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FMG Professional Liability Quarterly Report

A summary of the important professional liability topics by our expert team members for the third quarter.

THE BIG BEAUTIFUL BILL – HOW DOES IT AFFECT TAX TREATMENT FOR PROFESSIONAL SERVICES FIRMS?

By: James G. Bozza

The One Big Beautiful Bill Act was signed into law on July 4, 2025 following weeks of contentious debate. If your professional services firm operates as an LLC, an S corporation or a sole proprietorship, the BBB contains important tax implications for your business.

After strong pushback from industry leaders including the American Bar Association, the final bill removed the proposal to deny pass-through entity tax deductions to specified services trades or businesses such as law and accounting firms. Specifically, the original form of the bill sought to deny the state and local tax deduction at the entity level for pass-through entities which would have significantly raised tax burdens on professionals to the tune of approximately $75 billion over the next decade.

The final bill, however, increases the state and local tax deduction cap to $40,000 in 2025, preserves the full pass-through entity tax deduction for state and local taxes, and creates a phaseout of the state and local tax cap benefit for modified adjusted gross income above $500,000. This is particularly important for professionals such as accountants and lawyers because it maintains equal tax treatment for their learned professions compared to larger C-corporations that do not operate as pass-through entities.

Now that professional services firms can more accurately predict their tax liabilities moving forward, important business decisions lie ahead. Should a need for legal advice or services arise, the FMG professional liability team is prepared to assist. Contact FMG attorneys Scott Anderson and James Bozza for more information at scott.anderson@fmglaw.com and james.bozza@fmglaw.com.

ACCOUNTANTS BEWARE – THE IMPORTANCE OF OBTAINING CLIENT CONSENT PRIOR TO DISCLOSING TAX INFORMATION

By: Scott Eric Anderson and James G. Bozza

Internal Revenue Code § 7216 is a criminal provision that prohibits tax return preparers from knowingly or recklessly disclosing their clients' tax return information for a purpose other than completing an income tax return. Under 26 CFR § 301.7216-1, the penalty for providing tax return information is up to one year in prison, a fine of not more than $1,000, or both, as well as the costs of prosecution. These steep penalties are intended to preserve the privacy and confidentiality of client information and to prevent unauthorized or improper use.

Importantly, the criminal factor of this provision may lead some professionals to believe that an element of malicious intent is needed for the government to impose a penalty. But this is not the case – all that is required is for the tax return preparer to *know* that they released client tax return information to someone other than the taxpayer. An example is when tax information is requested by third parties in lawsuits such as probate contests, divorces (business and marital), when issues arise involving IRS or Department of Labor investigations or even when trusted financial players like national banks state their need for the information.

Another common misconception is that the exclusion in the provision for responding to court orders also applies to subpoenas. A subpoena is **not** a Court Order. Responding to a subpoena with client tax information requires client consent. A grand jury subpoena, however, *is* an exception to the written authorization requirement.

Section 7216 consent forms negate the possibility of criminal penalties. When seeking consent, the form must clearly explain the purpose, scope and duration of the disclosure, as well as the identity of the persons and/or entities seeking the information. It also must inform the client that they maintain the right to revoke their consent at any time and explain the consequences that may result from them doing so.

Navigating the disclosure of client tax information can be a difficult event for professionals. The FMG professional liability team is prepared to assist with each unique situation. Contact FMG attorneys Scott Anderson and James Bozza for more information at scott.anderson@fmglaw.com and james.bozza@fmglaw.com.

GEORGIA COURT CONFRONTS LAWYERS' APPARENT USE OF AI

By: P. Michael Freed

Courts throughout the country have been wrestling with litigants' use of artificial intelligence ("AI") in drafting legal briefs. Courts have discovered citations to fictitious cases in parties' legal briefs in several highly publicized cases. The Court of Appeals of Georgia is the latest court to confront the issue.

Shahid v. Essam involved an appeal from a trial court order in a divorce case denying the wife's petition to reopen the case and to set aside a final judgment in the husband's favor. It came to light during the appeal that the husband's lawyer had cited fictitious cases in opposing the wife's motion. The trial court incorporated two of those citations into its order. The husband's lawyer compounded the problem by citing additional fake cases in his appellate brief, including cases purporting to hold that a party can recover attorneys' fees incurred on appeal under O.C.G.A. § 9-15-14. Longstanding precedent holds to the contrary.

The Court of Appeals was rightly "troubled" by what it suspected to be the use of generative AI as the source of fake case citations. The court noted that "there is nothing inherently improper about using a reliable artificial intelligence tool for assistance." But attorneys remain responsible for ensuring the accuracy of their filings. They abandon that responsibility when they cite nonexistent AI-generated cases and deprive the opposing party of the opportunity to respond appropriately. Ultimately, the court imposed a $2,500 penalty against the husband's attorney, the maximum amount the court's rules allow.

Shahid provides yet another warning to attorneys about the use of generative AI in drafting legal briefs. Ethical uses of that technology may exist. But attorneys must stay diligent in ensuring that their filings accurately represent the law and its supporting authority.

For more information, please contact P. Michael Freed at michael.freed@fmglaw.com or your local FMG attorney.

SHARP CHANGE IN ILLINOIS TAX LAW CREATES SIGNIFICANT LIABILITIES FOR NON-ILLINOIS COMPANIES

By: Nancy M. Reimer and Matthew R. Stersic

Accountants in Illinois or with clients with dealings in Illinois should take note of a sea change in Illinois tax law. Under Illinois' newly passed H.B. 2755, Out-of-State and Out-of-Country businesses with dealings in Illinois are subject to state taxes. For businesses, the most notable changes may be the new sales tax rules and changes in the bases of taxation for GITLI, Pass-through entity sales and Multi-state Unitary Businesses.

Sales Tax Changes

Illinois, like most states in the last few years, amended its tax laws to levy sales taxes on out-of-state marketplaces selling tangible personal property in the state. With the passage of H.B. 2755, starting January 1, 2026, taxes will now apply not just to sellers of tangible personal property from out of state, but also to sellers of services via Illinois's service occupation tax and service use tax.

Additionally, beginning January 1, 2026, Illinois will move away from its 200-transaction threshold for an out-of-state retailer to be taxed and shift to a $100,000 sales per year threshold.

GILTI

Illinois has also begun taxation of global intangible low-taxed income ("GILTI"). The 2017 Tax Cuts and Jobs Act began taxation of income from intangible assets from foreign countries. Illinois previously treated the income as dividends, subject to a 100% dividends-received deduction. H.B. 2755 cuts that deduction to 50%. This change applies to the tax year ending December 31, 2025, and going forward. It is important to note that the One Big Beautiful Bill Act contains significant changes to the GILTI provisions in the 2017 Tax Cuts and Jobs Act.

Pass-Through Entity Sales

Under previous Illinois law, owners of interests in pass through entities, either S-corporations or partnerships, with taxable activities in Illinois, would only be taxed in their state of residence. Starting June 16, 2025, taxes are now payable in Illinois and not just the state of residence based on an apportionment of the gain or loss on the sale in relation to Illinois apportionment factors for the prior three years. Apportionment factors are a newer idea in taxation and some states, such as Massachusetts, have run into difficulty getting the method accepted into their tax codes.

Adoption of "Finnigan" approach

Unitary businesses with entities operating in Illinois previously operated under the "Joyce" approach for recognition of sales, recognizing Illinois-sourced sales only from entities with an Illinois nexus. For tax years ending December 31, 2025, and beyond, the "Finnigan" method will apply, getting rid of the requirement that the sales must be from an entity with an Illinois nexus. Now the sales must just be part of the combined group of entities.

Other Changes:

Several other changes also apply including tax changes to:

- Create tax amnesty programs to waive interest and penalties to applicable taxes;
- Increase the rate of tax on tobacco products and expand definition to include products with nicotine;

To read the full blog post, click here.

It is important for accountants to be aware of how these changes may affect both businesses and people that they advise or provide with tax or audit services. Should a need for legal advice or services arise, the FMG professional liability team is prepared to assist. Contact FMG attorneys Matthew Stersic and Nancy Reimer for more information at matthew.stersic@fmglaw.com and nancy.reimer@fmglaw.com.

KEY TAKEAWAYS FROM THE 11TH CIRCUIT COURT: AICPA GUIDELINES ARE CRITICAL IN THE ACCOUNTING PROFESSION

By: Scott Eric Anderson

The recent unpublished 11th Circuit Court decision in *Simmons v. AICPA, GSCPA, Georgia State Board of Accountancy, and Green, Mosier & Kemp, LLC* offers critical insights for accounting professionals navigating the regulatory landscape. The case involved a *pro se* challenge by Simmons—a longtime Georgia licensed CPA—against the AICPA (American Institute of CPAs®) and the Georgia State Board of Accountancy peer review process and the authority of private accounting organizations such as the Georgia Society of CPA's and private CPA firms tasked with peer review, with claims of constitutional violations and monopoly practices. Simmons brought his claims after he was denied renewal of his CPA license, which was issued in 1975 and has been continually renewed until now. The court's ruling, which affirmed the dismissal of the lawsuit, provides practical lessons for practitioners.

Why This Decision Matters to Your Practice

1. **Peer Review Programs Are Here to Stay**. The court upheld the legitimacy of peer review requirements, noting that private organizations like the AICPA and state societies, even when involved in regulatory processes, are not considered state actors unless there are plausible allegations supported by materials facts that there is significant state involvement or coercion. This means that participation in peer review programs remains a professional obligation for CPAs in states where it is required, and challenges to their legality are unlikely to succeed unless clear state action is involved.

2. **Private Entities and State Action**. The decision clarifies that private accounting organizations (such as the AICPA and the GSCPA) and peer review firms are not liable under federal civil rights statutes (such as § 1983) unless there are plausible claims supported by material facts that the private organizations are acting "under color of state law." For practitioners, this means that disputes with these private organizations over peer review outcomes or standards are generally not constitutional matters, but rather professional issues.

3. **Sovereign Immunity Protects State Boards**. The court reaffirmed the dismissal of the Georgia State Board of Accountancy on the grounds that Simmons abandoned his appeal of the District Court's determination that state boards of accountancy are protected by sovereign immunity under the 11th Amendment as an arm of the state, unless it can plausibly be shown that a specific exception applies.

4. **Importance of Professional Standards and Documentation**. The case highlights the importance of adhering to professional standards set by recognized bodies like the AICPA. Engagement letters, peer review documentation and compliance with established procedures are not just best practices – they are essential for maintaining licensure and defending your practice in the event of a challenge.

Practical Advice for Accountants

- **Stay Current on Peer Review Requirements**: Ensure your firm is up to date with all peer review obligations and that you understand the standards set by the AICPA and your State Board of Accountancy.

- **Maintain Thorough Documentation**: Keep detailed records of your peer review process, engagement letters and communications with clients and reviewers. This documentation is your best defense in the event of a dispute.

To read the full blog post, click here.

For information on how we may assist you and your accounting firm, please contact Scott Eric Anderson at scott.anderson@fmglaw.com.

MAINTAINING CONFIDENCE IN CONFIDANTS: THE SIXTH CIRCUIT UPHOLDS THE ATTORNEY-CLIENT PRIVILEGE IN THE CONTEXT OF INTERNAL INVESTIGATIONS

By: Grant A. Biggs

In the face of looming bankruptcy, FirstEnergy Solutions, an Ohio electric utility company, was saved in 2019 by House Bill 6, which flipped the script on renewable energies and subsidized the energy company to the tune of $1.3 billion. But no lunch is free, and this one was particularly costly—over $60 million dollars was wired by FirstEnergy to Generation Now, a 501(c)(4) organization controlled by Ohio House Speaker Larry Householder, who used the payments for his own personal benefit and to gain support for his candidacy as Speaker. After winning the speakership in January 2019, House Bill 6 passed just five months later and officially became law in October 2019.

When Householder was arrested for racketeering in July 2020, FirstEnergy immediately hired Jones Day—while its board of directors hired Squire Patton Boggs—to conduct internal investigations in anticipation of litigation. This proved prudent, as FirstEnergy became mired in multiple lawsuits, criminal and civil subpoenas, and federal and state investigations.

One of these lawsuits was a class of investors who sued for securities fraud and sought the results of the investigations the lawyers produced. The district court, in a shocking decision, ordered these results produced to the plaintiffs, alarming boardrooms and law firms throughout the nation. In doing so, the district court found that because the investigations were conducted for business purposes, rather than a predominantly legal purpose, the attorney-client privilege and work-product doctrine did not apply.

An amicus brief signed by thirty-nine law firms pleaded the Sixth Circuit Court of Appeals to stay that order pending resolution of FirstEnergy's petition for a writ of mandamus. The Court of Appeals granted this request, finding that the district court likely erred in applying the attorney-client privilege and work-product doctrine, and corrected the record.

In applying the attorney-client privilege, the Court of Appeals held, it is irrelevant why the legal advice was requested or given. All that matters is whether the subject communication constitutes "legal advice," or in other words, whether the communication's primary purpose is to request or give interpretation and application of legal principles to guide future conduct or to assess past conduct. Here, where the investigations were launched as a result of Householder's arrest, the doctrine directly applies and serves to protect the results of the investigations. Furthermore, the court noted, the district court's interpretation would swallow the attorney-client privilege whole as it would be rare to find a corporation that did not seek legal advice primarily to serve a business-related purpose.

The court also found that the work-product doctrine serves to protect the results of the internal investigations, as they were performed in anticipation of litigation.

By concluding that such communications are privileged, the Sixth Circuit not only aids corporations in maintaining legal compliance, but as a result, ensures public safety is prioritized as well. In allowing internal investigations to remain confidential, corporations are incentivized to freely share information with counsel, who are able to provide candid legal advice that facilitates compliance with law. This legal compliance, in turn, plays a critical role in protecting the public—particularly when it involves industries that affect health, safety and the environment. By ensuring that companies can proactively identify and correct potential violations without fear of exposure, the legal framework fosters safer business practices, reduces the risk of harm to consumers and the public at large, and reinforces accountability within corporate operations. Everyone wins.

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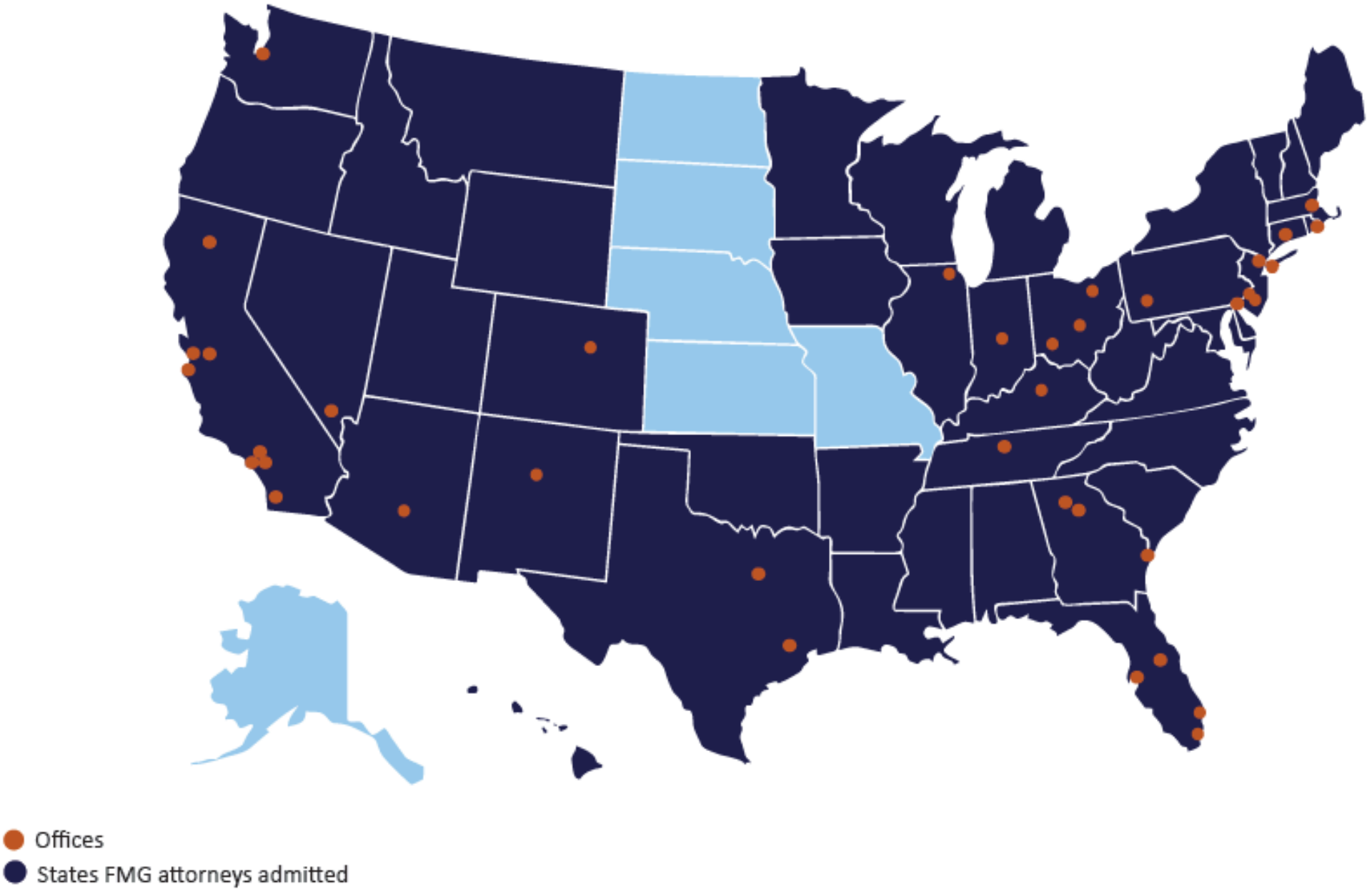

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