIONS TO ALLOW DISCRETIONARY AMENDMENTS THAT INCREASE PARTICIPANTS' BENEFITS TO BE ADOPTED BY THE DUE DATE OF THE EMPLOYER'S TAX RETURN.
- **EFFECTIVE FOR PLAN YEARS BEGINNING AFTER 2023.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- LONG-TERM CARE CONTRACTS PURCHASED WITH RETIREMENT ACCOUNT DISTRIBUTIONS. **(ACT §334)**.
- NEW LAW PERMITS UP TO $2,500 IN RETIREMENT DISTRIBUTIONS PER YEAR TO BE USED TO PAY FOR "HIGH QUALITY" LONG-TERM CARE INSURANCE COVERAGE.
- DISTRIBUTIONS WOULD ALSO AVOID THE 10% EXCISE TAX FOR EARLY DISTRIBUTIONS.
- "HIGH QUALITY" IN THIS CASE REFERS TO A POLICY THAT PROVIDES MEANINGFUL FINANCIAL COVERAGE FOR HOME-BASED ASSISTANCE OR NURSING HOME CARE.
- **EFFECTIVE THREE YEARS AFTER DATE OF ENACTMENT (2025).**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

SELECTED ITEMS IN SECURE 2.0 AS PASSED BY CONGRESS:

- ELECTIVE DEFERRALS GENERALLY LIMITED TO REGULAR CONTRIBUTION LIMIT. **(ACT §603)**.
- CURRENTLY, CATCH-UP CONTRIBUTIONS TO A QUALIFIED PLAN CAN BE MADE ON A PRE-TAX, OR ON A ROTH BASIS (IF PERMITTED BY PLAN SPONSOR).
- THE BILL PROVIDES ALL CATCH-UP CONTRIBUTIONS TO QUALIFIED RETIREMENT PLANS ARE SUBJECT TO ROTH TAX TREATMENT. THUS, CANNOT BE DONE ON A PRE-TAX BASIS.
- EXCEPTION EXISTS FOR EMPLOYEES WITH COMPENSATION OF $145,000 OR LESS (INDEXED FOR INFLATION).
- **EFFECTIVE FOR TAXABLE YEARS AFTER DECEMBER 31, 2023.**

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

IRS NOTICE 2023-54 ISSUED JULY 14, 2023.

- PROVIDES RELIEF FOR RMDs AS A RESULT OF SECURE 1.0 AND SECURE 2.0, AND CONFUSION WITH DATES, AMOUNTS, *ETC.*
- IRS HAD PREVIOUSLY INDICATED IN NOTICE 2022-53 THAT RMD DISTRIBUTION RULES FOR CHANGES UNDER SECTION 401(A)(9) MADE UNDER SECURE 1.0 WOULD BE EFFECTIVE NO SOONER THAN THE 2023 YEAR.
- NOTICE 2023-54 DELAYED THE EFFECTIVE DATE FOR REGULATIONS RELATED TO RMDs UNDER SECTION 401(A)(9) TO BE NO SOONER THAN THE 2024 YEAR.

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - "SECURE 2.0" RETIREMENT BILL

IRS NOTICE 2023-54 ISSUED JULY 14, 2023 *(CONTINUED).*

- PARTICIPANTS THAT RECEIVED DISTRIBUTIONS IN THE PERIOD JANUARY 1, 2023, THROUGH JULY 31, 2023, THAT WERE MISCLASSIFIED AS RMDs NOW HAVE UNTIL SEPTEMBER 30, 2023, TO ROLLOVER THESE AMOUNTS.
- FURTHER, IRA OWNERS BORN IN 1951 (AGE 72) THAT RECEIVED DISTRIBUTIONS FOR THE PERIOD JANUARY 1, 2023, THROUGH JULY 31, 2023, FROM THEIR IRAS THAT WOULD HAVE BEEN RMDs, NOW HAVE UNTIL SEPTEMBER 30, 2023, TO ROLLOVER THESE DISTRIBUTIONS. THIS SPECIAL ROLLOVER IS AVAILABLE EVEN IF THE IRA OWNER HAD A ROLLOVER WITHIN THE PAST 12 MONTHS.
- OTHER RELIEF WAS ALSO PROVIDED IN NOTICE 2023-54.

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2023 TAX LEGISLATION

- Scheduled TCJA Tax Changes in 2022, 2023, and 2026
- Possible Tax Legislation Still in 2023

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Scheduled TCJA Tax Changes in 2022, 2023, and 2026
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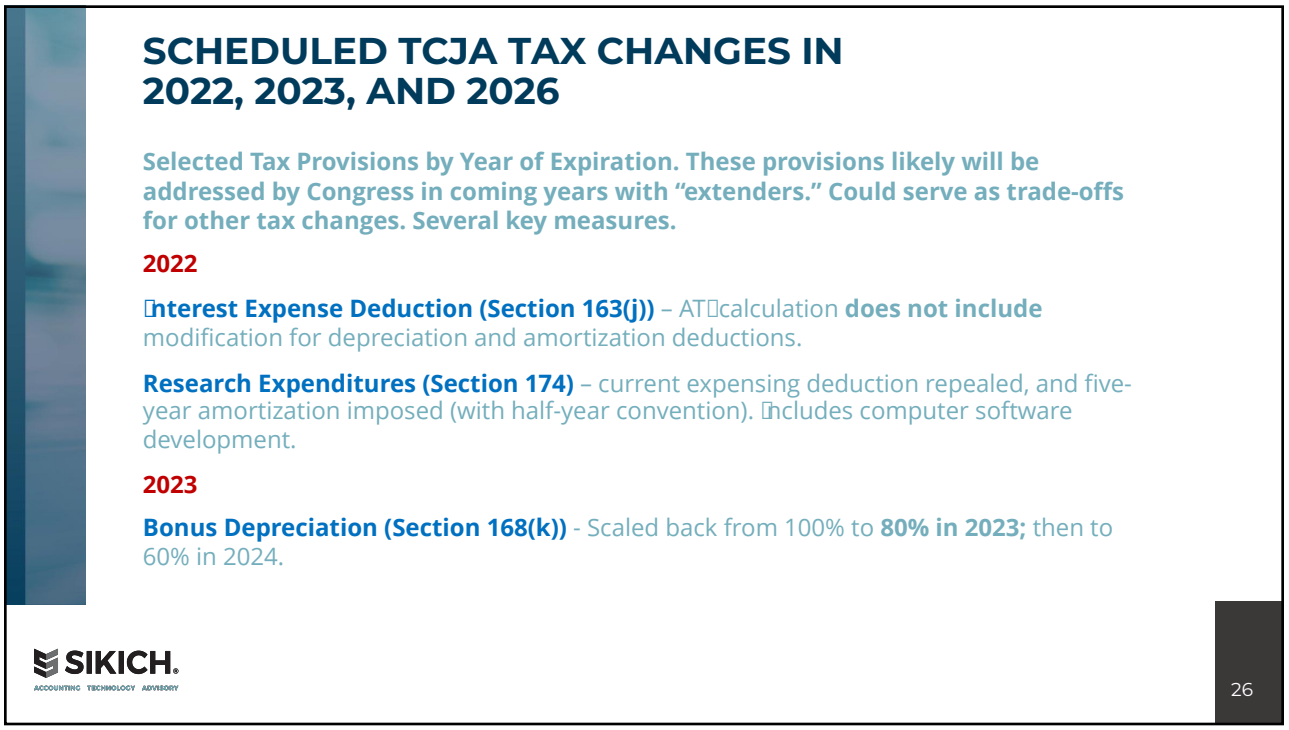
SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026
Selected Tax Provisions by Year of Expiration. These provisions likely will be addressed by Congress in coming years with "extenders." Could serve as trade-offs for other tax changes. Several key measures.
2022
nterest Expense Deduction (Section 163(j)) – AT calculation does not include modification for depreciation and amortization deductions.
Research Expenditures (Section 174) – current expensing deduction repealed, and five-year amortization imposed (with half-year convention). ncludes computer software development.
2023
Bonus Depreciation (Section 168(k)) - Scaled back from 100% to 80% in 2023; then to 60% in 2024.
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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

Selected Tax Provisions by Year of Expiration

2026

- **Individual tax rates (from TCJA)** – revert to Higher 2017 tax rates
- **Corporate tax rates (21%) not set to change**
- Expanded standard deduction (from TCJA)
- Higher child tax credit removed; personal exemption deduction returns
- **AMT exemption Reduced and Return to Lower starting point for AMT phase-out**
- **SALT deduction cap $10,000 removed**
- **20% QB Deduction (§199A) eliminated**
- **Higher estate/gift exemption reverts to 2017 levels**
- Others

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

Interest Expense Deduction (Section 163(j))

Interest limitation under §163(j) could have a much wider application in 2022 and going forward for **two primary reasons**:

1. **Tax Change.** Beginning in 2022, the limitation on interest deductibility is determined based on 30% of "Adjust Taxable Income" (ATI). ATI is calculated based on the company's taxable income without the interest deduction. In 2021 and prior, also added back in arriving at ATI was a company's tax depreciation/amortization. **This add back of depreciation/amortization does not apply in 2022 and beyond.**
2. **Change in Current Conditions.** As you know, interest rates have increased in recent years (along with everything else). This will add to amount of interest expense incurred, and this **interest deduction could be limited.** Any interest subject to the limitation and not deducted, carries over.

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023 AND 2026

Interest Expense Deduction (Section 163 (j))

Interest limitation under §163(j) - wider application in 2022 and going forward.

Example. ***Badger, Inc.*** is a manufacturer of high-tech widgets. It operates as a C Corporation.

For 2021, it has the following tax information:

Taxable Income before Interest Expense Deduction	$1,000,000
Tax Depreciation for 2021 year	1,500,000
Tax Amortization for 2021 year	500,000
Interest Expense incurred in 2021	600,000

For 2022, the exact same amounts were generated, except **the interest expense went up from $600,000 to $900,000** due to higher interest rates in 2022.

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

Interest Expense Deduction (Section 163 (j))

Interest limitation under §163(j) - wider application in 2022 and going forward.

Example (Continued). Here are **2021/2022** tax results factoring in revised §163(j) limitation:

	2021	2022
TAXABLE INCOME BEFORE INTEREST EXPENSE	$ 1,000,000	$ 1,000,000
LESS: DEDUCTIBLE INTEREST EXPENSE	< 600,000> *	<300,000> **
TAXABLE INCOME – FINAL	$ 400,000	$ 700,000
TAX	$ 84,000	$ 147,000 ***
DISALLOWED INTEREST EXPENSE	$ -0-	$ 600,000
"ADJUSTED TAXABLE INCOME" ("ATI")	$ 3,000,000	$ 1,000,000

* (1,000,000 + 1,500,000 + 500,000) @ 30% = 900,000

** (1,000,000) @30% = 300,000

*** THE $147,000 OF TAX IN 2022 EXCEEDS COMPANY'S 2022 BOOK INCOME OF $100,000 [$1,000,000 - $900,000].

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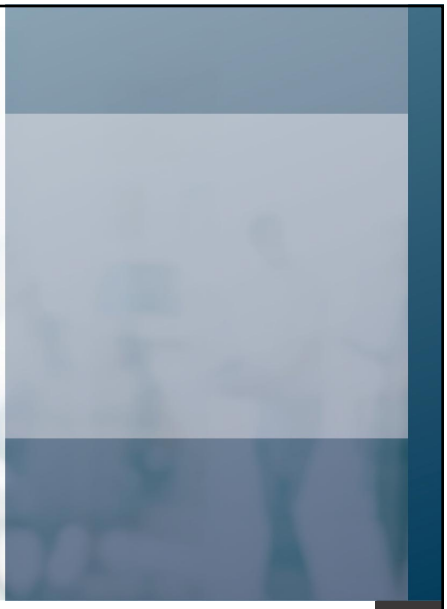
SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

RESEARCH EXPENDITURES (SECTION 174)

- Current expensing deduction of research expenditures (includes computer software development costs) is repealed.
- **Five-year amortization imposed for research expenditures, with half-year amortization in first year. Only 10% in first year. Thus, 90% deferred.**
- If the research is performed outside the US, then it is amortized over **15 years.**
- Congress has supported research incentives in the past, and strong bi-partisan backing exists to continue allowing current expensing of research expenditures.
- Lobbying efforts will continue in 2023 to allow current deduction of research expenditures.



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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

RESEARCH EXPENDITURES (SECTION 174) - CONTINUED

- In tax years prior to 2022, taxpayers could claim current deductions for ordinary and necessary business expenses (Section 162) and research expenditures (Section 174).
- Research expenditures were also part of the calculation for the research tax credit.
- As part of the 2017 *Tax Cuts and Jobs Act (TCJA)*, Congress included a change in the tax treatment of research expenditures. This change, however, did not tax effect until 2022. Key Members of Congress believed this provision would be extended and not implemented. This did not happen (at least not yet).

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

RESEARCH EXPENDITURES (SECTION 174) - CONTINUED

- Congress could have delayed this change for research expenditures with several bills in 2022, but this did not happen.
- Thus, taxpayers (AND tax practitioners) now faced with the task of identifying and capitalizing their research expenditures for their 2022 tax returns.
- IRS regulations state qualifying research expenditures include "all costs incident to the development or improvement of a product." IRS Planning for More §174 Guidance.

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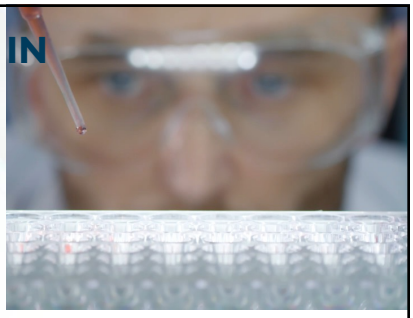

SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

RESEARCH EXPENDITURES (SECTION 174) - CONTINUED

IRS further offers the following types of research for Section 174 purposes (list is not all inclusive):

- Qualified Labor used in Research Activities
- Laboratory Costs
- Rent and Utilities for Research Facilities
- Patent Costs (including Legal Fees)
- Software Developed Costs for Taxpayer's Internal Use

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

RESEARCH EXPENDITURES (SECTION 174) - CONTINUED

Considerations on how to approach Section 174 issues with taxpayers for 2022 (and beyond) tax returns, unless tax law is changed:

1. Taxpayer Summarizes and Provides All Section 174 Expenses for year.
2. **If they are claiming a research tax credit in 2022,** The QRE's for the R&D Credit Could be Used for Section 174 Purposes (unless another amount is Provided). The amount of Section 174 Research expenses they provide should be ≥ amount of QRE's used for R&D Credit.
3. **If they are not claiming a research tax credit in 2022,** Taxpayer should provide the amount of research expenditures they incurred in 2022. These amounts will then be capitalized and amortized over five years under the IRS rules. **Responsibility of taxpayer to determine the Section 174 Amounts.**

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

Research Expenditures (Section 174) - Continued

How to approach Section 174 Reporting with taxpayers for 2022 tax returns:

1. See IRS ***Rev Proc 2023-11*** issued December 29, 2022. Replaced IRS ***Rev Proc 2023-08*** issued only a week before.
2. **See also IRS Notice 2023-63 issued by the IRS September 8, 2023. This Notice 2023-63 is effective for tax years ending after September 8, 2023. Taxpayers can elect to use Notice 2023 -63 for tax years ending before September 8, 2023. See details in Notice 2023-63. Need to become familiar with Notice 2023-63 details for 2023 tax returns.**
3. Change to capitalizing and amortizing Section 174 costs will be a statutory change of Accounting Method – due to tax law change. Automatic Change of accounting Method.
4. **No Form 3115 needed.** Include statement in 2022 tax return. Review ***Rev Proc 2023-11*** closely. Report §174 costs on **Form 4562**, bottom of Page 2 in Amortization Section. Run book-tax difference through Schedule M.
5. State tax treatment of Section 174 Expenses varies by State.

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

BONUS DEPRECIATION (SECTION 168(K))

- **Asset must be "placed in service" during the tax year**
  - READY AND AVAILABLE FOR ITS ASSIGNED BUSINESS FUNCTION
  - YOU DO NOT NEED TO BE ACTUALLY USING THE PROPERTY, BUT IT MUST BE READY AND AVAILABLE FOR USE (*I.E.*, PRESENT, INSTALLED, PERMITS APPROVED, AS APPLICABLE)
- **Useful life of 20 years or less**
  - TANGIBLE PERSONAL PROPERTY: FURNITURE, FIXTURES, EQUIPMENT, LAND IMPROVEMENTS, COMPUTERS, COMPUTER SOFTWARE, ETC.
  - DOES NOT INCLUDE LAND OR LAND IMPROVEMENTS
- **Must be purchased from an unrelated party**
  - CAN BE NEW OR USED PROPERTY (BEGINNING ON OR AFTER SEPTEMBER 28, 2017)

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SCHEDULED TCJA TAX CHANGES IN 2022, 2023, AND 2026

Dates	First Year Bonus Depreciation %
9/28/2018 – 12/31/2022	100%
01/01/2023 – 12/31/2023	80%
01/01/2024 – 12/31/2024	60%
01/01/2025 – 01/01/2025	40%
01/01/2026 – 12/31/2026	20%
01/01/2027 – forward	0%

Bonus Depreciation (Section 168(k))

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FEDERAL TAX LEGISLATION UPDATE 2022-2023

POSSIBLE TAX LEGISLATION STILL IN 2023

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - POSSIBLE TAX LEGISLATION STILL IN 2023

POSSIBLE TAX LEGISLATION IN 2023

- THE HOUSE WAYS & MEANS COMMITTEE PASSED LEGISLATION IN JUNE, 2023 DEALING WITH CHANGING SECTION 174 AND MAKING IN ONCE AGAIN CURRENTLY DEDUCTIBLE. THE EFFECTIVE DATE OF THIS PROVISION WOULD BE RETROACTIVE TO INCLUDE THE 2022 YEAR. THERE IS ALSO A TRANSITION TYPE RULE THAT WOULD ALLOW COMPANIES THAT CAPITALIZED AND AMORTIZED SECTION 174 AMOUNTS FOR 2022 AND ALREADY FILED THEIR 2022 TAX RETURNS TO BE ABLE TO TAKE THE REMAINING AMOUNT A NEGATIVE SECTION 481 ADJUSTMENT IN 2023.
- THUS, FOR 2023, A COMPANY WOULD BE ABLE TO DEDUCT ALL OF THEIR CURRENT YEAR 2023 RESEARCH EXPENSES AND 9/10 OF THEIR RESEARCH EXPENSES RELATED TO 2022. AMENDED TAX RETURNS WOULD NOT BE NEEDED IN THAT CASE.
- THIS BILL, HOWEVER, HAS NOT MOVED THROUGH THE FULL HOUSE YET. THE BILL ALSO INCLUDES CHANGES TO INTEREST EXPENSE LIMITATION UNDER SECTION 163(J) AND 100% BONUS DEPRECATION.

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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - POSSIBLE TAX LEGISLATION STILL IN 2023

POSSIBLE TAX LEGISLATION IN 2023 (CONTINUED)

- EVEN IF THIS BILL PASSES, IT IS UNCERTAIN WHAT THE SENATE WILL DO WITH THIS MATTER. THERE IS BI-PARTISAN SUPPORT FOR RESEARCH EXPENDITURES AND TO RETURN TO CURRENT EXPENSING. MANY DEMOCRATIC LEGISLATORS WANT TO LINK EXTENDING RESEARCH EXPENSES WITH EXPANDED CHILD TAX CREDIT AND CHILD CARE INCENTIVES. KEY LEADERS HAVE MADE SOME PROGRESS ON LINKING THESE PROVISIONS, AND POSSIBLY SOMETIME THIS SUMMER THEY WILL REACH A COMPROMISE.
- EVEN IF THEY DO REACH A COMPROMISE, IT IS STILL UNCERTAIN HOW AND WHEN ANY R&D BILL WILL MOVE FORWARD THIS YEAR IN CONGRESS TOWARD FINAL PASSAGE. IT COULD BE ATTACHED TO OTHER LARGER "MUST-PASS" BILLS, SUCH AS AN FAA REAUTHORIZATION BILL OR A FARM BILL, BOTH EXPECTED TO COME UP FOR VOTES IN SEPTEMBER. IF IT IS NOT ATTACHED TO ONE OF THESE BILLS, IT COULD MOVE WITH A DEFENSE BILL OR OTHER OMNIBUS SPENDING BILL COMING UP IN NOVEMBER OR DECEMBER.

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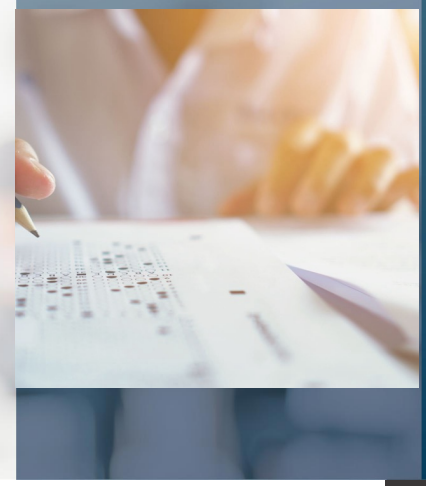
FEDERAL TAX LEGISLATION UPDATE 2022-2023 - POSSIBLE TAX LEGISLATION STILL IN 2023

POSSIBLE TAX LEGISLATION IN 2023 (CONTINUED)

- IF THEY CAN AGREE ON PAIRING UP THE RESEARCH EXPENSES WITH THE CHILD CREDITS AND CHILDCARE CREDITS, THEN THE CHANCES FOR PASSING A BILL THIS YEAR IMPROVE; IT IS JUST WHICH BILL THIS PROVISION IS ATTACHED TO.
- AS FAR AS TIMING, SURPRISED IF CAN GET A BILL ENACTED BY THE SEPTEMBER 15, 2023, OR OCTOBER 15, 2023, DUE DATES. IT COULD HAPPEN, BUT TIME IS RUNNING OUT.
- I THINK THE BEST CHANCE FOR PASSAGE THIS YEAR MIGHT BE WITH ANY YEAR-END LEGISLATION IN NOVEMBER OR DECEMBER 2023. IT OFTEN SEEMS THAT NOTHING MUCH HAPPENS FOR WEEKS/MONTHS ON AN ISSUE, THEN WITH A DEADLINE LOOMING, THINGS FALL IN LINE AND BILLS GET PASSED IN SHORTENED TIME FRAME.



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FEDERAL TAX LEGISLATION UPDATE 2022-2023 - POSSIBLE TAX LEGISLATION STILL IN 2023

POSSIBLE TAX LEGISLATION IN 2023 (CONTINUED)

- SO, WITH YOUR 2022 TAX RETURNS, IF YOU ARE WAITING FOR OTHER ITEMS ANYWAY TO COMPLETE THE TAX RETURNS, AND THE RETURN IS GOING TO BE PUSHED TO THE 9/15/2023 OR 10/15/2023 DEADLINE ANYWAY, THEN KEEP AN EYE ON THE RESEARCH EXPENDITURE AND INTEREST ISSUES AND GET THE LATEST JUST BEFORE YOU FILE THE TAX RETURNS BY THE DUE DATE.
- IF, HOWEVER, THE TAX RETURN IS DONE NOW, AND THE ONLY ITEM IS THE POSSIBLE CHANGE FOR RESEARCH EXPENDITURES, YOU COULD PROBABLY FILE NOW AND NOT WAIT UNTIL SEPTEMBER/OCTOBER. I THINK THIS SECTION 174 ISSUE MIGHT BE RESOLVED THIS YEAR, BUT I WOULD BE SURPRISED THAT ANYTHING IS ENACTED BY THE SEPTEMBER 15, 2023, OR OCTOBER 15, 2023, DUE DATES.

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EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

- THIRD-PARTY ERC PROVIDERS FLOURISH
- OTHER PLAYERS JOINED THE ERC MARKETPLACE
- IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED
- WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION
- LATEST IRS DEVELOPMENTS **(WITH 9/14/2023 CHANGES)**
- ERC STATUTE OF LIMITATIONS (SOL) ISSUES

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

THIRD-PARTY ERC PROVIDERS FLOURISH

- SENSING A BUSINESS OPPORTUNITY FOR THEMSELVES, MANY FIRMS POPPED UP ACROSS THE COUNTRY OFFERING HELP WITH ERC CLAIMS.
- THEY OFFERED TO ASSIST EMPLOYERS GATHER THE PAYROLL AND OTHER INFORMATION TO FILE THE ERC REFUND CLAIMS FOR THE EMPLOYERS. THESE PROVIDERS, IN TURN, CHARGED A FEE.
- FEES PAID TO ERC FIRMS RANGED FROM 15%-25%, OR MORE. THE FEE WAS OFTEN A SET PERCENTAGE OF THE ERC THEY HELPED THE EMPLOYER OBTAIN.
- THE FEE WAS SOMETIMES PAID UP-FRONT WHEN THE ERC CLAIM WAS FILED, AND THE EMPLOYER THEN NEEDED TO WAIT 8-12 MONTHS FOR THE ERC CLAIM TO BE PROCESSED AND PAID BY THE IRS.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

THIRD-PARTY ERC PROVIDERS FLOURISH

- SEVERAL PROVIDERS ADVERTISED HEAVILY ON TV AND RADIO. OTHERS PUSHED LITERATURE AND CONTACTED EMPLOYERS FROM COAST TO COAST.
- SOME OF THESE FIRMS WERE PROFESSIONAL, DILIGENT, AND REPUTABLE.
- OTHERS WERE NOT – OFTEN RELIED ON AGGRESSIVE INTERPRETATIONS OF THE IRS GUIDANCE IN TELLING EMPLOYERS THEY QUALIFIED FOR ERC, WHEN THEY LIKELY DID NOT.
- A **"GOVERNMENT ORDER LEADING TO A FULL OR PARTIAL SHUTDOWN"** WAS OFTEN USED TO SUPPORT ERC ELIGIBILITY. THIS IS A SUBJECTIVE STANDARD TO BEGIN WITH, AND MANY PROVIDERS APPLIED CREATIVE AND AGGRESSIVE INTERPRETATIONS.
- IRS OFTEN REFERS TO THESE THIRD-PARTY PROVIDERS AS "ERC MILLS."

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

THIRD-PARTY ERC PROVIDERS FLOURISH

- NOT ONLY HAVE SOME FIRMS PUSHED THE ENVELOPE IN THEIR ERC INTERPRETATIONS, BUT THEY ALSO EMPLOYED AGGRESSIVE MARKETING TACTICS.
- SOME PROVIDERS PRODUCED AN ERC REPORT OR STUDY FOR THE EMPLOYER; OTHERS DID NOT.
- THESE THIRD-PARTY PROVIDERS COME IN MANY SHAPES AND SIZES. BE CAREFUL IN DEALING WITH THEM. DO YOUR DUE DILIGENCE. TALK TO SEVERAL FIRMS.
- FIND OUT FROM EACH FIRM THEIR APPROACH TO THE ERC. INQUIRE ABOUT THE FOLLOWING:

- ❑ **Will they defend the ERC claim if audited by the IRS?**
- ❑ **Do you pay their fee up front, or after your ERC claim is paid?**
- ❑ **Will they refund some (or all) of fee if ERC claim is reduced by IRS audit?**
- ❑ **Will the firm be around years from now if the IRS shows up for an ERC audit?**
- ❑ **Will they provide you a detailed written report with all the required documentation that would be required in an IRS audit?**

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

THIRD-PARTY ERC PROVIDERS FLOURISH

NEED TO ADDRESS HOW TO VET A THIRD-PARTY PROVIDER:

- ❑ Discuss terms of engagement letter and ability to claw back fees if claim is disallowed fully or partially.
- ❑ Discuss documentation that provider should deliver to employer at end of engagement (checklist).
- ❑ Discuss whether provider has had any clients under IRS audit and what the outcome has been. Ask if third-party provider is under IRS review or investigation (including IRS criminal investigation).
- ❑ Review their claims in their marketing materials to assess credibility.
- ❑ If they are relying on the "government order" provision to justify eligibility for ERC, do they limit ERC eligibility only for the period of the order, or for all quarters in 2020/2021?
- ❑ Do they also inform you that the amount of the ERC they calculate must be added back to taxable income (by way of a reduction in wage expense), and thus amended income tax returns must be filed? Do they adjust ERC wages for PPP loan wages?

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

OTHER PLAYERS JOINED THE ERC MARKETPLACE

- THIRD-PARTY ERC PROVIDERS FOUND A MARKET IN OFFERING SERVICES TO ASSIST EMPLOYERS WITH FILING ERC CLAIMS.
- BESIDES THIRD-PARTY ERC PROVIDERS. OTHER BUSINESSES BEGAN OFFERING OTHER ERC SERVICES.
- ERC TAX INSURANCE.
- MONETIZING THE ERC CLAIM.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

OTHER PLAYERS JOINED THE ERC MARKETPLACE - ERC TAX INSURANCE.

ERC TAX INSURANCE CAN BE PURCHASED ON AN ERC CLAIM THAT HAS BEEN SUBMITTED. THE FOLLOWING SHOULD BE NOTED RELATED TO THIS INSURANCE:

- Approximately ten A-Rated insurance companies are willing to insure ERC claims.
- Insurance had been for larger claims (≥ $5,000,000), but insurance can now be purchased on claims that are ≥ $500,000.
- Insurance requires some underwriting to review the substance of the ERC claim.

❑ **Premiums:** Range from 3% - 10% of the claim submitted.

❑ **Deductible:** Any insurance claim that would result (disallowed ERC refund claim) may be reduced by a deductible that is estimated at 5%.

❑ **Underwriting fee:** Insurer may require employer to pay a fee for professionals to evaluate the claim and perform necessary due diligence to properly assess the risk and price the premiums.

- Insurance can be purchased prior to the ERC claim being sent to the IRS. (Do not need to wait to receive the ERC refund after the claim is processed)
- Insurance will generally cover all costs, including attorney fees to defend claim and additional tax costs if defense is unsuccessful

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

OTHER PLAYERS JOINED THE ERC MARKETPLACE - ERC TAX INSURANCE (CONTINUED)

- **INSURANCE IS IN EFFECT FOR 7 YEARS WHICH SHOULD COVER THE STATUTE FOR ANY CLAIM FILED, INCLUDING A "SUBSTANTIAL UNDERSTATEMENT OF INCOME" ASSESSMENT BY IRS, WHICH DOUBLES TO NORMAL STATUTE FROM 3 TO 6 YEARS.**
- **UNDERWRITING GENERALLY REQUIRES A LEGAL OPINION AND AN OVERALL DOCUMENT REVIEW PACKAGE.**
- **RISK AND INSURANCE PREMIUMS ARE BASED ON SEVERAL FACTORS:**

❑ **STATE OR STATES WHERE EMPLOYER IS LOCATED – SOME STATES HAS MORE RESTRICTIVE GOVERNMENT ORDERS OR SHUTDOWN REQUIREMENTS**

❑ **INDUSTRY OF EMPLOYER – CERTAIN INDUSTRIES WERE MORE CLEARLY IMPACTED SUCH AS HOSPITALITY AND HEALTHCARE AND HAVE LESS PERCEIVED RISK**

❑ **SIZE OF THE REFUND CLAIM**

❑ **REVIEW OF LEGAL OPINION AND FACTS AND CIRCUMSTANCES, DATA THAT SUBSTANTIATES CLAIM.**

❑ **AVERAGE ERC CLAIM WHERE INSURANCE IS PROCURED IS A CLAIM OF AT LEAST $5,000,000.**

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

OTHER PLAYERS JOINED THE ERC MARKETPLACE - MONETIZING THE ERC CLAIM

- EMPLOYERS CONTINUE TO EXPERIENCE SIGNIFICANT DELAY FROM THE TIME THEY SUBMIT A FORM 941-X UNTIL THE TIME THEY RECEIVE THEIR ERC REFUND CHECK.
- FOR THOSE EMPLOYERS THAT HAVE NOT YET RECEIVED THEIR REFUNDS, THERE ARE OPTIONS TO "MONETIZE" THEIR ERC CLAIMS. THIS INCLUDES THE FOLLOWING:

- ❑ Only applies to larger ERC claims - **$500,000 or more**
- ❑ Credit worthy companies – distressed companies may be declined
- ❑ If company has a lien on working capital assets, bank will need to release the ERC refund due from any lien
- ❑ ERC lender will perform due diligence on the claim submitted
- ❑ Approved companies will receive initial installment that approximates 70% of the total claim filed with IRS
- ❑ Second payment will be paid once the ERC claim is received and will vary, based on the time elapsed

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

OTHER PLAYERS JOINED THE ERC MARKETPLACE

EXAMPLE

HOW MUCH IS LEFT FOR **ABC COMPANY** AFTER ALL THESE EXPENSES AND RELATED INCOME TAXES ARE PAID FOR ITS $500,000 ERC CLAIM?

ERC Claim	$500,000
Less: ERC Consultant Fee	<150,000>
Less: Insurance Premium	<50,000>
Less: Factoring Fee	<75,000>
Net Amount after Fees	$225,000
Less: Income Taxes (40%)	<90,000>
Net Remaining for **ABC**	$135,000 27% of original ERC claim [$135,000 ÷ $500,000]

DOES NOT INCLUDE POTENTIAL IMPACT OF UNDERWRITING FEES THAT ARE NON-REFUNDABLE AND INSURANCE DEDUCTIBLE - IF THE RECIPIENT IS AUDITED – THIS COULD REDUCE THE NET AMOUNT EVEN FURTHER.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

- IRS SWAMPED WITH ERC CLAIMS.
- CLAIMS CONTINUE TO BE FILED. EVEN AS THE IRS PROCESSES SOME, MORE CONTINUE TO ROLL IN.
- BACKLOG IN PROCESSING CLAIMS. 6-12 MONTHS OR LONGER.
- IRS BACKLOG OF UNPROCESSED ERC CLAIMS HAS DECREASED, BUT HAS SINCE RISEN THIS SPRING/SUMMER AS IRS REALLOCATED RESOURCES TO IMPROVE CUSTOMER SERVICE. MORE CLAIMS CONTINUE TO FLOW IN.

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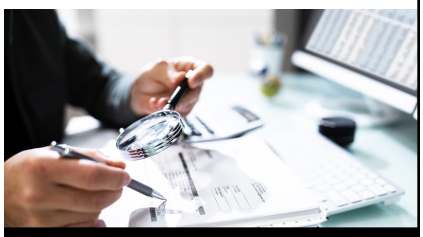
EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

- IRS NOTICED SURGE IN ERC CLAIMS.
- DEVELOPED TASK FORCE IN 2022 TO LEARN ERC. TRAINED OVER 300 AGENTS ON ERC AND HOW IT WOULD AUDIT THESE CLAIMS.
- ERC AUDITS BEGAN, BUT HAVE BEEN MODEST THUS FAR. SOME ERC CLAIMS WERE ADJUSTED OR DISALLOWED. IN A FEW SITUATIONS FRAUD WAS IDENTIFIED.
- APPEARS THE ERC INITIATIVE WAS DELAYED DURING TAX FILING SEASON, BUT EXPECT AUDIT ACTIVITY TO INCREASE FOR BALANCE OF YEAR AND INTO 2024.
- SOME PREDICT THE IRS WILL FIND SIGNIFICANT ERRORS AND ASK CONGRESS TO EXTEND THE STATUTE OF LIMITATIONS TO ALLOW MORE TIME TO AUDIT ERC RECIPIENTS. UNCERTAIN IF THIS WILL HAPPEN.



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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

- **(1)** IRS CRIMINAL INVESTIGATION GROUP AND JUSTICE DEPARTMENT INDICTED AN ERC MILL IN UTAH IN FEBRUARY OF 2023.
- THE FIRM IS ALLEGED TO HAVE SUBMITTED OVER 1,000 FRAUDULENT FORM 7200 AND FORM 941 ON BEHALF OF CLIENTS CLAIMING ERC AND FFCRA CREDITS WORTH ABOUT $11 MILLION (~$11,000 PER FALSE CLAIM).
- THE INDICTMENT ALLEGED THE DEFENDANTS LIED ABOUT THE CLAIMANTS' ELIGIBILITY; THE NUMBER OF EMPLOYEES; THE AMOUNT OF PAYROLL; AND WHETHER THERE WERE ANY SICK OR FAMILY LEAVE WAGES; ALL TO FRAUDULENTLY INCREASE AMOUNT OF THESE TAX CREDITS. OBJECTIVE WAS TO INCREASE THESE CREDITS; THUS, DEFENDANTS WOULD EARN MORE FEES.
- THE INDICTMENT CONTAINS NUMEROUS FORMS AS ACTS OF THE CONSPIRACY; COVERS 11 COUNTS OF AIDING IN FILING FALSE TAX RETURNS ON BEHALF OF CLIENTS; AND INCLUDES 13 WIRE FRAUD CHARGES FOR FRAUDULENT TAX FILINGS.
- **(2)** ANOTHER SIMILAR INDICTMENT OF NEW JERSEY TAX PREPARER FOR ERC FRAUD WAS ANNOUNCED ON JULY 31, 2023. LEON HAYNES OF TEANECK, NEW JERSEY, WAS ARRESTED ON FRAUD CHARGES FOR ALLEGEDLY SEEKING MORE THAN $124 MILLION BY FILING 1,387 RETURNS FALSELY CLAIMING THE ERC FOR HIMSELF AND HIS CLIENTS (~ $90,000 PER FALSE CLAIM).

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

- IRS BEGAN PUBLICITY CAMPAIGN WARNING ABOUT ERC ABUSES. STARTED IN 2022 AND CONTINUED MESSAGING INTO 2023.
- HERE IS AN EXCERPT FROM **IRS ANNOUNCEMENT IR-2023-40** ISSUED MARCH 7, 2023:

> The Internal Revenue Service today issued a renewed warning **urging people to carefully review the Employee Retention Credit (ERC) guidelines before trying to claim the credit as promoters continue pushing ineligible people to file**. The IRS and tax professionals continue to see third parties aggressively promoting these ERC schemes on radio and online. These promoters charge large upfront fees or a fee that is contingent on the amount of the refund. And the promoters may not inform taxpayers that wage deductions claimed on the business' federal income tax return must be reduced by the amount of the credit.
>
> ***"While this is a legitimate credit that has provided a financial lifeline to millions of businesses, there continue to be promoters who aggressively mislead people and businesses into thinking they can claim these credits,"*** said Acting IRS Commissioner Doug O'Donnell. ***"Anyone who is considering claiming this credit needs to carefully review the guidelines. If the tax professional they're using raises questions about the accuracy of the Employee Retention Credit claim, people should listen to their advice. The IRS is actively auditing and conducting criminal investigations related to these false claims. People need to think twice before claiming this."***

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

IRS BEGAN PUBLICITY CAMPAIGN WARNING ABOUT ERC ABUSES. STARTED IN 2022 AND CONTINUED MESSAGING INTO 2023.

- IRS **OFFICE OF PROFESSIONAL RESPONSIBILITY (OPR)** ISSUED A SPECIAL ALERT **(ALERT 2023-02)** TO TAX PRACTITIONERS ON MARCH 7, 2023, RELATED TO THE ERC.
- THIS ALERT FROM THE IRS OFFICE OF OPR REMINDS TAX PRACTITIONERS OF THEIR RESPONSIBILITIES UNDER **CIRCULAR 230** IN DEALING WITH ERC. NOTE, THE FOLLOWING EXCERPTS FROM THIS ALERT:

"IF THE PRACTITIONER CANNOT REASONABLY CONCLUDE (CONSISTENT WITH THE STANDARDS DISCUSSED IN THIS GUIDANCE) THAT THE CLIENT IS OR WAS ELIGIBLE TO CLAIM THE ERC, THEN THE PRACTITIONER SHOULD NOT PREPARE AN ORIGINAL OR AMENDED RETURN THAT CLAIMS OR PERPETUATES A POTENTIALLY IMPROPER CREDIT. ADDITIONALLY, IF A PRACTITIONER LEARNS THAT A CURRENT CLIENT DID NOT COMPLY WITH THE ERC REQUIREMENTS IN A PRIOR TAX YEAR, THE PRACTITIONER MUST, UNDER SECTION 10.21, PROMPTLY INFORM THE CLIENT OF THE "NONCOMPLIANCE, ERROR, OR OMISSION" AND ANY PENALTY OR PENALTIES THAT MAY APPLY."

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

IRS CAMPAIGN IN 2023 FILING SEASON. ERC MAKES TOP OF IRS **"DIRTY DOZEN LIST"** OF TAX SCAMS. RELEASED BY THE IRS ON MARCH 23, 2023:

> **IRS opens 2023 Dirty Dozen with warning about Employee Retention Credit claims; increased scrutiny follows aggressive promoters making offers too good to be true**
>
> In a further warning to people and businesses, the Internal Revenue Service added widely circulating promoter claims involving Employee Retention Credits as a new entry in the annual Dirty Dozen list of tax scams.
>
> For the start of the annual **Dirty Dozen List of tax scams**, the IRS spotlighted Employee Retention Credits following blatant attempts by promoters to con ineligible people to claim the credit. Renewing several earlier alerts, the IRS highlighted schemes from promoters who have been blasting ads on radio and the internet touting refunds involving Employee Retention Credits, also known as ERCs. These promotions can be based on inaccurate information related to eligibility for and computation of the credit. ***"The aggressive marketing of these credits is deeply troubling and a major concern for the IRS,"*** said IRS Commissioner Danny Werfel.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

THERE WAS ALSO AN ALERT SENT EARLIER IN 2023 FROM A MAJOR CPA MALPRACTICE INSURANCE CARRIER ABOUT EXPOSURE WITH ERC CLAIMS.

- THE ALERT INDICATED THAT CPAS MIGHT FACE A MALPRACTICE CLAIM WHEN PREPARING TAX RETURNS THAT REFLECT ERC, EVEN IF THEY DIDN'T CALCULATE THE ERC.
- THESE THIRD-PARTY PROVIDERS MAY BE TAKING IMPROPER POSITIONS RELATED TO TAXPAYER ELIGIBILITY AND COMPUTATION OF THE ERC AMOUNT AND MAY NOT FULLY APPRECIATE THE INTRICATE, SUBJECTIVE, AND COMPLEX RULES GOVERNING THE ERC.
- AS A RESULT, IF A CLIENT ASKS A CPA TO PREPARE OR AMEND TAX RETURNS USING INFORMATION PREPARED BY A THIRD-PARTY, INCLUDING ERC CALCULATIONS, THE CPA SHOULD FIRST OBTAIN A SIGNED ENGAGEMENT LETTER DEFINING WHICH FEDERAL AND STATE TAX RETURNS REQUIRE PREPARATION OR AMENDMENT, AND THEN EVALUATE THE INFORMATION IN ACCORDANCE WITH PROFESSIONAL STANDARDS.
- CPAS NEED TO BE CAREFUL. TALK WITH YOUR MALPRACTICE CARRIER ABOUT ERC.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

"PROFESSIONAL EMPLOYER ORGANIZATIONS" (PEOs)

- LETTER RELEASED BY THE IRS CHIEF COUNSEL'S OFFICE ON MARCH 31, 2023, IN RESPONSE TO INQUIRY FROM MEMBER OF CONGRESS ON PEOs AND THE ERC. THE CHIEF COUNSEL'S LETTER STATES, IN PART, AS FOLLOWS:

> *"When an employer uses a PEO to pay its employment taxes and satisfy its employment tax return filing obligations, the PEO is the taxpayer before the IRS. The PEO reports the wages, employment taxes, and credits on behalf of all its employer clients. If there is a refund owed to the PEO after applying the PEO's total credit amount for all clients to the PEO's total aggregate tax liability reported for all clients, the IRS will release the refund directly to the PEO. The IRS uses this process because the PEO deposits, pays, and reports the employment taxes under its own employer identification number (EIN) against which the PEO is claiming the ERC.* ***How the PEO distributes the refund amounts to its clients is a contractual matter between the PEO and its clients."***

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

IRS PUSHES BACK ON ERC: EXAMINATIONS PLANNED AND MARKETING CAMPAIGN LAUNCHED

"PROFESSIONAL EMPLOYER ORGANIZATIONS" (PEOs) – (CONTINUED)

- THE CHIEF COUNSEL'S LETTER FURTHER STATES THE FOLLOWING IN ITS CLOSING:

"After the IRS processes the ERC, the PEO is responsible for making sure each of its clients receives any credit or overpayment (including any ERC refund) owed to the client.

In accordance with their liability under the Code and applicable regulations, the client and the PEO will each be liable for employment taxes owed because of any improper ERC claim for employment taxes reported on the federal employment tax return the PEO filed claiming the credit. This joint liability isn't solely for the claiming of the ERC. In general, the client and the PEO are both liable for paying the client's employment taxes, filing returns, and making deposits and payments for the taxes reported."

- ANY EMPLOYERS USING PEOs AND CONSIDERING THEM FOR ANY ERC CLAIMS SHOULD CAREFULLY REVIEW THE AGREEMENT WITH THEIR PEO.
- FURTHER, ANY PEO NEEDS TO RECOGNIZE THE RESPONSIBILITY IT HAS WITH ANY ERC CLAIMS AND SHOULD ALSO EVALUATE ITS AGREEMENT WITH ITS EMPLOYERS TO PROVIDE PAYROLL SERVICES.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

- DOCUMENTATION CHECKLIST - COVERS A NUMBER OF THESE DOCUMENTATION ITEMS. HELPFUL TO COMPLETE ALL ITEMS THAT APPLY.
- GATHER DOCUMENTATION NOW WHILE ITEMS ARE STILL AVAILABLE AND RELATIVELY FRESH IN EVERYONE'S MINDS. DO NOT WAIT FOR IRS AUDIT TO COMMENCE.

Situation 1 - Employer filed for ERC two years ago and already obtained ERC refund. A third-party assisted with the ERC claim. In this case, still check documentation that the third-party provided employer. If not sufficient, go through and compete the checklist.

Situation 2 - Employer is thinking about filing an ERC claim. Important to gather all ERC information and complete the ERC checklist at time claim is submitted.

RECOMMEND OBTAINING THIS DOCUMENTATION FROM CONSULTANTS THAT PERFORMED THE ANALYSIS, IF APPLICABLE.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

DOCUMENTATION IS ESSENTIAL FOR AN EMPLOYER THAT HAS CLAIMED OR IS THINKING ABOUT CLAIMING THE ERC. SOME KEY AREAS OF DOCUMENTATION:

- Did the employer receive any PPP Loans, and if so, did this overlap with the period the ERC was claimed? Did the employer adjust properly so it did not double up with the wages for the PPP Loan and ERC? Can these wages be provided on spreadsheet listing each employee?
- Did the employer satisfy the ERC wage limits for 2020 ($10,000 per employee per year), and for 2021 ($10,000 per employee per calendar quarter)?
- How many employees did the employer have (determined in 2019)? Was the employer a small employer in 2020 (≤100 employees) and/or 2021 (≤500 employees)? Is this documented?
- Did the employer include in taxable income (as a reduction in wages) the amount of the ERC claim it filed for the income tax return for the period the wages were paid? *Note: the IRS will likely look to see that wages are adjusted for income tax purposes for the ERC claim in its processing.*

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

WHAT DOCUMENTATION SHOULD AN EMPLOYER RETAIN IN THE EVENT OF AN IRS AUDIT?

- Do you pass all the objective tests for ERC qualification?
- Were you an "Active Trade or Business" prior to February 15, 2020?
- How many full-time employees did you have (measured in 2019)?
- Do you qualify because of the "Gross Receipts Test" comparing revenue for a quarter in 2020 or 2021 *vs.* the same quarter in 2019?
- Do you need to aggregate the business with other related businesses?
- Did you properly compute the amount by excluding wages used for PPP forgiveness or other credits such as R&D or FFCRA?
- Did you consider only wages incurred for the period of time the government order was in effect (applies only to employers that qualify under the full or partial suspension rules)?

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIM

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

WHAT DOCUMENTATION SHOULD AN EMPLOYER RETAIN IN THE EVENT OF AN IRS AUDIT? (CONTINUED)

- Can you document all the other tests necessary for ERC qualification?
- Is there a government order which impacted the employer?
- Did the employer comply with the government order?
- Does the partial suspension meet the safe harbor of being "more than nominal" (more than 10% of the business being impacted), measured in hours or revenues?
- For the portion of the business that was impacted, was the impact more than 10% measured by industry metrics showing a more than 10% decline?
- Can the employer provide quantitative evidence? Don't just rely on a narrative. What was the government order? What was the duration of the order? How did it impact the employer/business? Was the impact to the employer more that "nominal?" Can the employer demonstrate the impact to the business through quantifiable metrics? (See also *IRS Notice 2021-20*)?

SHOULD YOU OBTAIN A LEGAL OPINION OR PROFESSIONAL REVIEW OF YOUR SUPPORTING DOCUMENTATION FOR THE PREMISE THAT A GOVERNMENT ORDER LEAD TO THE FULL OR PARTIAL SUSPENSION OF THE BUSINESS?

CONSIDER OBTAINING AN INDEPENDENT REVIEW OF THE ERC EVEN IF YOU USED A THIRD-PARTY ERC PROVIDER? PERHAPS CONSULT WITH AN OUTSIDE PROFESSIONAL ADVISOR, OR SEEK COUNSEL FROM A TAX ATTORNEY, ESPECIALLY IF RELYING UPON A GOVERNMENT ORDER FOR ERC ELIGIBILITY.

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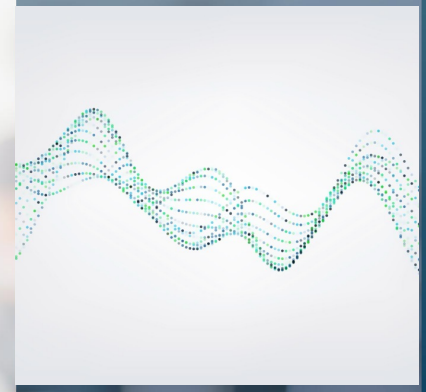
EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

What documentation should an employer retain in the event of an IRS Audit? (continued)

- Detailed payroll records;
- PPP loan forgiveness records;
- Employee leave records;
- **Support for ERC eligibility under either: (1) gross receipts test; or (2) rules for a full or partial suspension from a government order.**



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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

WHAT'S AN EMPLOYER TO DO? DOCUMENTATION, DOCUMENTATION, DOCUMENTATION

- IRS WILL REQUEST THIS UPON ERC AUDIT IN NEXT SEVERAL YEARS. DON'T WAIT FOR IRS AUDIT NOTICE TO BEGIN COLLECTING ERC DOCUMENTATION.
- IF OBTAINED AN OUTSIDE STUDY FOR ERC CLAIM, DOCUMENTATION IS STILL NEEDED. FIND OUT IF DOCUMENTATION IS INCLUDED IN STUDY. IF NOT, REQUEST IT FROM PROVIDER OF ERC STUDY. IF PROVIDER DOES NOT HAVE OR WON'T PROVIDE, STILL BUILD A FILE.
- IF NO ERC STUDY OBTAINED, BUILD DOCUMENTATION NOW TO SUPPORT CLAIM.

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NEW SLIDE ADDED
EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

IRS ANNOUNCEMENT ON SEPTEMBER 14, 2023

- With an endless surge of ERC Claims, many of which the IRS believed to be unmerited, frivolous, or even fraudulent, the IRS hit the "Pause Button" on September 14, 2023.
- The IRS announced a moratorium on the processing of New ERC claims. The IRS announcement indicated:
- "an immediate moratorium through at least the end of the year on processing new claims for the pandemic-era relief program to protect honest small business owners from scams."
- The IRS announcement went on to state:
- "IRS Commissioner Danny Werfel ordered the immediate moratorium, beginning today, to run through at least December 31, 2023, following growing concerns inside the tax agency, from tax professionals as well as media reports that a substantial share of new claims from the aging program are ineligible and increasingly putting businesses at financial risk by being pressured and scammed by aggressive promoters and marketing."

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NEW SLIDE ADDED
EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

IRS ANNOUNCEMENT ON SEPTEMBER 14, 2023

- THE IRS OUTLINED THE FOLLOWING DEPENDING UPON WHERE THE BUSINESS STOOD IN THE ERC PROCESS.

A. **ERC Claim Filed, But Not Paid Yet – Longer Wait.** First, the IRS indicated it will slow down the processing of these claims and implement additional review procedures. It noted the review process would take 180 days or more to complete. The IRS may also request additional ERC documentation from businesses in this expanded review.

B. **ERC Claimed Filed, But Not Paid Yet – Claim Withdrawal Option.** The IRS announced it would soon provide guidance for businesses with pending ERC claims the option to withdraw their claims if they now believe they no longer qualify for the ERC. They may then avoid not only possible ERC penalties, but could avoid paying a large contingent fee.

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NEW SLIDE ADDED
EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

IRS ANNOUNCEMENT ON SEPTEMBER 14, 2023

- THE IRS OUTLINED THE FOLLOWING DEPENDING UPON WHERE THE BUSINESS STOOD IN THE ERC PROCESS.

C. **ERC Claim Filed, ERC Refund Received – Repay ERC Refund Option.** Some businesses may have filed an ERC claim a while back, perhaps a year or more ago, and received their refund. They now, however, believe they are not eligible for the ERC. The IRS plans to provide a method for these businesses to repay their ERC. This ERC settlement program is being finalized by the IRS. One of the issues according to the IRS with this approach is "how to deal with businesses that had a promoter contingency fee paid for out of the ERC payment."

D. **ERC Claim Not Filed Yet.** In this situation, the IRS will not process these ERC claims for the balance of the year, and perhaps longer. The IRS hopes/expects these businesses to carefully review their ERC situation with the assistance of a trusted tax professional and not a third-party ERC promoter. The business may then decide whether to file or not its ERC claim, and if it is filed, the ERC claim will wait for later processing.

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NEW SLIDE ADDED
EMPLOYEE RETENTION CREDIT (ERC) DEVELOPMENTS

IRS ANNOUNCEMENT ON SEPTEMBER 14, 2023

THE IRS OUTLINED OTHER CONSIDERATIONS IN ITS ANNOUNCEMENT

- **The IRS released a new ERC Checklist for businesses to follow.** This checklist will assist a business determine whether it is eligible or not for the ERC. It can be used by those considering filing an ERC claim, and those that have already filed an ERC claim.

- **The IRS is encouraging businesses to seek advice from a "trusted tax professional" in working on ERC matters**, and not rely on third-party ERC promoters. Thus, some businesses may turn to CPAs for guidance with their ERC filings, *etc.*

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

LATEST IRS DEVELOPMENTS

IRS "GENERIC LEGAL ADVICE MEMORANDUM" ("GLAM") 2023-05. RELEASED BY THE IRS JULY 21, 2023.

- THIS GLAM OFFERS ANALYSIS ON SUPPLY CHAIN DISRUPTION AS POSSIBILITY OF BEING TREATED AS A GOVERNMENT ORDER FOR ERC ELIGIBILITY.
- FIVE SCENARIOS ARE PRESENTED IN GLAM 2023-05. THESE SCENARIOS ADDRESS SUPPLY CHAIN DISRUPTIONS OF A TRADE OR BUSINESS AND WHETHER EACH SCENARIO ALLOWS AN EMPLOYER TO MEET THE DEFINITION OF AN ELIGIBLE EMPLOYER FOR ERC.
- IN FOUR OF THE FIVE SCENARIOS, THE IRS DETERMINED THAT THE SUPPLY CHAIN ISSUES DID NOT RISE TO THE LEVEL OF A GOVERNMENT ORDER LEADING TO A FULL OR PARTIAL SHUTDOWN TO QUALIFY FOR ERC.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

LATEST IRS DEVELOPMENTS

IRS "GENERIC LEGAL ADVICE MEMORANDUM" ("GLAM") 2023-05. RELEASED BY THE IRS JULY 21, 2023 *(CONTINUED)*

- IN SCENARIO #3, HOWEVER, THE IRS DETERMINED THAT THE COMPANY WAS ELIGIBLE FOR ERC, BUT ONLY FOR THE ONE MONTH THAT THE COMPANY AND THE SUPPLIER WERE ORDERED SHUT DOWN BY A LOCAL GOVERNMENT ORDER. AFTER THE ORDER WAS LIFTED, THE IRS NOTED IN SCENARIO #3 THERE WAS NO RESIDUAL IMPACT OF THE GOVERNMENT ORDER TO QUALIFY FOR ERC BEYOND THE INITIAL PERIOD.
- PRACTITIONERS SHOULD CAREFULLY REVIEW THIS GLAM, AND CONSIDER SENDING IT TO CLIENTS AND OTHERS LOOKING AT ERC ELIGIBILITY UNDER "GOVERNMENT ORDER" ROUTE.
- MANY THIRD-PARTY ERC PROVIDERS HAVE USED THE SUPPLY CHAIN ARGUMENT TO QUALIFY COMPANIES FOR ERC REFUNDS. THIS GLAM HIGHLIGHTS THE RISK IN THESE CLAIMS.
- MANY COMPANIES AND PRACTITIONERS ARE HOPING FOR MORE GLAMS TO BE ISSUED.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

LATEST IRS DEVELOPMENTS

- IMPORTANT TO UNDERSTAND WHAT ERC CLAIM WAS BASED ON.
- WAS IT BASED ON A SIGNIFICANT DECLINE IN GROSS RECEIPTS? [OBJECTIVE]
- OR, WAS IT BASED ON A FULL OR PARTIAL SHUTDOWN FROM A GOVERNMENT ORDER? [SUBJECTIVE]
- THERE HAVE BEEN A NUMBER OF OUTFITS SELLING ERC SERVICES THAT HAVE FOCUSED ON THE GOVERNMENT ORDER APPROACH TO QUALIFY FOR ERC. SOME ASSERT THAT NEARLY ANY BUSINESS CAN QUALIFY FOR ERC UNDER THE GOVERNMENT ORDER APPROACH. THEY ASSERT THIS IN SPITE OF IRS GUIDANCE THAT INDICATES OTHERWISE (THAT NO ERC IS ALLOWED).
- BE CAREFUL WITH THESE OUTFITS. CHALLENGE THEM. REVIEW ERC DOCUMENTATION AND SUPPORT CLOSELY. THESE ERC CLAIMS MIGHT BE CHALLENGED BY IRS, AND THESE OUTFITS MAY NOT BE AROUND TO DEFEND THEM, OR REFUND ANY FEE PAID TO THEM.

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EMPLOYEE RETENTION CREDIT (ERC) – IRS REVIEW OF ERC CLAIMS

ERC STATUTE OF LIMITATIONS (SOL) ISSUES.

IRS BEGINNING REVIEW OF ERC CLAIMS. ACTIVITY WILL EXPAND IN 2023. STATUTE OF LIMITATIONS (SOL) FOR ERC BY ARP:

- General rule is **three years** (SOL is two years after tax is paid, **if this time is later**).
- Extended by ARP to **five years** for ERC claims for **Q3 of 2021. Applies only for IRS assessments, not refund claims.**
- All others have **three years [Q1, Q2, Q3, and Q4 of 2020; and Q1, Q2 of 2021].**
- ARP did not change in SOL for income tax returns. **Remains at three years.**

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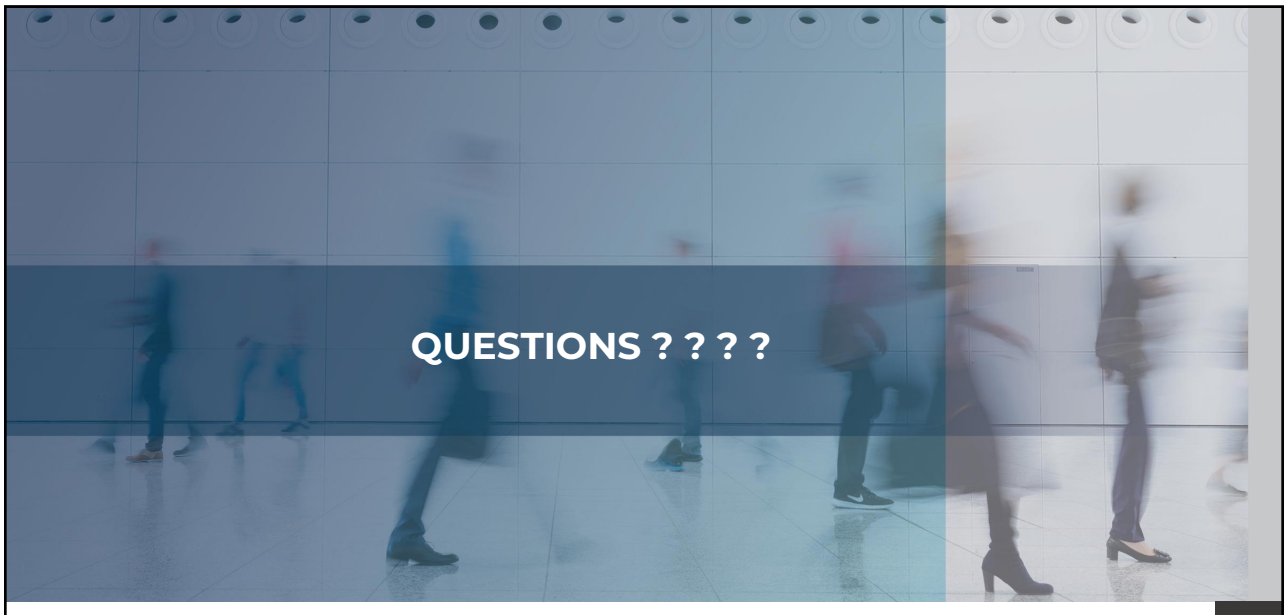

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Office of Chief Counsel
Internal Revenue Service
memorandum

Number: **AM 2023-005**
Release Date: 7/21/2023

CC:EEE
POSTN-113151-23

UILC: 3134.00-00

date: June 30, 2023

to: Mark L. Hulse
Division Counsel
(Tax Exempt & Government Entities Division Counsel)

from: Rachel D. Leiser Levy
Associate Chief Counsel
(Employee Benefits, Exempt Organizations and Employment Taxes)

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subject: Whether an Employer Experienced a Full or Partial Suspension of the Operation of a Trade or Business under Section 2301 of the Coronavirus Aid, Relief, and Economic Security Act or Section 3134 of the Internal Revenue Code due to a Supply Chain Disruption

This Generic Legal Advice Memorandum (GLAM) responds to your request for assistance. This GLAM may not be used or cited as precedent.

ISSUES:

Whether, under the scenarios involving supply chain disruptions described below, the operation of an employer's trade or business was fully or partially suspended during a 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) (also referred to as the "suspension test") such that the employer satisfies the definition of an "eligible employer" under section 2301(c)(2)(A)(ii)(I) of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, 134 Stat. 281 (March 27, 2020), and section 3134(c)(2)(A)(ii)(I) of the Internal Revenue Code (Code).

FACTS:

Scenario 1

Employer A was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. However, during 2020 and 2021, Employer A experienced several delays in receiving critical goods from Supplier 1. At all times during 2020 and 2021, Employer A continued to operate because Employer A had a surplus of the critical goods normally provided by Supplier 1. Employer A assumed that Supplier 1's delay in delivering critical goods was caused by COVID-19. Employer A inquired and Supplier 1 vaguely confirmed that the delay was due to COVID-19. Supplier 1 did not provide a governmental order from an appropriate governmental authority and Employer A was unable to locate one.

Scenario 2

Employer B was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. However, certain critical goods from Supplier 2 were stuck at port in State X. Employer B assumed the bottleneck at the port was a result of COVID-19. Employer B could not identify any specific governmental order applicable to Supplier 2 or any specific governmental order that caused the bottleneck at the port. Some news sources stated that COVID-19 was the reason for the bottleneck, while others cited reasons such as increases in consumer spending and aging infrastructure. In addition, Supplier 2 mentioned to Employer B that other critical goods that were not stuck at port would be delayed due to a truck driver shortage. Employer B saw some discussion on social media that the truck driver shortage was because drivers were out sick due to COVID-19.

Scenario 3

Employer C and Supplier 3 are located in a jurisdiction that issued governmental orders suspending both of their business operations for the duration of April 2020. Employer C and Supplier 3's jurisdiction lifted all orders related to COVID in May 2020. For the remainder of 2020 and 2021, Employer C experienced a delay in receiving critical goods from Supplier 3. Supplier 3 does not provide a reason for the delay, but Employer C assumes the delay is due to the governmental order in place in April 2020.

Scenario 4

Employer D was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. During 2020 and 2021, Employer D could not obtain critical goods from Supplier 4. However, Employer D was able to obtain the goods from an alternate supplier. The critical goods from the alternate supplier cost 35% more than those from Supplier 4. Employer D could continue to operate its trade or business even though it was not as profitable as in 2019.

Scenario 5

Employer E operates a large retail business selling a wide variety of products. Employer E was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 in 2021. Due to various supply chain disruptions, Employer E was not able to stock a limited number of products and was forced to raise prices on other products that were in limited supply. However, at no time did the product shortage prevent Employer E from continuing to fully operate as a retail business during 2021.

LAW:

Section 2301 of the CARES Act, as amended by section 206 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (Relief Act) (enacted as Division EE of the Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, 134 Stat. 1182 (December 27, 2020)), provides an employee retention credit for employers subject to closure due to COVID-19.

Section 2301(a) of the CARES Act, as amended by section 206 of the Relief Act, provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 50 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 2301(m) of the CARES Act, as amended by section 206 of the Relief Act, limits the employee retention credit under section 2301 of the CARES Act to wages paid after March 12, 2020, and before January 1, 2021.

Section 2301(a) of the CARES Act, as amended by section 207 of the Relief Act, provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 70 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 2301(m) of the CARES Act, as amended by section 207 of the Relief Act, limits the employee retention credit under section 2301 of the CARES Act to wages paid after March 12, 2020, and before July 1, 2021.

Section 207(k) of the Relief Act provides that the amendments made by section 207 of the Relief Act shall apply to quarters beginning after December 31, 2020. Therefore, the employee retention credit under section 2301 of the CARES Act is equal to 50 percent of the qualified wages with respect to each employee of an eligible employer for calendar quarters in 2020 and 70 percent of the qualified wages with respect to each employee of an eligible employer for the first and second calendar quarters in 2021.

Section 9651 of the American Rescue Plan Act of 2021 (ARP), Pub. L. 117-2, 135 Stat. 4, enacted section 3134 of the Code. Section 3134 of the Code provides an employee retention credit for employers subject to closure due to COVID-19 that is substantially similar in structure to that of section 2301 of the CARES Act, as amended by section 207 of the Relief Act, with certain changes.

Section 3134(a) of the Code provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 70 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 3134(n) of the Code, as amended by section 80604 of the Infrastructure Investment and Jobs Act, Pub. L. 117-58, 135 Stat. 429 (2021), limits the employee retention credit under section 3134 of the Code to wages paid after June 30, 2021, and before October 1, 2021 (or, in the case of wages paid by an eligible employer which is a recovery startup business, January 1, 2022).

Section 2301(c)(2)(A)(ii)(I) of the CARES Act defines the term “eligible employer,” in part, as any employer which was carrying on a trade or business during the calendar quarter for which the credit is determined under section 2301(a) of the CARES Act, and with respect to any calendar quarter, for which the operation of the trade or business is 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 COVID-19.

Section 3134(c)(2)(A)(ii)(I) of the Code similarly defines the term “eligible employer,” in part, as any employer which was carrying on a trade or business during the calendar quarter for which the credit is determined under section 3134(a) of the Code, and with respect to any calendar quarter, for which the operation of the trade or business is 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 COVID-19.

Notice 2021-20, 2021-11 I.R.B. 922, provides guidance on the employee retention credit under section 2301 of the CARES Act, as amended by section 206 of the Relief Act.

Section III.C. of Notice 2021-20 provides specific guidance on orders from an appropriate governmental authority (also referred to as governmental orders).

Section III.D. of Notice 2021-20 provides specific guidance on when the operation of an employer’s trade or business is fully or partially suspended for purposes of the employee retention credit under section 2301 of the CARES Act.

Notice 2021-23, 2021-16 IRB 1113, provides guidance on the employee retention credit under section 2301 of the CARES Act, as amended by section 207 of the Relief Act.

Notice 2021-23 amplified Notice 2021-20; under Notice 2021-23, the provisions of section III.D. of Notice 2021-20 continued to apply to section 2301 of the CARES Act, as amended by section 207 of the Relief Act.

Notice 2021-49, 2021-34 IRB 316, provides guidance on the employee retention credit under section 3134 of the Code. Notice 2021-49 amplified Notice 2021-20 and Notice 2021-23; under Notice 2021-49, the provisions of section III.D. of Notice 2021-20 continued to apply to the third and fourth calendar quarters of 2021 for purposes of the employee retention credit under section 3134 of the Code.

Notice 2021-65, 2021-51 IRB 880, modified Notice 2021-49 to implement statutory changes made by the Infrastructure Act. Under Notice 2021-65, section III.D. of Notice 2021-20 no longer applied to the fourth calendar quarter of 2021 for purposes of the employee retention credit under section 3134 of the Code.

Section III.D., Q&A 12 of Notice 2021-20 provides that an employer may be considered to have a full or partial suspension of operations due to a governmental order if, under the facts and circumstances, the business's suppliers are unable to make deliveries of critical goods or materials due to a governmental order that causes the supplier to suspend its operations. If the facts and circumstances indicate that the business's operations are fully or partially suspended as a result of the inability to obtain critical goods or materials from its suppliers because the suppliers were required to suspend operations, then the business would be considered an eligible employer for calendar quarters during which its operations are fully or partially suspended and may be eligible to receive the employee retention credit.

Section III.N., Q&A 70 of Notice 2021-20 provides guidance on the records an eligible employer should maintain to substantiate eligibility for the employee retention credit.

ANALYSIS:

The statutory language in section 2301(c)(2)(A)(ii)(I) of the CARES Act and section 3134(c)(2)(A)(ii)(I) of the Code does not include supply chain disruptions. Instead, section III.D., Q/A-12 of Notice 2021-20 provides a narrow, limited exception for employers that had to fully or partially suspend their business operations because the employers' suppliers who provided critical goods or materials to the employer were fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority. This limited exception provides that "[a]n employer may be considered to have a full or partial suspension of operations due to a governmental order if, under the facts and circumstances, the business's suppliers are unable to make deliveries of critical goods or materials due to a governmental order that causes the supplier to suspend its operations."

Section 2301(c)(2)(A)(ii)(I) of the CARES Act and section 3134(c)(2)(A)(ii)(I) of the Code require that the operation of the employer's trade or business be fully or partially

suspended due to orders from an appropriate governmental authority. A supply chain disruption, by itself, does not rise to the level of a full or partial suspension primarily because no governmental order applies to the employer's operations. In addition, the goods or materials that are disrupted may not have had an impact on the employer's operations that rises to the level of a full or partial suspension, or the employer may have been able to obtain the goods or materials from an alternate supplier.

The guidance provided by section III.D., Q/A-12 of Notice 2021-20 allows the employer to "step into the shoes" of its supplier for purposes of the suspension test. To meet the terms of this exception, as explained in Q/A-12, the supplier must have been subject to a governmental order that causes the supplier to suspend its operations. In addition to having a governmental order, the employer must substantiate its eligibility for the credit by providing records or documentation demonstrating that (i) the governmental order caused the supplier to suspend operations, (ii) the inability to obtain the supplier's goods or materials caused a full or partial suspension of the employer's business operations, and (iii) the employer was not able to obtain these critical goods or materials from an alternate supplier. See Section III.N., Q&A 70 of Notice 2021-20; see also Treas. Reg. § 31.6001-1 and Treas. Reg. § 1.6001-1. If the facts and circumstances dictate that the employer's operations are fully or partially suspended because of the governmental order suspending the supplier from providing the critical goods or materials, then the employer may be considered an eligible employer under the guidance provided by Q/A-12.

CONCLUSION:

Scenario 1

Employer A does not meet the definition of eligible employer provided under section III.D., Q/A-12 of Notice 2021-20 because Employer A cannot demonstrate that a governmental order applicable to Supplier 1 fully or partially suspended Supplier 1's trade or business operations.

Even if Employer A received or could locate the governmental orders applicable to Supplier 1, Employer A did not have to cease operations because Employer A had a reserve of critical goods allowing Employer A to continue operations; thus, Employer A did not experience a full or partial suspension of operations due to an inability to obtain Supplier 1's critical goods. The relevant inquiry is whether Employer A's trade or business operations could continue; since Employer A was able to continue its own business operations despite the supply chain disruption, it was not subject to a full or partial suspension of operations.

Scenario 2

Employer B does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 because Employer B cannot demonstrate that a

governmental order applicable to Supplier 2 fully or partially suspended Supplier 2's trade or business operations. In addition, while COVID-19 may have been a contributing factor to the bottleneck at the port or the truck driver shortage, Employer B could not substantiate that any specific governmental order caused a bottleneck at the port. Even if Employer B could identify governmental orders applicable to the bottleneck, Employer B must substantiate that the bottleneck and thus the suspension of Supplier 2 was due to the orders.

Scenario 3

Employer C is an eligible employer in the second calendar quarter of 2020 because its business operations were fully or partially suspended due to a governmental order. However, only wages paid with respect to the period during which Employer C is fully or partially suspended due to a governmental order may be considered qualified wages. See section III.D., Q/A-22 of Notice 2021-20.

Employer C does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 for any subsequent calendar quarter in 2020 or 2021 because Employer C cannot demonstrate that a governmental order applicable to Supplier 3 fully or partially suspended Supplier 3's trade or business operations. The residual delays caused by a governmental order in place during a prior calendar quarter will not constitute a governmental order in subsequent calendar quarters once the order has been lifted.

Scenario 4

Employer D does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 because Employer D could continue to operate its trade or business. Employer D was not prevented from operating its trade or business at any point during 2020 or 2021. Incurring a higher cost for critical goods does not result in a full or partial suspension of operations.

Scenario 5

Employer E does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 during calendar year 2021 because Employer E cannot demonstrate that a governmental order applicable to a supplier of critical goods or materials caused the supplier to suspend operations and that Employer E was unable to obtain critical goods and materials causing a full or partial suspension of Employer E's business operations. At all points during 2021, Employer E was able to operate its retail business. While a limited number of products were not available, Employer E was still able to offer a wide variety of products to its customers and Employer E was not forced to partially suspend operations.

* * *

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call Matthew Leiwant (202) 317-4774 if you have any further questions.

Part III – Administrative, Procedural, and Miscellaneous

Guidance on Amortization of Specified Research or Experimental Expenditures under Section 174

Notice 2023-63

SECTION 1. OVERVIEW

This notice announces that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) intend to issue proposed regulations (forthcoming proposed regulations) addressing (1) the capitalization and amortization of specified research or experimental (SRE) expenditures under § 174 of the Internal Revenue Code (Code)[1], as amended by Public Law 115-97, 131 Stat. 2054 (Dec. 22, 2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA), (2) the treatment of SRE expenditures under § 460, and (3) the application of § 482 to cost sharing arrangements involving SRE expenditures. The Treasury Department and the IRS intend to propose rules in the forthcoming proposed regulations consistent with the interim guidance provided in sections 3 through 9 of this notice. Section 10 of this notice provides that taxpayers may rely on the interim guidance provided in sections 3 through 9 of this notice prior to the publication date of the forthcoming proposed

[1] Unless otherwise specified, all "section" or "§" references are to sections of the Code or the Income Tax Regulations (26 CFR part 1).

regulations in the Federal Register. Section 11 of this notice requests comments, including comments on specific issues and issues not addressed in this notice.

The guidance in this notice does not apply for purposes of determining whether an expenditure paid or incurred for taxable years beginning before January 1, 2022, is a research or experimental expenditure under § 174 as in effect for taxable years beginning before January 1, 2022 (former § 174). This notice provides guidance regarding expenditures that are treated as SRE expenditures under § 174 and, therefore, affects expenditures that may be treated as SRE expenditures for purposes of § 41(d)(1)(A) and § 1.41-4(a)(2)(i). However, this notice is not intended to change the rules for determining eligibility for or computation of the research credit under § 41 and the regulations thereunder, including rules for "research with respect to computer software," and the definitions of "qualified research" and "qualified research expenses."

SECTION 2. BACKGROUND

.01 Prior law treatment of research or experimental expenditures.

(1) In general. Former § 174 was first enacted in 1954 to provide certainty to taxpayers regarding the treatment of otherwise capitalizable research or experimental expenditures with no determinable useful life. See H.R. Rep. No.1337, 83d Cong., 2d Sess. 28 (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. 33 (1954). Before the enactment of former § 174, courts consistently held that the law required capitalization of product research and development costs, including production costs of tangible property used in the research process. Under such prior law, expenditures related to a taxpayer's research and experimentation generally were capitalized and held in suspense until the taxpayer could determine (1) whether

or not the research had failed; and (2) if the research was successful, whether or not the research resulted in property that had a useful life determinable with reasonable accuracy.

Former § 174 allowed taxpayers to elect to deduct research or experimental expenditures paid or incurred in connection with a trade or business as currently deductible expenses, to capitalize and amortize such expenditures over a period of not less than 60 months, or to charge such expenditures to capital account.

(2) Definition of research or experimental expenditures under former § 174.

The provisions of § 1.174-2 address the scope and definition of research or experimental expenditures under former § 174. Specifically, § 1.174-2(a)(1) provides that the term "research or experimental expenditures" means those expenditures incurred in connection with a taxpayer's trade or business that represent research and development costs in the experimental or laboratory sense, and generally includes all such costs incident to the development or improvement of a product or a component or subcomponent of the product, as well as the costs of obtaining a patent. Expenditures represent research and development costs in the experimental or laboratory sense if they are for activities intended to discover information that would eliminate uncertainty concerning the development or improvement of a product. Section 1.174-2(a)(3) defines the term "product" to include any pilot model, process, formula, invention, technique, patent, or similar property, and includes products to be used by the taxpayer in its trade or business as well as products to be held for sale, lease, or license.

Section 1.174-2(a)(10) and (b)(3) generally provide that former § 174 also

applies to expenditures paid or incurred by a taxpayer for research or experimentation carried on by another person or organization (such as a research institute, foundation, engineering company, or similar contractor) on behalf of the taxpayer, provided that such expenditures are made at the taxpayer's order and risk. However, § 1.174-2 does not explicitly address expenditures paid by a contractor for research or experimentation carried on for another person or organization.

Section 1.174-2(a) also provides guidance on expenditures that are not subject to former § 174, including costs paid or incurred in the production of a product after the elimination of uncertainty concerning the development or improvement of the product, and expenditures for: quality control testing, efficiency surveys, management studies, consumer surveys, advertising or promotions, the acquisition of another's product, and research in connection with literary, historical or similar projects. In addition, § 1.174-2(b) and former § 174(c) provide that any expenditure for the acquisition or improvement of land or depreciable property to be used in connection with the research or experimentation and of a character which is subject to the allowance under section 167 or section 611 are not research or experimental expenditures. However, allowances for depreciation and depletion with respect to such property are treated as research or experimental expenditures. Finally, § 1.174-2(c) and former § 174(d) provide that the provisions of former § 174 are not applicable to any expenditures paid or incurred for the purpose of ascertaining the existence, location, extent, or quality of any deposit of ore, oil, gas, or other mineral.

(3) Software development. Prior to the effective date of the TCJA amendments to former § 174, section 5 of Rev. Proc. 2000-50, 2000-2 C.B. 601, permitted

taxpayers to treat costs to develop computer software that were not otherwise treated as research or experimental expenditures under former § 174 as currently deductible expenses or capital expenditures that are amortized over 60 months or 36 months. Accordingly, under section 5 of Rev. Proc. 2000-50, costs to develop computer software that did not otherwise meet the definition of research or experimental expenditures under former § 174 were afforded generally similar treatment to research or experimental expenditures under former § 174. Rev. Proc. 2000-50 does not define software development or otherwise describe software development activities. See also Kellett v. Commissioner, T.C. Memo. 2022-62 (discussing, and questioning the statutory support for, deduction of software development expenditures under Rev. Proc. 2000-50).

.02 Treatment of research or experimental expenditures under the TCJA.

(1) Requirement to capitalize and amortize SRE expenditures. Section 13206(a) of the TCJA amended former § 174 for amounts paid or incurred in taxable years beginning after December 31, 2021. For such amounts, § 174(a)(1) disallows deductions for SRE expenditures, except as provided in § 174(a)(2). Section 174(a)(2) requires taxpayers to charge SRE expenditures to capital account and allows amortization deductions of such capitalized expenditures ratably over the applicable § 174 amortization period, beginning with the midpoint of the taxable year in which such expenditures are paid or incurred. As used in this notice, the term “applicable § 174 amortization period” refers to a 5-year (60-month) period in the case of SRE expenditures attributable to domestic research or a 15-year (180-month) period in the case of SRE expenditures attributable to foreign research, as defined in section 3.03 of

this notice.

(2) Definition of SRE expenditures. Section 174(b), as amended by section 13206(a) of the TCJA, defines "SRE expenditures" to mean, with respect to any taxable year beginning after December 31, 2021, research or experimental expenditures that are paid or incurred by the taxpayer during such taxable year in connection with the taxpayer's trade or business. See Snow v. Commissioner, 416 U.S. 500 (1974) ("in connection with" a trade or business is broader than "in carrying on" a trade or business).

(3) Software development. Section 13206(a) of the TCJA added new § 174(c)(3) to require that any amount paid or incurred in connection with the development of any software in taxable years beginning after December 31, 2021, be treated as a research or experimental expenditure (and thus an SRE expenditure to the extent paid or incurred by the taxpayer during the taxable year in connection with the taxpayer's trade or business).

(4) Amortization deductions for disposed of, retired, or abandoned property. Section 13206(a) of the TCJA added new § 174(d) to provide that deductions of SRE expenditures may not be taken on account of the disposition, retirement, or abandonment of property with respect to which such SRE expenditures are paid or incurred. If such property is disposed of, retired, or abandoned during the applicable § 174 amortization period, § 174(d) requires that the amortization deductions for such SRE expenditures continue over that period.

(5) Other changes to former § 174. Section 13206(a) of the TCJA redesignated former § 174(c) to § 174(c)(1) and former § 174(d) to § 174(c)(2), removed former

§ 174(e), which provided that only reasonable expenditures are considered research or experimental expenditures under former § 174, and also removed former § 174(f), which contained cross-references to basis adjustments under § 1016(a)(14) and to an election for 10-year amortization under § 59(e).

(6) Change in method of accounting.

(a) TCJA requirement. Section 13206(b) of the TCJA requires taxpayers to apply the provisions of § 174, as amended by section 13206(a) of the TCJA, as a change in method of accounting for purposes of § 481, initiated by the taxpayer and made with the consent of the Secretary of the Treasury or her delegate, and applied on a cutoff basis to SRE expenditures paid or incurred in taxable years beginning after December 31, 2021. Thus, no adjustments under § 481(a) are permitted or required with respect to research or experimental expenditures paid or incurred in taxable years beginning before January 1, 2022.

(b) Procedural guidance. On December 12, 2022, the Treasury Department and the IRS issued Rev. Proc. 2023-8, 2023-3 I.R.B. 407, to provide procedures for taxpayers to obtain automatic consent to change methods of accounting to comply with § 174, as amended by the TCJA. On December 29, 2022, the Treasury Department and the IRS issued Rev. Proc. 2023-11, 2023-3 I.R.B. 417, to modify and supersede Rev. Proc. 2023-8. The change in method of accounting provided by Rev. Proc. 2023-11 was subsequently included in section 7.02 of Rev. Proc. 2023-24, 2023-28 I.R.B. 1207. Section 7.02 of Rev. Proc. 2023-24 implements the requirement imposed by § 13206(b) of the TCJA that a taxpayer must make this change in method of accounting on a cutoff basis if the change was made during the taxpayer's first taxable year

beginning after December 31, 2021. However, section 7.02 of Rev. Proc 2023-24 provides that a taxpayer making the change for a taxable year subsequent to the taxpayer's first taxable year beginning after December 31, 2021, is required to make that change with a modified § 481(a) adjustment that takes into account only SRE expenditures paid or incurred in taxable years beginning after December 31, 2021. Section 7.02(7) of Rev. Proc. 2023-24 also provides that a taxpayer that changes its method of accounting for SRE expenditures under the revenue procedure will receive limited audit protection. Specifically, audit protection will not apply for expenditures paid or incurred in taxable years beginning before January 1, 2022. Audit protection also will not apply for expenditures paid or incurred in taxable years beginning after December 31, 2021, if a change in method of accounting is made for the taxable year immediately subsequent to the first taxable year beginning after December 31, 2021. See section 10.02 of this notice for additional procedural guidance the Treasury Department and IRS intend to issue.

SECTION 3. CAPITALIZATION AND AMORTIZATION OF SRE EXPENDITURES

.01 Purpose. The Treasury Department and the IRS intend to propose rules in forthcoming proposed regulations consistent with the interim guidance provided in this section 3, which provides taxpayers with clarity regarding the requirement in § 174(a) to capitalize and amortize SRE expenditures and the treatment of short taxable years.

.02 Requirement to capitalize and amortize SRE expenditures. Taxpayers are required to capitalize SRE expenditures (as defined in section 4.02(2) of this notice) and amortize such expenditures ratably over the applicable § 174 amortization period beginning with the midpoint of the taxable year in which such expenditures are paid or

incurred.

.03 Definition of foreign research. The term foreign research means any research conducted outside the United States, the Commonwealth of Puerto Rico, or any U.S. territory or other possession of the United States. See §§ 174(a)(2)(B) and 41(d)(4)(F).

.04 SRE expenditures attributable to foreign research. Taxpayers must look to where the SRE activities (as defined in section 4.02(4) of this notice) are performed to determine whether the corresponding SRE expenditures are attributable to foreign research for purposes of section 3.02 of this notice.

.05 Definition of midpoint. Except as provided in section 3.06 of this notice, for purposes of determining when amortization begins under § 174(a)(2)(B) and section 3.02 of this notice, the term midpoint means the first day of the seventh month of the taxable year in which the SRE expenditures are paid or incurred. See section 7.03 of this notice for interim guidance with respect to SRE expenditures that relate to property disposed of before the midpoint of the taxable year in which such SRE expenditures are paid or incurred.

.06 Short taxable years.

(1) In general. The amortization deduction for a short taxable year is based on the number of months in the short taxable year. If a short taxable year includes part of a month, the entire month is included in the number of months in the taxable year, but the same month may not be counted more than once. If a taxpayer has two successive short taxable years and the first short taxable year ends in the same month that the second short taxable year begins, the taxpayer should include that month in the first short taxable year and not in the second short taxable year.

(2) Midpoint for short taxable years. The midpoint of a short taxable year is the first day of the midpoint month. In the case of a short taxable year with an even number of months (as determined under section 3.06(1) of this notice), the midpoint month is determined by dividing the number of months in the short taxable year by two and then adding one (for example, for a short taxable year consisting of ten months, the midpoint month is the sixth month of the short taxable year ((10 / 2) + 1 = 6)). In the case of a short taxable year with an odd number of months (as determined under section 3.06(1) of this notice), the midpoint month is the month for which there are an equal number of months before and after such month (for example, for a short taxable year consisting of seven months, the mid-point month is the fourth month of the short taxable year).

.07 Example.

(1) Facts. Taxpayer is a calendar-year taxpayer that incorporated and began operations on October 17, 2022. In 2022, Taxpayer paid or incurred $60,000 in SRE expenditures that were not attributable to foreign research. Taxpayer has no short taxable years after its initial taxable year.

(2) Analysis. Taxpayer has a short taxable year that begins on October 17, 2022, and ends on December 31, 2022, and thus is treated as having a three-month taxable year under section 3.06(1) of this notice. The midpoint month is November, and thus November 1, 2022, will be treated as the midpoint under section 3.06(2) of this notice. In 2022, Taxpayer amortizes $2,000 of SRE expenditures ($60,000 / 60 months × 2 months). In taxable years 2023 through 2026, each a full 12-month taxable year, Taxpayer amortizes $12,000 ($60,000 / 60 months × 12 months) each year, or $48,000 total. In 2027, Taxpayer amortizes the remaining $10,000 ($60,000 / 60 months × 10

months).

SECTION 4. SCOPE OF SECTION 174

.01 Purpose. The Treasury Department and the IRS intend to propose rules in forthcoming proposed regulations consistent with the interim guidance provided in this section 4, which provides taxpayers with clarity in determining whether expenditures are SRE expenditures subject to capitalization and amortization under § 174.

.02 Definition of SRE expenditures and other relevant terms. For purposes of this notice:

(1) Terms used in § 1.174-2. Unless otherwise provided, all terms used in this notice have the same meaning as those in § 1.174-2. For example, the term product has the meaning set forth in § 1.174-2(a)(3).

(2) SRE expenditures defined. The term SRE expenditures means, with respect to any taxable year beginning after December 31, 2021, research or experimental expenditures (as defined in section 4.02(3) of this notice), which are paid or incurred by the taxpayer during such taxable year in connection with the taxpayer's trade or business.

(3) Research or experimental expenditures defined. The term research or experimental expenditures means expenditures that--

(a) satisfy the requirements under § 1.174-2 to be research or experimental expenditures, or

(b) are paid or incurred in connection with the development of any computer software (as provided in section 5 of this notice), regardless of whether such expenditures are research or experimental expenditures under § 1.174-2.

See section 6 of this notice for rules to determine whether expenditures paid or incurred pursuant to a contract meet the definition of research or experimental expenditures under this section 4.02(3).

(4) SRE activities defined. The term SRE activities means—

(a) software development activities described in section 5.03 of this notice, or

(b) research or experimental activities described in § 1.174-2 (that is, activities in the experimental or laboratory sense intended to discover information that would eliminate uncertainty concerning the development or improvement or appropriate design of a product or a component or subcomponent of a product).

.03 Identification and allocation of SRE expenditures. As provided in section 4.02(2) and (3) of this notice, SRE expenditures include expenditures that satisfy the requirements under § 1.174-2 or are paid or incurred in connection with the development of any computer software, regardless of whether such software expenditures satisfy the requirements under § 1.174-2. Section 1.174-2(a)(1) and (5) provide that research or experimental expenditures under § 1.174-2 include all costs incident to the development or improvement of a product, a component of a product, or subcomponent of a product, as applicable (that is, research or experimental expenditures under § 1.174-2 include all costs incident to SRE activities described in section 4.02(4)(b) of this notice). Section 4.03(1) of this notice provides a non-exhaustive list of examples of the types of costs that are incident to SRE activities described in section 4.02(4)(b) of this notice or paid or incurred in connection with software development activities described in sections 4.02(4)(a) and 5.03 of this notice. In other words, section 4.03(1) of this notice provides a non-exhaustive list of examples

of the types of costs that are SRE expenditures. Section 4.03(2) of this notice provides a list of costs that are not permitted or required to be treated as SRE expenditures, regardless of whether they may be incident to SRE activities described in section 4.02(4) of this notice. Section 4.03(3) of this notice provides interim guidance addressing the allocation of costs, including those described in section 4.03(1) of this notice, to SRE activities.

(1) Examples of costs that are SRE expenditures. The types of costs that are considered incident to SRE activities described in section 4.02(4)(b) of this notice or paid or incurred in connection with software development activities described in sections 4.02(4)(a) and 5.03 of this notice include but are not limited to:

(a) Labor costs. Labor costs of full-time, part-time, and contract employees and independent contractors who perform, supervise, or directly support SRE activities. Labor costs include all elements of compensation other than severance compensation, such as basic compensation, stock-based compensation, overtime pay, vacation pay, holiday pay, sick leave pay, payroll taxes, pension costs, employee benefits, and payments to a supplemental unemployment benefit plan.

(b) Materials and supplies costs. Costs of materials and supplies, including tools and equipment that are not depreciable under § 168, which are used or consumed in the performance of SRE activities or in the direct support of SRE activities. For example, a cost described in § 1.162-3, relating to the cost of a material or supply, may be an SRE expenditure.

(c) Cost recovery allowances. Depreciation, amortization, or depletion allowances with respect to property used in the performance of SRE activities or in the

direct support of SRE activities, including property placed in service in a taxable year that begins on or before December 31, 2021. For example, depreciation with respect to a test bed used in the performance of SRE activities, or allocable depreciation with respect to a facility in which SRE activities, or services that directly support SRE activities, are performed.

(d) Patent costs. Costs of obtaining a patent, such as attorneys' fees expended in making and perfecting a patent application.

(e) Certain operation and management costs. Rent, utilities, insurance, taxes, repairs and maintenance costs, security costs, and similar overhead costs with respect to facilities, equipment and other assets used in the performance of SRE activities or in the direct support of SRE activities.

(f) Travel costs. Travel costs for the performance of SRE activities or the direct support of SRE activities.

(2) Costs that are not treated as SRE expenditures. The following costs are not permitted or required to be treated as SRE expenditures, regardless of whether they may be incident to SRE activities described in section 4.02(4)(b) of this notice or paid or incurred in connection with software development activities described in sections 4.02(4)(a) and 5.03 of this notice:

(a) Costs paid or incurred by general and administrative service departments (or functions) that only indirectly support or benefit SRE activities (for example, services of payroll personnel in preparing salary checks of research personnel, services of human resources personnel who hire research personnel, or services of accounting personnel who account for research expenses);

(b) Interest on debt to finance SRE activities;

(c) Costs paid or incurred for activities described in section 5.05 of this notice;

(d) Costs to input content into a website;

(e) Costs for website hosting that involve the payment of a specified, periodic fee to an Internet service provider in return for hosting a website on its server(s) connected to the Internet;

(f) Costs to register an Internet domain name or trademark;

(g) Costs listed in § 1.174-2(a)(6)(i)-(vii);

(h) Amounts representing amortization of SRE expenditures; and

(i) Amounts representing amortization of research or experimental expenditures paid or incurred in taxable years beginning before January 1, 2022.

(3) Allocation method. To determine total SRE expenditures for a taxable year, taxpayers must allocate costs, including the types of costs described in section 4.03(1) of this notice, to SRE activities on the basis of a cause-and-effect relationship between the costs and the SRE activities or another relationship that reasonably relates the costs to the benefits provided to the SRE activities. The allocation method used for one type of cost may be different than the allocation method used for another type of cost. However, the allocation method used for each type of cost must be applied on a consistent basis. For example, a taxpayer that consistently allocates labor costs described in section 4.03(1)(a) of this notice to SRE activities by multiplying such labor costs by the ratio of the total time the person or people actually spent performing, supervising, or directly supporting SRE activities during the taxable year to the total time the person or people spent performing all services for the taxpayer during the taxable

year, meets the requirements in this section 4.03(3). Similarly, a taxpayer that consistently allocates facility cost recovery allowances described in section 4.03(1)(c) of this notice to SRE activities by multiplying such cost recovery allowances by the ratio of the square footage of the area used to conduct or directly support SRE activities to the total square footage of the facility, meets the requirement of this section 4.03(3). An allocation method for a particular type of cost that meets the requirements of this section 4.03(3) may not be appropriate for purposes of allocating that same type of cost under other sections of the Code.

(4) Example. The following example illustrates the rules set forth in section 4.03 of this notice.

(a) Facts. Company A, a calendar year taxpayer, is engaged in the business of manufacturing chemical products. On January 1, 2023, Company A begins a research project to develop a new product. This research project constitutes an SRE activity. Company A does not undertake any other SRE activities during its 2023 taxable year. Company A is comprised of six departments: (1) the Manufacturing Department, (2) the Research Department, (3) the Engineering Department, (4) the Legal Department, (5) the Personnel Department, and (6) the Accounting Department. The Manufacturing Department does not provide any support services to the Research Department. The Personnel Department provides indirect support services to the Research Department by hiring research personnel and preparing their paychecks but does not directly support any aspect of the research project. The Accounting Department provides indirect support services to the Research Department by paying Research Department invoices and accounting for research costs but does not directly support any aspect of

the research project. The Engineering Department provides direct support services to the Research Department with respect to the research project by collaborating with the Research Department to develop the new product. The Legal Department provides direct support services to the Research Department with respect to the research project by preparing patent applications for the new product. Company A owns the following assets, each of which is used, in whole or in part, to perform research or directly support the research project:

Description	**Department(s)**	**Depreciation for 2023**
10,000 square foot facility	The Manufacturing Department occupies 5,000 square feet of the facility. The other departments each occupy 1,000 square feet.	$200,000
Computers, furniture, and equipment used exclusively for the research project	Research Department	$150,000
Computers, furniture, and equipment used by the Engineering Department	Engineering Department	$100,000
Computers and furniture used by the Legal Department	Legal Department	$20,000

In addition to interest on debt used to finance operations and research and costs specific to the Manufacturing, Personnel, and Accounting Departments, Company A incurs the following costs during its 2023 taxable year:

Description	**Department(s)**	**Total Cost**
Materials and supplies used exclusively for the research project	Research Department	$50,000
Materials and supplies used by the Engineering Department	Engineering Department	$40,000
Materials and supplies used by the Legal Department	Legal Department	$10,000

Labor costs of Research Department employees and their direct supervisor, each of which spends 100% of their time on the research project	Research Department	$600,000
Labor costs of all Engineering Department employees, each of which spends 20% of their time on the research project	Engineering Department	$200,000
Labor costs of all Legal Department employees, each of which spends 10% of their time on the research project	Legal Department	$100,000
Electricity for the facility	The Research Department and the Manufacturing Department consume large amounts of electricity relative to the other departments. The Research Department uses 100,000 kilowatt-hours of electricity. The Manufacturing Department uses 220,000 kilowatt-hours of electricity. The other departments each use 20,000 kilowatt-hours of electricity.	$200,000
Other utilities and overhead costs for the facility	All departments benefit from such costs in proportion to square footage occupied	$100,000
Other miscellaneous overhead costs incurred by the Research Department	Research Department	$50,000
Other miscellaneous overhead costs incurred by the Engineering Department	Engineering Department	$50,000
Other miscellaneous overhead costs incurred by the Legal Department	Legal Department	$50,000

(b) Analysis. Pursuant to section 4.03(1) of this notice, Company A determines that the costs described in the tables in section 4.03(4)(a) are the types of costs that are incident to SRE activities described in section 4.02(4) of this notice. Pursuant to section

4.03(2)(a) of this notice, Company A determines that the costs incurred by the Manufacturing, Personnel, and Accounting Departments are not treated as SRE expenditures because the activities of those departments are not SRE activities and such costs either do not, or only indirectly, support or benefit SRE activities. Similarly, pursuant to section 4.03(2)(b) of this notice, Company A determines that interest on debt used to finance operations and research is not treated as an SRE expenditure. Pursuant to section 4.03(3) of this notice, Company A determines its total SRE expenditures for 2023 by allocating the costs described in the tables in section 4.03(4)(a) of this notice to its SRE activities on the basis of a cause-and-effect relationship between the costs and the SRE activities or another relationship that reasonably relates the costs to the benefits provided to the SRE activities as provided in the following table. This allocation method generally relates the costs described in the tables in section 4.03(4)(a) of this notice to SRE activities on the basis of total labor hours spent on such activities; however, for certain costs, Company A determines that a different allocation method more appropriately relates the costs to the benefits that they provide to the SRE activities, such as an allocation method based on the relative square footage of each department. As noted in section 4.03(4)(a), employees in the Research Department spent 100% of their time on SRE activities, employees in the Engineering Department spent 20% of their time on SRE activities, and employees in the Legal Department spent 10% of their time on SRE activities.

Description	**Allocation Method**	**Amount of SRE Expenditure**
Depreciation on facility - $200,000	Research Department: $20,000 ($200,000 × 1,000/10,000 square feet × 100% of time spent by Research Department on research project) + Engineering Department: $4,000 ($200,000 × 1,000/10,000 square feet × 20% of time spent by Engineering Department on research project) + Legal Department: $2,000 ($200,000 × 1,000/10,000 square feet × 10% of time spent by Legal Department on research project)	$26,000
Depreciation on computers, furniture, and equipment used by the Research Department exclusively for the research project - $150,000	$150,000 × 100% use for research project	$150,000
Depreciation on computers, furniture and equipment used by the Engineering Department - $100,000	$100,000 × 20% of time spent by Engineering Department employees on the research project	$20,000
Depreciation on computers and furniture used by the Legal Department - $20,000	$20,000 × 10% of time spent by Legal Department employees on the research project	$2,000
Materials and supplies used exclusively by the Research Department for the research project - $50,000	$50,000 × 100% use for research project	$50,000
Materials and supplies used by the Engineering Department - $40,000	$40,000 × 20% of time spent by Engineering Department employees on the research project	$8,000

Materials and supplies used by the Legal Department - $10,000	$10,000 × 10% of time spent by Legal Department employees on the research project	$1,000
Labor costs of Research Department employees and their direct supervisor - $600,000	$600,000 × 100% of time spent by Research Department employees on the research project	$600,000
Labor costs of Engineering Department employees - $200,000	$200,000 × 20% of time spent by Engineering Department employees on the research project	$40,000
Labor costs of Legal Department employees - $100,000	$100,000 × 10% of time spent by Legal Department employees on the research project	$10,000
Electricity for the facility - $200,000	Research Department $50,000 ($200,000 × 100,000/400,000 kilowatt-hours used for research project) + Engineering Department $2,000 ($200,000 × 20,000/400,000 kilowatt-hours used by Engineering Department × 20% of time spent by Engineering Department employees on the research project) + Legal Department $1,000 ($200,000 × 20,000/400,000 kilowatt-hours used by Legal Department × 10% of time spent by Legal Department employees on research project)	$53,000

Other utilities and overhead costs for the facility - $100,000	Research Department $10,000 ($100,000 × 1,000/10,000 square feet × 100% of time spent by Research Department on research project) + Engineering Department $2,000 ($100,000 × 1,000/10,000 square feet × 20% of time spent by Engineering Department on research project) + Legal Department $1,000 ($100,000 × 1,000/10,000 square feet × 10% of time spent by Legal Department on research project)	$13,000
Other miscellaneous overhead costs incurred by the Research Department - $50,000	$50,000 × 100% of time spent by Research Department employees on the research project	$50,000
Other miscellaneous overhead costs incurred by the Engineering Department - $50,000	$50,000 × 20% of time spent by Engineering Department employees on the research project	$10,000
Other miscellaneous overhead costs incurred by the Legal Department - $50,000	$50,000 × 10% of time spent by Legal Department employees on the research project	$5,000
Total SRE Expenditures		**$1,038,000**

.04 Consistency requirement. SRE expenditures must be treated consistently for purposes of all provisions under subtitle A of the Code (subtitle A). Thus, expenditures that are defined as SRE expenditures under section 4.02(2) of this notice must be treated as SRE expenditures for all purposes under subtitle A. Such expenditures may not be treated as ordinary and necessary expenses under § 162 or capitalized under § 195, § 263(a), § 263A, or § 471. The amortization deductions arising from such SRE

expenditures must also be allocated and apportioned consistent with the rules under §§ 1.861-8 and 1.861-17.

SECTION 5. SOFTWARE DEVELOPMENT

.01 Purpose. The Treasury Department and the IRS intend to propose rules in forthcoming proposed regulations consistent with the interim guidance provided in this section 5, which provides taxpayers with clarity in determining whether certain activities constitute software development for purposes of § 174(c)(3).

.02 Defined terms. For purposes of this notice:

(1) Computer software. The term computer software generally means any computer program or routine (that is, any sequence of code) that is designed to cause a computer to perform a desired function or set of functions, and the documentation required to describe and maintain that program or routine. The code may be stored on a computing device, affixed to a tangible medium (for example, a disk or DVD), or accessed remotely via a private computer network or the Internet, for example, via cloud computing. Computer software generally includes system software, programming software, application software, embedded software, and all forms and media in which the software is contained, whether written, magnetic, or otherwise. Computer software also generally includes computer programs of all classes, for example, operating systems, executive systems, software monitors, compilers and translators, assembly routines, and utility programs as well as application programs.

Computer software includes a computer program, a group of programs, and upgrades and enhancements (as defined in section 5.02(2) of this notice). Computer software also includes any incidental and ancillary rights that are necessary to effect the

acquisition of the title to, the ownership of, or the right to use the computer software, and that are used only in connection with that specific computer software. Computer software includes software developed for use by the taxpayer in its trade or business or for sale or licensing to others. Computer software does not include any data or information base described in § 1.197-2(b)(4) unless the database or item is in the public domain and is incidental to a computer program. For example, customer lists or client files are not included in computer software unless such items are in the public domain and incidental to a computer program. Additionally, computer software does not include any procedures that are external to the computer's operation.

(2) Upgrades and enhancements. The term upgrades and enhancements generally means modifications to existing computer software that result in additional functionality (enabling the software to perform tasks that it was previously incapable of performing), or materially increase speed or efficiency of the software.

.03 Activities that are treated as software development. Activities that are treated as software development for purposes of § 174 generally include but are not limited to:

(1) Planning the development of the computer software (or the upgrades and enhancements to such software), including identification and documentation of the software requirements;

(2) Designing the computer software (or the upgrades and enhancements to such software);

(3) Building a model of the computer software (or the upgrades and enhancements to such software);

(4) Writing source code and converting it to machine-readable code;

(5) Testing the computer software (or the upgrades and enhancements to such software) and making necessary modifications to address defects identified during testing, but only up until the point in time that:

(a) In the case of computer software developed for use by the taxpayer in its trade or business, the computer software is placed in service; and

(b) In the case of computer software developed for sale or licensing to others, technological feasibility has been established, product masters(s) have been produced, and the computer software is ready for sale or licensing to others; and

(6) In the case of computer software developed for sale or licensing to others (or the upgrades and enhancements to such software), production of the product master(s).

.04 Software development activities related to purchased computer software. In the case of upgrades and enhancements to purchased computer software, the principles set forth in section 5.03 of this notice apply. However, the purchase and installation of purchased computer software, including the configuration of pre-coded parameters to make such software compatible with the business and reengineering the business to make it compatible with the purchased software, and any planning, designing, modeling, testing, or deployment activities with respect to the purchase and installation of such software, are not activities that constitute software development for purposes of § 174.

.05 Activities that are not treated as software development. The following activities associated with software development projects are not treated as software development for purposes of § 174:

(1) Computer software developed by a taxpayer for use in its trade or business. In the case of computer software that is developed for use by the taxpayer in its trade or

business (or upgrades and enhancements to such software):

(a) Training employees and other stakeholders that will use the computer software;

(b) Maintenance activities after the computer software is placed in service that do not give rise to upgrades and enhancements (for example, corrective maintenance to debug, diagnose, and fix programming errors);

(c) Data conversion activities, except for activities to develop computer software that facilitate access to existing data or data conversion; and

(d) Installing the computer software and other activities relating to placing the computer software in service.

(2) Computer software developed for sale or licensing to others. In the case of computer software that is developed for sale or licensing to others (or upgrades and enhancements to such software), activities that occur after such software (or upgrades and enhancements to such software) is ready for sale or licensing to others, such as marketing and promotional activities, maintenance activities that do not give rise to upgrades and enhancements, distribution activities (for example, making the software available via remote access), and customer support activities.

SECTION 6. RESEARCH PERFORMED UNDER CONTRACT

.01 Purpose. The Treasury Department and the IRS intend to propose rules in forthcoming proposed regulations consistent with the interim guidance provided in this section 6, which provides taxpayers with clarity in determining whether costs paid or incurred for research performed under contract are SRE expenditures under § 174.

.02 Defined terms. For purposes of this section 6:

(1) Research provider. The term research provider means the party that contracts with a research recipient (as defined in section 6.02(2) of this notice) to:

(a) perform research services for the research recipient with respect to an SRE product, or

(b) develop an SRE product (as defined in section 6.02(4) of this notice) that the research recipient acquires from the research provider.

(2) Research recipient. The term research recipient means the party that contracts with the research provider to:

(a) perform research services for the research recipient with respect to an SRE product, or

(b) develop an SRE product that the research recipient acquires from the research provider.

(3) Financial risk. The term financial risk means the risk that the research provider may suffer a financial loss related to the failure of the research to produce the desired SRE product.

(4) SRE product. The term SRE product means any pilot model, process, formula, invention, technique, patent, computer software, or similar property (or a component thereof) that is subject to protection under applicable domestic or foreign law. For example, mere know-how gained by a research provider through the performance of research services for a research recipient that is not subject to protection under applicable domestic or foreign law does not give rise to an SRE product in the hands of the research provider.

.03 Treatment of costs paid or incurred by research recipient. The treatment of costs

paid or incurred by the research recipient is governed by the principles set forth in § 1.174-2(a)(10) and (b)(3).

.04 Treatment of costs paid or incurred by research provider. If the research provider bears financial risk under the terms of the contract with the research recipient, then costs paid or incurred by the research provider that are incident to the SRE activities (see section 4.03 of this notice) performed by the research provider under the contract are SRE expenditures. However, even if the research provider does not bear financial risk under the terms of the contract with the research recipient, if the research provider has a right to use any resulting SRE product in the trade or business of the research provider or otherwise exploit any resulting SRE product through sale, lease, or license, then costs paid or incurred by the research provider that are incident to the SRE activities performed by the research provider under the contract are SRE expenditures of the research provider for which no deduction is allowed except as provided in § 174(a)(2), regardless of whether the research recipient is required to treat its costs as SRE expenditures under section 6.03 of this notice. For purposes of the preceding sentence, a research provider will not be treated as having a right to use the SRE product in the trade or business of the research provider or otherwise exploit the SRE product through sale, lease, or license if such right is available to the research provider only upon obtaining approval from another party to the research arrangement that is not related to the research provider within the meaning of § 267 or § 707.

.05 Example. The following example illustrates the rules set forth in section 6 of this notice.

(1) Facts. Company C engages Company D, a contractor located in the United

States, to develop an SRE product for use in Company C's trade or business. The activities undertaken by Company D are undertaken upon Company C's order, and Company D makes no performance guarantees with respect to the SRE product. Company C will pay Company D a fixed sum of $25,000 plus an amount equivalent to Company D's actual expenditures. Company D does not have any right to use or otherwise exploit any resulting SRE product. In 2023, Company D incurs $125,000 of expenditures to successfully develop the product in the United States, and Company C pays to Company D $150,000 pursuant to the terms of the contract.

(2) Analysis. Under section 6.04 of this notice, Company D may not treat the $125,000 of expenditures it incurs to develop the SRE product on behalf of Company C as SRE expenditures under § 174 because (i) Company D does not bear financial risk, and (ii) Company D does not have any right to use or otherwise exploit any resulting SRE product. Under section 6.03 of this notice, the $150,000 paid by Company C is an amount paid to another party for research or experimentation undertaken on Company C's behalf under § 1.174-2(a)(10) and (b)(3) and is thus an SRE expenditure under section 4.02(2) of this notice. The applicable § 174 amortization period is 5 years (60 months) because the research is performed by Company D in the United States. Company C's location is not relevant for determination of the applicable § 174 amortization period.

SECTION 7. DISPOSITION, RETIREMENT, OR ABANDONMENT OF PROPERTY

.01 Purpose. The Treasury Department and the IRS intend to propose rules in forthcoming proposed regulations consistent with the interim guidance provided in this section 7, which provides taxpayers with clarity in determining the treatment of

unamortized SRE expenditures if property with respect to which such expenditures are paid or incurred is disposed of, retired, or abandoned in certain transactions during the applicable § 174 amortization period.

.02 In general. Except as provided in section 7.04 of this notice, if any property with respect to which SRE expenditures are paid or incurred is disposed of, retired, or abandoned during the applicable § 174 amortization period, no recovery is allowed with respect to the unamortized SRE expenditures on account of such disposition, retirement, or abandonment, and the taxpayer that disposed of, retired, or abandoned such property continues to amortize such expenditures under § 174 over the remainder of the applicable § 174 amortization period. For purposes of this section 7, the term unamortized SRE expenditures means the amount of any SRE expenditures paid or incurred by the corporation (or its predecessor), less the amount of any amortization deductions previously allowed to the corporation (or its predecessor) under § 174.

.03 Transactions occurring before the midpoint of the taxable year. An amortization deduction is allowed under § 174 for SRE expenditures even if such expenditures relate to property that is disposed of, retired, or abandoned prior to the midpoint of the taxable year in which such expenditures are paid or incurred. Accordingly, such expenditures are subject to the rules in sections 7.02 and 7.04 of this notice.

.04 Transaction in which corporation ceases to exist.

(1) Transaction described in § 381(a). If a corporation ceases to exist for Federal income tax purposes in a transaction or series of transactions described in § 381(a), the acquiring corporation will continue to amortize the distributor or transferor corporation’s unamortized SRE expenditures over the remainder of the distributor or transferor

corporation's applicable § 174 amortization period beginning with the month of transfer.

(2) Transaction not described in § 381(a).

(a) In general. Except as provided in section 7.04(2)(b), if a corporation ceases to exist for Federal income tax purposes in a transaction or series of transactions to which § 381(a) does not apply, the corporation is allowed a deduction equal to the unamortized SRE expenditures in its final taxable year.

(b) Anti-abuse exception. Section 7.04(2)(a) of this notice does not apply if a principal purpose of the transaction(s) described in section 7.04(2)(a) of this notice is to claim a deduction for the unamortized SRE expenditures.

.05 Examples. The following examples illustrate the rules set forth in section 7 of this notice.

(1) Sale of property with respect to which SRE expenditures were incurred.

(a) Facts. Company X, an accrual method, calendar-year taxpayer, incurs $100,000 in SRE expenditures in 2023 for research performed in the United States. On September 30, 2025, Company X sells the property with respect to which such expenditures were incurred to Company Y and recognizes gain under § 1001.

(b) Analysis. In 2023, Company X amortizes $10,000 (10% × $100,000). See section 3.05 of this notice. In 2024, Company X amortizes $20,000 (20% × $100,000). In 2025 through 2028, Company X ratably amortizes the remaining $70,000 ($100,000 – $10,000 – $20,000) notwithstanding Company X's disposition of the assets with respect to which Company X's SRE expenditures were incurred. Company Y does not amortize any portion of the SRE expenditures originally paid or incurred by Company X. Company X does not factor its unamortized SRE expenditures into the computation of

gain or loss under § 1001. See section 7.02 of this notice.

	2023	**2024**	**2025**	**2026**	**2027**	**2028**
Company X amortization %	10%	20%	20%	20%	20%	10%
Company X Dollar amount	$10,000	$20,000	$20,000	$20,000	$20,000	$10,000

(c) Applicable asset acquisition. The results would be the same as in section 7.05(1)(b) of this notice if the sale of property with respect to which the SRE expenditures were incurred were part of an applicable asset acquisition within the meaning of § 1060(c).

(d) Section 351 exchange. The results would be the same as in section 7.05(1)(b) of this notice if X transferred the property with respect to which the SRE expenditures were incurred in an exchange described in § 351.

(2) Section 381 transaction.

(a) Facts. The facts are the same as in section 7.05(1)(a) of this notice, except that, on October 16, 2025, Company X is acquired by Company Z, an accrual method, calendar-year taxpayer, in a transaction described in § 381(a).

(b) Analysis. In 2023, Company X amortizes $10,000 (10% × $100,000). See section 3.05 of this notice. In 2024, Company X amortizes $20,000 (20% × $100,000). In 2025, Company X amortizes $15,000 ((9 months/12 months) × 20% × $100,000), and Company Z amortizes $5,000 ((3 months/12 months) × 20% × $100,000). See sections 3.06(1), 7.02, and 7.04(1) of this notice. In 2026 through 2028, Company Z ratably amortizes the remaining $50,000 ($100,000 – $10,000 – $20,000 – $15,000 – $5,000).

	2023	**2024**	**2025**	**2026**	**2027**	**2028**
Company X amortization %	10%	20%	15%	0%	0%	0%
Company Z amortization %	0%	0%	5%	20%	20%	10%
Company X Dollar amount	$10,000	$20,000	$15,000			
Company Z Dollar amount			$5,000	$20,000	$20,000	$10,000

SECTION 8. LONG-TERM CONTRACTS UNDER § 460

.01 Purpose. The Treasury Department and the IRS are providing this interim guidance to provide taxpayers with information about a proposed revision to the regulations under § 460 in forthcoming proposed regulations regarding how to apply the percentage-of-completion method (PCM) to account for income from long-term contracts when allocable contract costs include SRE expenditures.

.02 Background. Section 460(a) generally requires use of the PCM to account for taxable income from a long-term contract. Section 1.460-4(b)(2)(i) provides that under the PCM, the portion of the contract price a taxpayer must report in a tax year corresponds to the ratio of incurred allocable contract costs to total estimated allocable contract costs. This ratio represents the portion of a contract considered completed for purposes of the PCM. Under the PCM, a taxpayer generally deducts allocable contract costs as they are incurred. As provided by § 1.460-4(b)(2)(iv), an increase in the percentage of the contract price to be reported is matched by deduction of the incurred

costs that cause the increase. Under the current § 460 regulations in § 1.460-5(b)(2)(vi), allocable contract costs include research or experimental expenses, other than independent research and development expenses. Thus, when these expenses are incurred, they increase the portion of a contract considered completed and the percentage of the contract price required to be reported. The current § 460 regulations were drafted when a taxpayer could deduct currently research or experimental expenses under former § 174. Section 174(a), as amended by the TCJA, requires that SRE expenditures be charged to capital account and deducted over the applicable § 174 amortization period. As a result, the current § 460 regulations provide that incurred research or experimental expenses increase the percentage of the contract price required to be reported, although § 174(a) prevents a corresponding current deduction of incurred SRE expenditures. The resulting mismatch of contract price and contract costs is inconsistent with the contemplated operation of the PCM.

.03 Treatment of SRE expenditures under § 460. The Treasury Department and the IRS anticipate issuing proposed regulations that would amend the existing § 460 regulations, including § 1.460-5(b)(2)(vi), to provide that the costs allocable to a long-term contract accounted for using the PCM include amortization of SRE expenditures under § 174(a)(2)(B), rather than the capitalized amount of such expenditures, and that such amortization is treated as incurred for purposes of determining the percentage of contract completion as deducted. The amendments would not apply to expenditures previously capitalized under § 59(e)(2)(B) or under former § 174(b), or to independent research and development expenditures, as defined in § 460(c)(5), which are not allocable contract costs. Research or experimental expenditures that are not

independent research and development expenditures, however, would remain subject to allocation under § 460(c)(1) regardless of whether they are SRE expenditures.

SECTION 9. COST SHARING REGULATIONS AT § 1.482-7

.01 Purpose. The Treasury Department and the IRS are providing this interim guidance to provide taxpayers with information about a proposed revision to § 1.482-7(j)(3)(i) in forthcoming proposed regulations.

.02 Background. Section 1.482-7(j)(3)(i) addresses cost sharing transaction payments (CST Payments) between controlled participants in a cost sharing arrangement (CSA) that are made to ensure that each controlled participant's share of intangible development costs (IDCs) is in proportion to its share of reasonably anticipated benefits from exploitation of the developed intangibles (RAB share). Section 1.482-7(j)(3)(i) generally provides that CST Payments reduce deductible IDCs borne by the controlled participant to which the CST Payments are owed. Any amount of CST Payment in excess of such deductible IDCs is treated as in consideration for the use of land and tangible property furnished for purposes of the CSA by the controlled participant to which the CST Payment is owed. CST Payments generally are considered the payor's costs of developing intangibles at the location where such development is conducted. See also § 1.482-7(j)(3)(iii), Example 1.

.03 Anticipated revisions to § 1.482-7(j)(3)(i).

(1) The Treasury Department and the IRS anticipate issuing proposed regulations that would replace the second through fourth sentences of § 1.482-7(j)(3)(i) with rules providing that CST Payments owed to a controlled participant reduce:

(a) The amount of the category of IDCs borne directly by that participant that are

required to be charged to capital account, and

(b) The amount of the category of IDCs borne directly by that participant that are not described in section 9.03(1)(a) of this notice and that are deductible.

(2) CST Payments not in excess of the payor's RAB share of the total amount of the IDCs in both categories described in section 9.03(1)(a) and (b) of this notice reduce the amount of each such category of IDCs in the same proportion that the total amount of the IDCs in each category bears to the total amount of IDCs in both categories. CST Payments in excess of the payor's RAB share of the total amount of IDCs in both categories described in section 9.03(1)(a) and (b) of this notice will be treated as income.

.04 Examples. The examples provided below illustrate the anticipated revisions to § 1.482-7(j)(3)(i).

(1) Example 1.

(a) Facts. U.S. Parent (USP) and its wholly owned Foreign Subsidiary (FS) form a CSA to develop a miniature widget, the Small R. Based on RAB shares, USP agrees to bear 40% and FS agrees to bear 60% of the IDCs incurred during the term of the agreement. USP incurs $100,000 of IDCs to perform research in the United States annually and FS incurs $100,000 of IDCs to perform research in country X annually. USP's IDCs are required under U.S. Federal income tax rules to be charged to capital account and amortized ratably over the 5-year applicable § 174 amortization period beginning with the midpoint of the taxable year in which such expenditures are paid or incurred, and FS's IDCs incurred in country X are required under U.S. Federal income tax rules to be charged to capital account and amortized ratably over the 15-year

applicable § 174 amortization period beginning with the midpoint of the taxable year in which such expenditures are paid or incurred.

(b) Analysis. Of the total IDCs of $200,000, USP's share is $80,000 ($200,000 × 40%) and FS's share is $120,000 ($200,000 × 60%) so that FS must make a payment to USP of $20,000 ($120,000 – $100,000). The CST Payment reduces USP's IDCs in the United States that are required to be charged to capital account by $20,000. Accordingly, USP is required to charge $80,000 to capital account, all of which is required to be amortized over 5 years, while FS is required to charge $120,000 to capital account, $100,000 of which is required to be amortized over 15 years, and $20,000 of which is required to be amortized over 5 years.

(2) Example 2.

(a) Facts. The facts are the same as in Example 1, except that the $100,000 of IDCs borne by USP consist of (1) $5,000 of IDCs incurred by USP in the United States that are required to be charged to capital account and amortized ratably over the 5-year applicable § 174 amortization period beginning with the midpoint of the taxable year in which such expenditures are paid or incurred, (2) $5,000 of deductible IDCs, and (3) $90,000 of arm's length rental charge, as described in § 1.482-7(d)(1)(iii), for the use of USP's facility in the United States.

(b) Analysis. As in Example 1, of the total IDCs of $200,000, USP's share is $80,000 and FS's share is $120,000, so that FS must make a payment to USP of $20,000. The $20,000 CST Payment from FS to USP will first be treated as reducing the $5,000 of IDCs that are required to be charged to capital account and the $5,000 of deductible IDCs pro rata to the extent of FS's RAB share of such IDCs. Because the

IDCs required to be charged to capital account make up 50% of the combined amount of IDCs chargeable to capital account and the deductible IDCs directly borne by USP (i.e., $5,000 = 50% × $10,000), and because FS's RAB share of the total amount of IDCs in both categories is $6,000 (i.e., 60% × $10,000), $3,000 of the $20,000 CST Payment reduces USP's IDCs chargeable to capital account, $3,000 of the CST Payment reduces USP's deductible IDCs, and the remaining $14,000 ($20,000 – $6,000) of the CST Payment is treated as income.

(3) Example 3.

(a) Facts. The facts are the same as in Example 1, except that the $100,000 of IDCs borne by USP consist of (1) $15,000 of IDCs incurred by USP in the United States that are required to be charged to capital account and amortized ratably over the 5-year applicable § 174 amortization period beginning with the midpoint of the taxable year in which such expenditures are paid or incurred, (2) $45,000 of deductible IDCs, and (3) $40,000 of arm's length rental charge, as described in § 1.482-7(d)(1)(iii), for the use of USP's facility in the United States.

(b) Analysis. As in Example 1, of the total IDCs of $200,000, USP's share is $80,000 and FS's share is $120,000, so that FS must make a payment to USP of $20,000. The $20,000 CST Payment from FS to USP will first be treated as reducing the $15,000 of IDCs that are required to be charged to capital account and the $45,000 of deductible IDCs pro rata to the extent of FS's RAB share of such IDCs. Because the IDCs required to be charged to capital account make up 25% (that is, $15,000 / ($15,000 + $45,000)) of the combined amount of IDCs chargeable to capital account and deductible IDCs directly borne by USP, and because the deductible IDCs make up

75% (that is, $45,000 / ($15,000 + $45,000)) of the combined amount of IDCs chargeable to capital account and deductible IDCs directly borne by USP, 25% of the $20,000 CST Payment, or $5,000, reduces USP's IDCs chargeable to capital account, and 75%, or $15,000, reduces USP's deductible IDCs. Because all $20,000 of the CST Payment is applied against deductible IDCs directly borne by USP and IDCs incurred by USP that are chargeable to capital account, there is no amount of the CST Payment that is treated as income.

SECTION 10. APPLICABILITY DATES

.01 In general. It is anticipated that the forthcoming proposed regulations will provide that rules consistent with the rules described in sections 3 through 9 of this notice would apply for taxable years ending after September 8, 2023. Except as otherwise provided in this section 10.01, prior to the publication date of the forthcoming proposed regulations in the Federal Register, a taxpayer may choose to rely on the rules described in sections 3 through 9 of this notice, including for expenditures paid or incurred in taxable years beginning after December 31, 2021, provided the taxpayer relies on all the rules in sections 3 through 9 of this notice and applies them in a consistent manner. However, taxpayers may not rely on the rules in section 7 of this notice for SRE expenditures paid or incurred with respect to property that is contributed to, distributed from, or transferred from a partnership.

.02 Additional procedural guidance. The Treasury Department and IRS intend to issue guidance in the Internal Revenue Bulletin (see § 601.601(d) of the Procedural Rules) to provide procedures for taxpayers to obtain automatic consent to change methods of accounting to comply with this notice. Until the issuance of

such procedural guidance, taxpayers may rely on section 7.02 of Rev. Proc. 2023-24 to change their methods of accounting under § 174 to comply with this notice. The Treasury Department and IRS anticipate issuing updated procedures that will address situations in which taxpayers have, prior to the issuance of this notice, changed methods of accounting to comply with § 174 as amended by the TCJA but whose treatment of SRE expenditures is not entirely consistent with this notice. Unless specifically authorized by the Commissioner of Internal Revenue or by statute, a taxpayer may not request, or otherwise make, a retroactive change in method of accounting by filing an amended return. See Rev. Rul. 90-38, 1990-1 C.B. 57; Rev. Rul. 2023-8, 2023-18 I.R.B. 801.

SECTION 11. REQUEST FOR COMMENTS

.01 Comments regarding guidance provided in this notice. The Treasury Department and the IRS request comments on issues arising from the interim guidance set forth in this notice. In addition to general comments regarding the provisions of this notice, the Treasury Department and the IRS request comments to address the following issues:

(1) Scope of § 174 (section 4 of this notice).

(a) Whether additional guidance is needed regarding identifying expenditures allocable to SRE activities and allocating such expenditures to SRE activities.

(b) Whether simplified methods or safe harbors should be provided for identifying expenditures allocable to SRE activities and allocating such expenditures to SRE activities. If so, what methods or safe harbors should be provided? Are special methods needed for government research contracts?

(2) Software development (sections 4 and 5 of this notice).

(a) The definition of computer software is based on section 2 of Rev. Proc. 2000-50 and § 1.197-2(c)(4)(iv). Is there a more appropriate definition under the Financial Accounting Standards Board Accounting Standards Codifications (ASCs) or an appropriate industry standard that should be used instead? If so, what ASC or industry standard definition should be used? Additionally, to what extent should ASC guidance or an appropriate industry standard be used to determine activities that are software development activities, and costs that are software development costs, for purposes of § 174?

(b) What examples of costs that are, or are not, software development costs would be helpful to include in the forthcoming proposed regulations?

(c) Are special rules and examples needed to determine what activities related to developing a website would be software development?

(3) Research performed under contract (section 6 of this notice).

(a) Should the rules for determining whether a party to a research contract has SRE expenditures under § 174 be similar to the funded research rules under § 41(d)(4)(H)?

(b) Are special rules needed for service or manufacturing production contracts with the government, including § 460 long-term contracts?

(c) Are there other factors that should be considered in determining whether a party to a research contract has SRE expenditures?

(d) Are special rules or safe harbors needed to determine if research performed under a contract is foreign research (for example, where a research recipient pays the research provider for research that is performed by the research provider both inside

and outside the U.S.)?

(e) Are special rules needed for contracts with related foreign research providers and recipients?

(4) Disposition, retirement, or abandonment of property (section 7 of this notice). What, if any, changes to the rules in section 7 of this notice are appropriate to address potential abuses?

(5) Long-term contracts under § 460 (section 8 of this notice). In the case of SRE expenditures allocable to long-term contracts accounted for under the PCM set forth in § 460, do estimated total allocable contract costs include all SRE expenditures that directly benefit or are incurred by reason of the performance of the long-term contract or, alternatively, only that portion of the SRE expenditures expected to be amortized during the term of the contract? Under the first alternative, a taxpayer would be required to report any remaining portion of the contract price not previously reported by the tax year following the tax year in which the contract is completed, notwithstanding that some portion of the SRE expenditures remain unamortized. See § 460(b)(1).

.02 Comments regarding rules not included in this notice. The Treasury Department and the IRS continue to study issues that are not addressed in this notice, including but not limited to whether the general requirements governing record retention under § 1.6001-1 are adequate for purposes of substantiating expenditures under § 174, whether the definition of “pilot model” under § 1.174-2(a)(4) should be amended, and whether and how § 59(e) applies to § 174 expenditures. In addition to requests for comments on these issues, the Treasury Department and the IRS request comments on the following specific issues not addressed by this notice:

(1) Under what circumstances should unamortized SRE expenditures continue to be amortized or accelerated with respect to property that is contributed to, distributed from, or transferred from a partnership?

(2) Under what circumstances should unamortized SRE expenditures continue to be amortized or accelerated with respect to property of a partnership that is a party to a merger, consolidation, division, or liquidation, or that otherwise terminates under § 708 and the regulations thereunder? Is there potential for abuse as a result of allowing a deduction for unamortized SRE expenditures in the final year of a partnership that liquidates or otherwise terminates? If so, what rules are appropriate to address such abuse?

(3) Should special rules apply to start-up companies or small taxpayers? If so, how should § 174 be applied in such cases?

(4) Sections 280C(c)(1)(B) and 56(b)(2)(A) each refer to an "amount allowable as a deduction" for qualified research expenses or basic research expenses (in the case of § 280C(c)(1)(B)), and § 174(a) (in the case of § 56(b)(2)(A)). On the one hand, § 174(a)(1) (as amended by the TCJA) does not allow a deduction for qualified research expenses or basic research expenses because such expenses are required to be charged to capital account. On the other hand, § 174(a)(2) allows an amortization deduction with respect to the capitalized amount of such expenses. Should the "amount allowable as a deduction" references in §§ 280C(c)(1)(B) and 56(b)(2)(A) be interpreted to refer to the amortization deduction allowed under § 174(a)(2) or to $0, which is the deduction allowed for the qualified research expenses or basis research expenses under § 174(a)(1)? The Treasury Department and IRS request comments on this

interpretation and how to resolve any potential issues that might arise by applying the same interpretation to both §§ 280C(c)(1)(B) and 56(b)(2)(A).

.03 Procedures for submitting comments.

(1) Deadline. Written comments should be submitted by November 24, 2023. Consideration will be given, however, to any written comment submitted after November 24, 2023, if such consideration will not delay the issuance of the forthcoming proposed regulations.

(2) Form and manner. The subject line for the comments should include a reference to Notice 2023-63. All commenters are strongly encouraged to submit comments electronically. However, comments may be submitted in one of two ways:

(a) Electronically via the Federal eRulemaking Portal at www.regulations.gov (type IRS-2023-0040 in the search field on the regulations.gov homepage to find this notice and submit comments); or

(b) By mail to: Internal Revenue Service, CC:PA:LPD:PR (Notice 2023-63), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, D.C., 20044.

(3) Publication of comments. The Treasury Department and the IRS will publish for public availability any comment submitted electronically or on paper to its public docket on www.regulations.gov.

SECTION 12. EFFECT ON OTHER DOCUMENTS

As a result of the TCJA amendments to § 174 and the rules in sections 3 through 5 of this notice, section 5 of Rev. Proc. 2000-50 is obsolete.

SECTION 13. DRAFTING AND CONTACT INFORMATION

The principal author of this notice is Bruce Chang of the Office of the Associate

Chief Counsel (Income Tax and Accounting). Other personnel from the Treasury Department and the IRS participated in its development. For further information regarding this notice, please contact Mr. Chang at (202) 317-4870 (not a toll-free number). For further information regarding corporate matters in section 7 of this notice, please contact Austin Diamond-Jones of the Office of Associate Chief Counsel (Corporate) at (202) 317-5085 (not a toll-free number). For further information regarding section 9 of this notice, please contact Annette Ofori of the Office of Associate Chief Counsel (International) at (202) 317-4910 (not a toll-free number).

10:55 – 11:55 a.m.

Cyber Liability Insurance

Matthew Thomson, *Director of Cyber Liability, M3 Insurance*

yes and

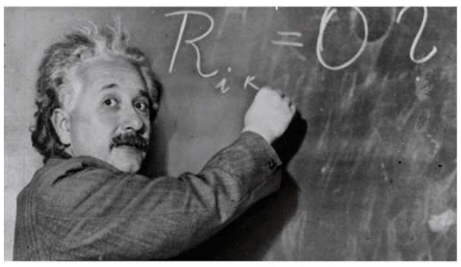
world-class expertise + individual attention

State of the Cyber Insurance Market

September 18, 2023

M3 INSURANCE

How I think I look explaining cyber risk to the board



How I actually look

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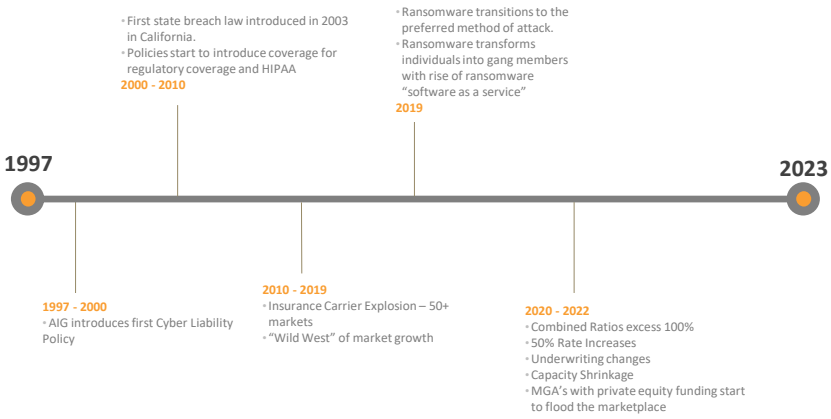
Cyber Insurance History



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2023

Pricing

- Rates trending down, flat to 15% given positive claim trend.

Capacity

- Return of larger capacity, $10M tranches available above $20M on towers

Coverage

- Retentions will remain the focus in addition to rewrites of War Exclusions and Catastrophic Containment
- Catastrophic risk

Underwriting

- Reached the plateau of underwriting information needs, no new amendments likely

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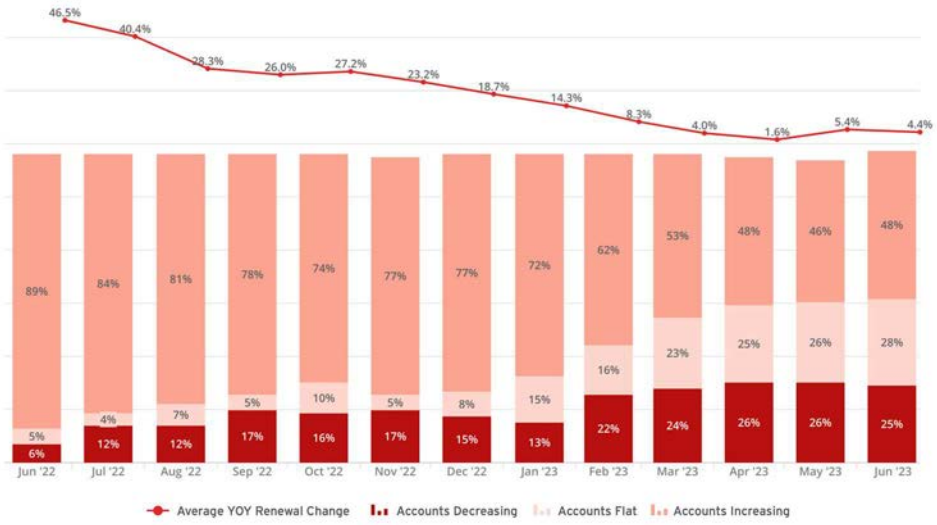
Premium Pricing Trend



Exclusions/Omissions to Be Aware Of

- Ransomware Sub-limits
- Social Engineering Callback Requirements
  - *Funds transfer fraud will not include loss arising out of any fraudulent request […] this is not authenticated by you or your financial institution by means of a secondary method of authentication to verify the authenticity or validity of such instruction in addition to the original method of authentication undertaken.*
- Widespread Events
  - MoveIT, Solarwinds, Log4j
- War Exclusions
- BIPA, CCPA, GDPR, etc.
- Online Tracking **(Meta-Pixel)**

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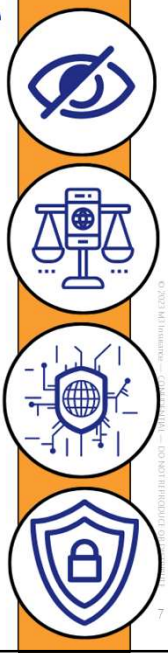
Emerging Impacts to Cyber Insurance

- Government Regulation
  - SEC
  - Privacy Laws
  - CMMC
- Contract Requirements
  - *$5,000,000 per claim and with not less than $5,000,000 sub-limit for privacy/security/regulatory breach, remediation, and privacy/security notification solely for losses arising out of the business or operations of Subcontractor (or any of its agents' or subcontractors') under this Agreement covering liabilities for loss resulting or arising from acts, errors or omissions, in connection with Subcontractor's (or any of its agents' or subcontractors') services or operations in connection with its business or operations, including its Products and/or Services, including Security Breaches, violation or infringement of any right of privacy, breach of federal, state or foreign privacy laws or regulations, data theft, damages, destruction, or corruption.*
- Artificial Intelligence



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Ransomware Attack Trend

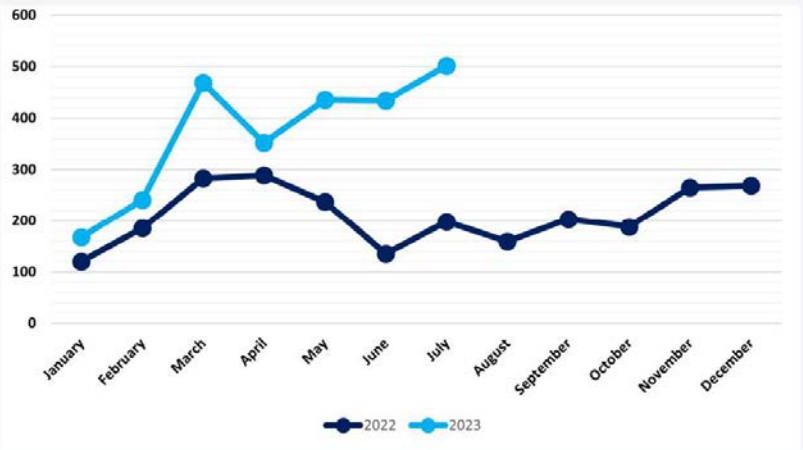

Figure 1 - Global Ransomware Attacks by Month 2022 - 2023

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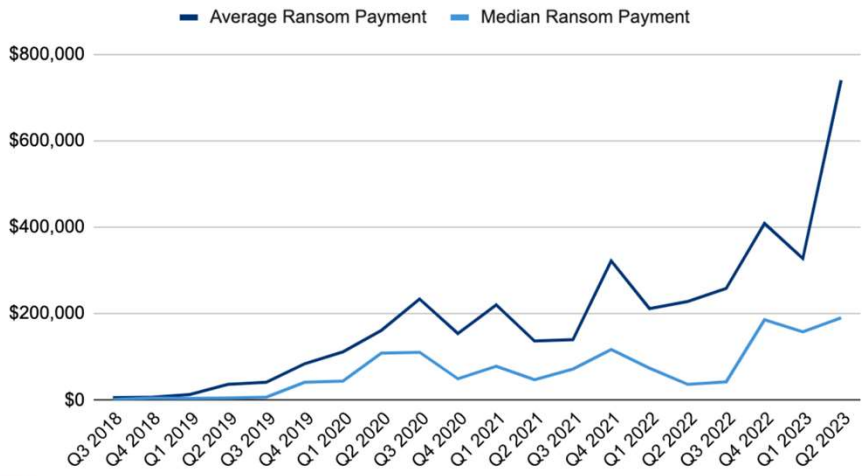
Ransom Payments By Quarter



COVEWARE

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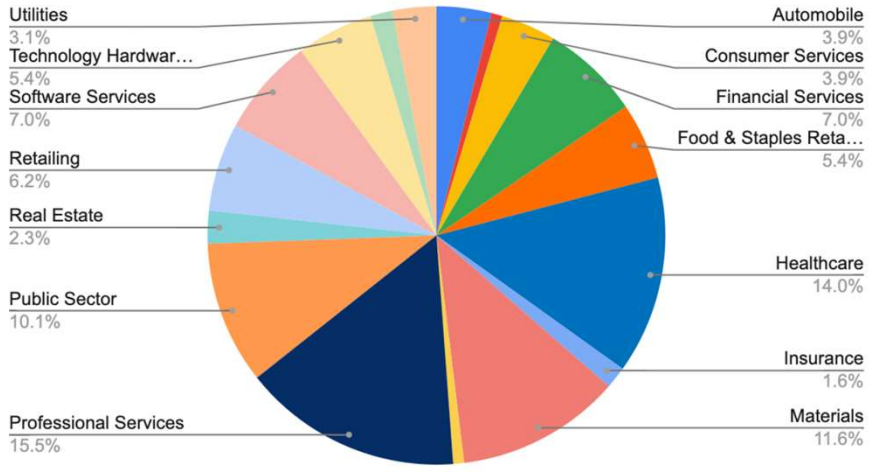
9

Industries Impacted by Ransomware Q2 2023



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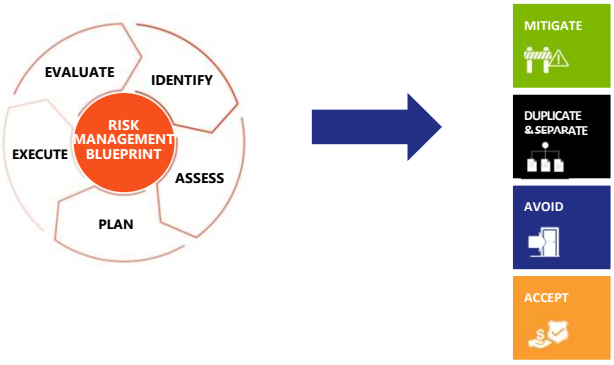
Cyber Risk Management



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Components to Cyber Resilience

- Multi-Factor Authentication
- Endpoint Detection Software
- Incident Response Planning
- Next Generation Firewalls
- Encryption
- Operational Technology (OT)
- Email Protection
- Vulnerability Scanning
- Backups
- Security Awareness Training
- System & Data Classification
- Data Retention
- 3rd Party Vendor Management
- Cloud Security Posture Management
- Protected DNS

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Questions?

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12:55 – 1:55 p.m.

Regional Bank Update

Ashley Farrell, CPA, CFE, CFF, *Director, Baker Tilly*

Kevin Schalk, CPA, *Partner, Baker Tilly*

Sean Statz, CPA, *Director, Baker Tilly*

bakertilly

Regional Bank Update

September 18, 2023

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Agenda

- Business of banking
- Current events and market update
- M&A environment
- BSA/AML
- Questions

3

Business of banking

bakertilly

BUSINESS OF BANKING

Banking Overview

- History
- How banks make (or lose) money
- Regulation
- Competition
  - Credit unions
  - Specialty lenders
  - Fintech
- Role of the public
- Future of the industry

5

Current events and market update

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CURRENT EVENTS AND MARKET UPDATE

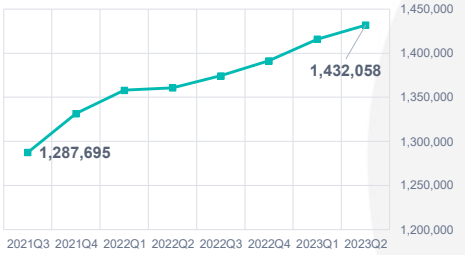
Bank Failures

- Historical Bank Failures
- 2023 Bank Failures
  - Silicon Valley Bank
  - Signature Bank
  - First Republic Bank
  - Heartland Tri-State Bank
- Why Do Banks Fail?
- Fallout of Bank Failures
  - Industry
  - Regulatory
  - Public

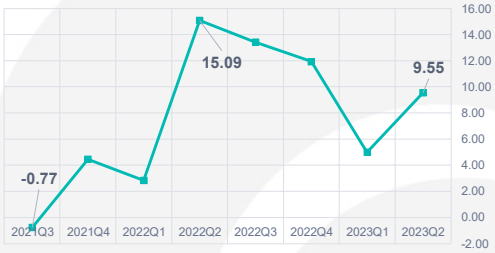
CURRENT EVENTS AND MARKET UPDATE

Banking Industry – Balance Sheet KPIs

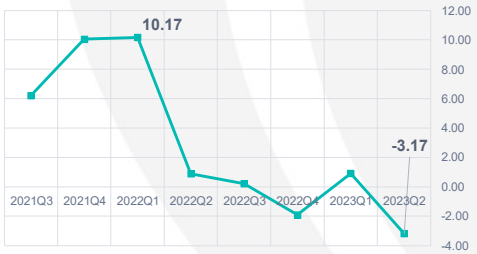
Average Total Assets



Loan Growth Rate



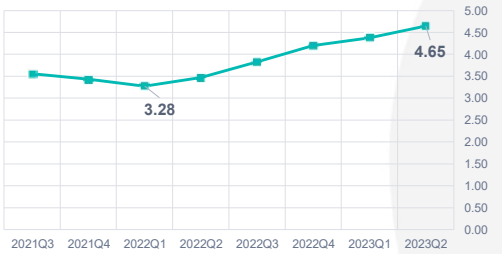
Deposit Growth Rate



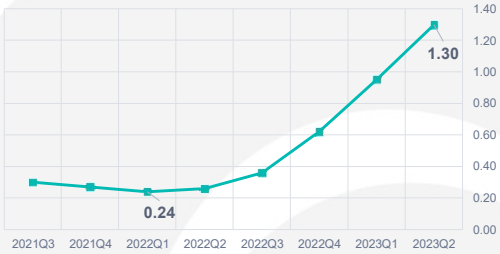
CURRENT EVENTS AND MARKET UPDATE

Banking Industry – Yield / Cost of Funds

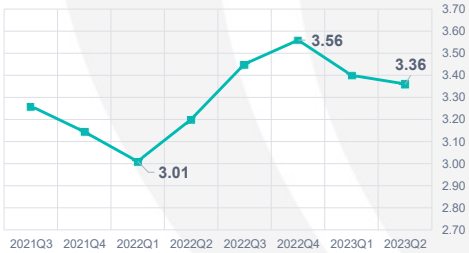
Yield on Earning Assets (%)



Cost of Funds (%)



Net Interest Margin (%)

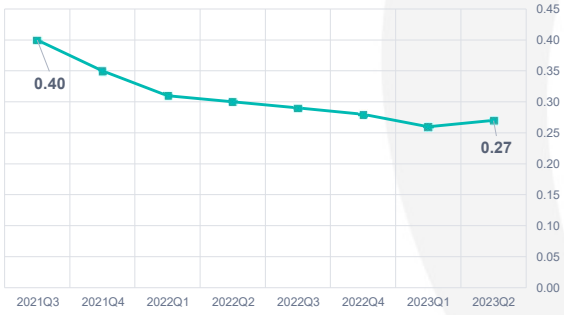


9

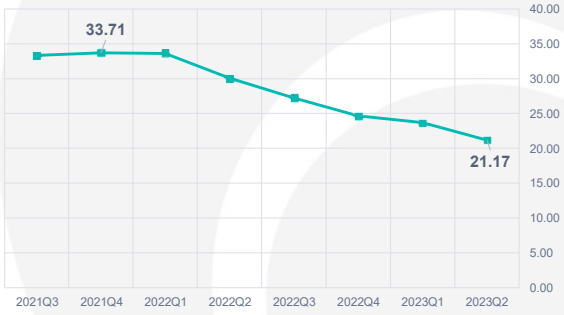
CURRENT EVENTS AND MARKET UPDATE

Banking Industry – Credit & Liquidity

NPAs + 90 Days PD / Total Assets (%)



Liquidity Ratio (%)



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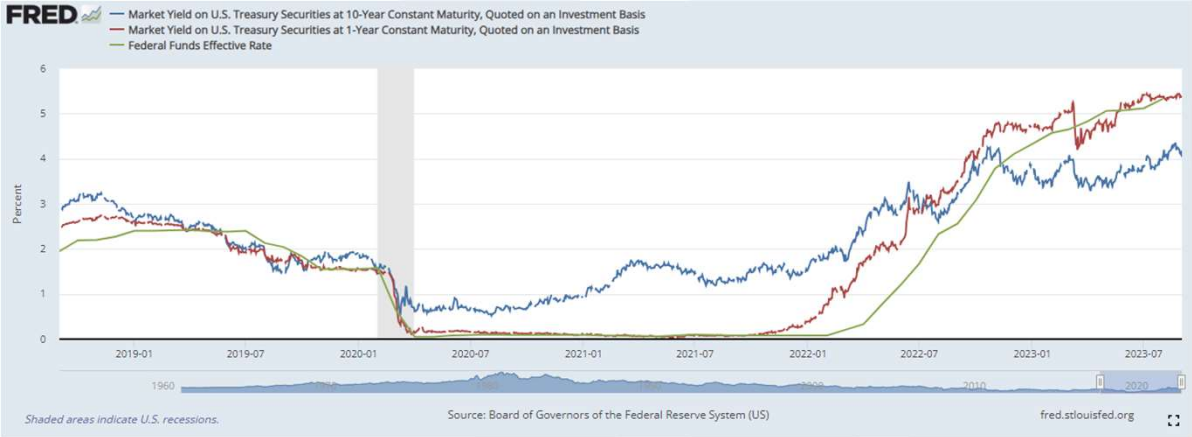
CURRENT EVENTS AND MARKET UPDATE

Today's interest rate environment



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M&A environment

bakertilly

M&A ENVIRONMENT

Merger activity summary (2018 – today)

Year	Count of Mergers	Average of Deal Premium 1 Month Before (%)	Average of Target Total Assets (Reported)	Average of Deal Value/ Assets (%)
2018	138	38.3	441,711	16.59
2019	223	29.4	1,844,400	17.13
2020	136	29.4	945,058	16.33
2021	164	48.0	1,680,509	14.43
2022	132	27.4	3,373,518	14.71
2023	70	36.9	2,200,490	14.18
Grand Total	**863**	**34.8**	**1,701,165**	**15.95**

State	Count of Mergers
TX	77
IL	75
IA	47
WI	44
FL	44
MN	43
MO	41
GA	35
KS	35
CA	33

M&A ENVIRONMENT

M&A Outlook

- Slowdown in the M&A space as management teams wait for market volitlity and interest rates to stabilize
- Deal valuations (deal value to tangible common equity) for deals announced in 2023 was at lowest valuation since late 2020
- Credit unions continue to acquire banks
  - Two announced in 2023 already
  - 16 deals announced in 2022
- Midwest continues to be most targeted region
- Mergers of equals on the rise

M&A ENVIRONMENT

M&A Outlook for 2023 and beyond

According to a 2023 Bank Director M&A survey: 85% of respondents said their bank either ***"plans to be active acquirers or were at least open to acquisitions"***

- only 11% were very likely to acquire a bank this year

- Of the 85% that were actively looking for or open to acquisitions, 34% said there was not enough suitable acquisition targets.

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BSA/AML

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BSA/AML KEY TOPICS

AML compliance is more complex than ever

Global fines from enforcement actions

$55B* — From 2008-2022

$5B* — 2022

17

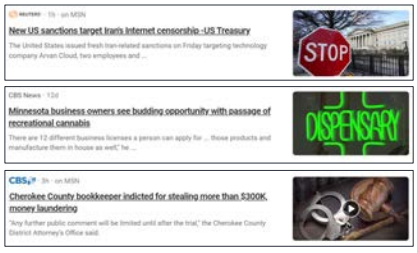
*Noonan, Laura and Smith, Alan. (2023, January 18). Global anti-money laundering fines surge 50% Retrieved from Global anti-money laundering fines surge 50% | Financial Times (ft.com)

BSA/AML KEY TOPICS

Leveraging Technology

Fight financial crime

Focus on the right things



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Questions

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How to Combat the Biggest Risks to Your Retirement

KEIL FINANCIAL PARTNERS

Jeremy Keil, CFP®, CFA
Owner, Keil Financial Partners
Host, Retirement Revealed Podcast

www.KeilFP.com

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Required Disclosures

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2

Why I do what I do

Jeremy Keil CFP®, CFA

3

Musical Instruments
Logic Grid Puzzle

brainzilla

Can you find out which girl is learning about the ukulele?

1. Ariella is learning about the accordion.
2. The kid learning about the xylophone is 2 years younger than Valeria.
3. Kallie is either 6 or 8-year-old.
4. The 7-year-old girl is learning about the oboe.

		Instruments				Ages			
	© Brainzilla.com	accordion	oboe	ukulele	xylophone	6 years	7 years	8 years	9 years
Girls	Ariella								
	Kallie								
	Stella								
	Valeria								
Ages	6 years								
	7 years								
	8 years								
	9 years								

Play This Logic Grid
brainzilla.com/xj/lgp/26

	Instruments	Ages
Ariella		
Kallie		
Stella		
Valeria		

4

5

6

How to Combat the Biggest Risks to Your Retirement

- How to get the most out of Social Security
- How to Lower your Lifetime Taxes
- Get More Interest on your Cash
- Avoid the Biggest Mistakes most investors make

7

The 3 Biggest Risks to Your Retirement

What is the biggest risk to your retirement?

- Stock Market Going Down
- Inflation Going Up
- Low Interest Rates
- How Long I Live
- Healthcare Costs

8

The 3 Biggest Risks to Your Retirement

What are the 3 biggest risk to your retirement?

- Longevity
- Inflation
- You!

9

Longevity

- What is the average life expectancy for retirees in the US?
- 79?
- 85
- 88
- 92

10

Longevity

- What is the biggest longevity risk?
- Living too long?
- Dying too soon!
- It's the combo!

11

Why Averages Don't Matter

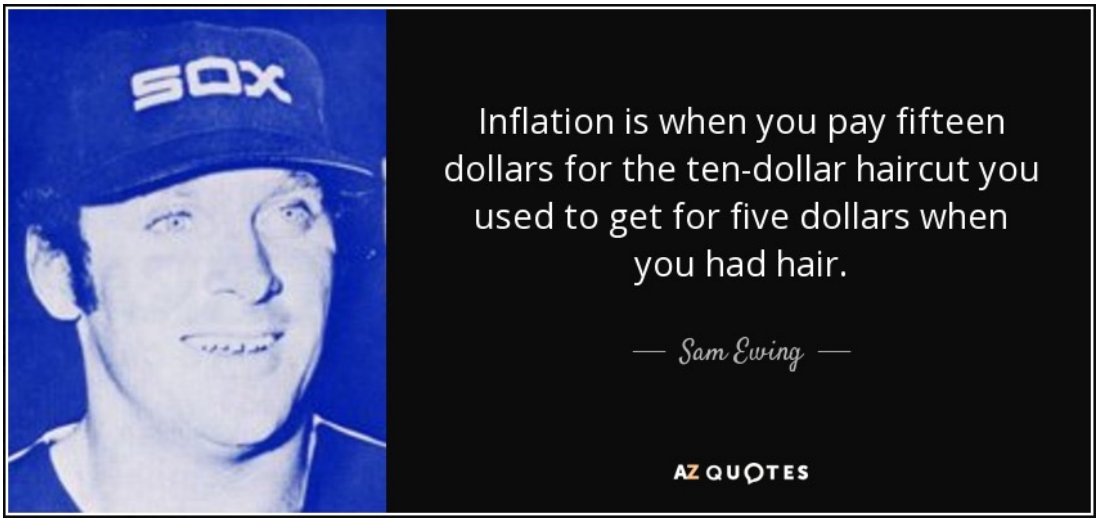
12

Your 3-Step Longevity Action Plan

1. Decide your longevity risk tolerance
2. Get your Personalized Longevity Estimate
3. Plan for Success, but prepare for failure

13

Inflation



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Inflation

- Rule of 72
  - 3% inflation
  - 24 years
  - = Prices Double

15

How to Beat Inflation?

- Stocks
- Real Estate
- Commodities
- Gold?

16

How to Beat Inflation?

- US Government!
  - The same people who created inflation can sell you something to combat it!
    - TIPs
    - I Bonds
    - Social Security

17

You are the biggest risk!

- Studies show people:
  - Take Social Security at the wrong time
  - Buy & Sell stocks at the wrong time
  - Even retire and die at the wrong time!

18

You are the biggest risk!

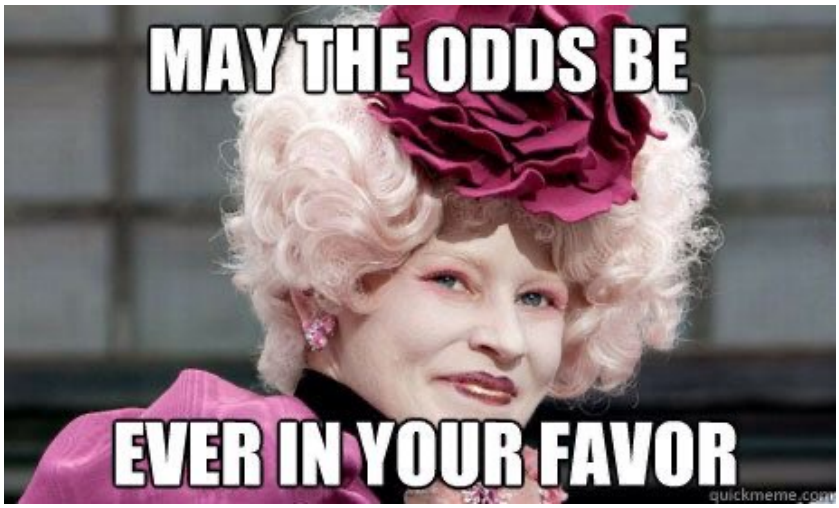
- Learn the Math
- Do the Math
- Follow the Math

19

You are the biggest risk!

20

Learn Longevity to Beat Social Security



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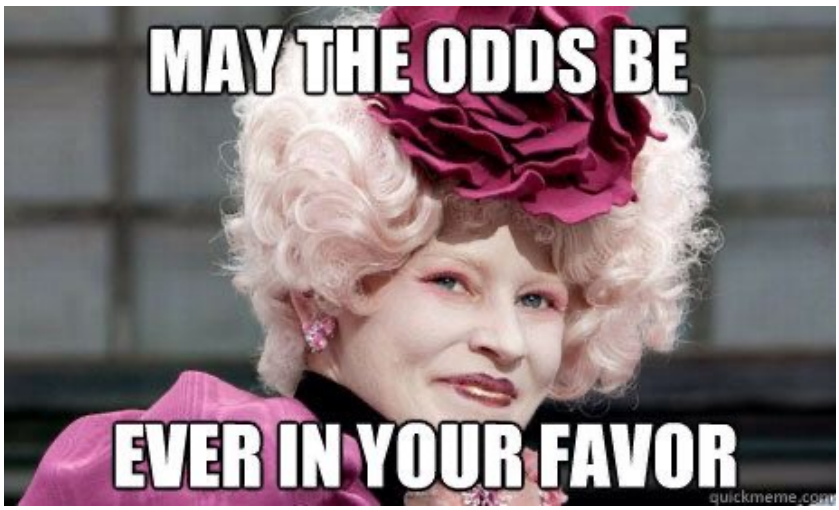
Learn the Market to Beat the Market



22

Learn About Interest Rates

23

Learn Taxes to Save on Taxes

- Three ways to save on taxes
  - Earn less money
  - Learn, and follow the tax rules
  - Lie & Cheat

24

How to Pay Less in Taxes

- When your tax rate is high, recognize less income
- When your tax rate is low, recognize more income

25

When is your Tax Rate lower?

Before/After?

- Retirement
- 2026
- MFJ vs. Single
- RMD age
- Social Security

26

Name that Financial Instrument

- Guaranteed to last as long as you live
  - Longevity risk
- Grows with inflation
  - Inflation risk
- Pays you every single month
  - Behavior Risk

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Max Retirement Savings

- $25k/yr SS now
- Or, wait 4 years and take $25k/yr * 4 out of your accounts
- $500k with lower SS or $400k with higher SS?

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Max Retirement Savings

- $25k/yr SS now
- Or, wait 4 years and take $25k/yr * 4 out of your accounts
- $500k with lower SS or $400k with higher SS?

- What if you add the tax savings in?

29

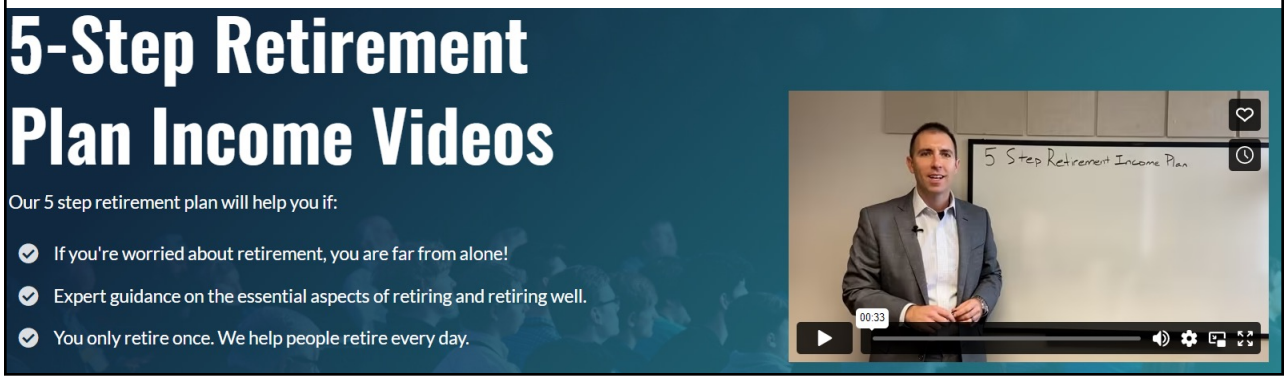
Avoid Mistakes & Get the Most Money

1. Learn the Math
2. Do the Math
3. Follow the Math

30

Free Retirement Risk Resources

- Email Talk@KeilFP.com
- Subject: WICPA Risk



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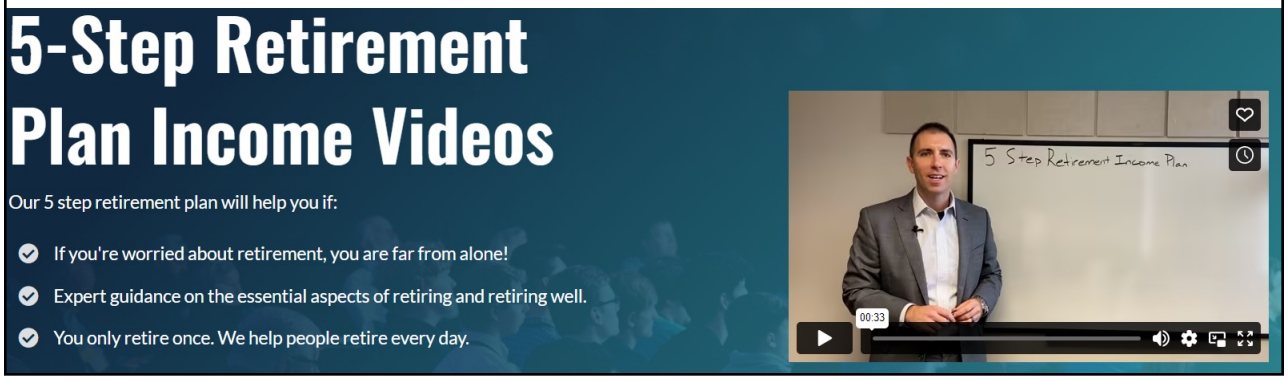
Combat the biggest risks to your retirement

1. Beat the Longevity odds by Maximizing your Social Security
2. Beat Inflation by Maximizing your Social Security
3. You can't beat the market – join the market!
4. Beat the banks by acting like a bank
5. Pay your taxes when they are low / defer when they are high

32

Free Retirement Risk Resources

- Email Talk@KeilFP.com
- Subject: WICPA Risk



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3:30 – 4:30 p.m.

Leadership Ethics

John Minnich, CPA, CGMA, MAcct, *Founder & Executive Advisor,*

John Minnich LLC

Strategic Executive Advisory

Leadership Ethics

Advising and Coaching Business Leaders on Business Performance and Strategy

John Minnich, MAcct, CPA, CGMA

- Founder, John Minnich, LLC dba **Strategic Executive Advisory**
  - Business performance and strategy
- MBA Faculty, **Purdue University Fort Wayne** | Financial Management and Strategy
- Immediate Past President, **Financial Executives International-Fort Wayne**
- Experienced CFO with business operations
- 10 years public accounting | A&A
- 6 years systems consulting | CPA firm tech division
- Nonprofit boards including executive committees/board chair

Proud Member Of

financial executives international

Agenda

WELCOME

LEADERSHIP VS MANAGEMENT

LEADERSHIP ETHICS

RESOURCES

EXAMPLES + RECOMMENDATIONS

HOLISTIC APPROACH

OPPORTUNITIES

Leadership Ethics

Integrity and trust are core to the accounting profession. As business continues to evolve and is increasingly more complex, so too are ethical situations. To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity. Join us to develop leadership skills while understanding and upholding ethics and professional conduct.

Highlights

Leadership vs management

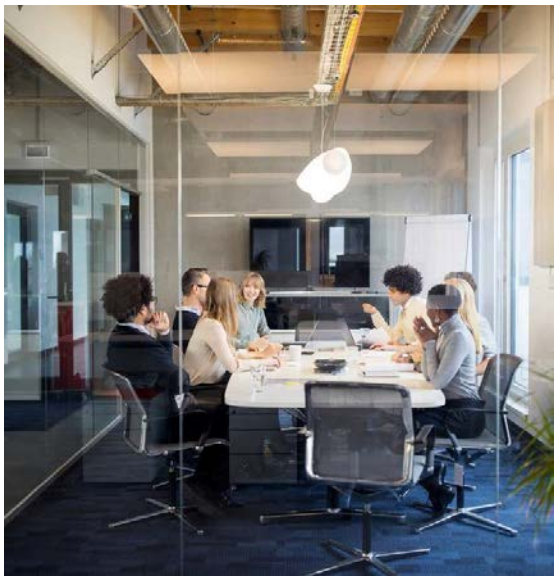
Leadership ethics

Business leadership and strategy

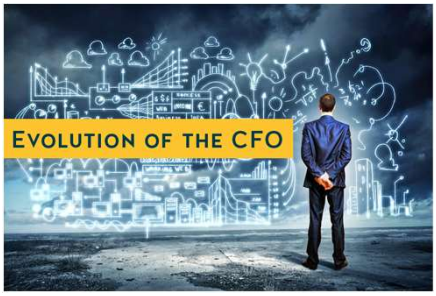
Resources

This session will

Cover ethical business leadership and investing in leadership development



Business/Industry



Public

"Leadership is lifting a person's vision to high sights, the raising of a person's performance to a higher standard, the building of a personality beyond its normal limitations."

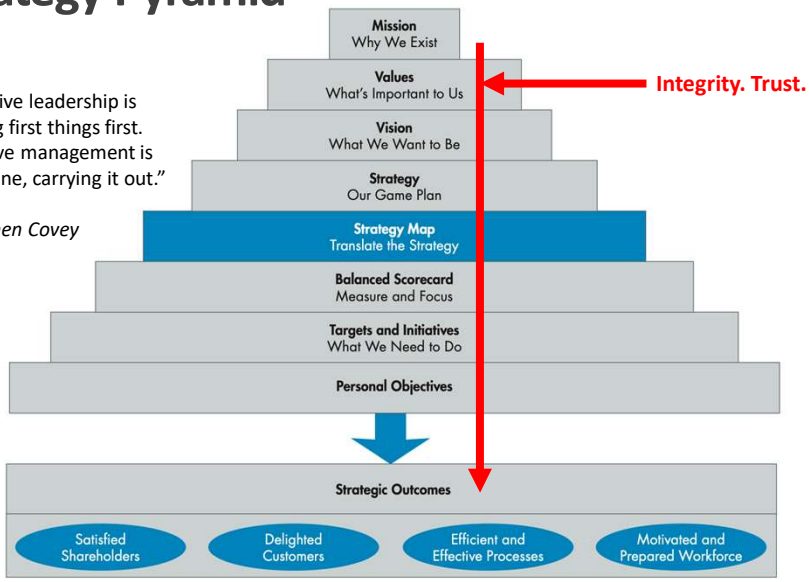
- Peter F. Drucker

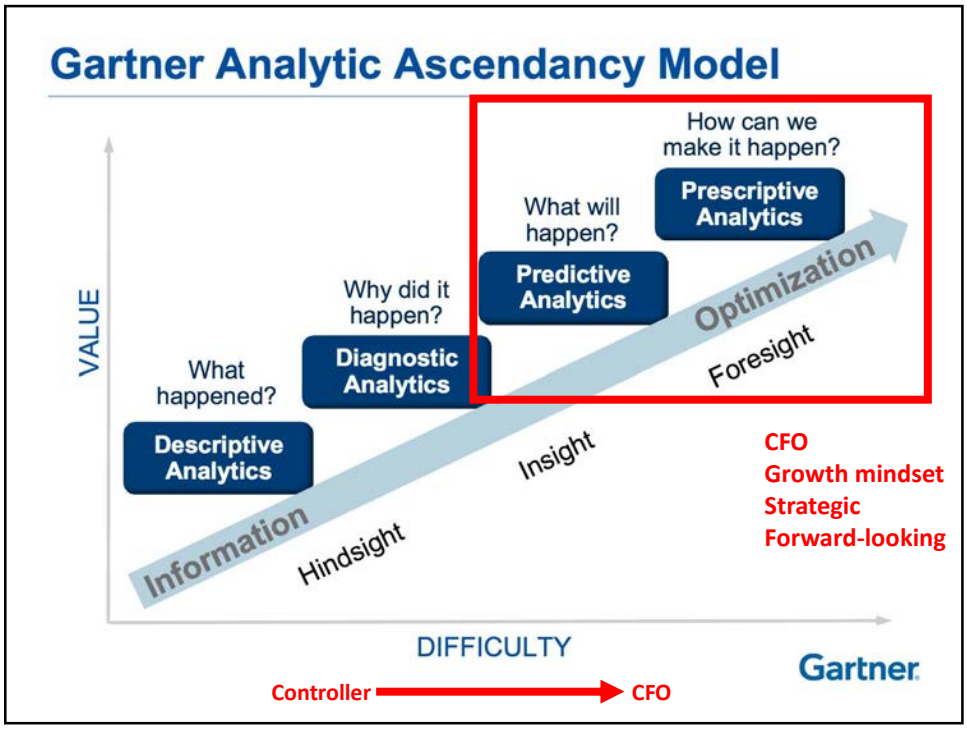
Strategy Pyramid

Tone at the Top

"Effective leadership is putting first things first. Effective management is discipline, carrying it out."

- Stephen Covey




Gartner Analytic Ascendancy Model
How can we make it happen?
Prescriptive Analytics
What will happen?
Predictive Analytics
Why did it happen?
Diagnostic Analytics
What happened?
Descriptive Analytics
VALUE
Optimization
Foresight
Insight
Hindsight
Information
DIFFICULTY
Gartner
CFO
Growth mindset
Strategic
Forward-looking
Controller
CFO

Leadership vs Management
"Management is doing things right; leadership is doing the right thing." - *Peter F. Drucker*
johnjminnich.com
JOHNMINNICH
8

Business Leadership + Strategy

Leadership

- Motivating
- Inspiring
- Persuading
- Coaching
- Mentoring
- Visioning
- Anticipating

Management

- Planning
- Budgeting
- Directing
- Staffing
- Organizing
- Controlling
- Coordinating
- Decision-making
- Problem-solving

Why

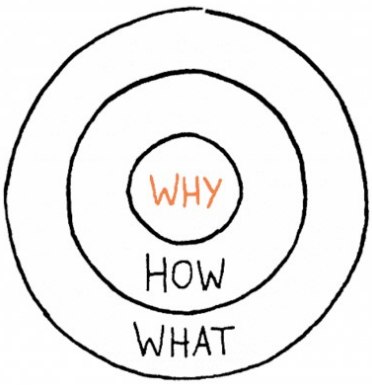
"People don't buy what you do; they buy why you do it. And what you do simply proves what you believe."
- Simon Sinek

The Golden Circle

WHAT
Every organization on the planet knows WHAT they do. These are products they sell or the services

HOW
Some organizations know HOW they do it. These are the things that make them special or set them apart from their competition.

WHY
Very few organizations know WHY they do what they do. WHY is not about making money. That's a result. WHY is a purpose, cause or belief. It's the very reason your organization exists.



Leadership Concepts

- Credibility and Trust via Action
- Integrity and Ethics
- Positional Authority | Leadership

- Qualities
- Styles
- Lead
- Follow

Leadership Styles

"Leadership is the art of giving people a platform for spreading ideas that work." - *Seth Godin*

- Democratic
- Autocratic
- Laissez-faire
- Strategic
- Transformational
- Transactional
- Coach-Style
- Bureaucratic

Leadership Ethics

"It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you'll do things differently."

- Warren Buffett

AICPA Code of Conduct

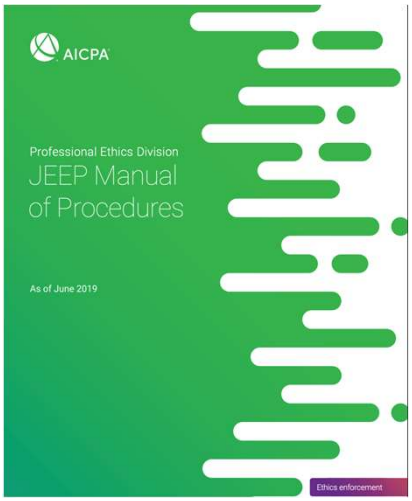
AICPA members are bound by the AICPA Code of Professional Conduct. Rule 201 requires that members provide professional services with competency. In the delivery of personal financial planning services, a member shall adhere to the following Principles of Professional Conduct.

- **ET Section 52 – Article I – Responsibilities**
  In carrying out their responsibilities as professionals, members should exercise sensitive professional and moral judgments in all their activities.
- **Section ET 53 – Article II – The Public Interest**
  Members should accept the obligation to act in a way that will serve the public interest, honor the public trust and demonstrate commitment to professionalism.
- **Section ET 54 – Article III - Integrity**
  To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.
- **Section ET 55 – Article IV – Objectivity and Independence**
  A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public practice should be independent in fact and appearance when providing auditing and other attestation services.
- **Section ET 56 – Article V – Due Care**
  A member should observe the profession's technical and ethical standards, strive continually to improve competence and the quality of services, and discharge professional responsibility to the best of the member's ability.

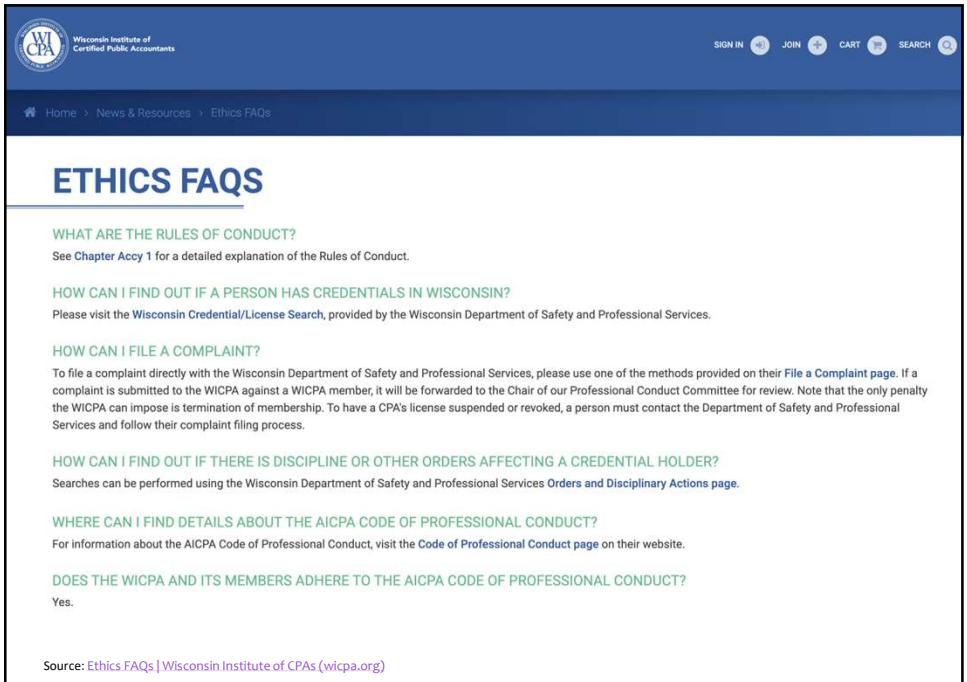
Source: AICPA Code of Conduct

Joint Ethics Enforcement Program

Source: AICPA



- The AICPA and each of the state societies have respective codes of professional conduct that their members are obligated to observe as a condition of their membership.
- The provisions of the codes of many state societies are identical with, or similar to, the provisions of the AICPA Code of Professional Conduct.
- Because of this identity and similarity, and because it is not uncommon for a CPA to be a member of both the AICPA and one or more state societies, the AICPA and virtually all of the state societies have joined together to create the **Joint Ethics Enforcement Program (JEEP)**.



Source: Ethics FAQs | Wisconsin Institute of CPAs (wicpa.org)

Published under s. 35.93, Wis. Stats., by the Legislative Reference Bureau.

Chapter Accy 1

RULES OF CONDUCT

Subchapter I — Applicability and Definitions
Accy 1.001 Applicability of rules of conduct to certified public accountants.
Accy 1.002 Applicability of rules of conduct to certified public accountants who have a significant influence over a CPA–related business or who advertise as a CPA.
Accy 1.003 Definitions.

Subchapter II — Professional Conduct, Integrity, and Objectivity
Accy 1.101 Professional conduct.
Accy 1.102 Integrity and objectivity.

Subchapter III — Competence and Technical Standards
Accy 1.201 General standards.
Accy 1.202 Auditing standards.
Accy 1.203 Accounting principles.
Accy 1.204 Other technical standards.
Accy 1.205 Standards for auditing, accounting and review services, and attestation engagements.

Subchapter IV — Responsibilities to Clients
Accy 1.301 Confidential client information.
Accy 1.302 Contingent fees, commissions and referral fees.

Subchapter V — Other Responsibilities and Practices
Accy 1.401 Acts discreditable.
Accy 1.402 Advertising or other forms of solicitation.
Accy 1.404 Incompatible occupations.
Accy 1.405 Firm Names.
Accy 1.406 Practice while suspended.
Accy 1.407 Communications.
Accy 1.408 Ownership requirements.

Note: Chapter Accy 1 as it existed on June 30, 1974 was repealed and a new Chapter Accy 1 was created, Register, June, 1974, No. 222, effective July 1, 1974.

Subchapter I — Applicability and Definitions

Accy 1.001 Applicability of rules of conduct to certified public accountants. (1) Chapters Accy 1 to 6 apply to a person who practices as a certified public accountant in this state.

(2) A certified public accountant may be held responsible for compliance with the rules of the board by any person associated in the opinion of the certified public accountant, the statements conform with generally accepted accounting principles or, if applicable, with another comprehensive basis of accounting.

(2m) "Board" means the accounting examining board.

(2r) "Certified public accountant" or "CPA" means a person considered to be in practice as a certified public accountant under s. 442.02, Stats.

(3) "Commission" means compensation, except a referral fee, for recommending or referring any product or service to be supplied by another person.

Source: https://docs.legis.wisconsin.gov/code/admin_code/accy/1.pdf

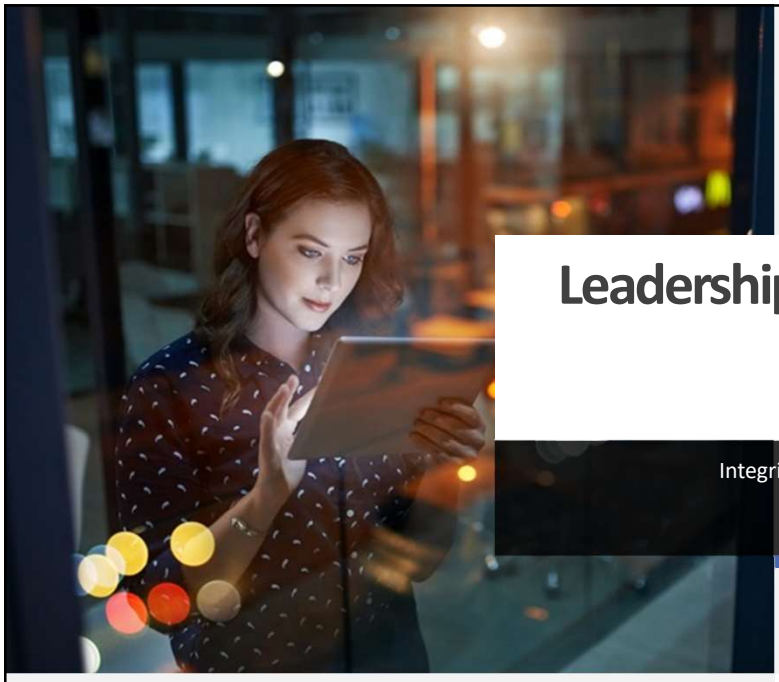
Fraud Triangle

ACFE
Association of Certified Fraud Examiners

Source: Association of Certified Fraud Examiners

Business Leadership

- **Personal Leadership**
  - Core values
  - Character
  - How we "show up"
- **Business Leadership**
  - Extension of our personal leadership style
  - Our personal leadership style impacts how we lead
  - How we fulfill role(s)



Leadership Ethics

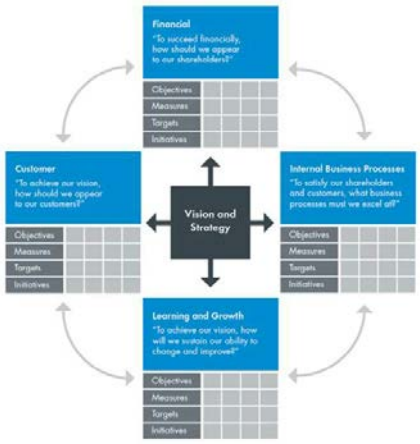
Integrity | Core Values

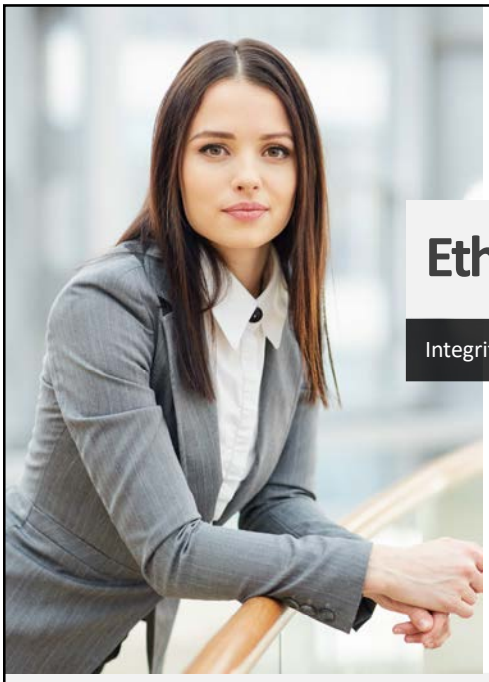
Business Leadership

Create an Ethical Organizational Culture

- Tone at top
- Opportunity when launching business
  - Early days, establish ethical practices as a way of doing business
- Include mission statement, vision, core values on meeting agendas and minutes
- Broader view of stakeholder interests
  - Employees, customers, communities, and the relationships you have
  - Example: Harvard Business Review ESG Rankings (i.e., Top 100)

[1]Adapted from Robert S Kaplan and David P Norton, Using the Balanced Scorecard as a strategic management system, Harvard Business Review, January-February 1996





Ethical Leadership

Integrity

- Ethical leaders inspire good values through their actions and words
- Ethical leaders do not overlook wrongdoing, even if doing so may benefit their business
- Displaying integrity and doing what is right, core of being an ethical leader
- Tone at the top: Ethical leaders set an example for company teams

Ethical Leadership

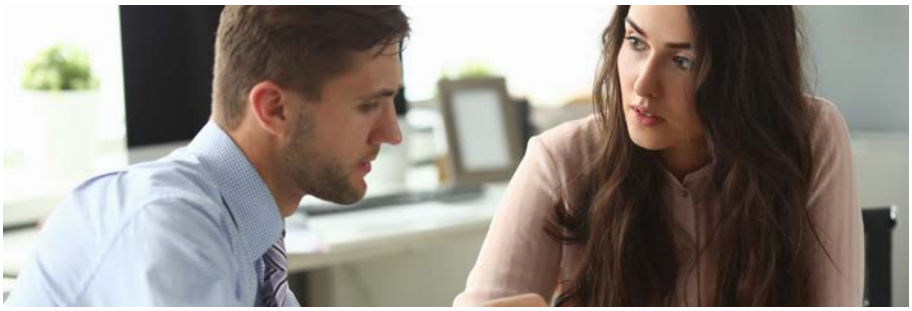
- Leadership involves inspiring and motivating others
- Setting the tone and standard for others
- Leadership is formal, positional and informal, non-positional

Ethical leadership qualities

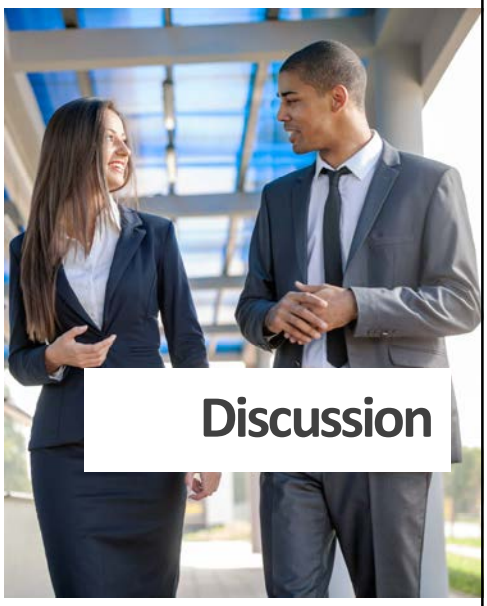
- Honesty
- Respect
- Integrity
- Authentic
- Open culture of trust and communication
- Responsible, owning actions

Ethical Leadership Recommendations

- Deal with ethical dilemmas as they arise
- As ethical leaders, model and communicate ethical behavior
  - Strong team relations are built on integrity and trust
- Know your organization's core values
  - Include mission statement or core values on meeting agendas and/or minutes
- Lead by example
- Take ownership of your actions



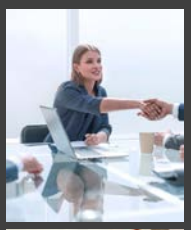
- How do you define ethical leadership?
- What makes a leader or manager effective?
- What traits/qualities do you look for in a great leader?
- Share an example of leadership whether business or personal.
- What are some of the leadership challenges that you have experienced within an organization?
- How do you continue to improve your leadership?



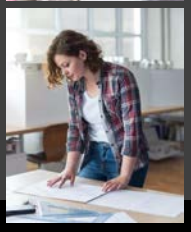
Discussion

Resources

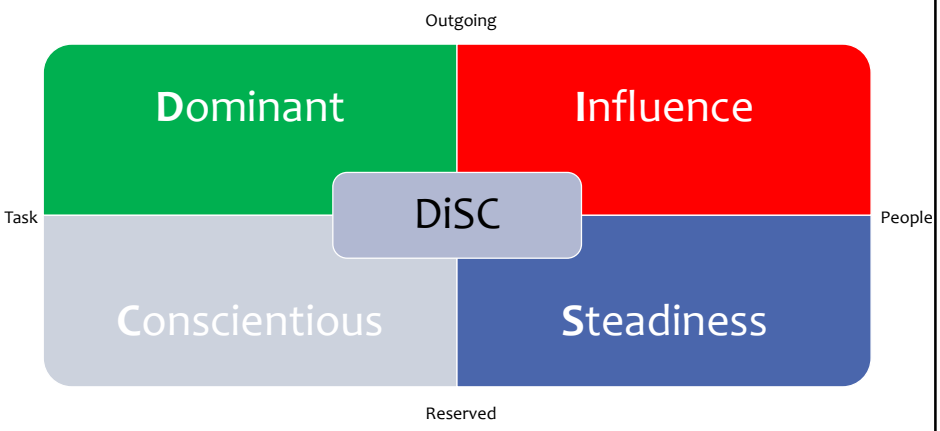
Resources

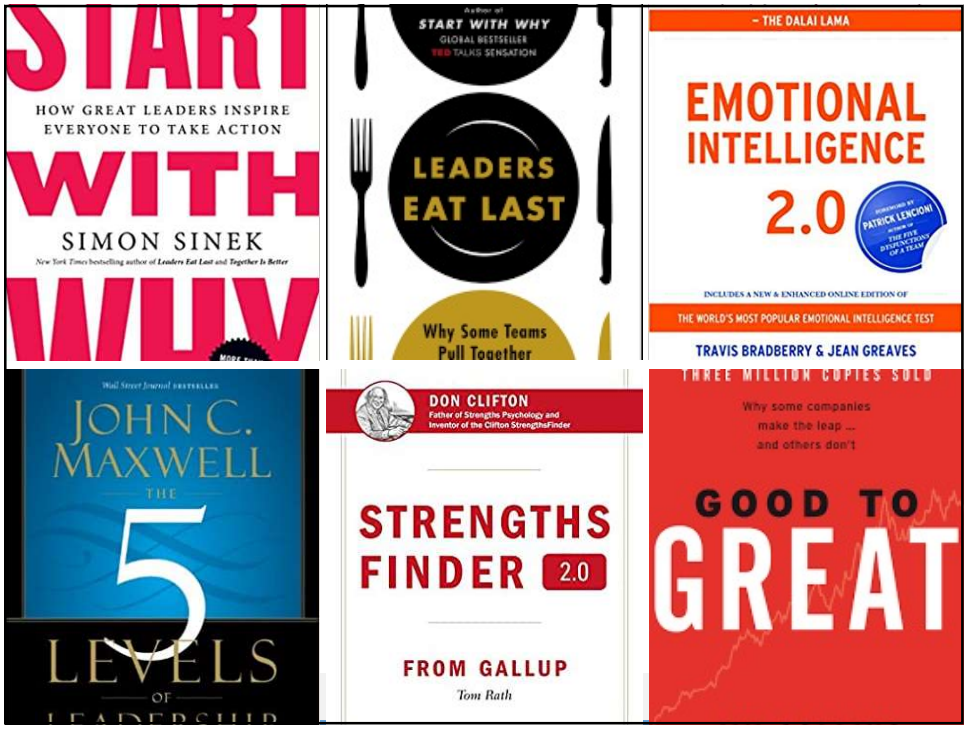


- AICPA Professional Code of Conduct
- Joint Ethics Enforcement Program
- WICPA Ethics FAQs
- Emotional Intelligence
- DiSC
- Myers-Briggs
- StrengthsFinder
- Kolbe



DiSC





PEER NOVATION

What Peer Advisory Groups Can Teach Us about Building High-Performing Teams

Circle of Trust

"Remember teamwork begins by building trust." - *Patrick Lencioni*

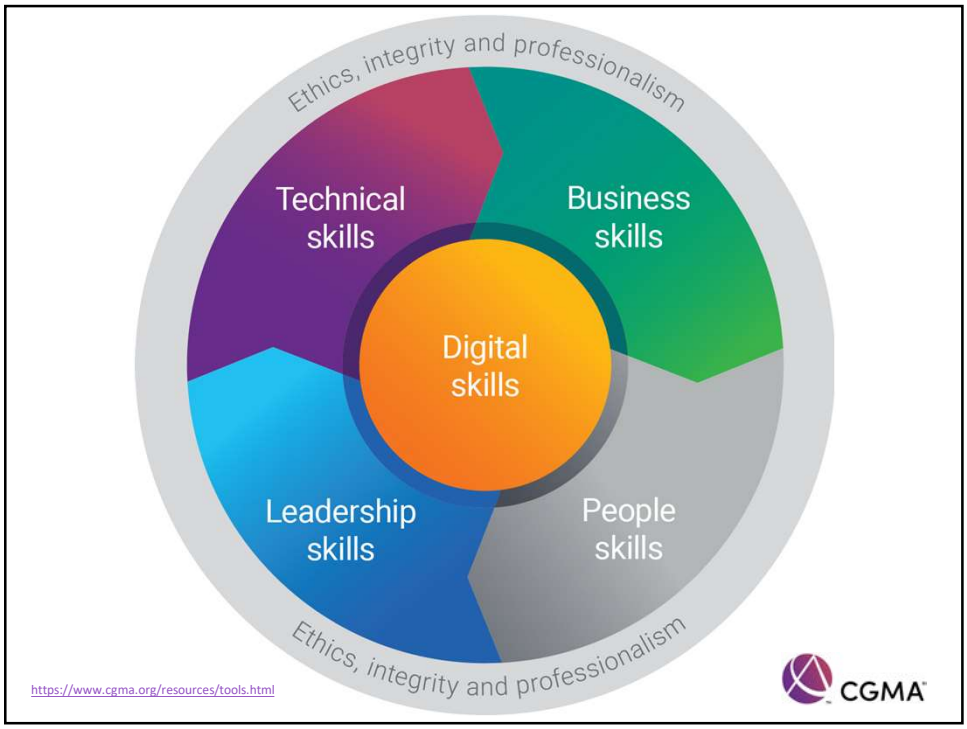
- Surround yourself with diversity of perspective and experiences
- Build a circle of trust with proven business leaders with high business acumen
- Someone or a group that will challenge you and your team to be the best

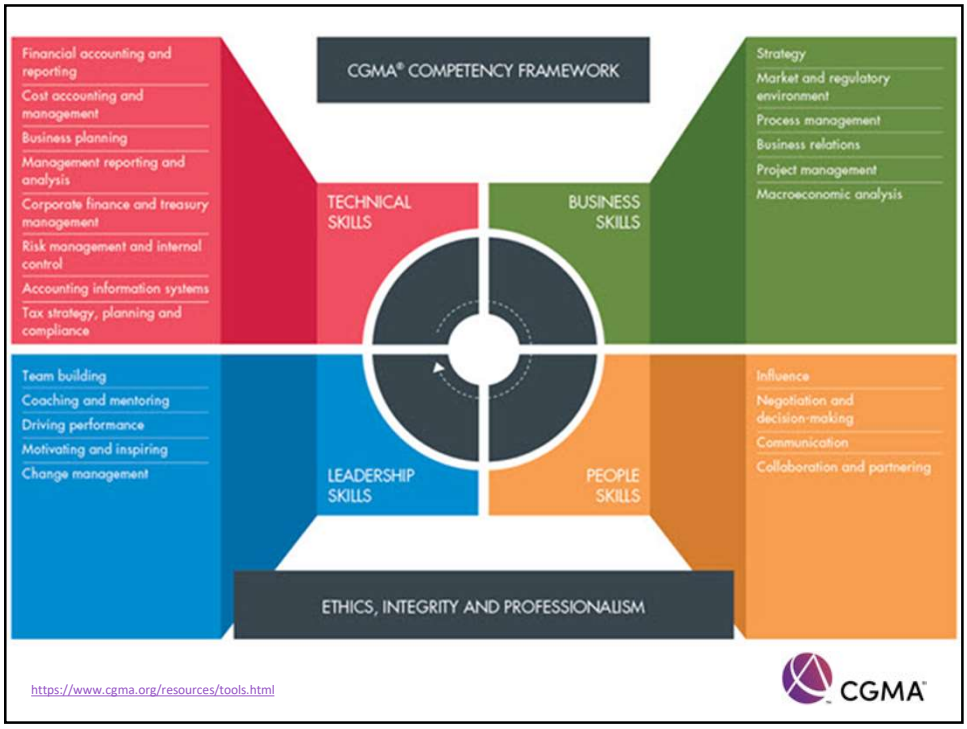
Peer Advisory Board

- 12-15 Business Leaders
- High business acumen
- Confidential

- Top Executives | Owner, President, CEO
- Key Executives | C-Suite Succession Line
- High Potential | High Performers

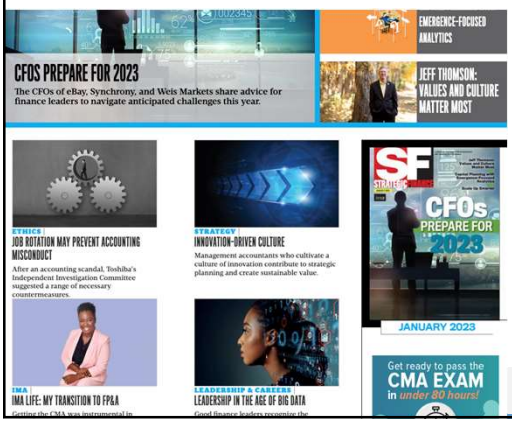
- **Educational Component** – Continuous learning through thought leaders and leading practitioners
- **Round Table** – Space for reflection and planning based on focused leadership and self-development
- **Case** – Members present their most critical challenges in a rigorous and structured manner

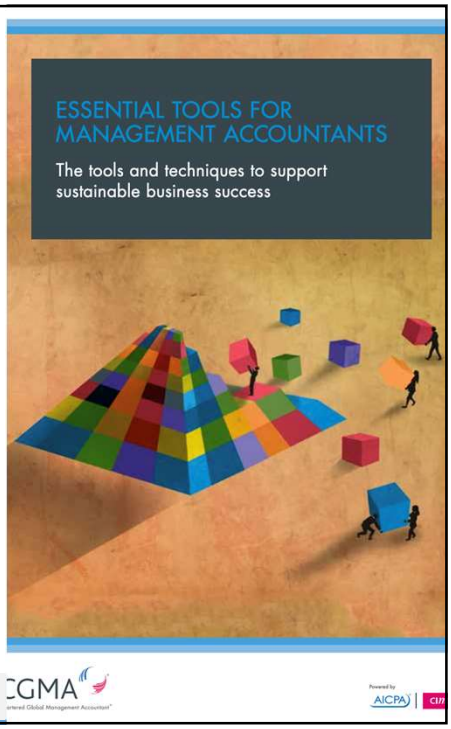

Ethics, integrity and professionalism
Technical skills
Business skills
Digital skills
Leadership skills
People skills
Ethics, integrity and professionalism
https://www.cgma.org/resources/tools.html
CGMA


CGMA® COMPETENCY FRAMEWORK
Financial accounting and reporting
Cost accounting and management
Business planning
Management reporting and analysis
Corporate finance and treasury management
Risk management and internal control
Accounting information systems
Tax strategy, planning and compliance
TECHNICAL SKILLS
BUSINESS SKILLS
Strategy
Market and regulatory environment
Process management
Business relations
Project management
Macroeconomic analysis
Team building
Coaching and mentoring
Driving performance
Motivating and inspiring
Change management
LEADERSHIP SKILLS
PEOPLE SKILLS
Influence
Negotiation and decision-making
Communication
Collaboration and partnering
ETHICS, INTEGRITY AND PROFESSIONALISM
https://www.cgma.org/resources/tools.html
CGMA

Strategic Finance Magazine

CGMA Essential Tools for Management Accountants

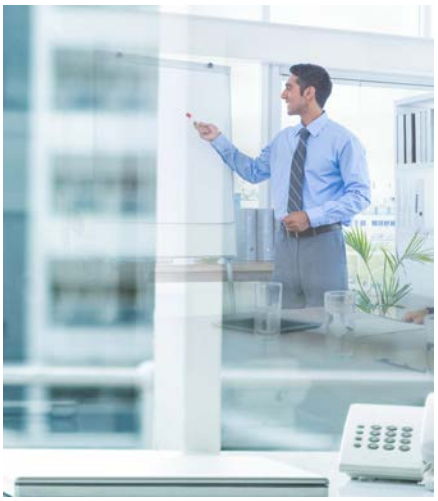




Examples + Recommendations

Look for Growth Opportunities

"Find the smartest people you can and surround yourself with them." - *Marissa Meyer*



- Board opportunities
- Leadership development opportunities through professional associations or peer advisory boards/groups
- Cross-functional team development opportunities
- Mentor program
- Coach
- Engagement
- Grow and cultivate your business network

Leadership Development

Investing in Leadership

- Leading Self
- Leading in the Community
- Leading Organization

Holistic Approach

- Business Growth
- Professional Growth
- Personal Growth

Self-awareness and reflection are key

Leadership Development

Investing in Leadership

- Build trust
- Business culture
- Embrace diversity of thought
- Own decisions and actions
- Continuous review and improvement
- Communicate ethical core values
- Be consistent and follow through
- Transparency with teams
- Continuous improvement

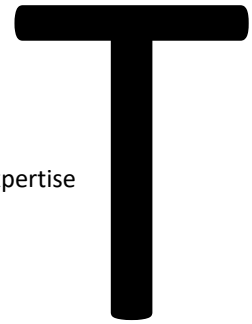
Core Values

Authentic
Balanced
Committed
Connected
Growth-Minded
Innovative
Integrity
Open-Minded
Progressive
Visionary

T-Shaped Skills

- Valuable employee
- Breadth and depth skill sets

Cross-Discipline Expertise

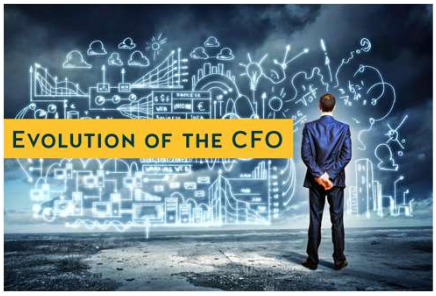


Deep-Discipline Expertise

Ever-Changing Role

Why Ethical Leadership is Important

Business/Industry



Public

"Leadership is lifting a person's vision to high sights, the raising of a person's performance to a higher standard, the building of a personality beyond its normal limitations."

- Peter F. Drucker

Ever-Changing Role | Business Partner

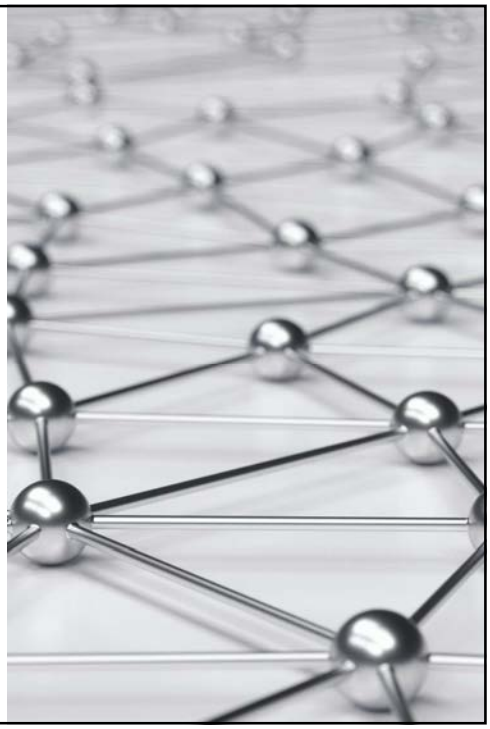
Strategic Planning

Business Analytics

HR and IT Oversight

Aligning Strategy

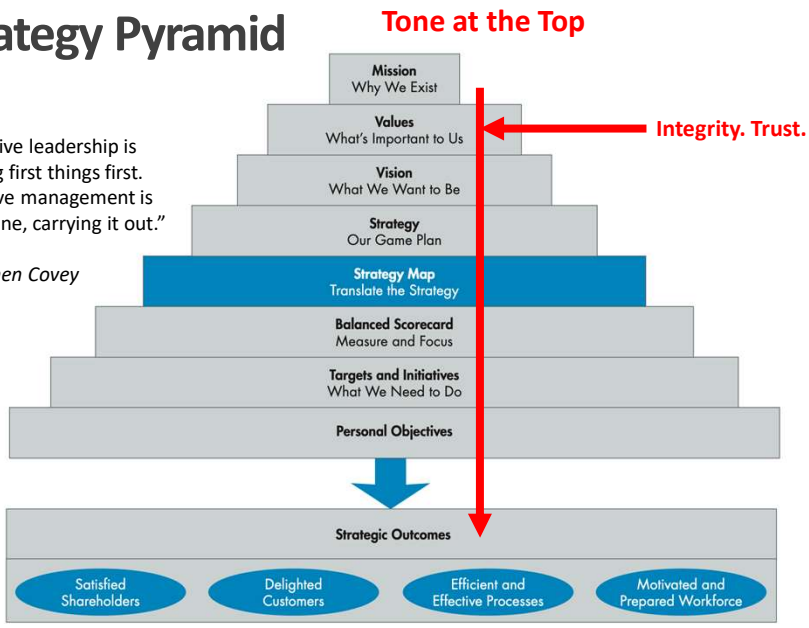
- CPAs and CFOs are strategic business partners
  - Strategy, board, revenue opportunities, and cost management
  - Human resources, legal, technology, and/or operations



Strategy Pyramid

"Effective leadership is putting first things first. Effective management is discipline, carrying it out."

- Stephen Covey

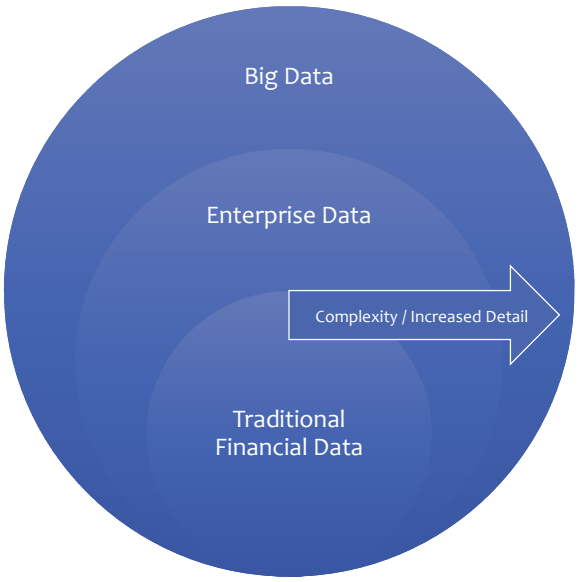


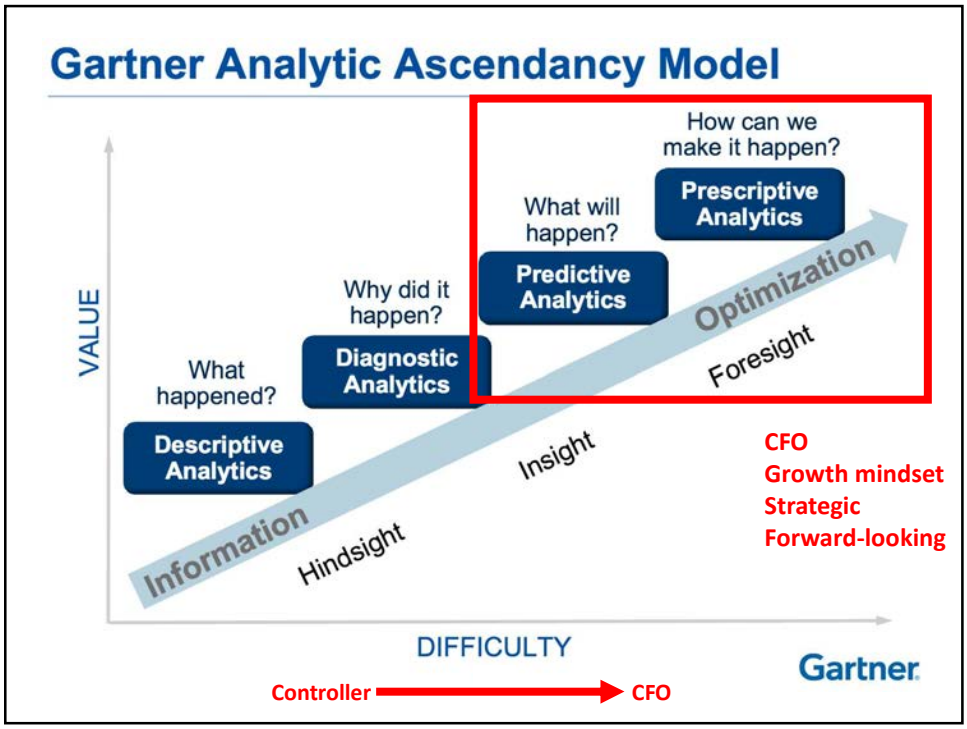
Digital Revolution

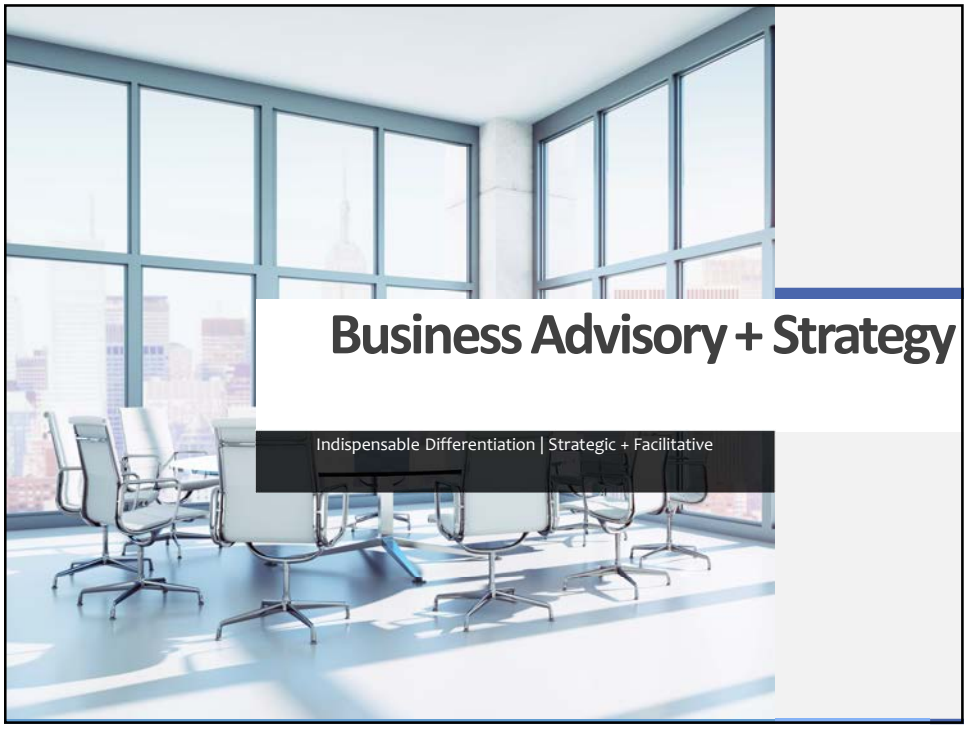
"From the dawn of civilization until 2003, humankind generated five exabytes of data. Now we produce five exabytes every two days…and the pace is accelerating."

Eric Schmidt,

Executive Chair, Google




Gartner Analytic Ascendancy Model
How can we make it happen?
Prescriptive Analytics
What will happen?
Predictive Analytics
Why did it happen?
Diagnostic Analytics
What happened?
Descriptive Analytics
VALUE
Optimization
Foresight
Insight
Information
Hindsight
DIFFICULTY
Gartner
CFO
Growth mindset
Strategic
Forward-looking
Controller
CFO


Business Advisory + Strategy
Indispensable Differentiation | Strategic + Facilitative

Performance Review

Tone at the Top

Business Performance Review	People Performance Review	Profit Improvement
Top-Line Growth	Key Performance	Risk Management
People Development	Innovation	Culture and Brand

Ethical Culture

- Strategy
- Balanced Scorecard
- KPIs
- Dashboards + Analytics

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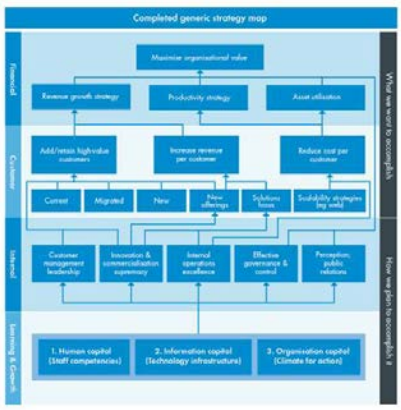
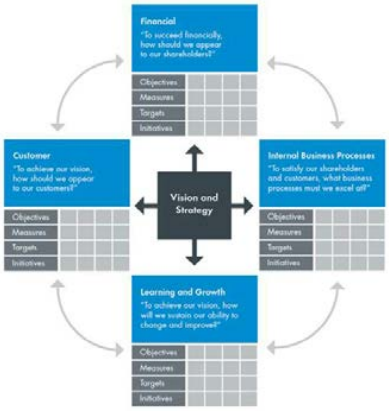
Opportunities

Tone at the Top

Opportunities

Opportunities





Source: CGMA Essential Tools for Management Accountants[1]

[1]Adapted from Robert S Kaplan and David P Norton, Using the Balanced Scorecard as a strategic management system, Harvard Business Review, January-February 1996

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Integrated Report

- Concise communication about how an organization's strategy, governance, performance and prospects, in the context of its external environment, create value over the short-, medium-, and long-term.
- Provides more information about an organization.
- Not just the past, looking to the future.
- Addresses an organization's governance, strategy, business model, risks and opportunities, and future outlook.
- Exploring what's possible related to improved performance and profitability.
- integrated-report.pdf (incpas.org)

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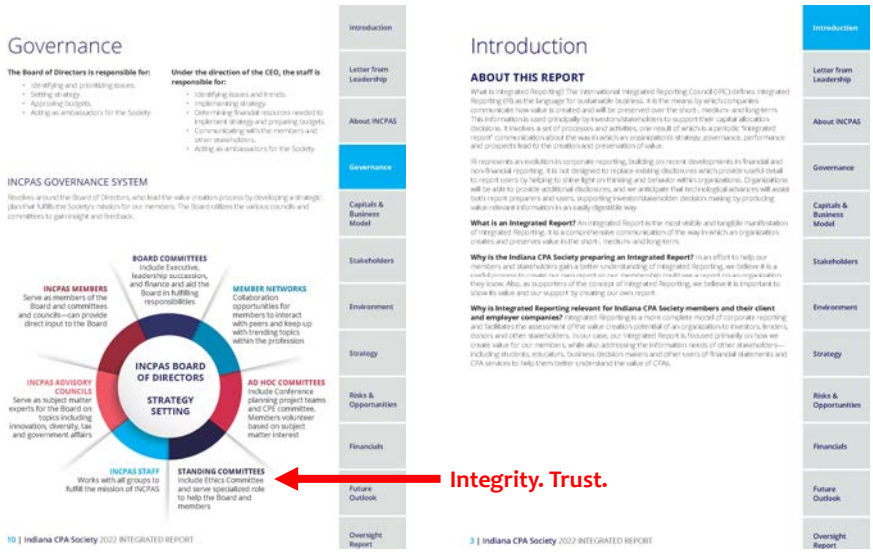

Governance

The Board of Directors is responsible for:
- Identifying and prioritizing issues.
- Setting strategy.
- Approving budgets.
- Acting as ambassadors for the Society.

Under the direction of the CEO, the staff is responsible for:
- Identifying issues and trends.
- Implementing strategy.
- Determining financial resources needed to implement strategy and preparing budgets.
- Communicating with the members and other stakeholders.
- Acting as ambassadors for the Society.

INCPAS GOVERNANCE SYSTEM

Revolves around the Board of Directors, who lead the value creation process by developing a strategic plan that fulfills the Society's mission for our members. The Board utilizes the various councils and committees to gain insight and feedback.

10 | Indiana CPA Society 2022 INTEGRATED REPORT

Introduction
Letter from Leadership
About INCPAS
Governance
Capitals & Business Model
Stakeholders
Environment
Strategy
Risks & Opportunities
Financials
Future Outlook
Oversight Report

Introduction

ABOUT THIS REPORT

What is Integrated Reporting? The International Integrated Reporting Council (IIRC) defines Integrated Reporting (IR) as the language for sustainable business. It is the means by which companies communicate how value is created and will be preserved over the short-, medium- and long-term. This information is used principally by investors/stakeholders to support their capital allocation decisions. It involves a set of processes and activities, one result of which is a periodic "integrated report" communication about the way in which an organization's strategy, governance, performance and prospects lead to the creation and preservation of value.

It represents an evolution in corporate reporting, building on recent developments in financial and non-financial reporting. It is not designed to replace existing disclosures which provide useful detail to report users by helping to shine light on thinking and behavior within organizations. Organizations will be able to provide additional disclosures, and we anticipate that technological advances will assist both report preparers and users, supporting investor/stakeholder decision making by producing value-relevant information in an easily digestible way.

What is an Integrated Report? An Integrated Report is the most visible and tangible manifestation of Integrated Reporting. It is a comprehensive communication of the way in which an organization creates and preserves value in the short-, medium- and long-term.

Why is the Indiana CPA Society preparing an Integrated Report? In an effort to help our members and stakeholders gain a better understanding of Integrated Reporting, we believe it is a useful process to create our own report on our membership model as a report on organizations they know. Also, as supporters of the concept of Integrated Reporting, we believe it is important to show its value and our support by creating our own report.

Why is Integrated Reporting relevant for Indiana CPA Society members and their client and employer companies? Integrated Reporting is a more complete record of corporate reporting and facilitates the assessment of the value creation potential of an organization to investors, lenders, donors and other stakeholders. In our case, our Integrated Report is focused primarily on how we create value for our members, while also addressing the information needs of other stakeholders—including students, educators, business decision makers and other users of financial statements and CPA services to help them better understand the value of CPAs.

3 | Indiana CPA Society 2022 INTEGRATED REPORT

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Integrity. Trust.

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Summary

- Leadership vs management
- Leadership ethics
- Leadership styles
- Resources
- Recommended reading
- Examples and recommendations for continued leadership development
- Leading self, leading business, and leading in the community
- Holistic approach including developing T-shaped skills
- The "why" including opportunities

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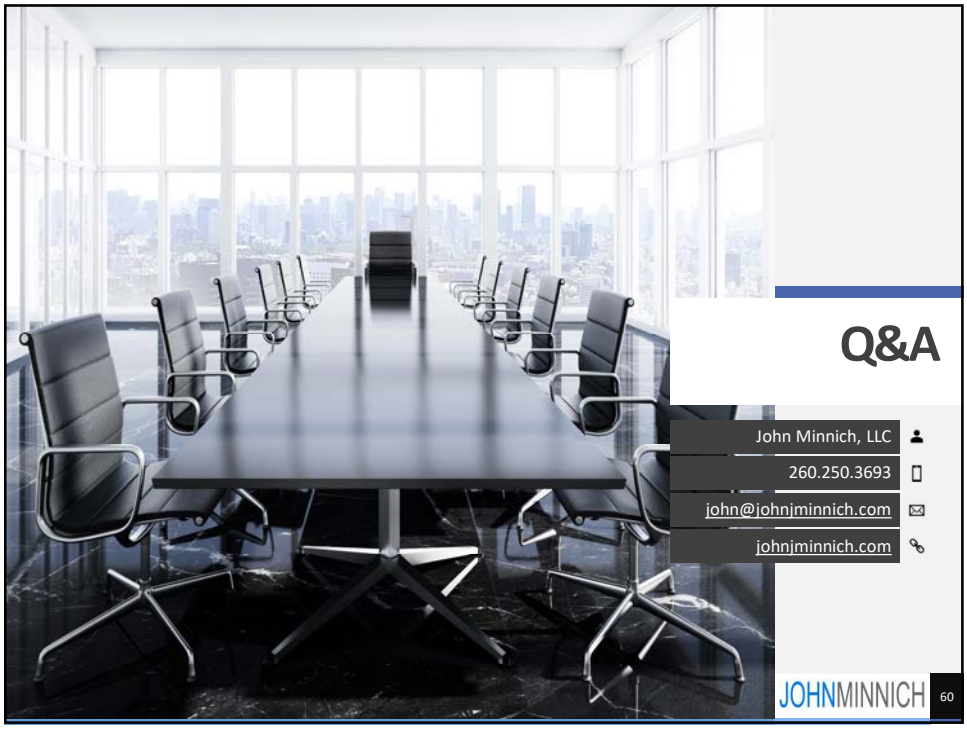
Summary + Key Takeaways

Investing in Ethical Leadership

- Build trust
- Business culture
- Embrace diversity of thought
- Own decisions and actions
- Continuous review and improvement
- Communicate ethical core values
- Be consistent and follow through
- Transparency with teams
- Continuous improvement

Core Values

Authentic
Balanced
Committed
Connected
Growth-Minded
Innovative
Integrity
Open-Minded
Progressive
Visionary



Q&A

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