YLD
Allegheny County Bar Association

Point of Law

The E-Newsletter of the Young Lawyers Division of the Allegheny County Bar Association

Winter 2020

YLD Continues National Excellence

By Andrew Rothey, YLD Chair

Pittsburgh has long been known for its highly successful sports franchises, which have brought home championship trophies and individual accolades much to our city's pride and delight. But our sports teams are not alone in receiving national recognition – the Young Lawyers Division of the Allegheny County Bar Association keeps bringing home the hardware as well! For the second year in a row, the American Bar Association (ABA) has bestowed four separate awards on the YLD.

Last February, the YLD held one of its most fun annual events with a new twist. What was once known as Judicial Trivia, with judges from our various state and federal courts teaming up with groups of young lawyers to answer trivia questions on nearly any topic imaginable, was transformed into "Family Feud: Judgment Day." Instead of answering trivia questions, judges and young lawyers were placed on teams together and tried to guess how a survey of other young lawyers responded to various legally-themed questions. Not only was YLD Chair-Elect Amanda Thomas an emcee worthy of a future invitation to host the Oscars, but the "Family Feud" format was universally lauded as a fun and exciting new variation of an old favorite. The ABA conferred its Service to the Bar Award to the YLD for this event.

Members of the YLD certainly enjoy light-hearted social games like Family Feud, but they also are dedicated to giving back to the community. Each year, several promising young lawyers are selected to serve on the YLD's Bar Leadership Initiative (BLI). The BLI is designed to educate young lawyers about the values, goals, and structure of the ACBA and the YLD to prepare them for future leadership positions in the bar. This year, the BLI teamed up with a veterans' organization known as the Veterans Breakfast Club to put on an event designed to educate young lawyers on legal issues many veterans often face. In additional to a panel discussion, a reception was held to allow young lawyers a less formal opportunity to talk to the veterans in attendance. Sponsorships and a silent auction raised just under $2,300, which the BLI promptly donated to the Veterans Breakfast Club. For its efforts, the YLD was granted the ABA Award for Service to the Public.

Key to the continued success of the YLD is promoting an inclusive environment where attorneys from all backgrounds and walks of life feel welcome. To that end, the YLD organized a CLE at the Bench-Bar Conference called "Finding Success in Workplace Interactions." This CLE garnered the ABA Award for Diversity. Navigating workplace interactions can be tricky for all young attorneys, but young attorneys from diverse backgrounds often face unique obstacles. During presentation, an experienced panel discussed hypothetical scenarios which associates may find themselves in and

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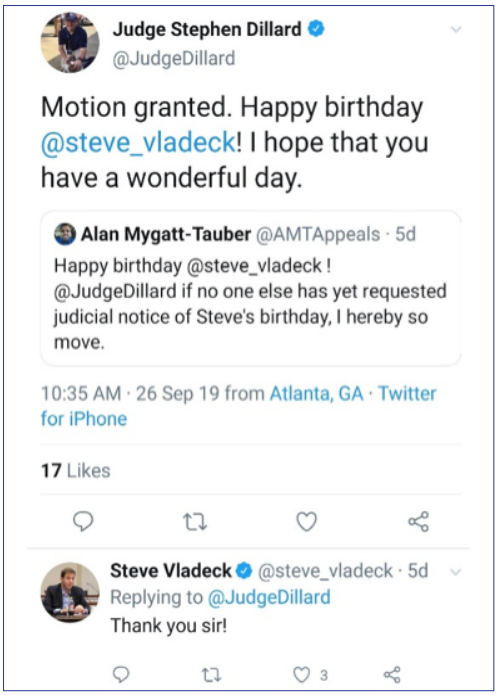
Civic Engagement by Tweet:
Judges Across America Find Comradery, Insight, from Law-Twitter Participation

By Thomas Cocchi

It is no secret that social media, and Twitter in particular, has become an increasingly important part of life in America and around the globe in recent years. Discourse now regularly takes place on online platforms in addition to, or rather than the more traditional halls of power. Despite the many changes brought on by the internet and the development of social networks that transmit thoughts, opinions, and ideas at the speed of an electron, the Supreme Court of the United States has managed to stay mostly out of the fray. On Twitter, the SCOTUS has become conspicuous in its absence, leaving the popular, but decidedly non-governmental @SCOTUSblog account to soak up angry tweets every time the High Court releases a blockbuster opinion. The individual justices likewise seem to avoid social media, perhaps feeling at a loss if asked to express themselves in the limited character space available in a tweet.

This is not to say that there are no productive areas of discussion on Twitter related to the law or the legal industry to be found. In fact, many members of the self-creating and self-regulating law-twitter network interact with productive and interesting conversations on a near daily basis. Being a group that self-organizes around the occasional to frequent use of the #lawtwitter hashtag, law-twitter is a subset of Twitter users that are interested in discussing the law and the legal industry. Members of law-twitter, if they can be called such, range from



0L (pre-law) students to partners in large law firms, authors of legal writing guides and practice manuals, and yes, even some judges.

Some law-twitter contributors boast a certain amount of renown in the real world, such as Ken "Popehat" White (@popehat), a criminal defense lawyer and First Amendment pundit who may regularly be found in nationally published editorial pages or cable news talk-boxes. Others choose to remain anonymous, contributing to the law-twitter world without hope of reaping any sort of direct benefit from their participation. On law-twitter, perennial discussions about the efficacy of the bar exam give way to thoughtful arguments about proposed amendments to ethical rules and memes about the billable hour.

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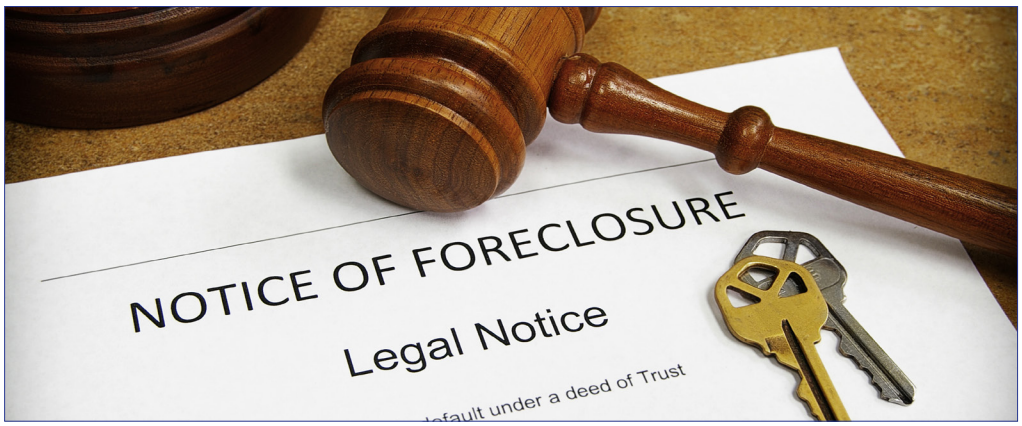
The Right to a Jury Trial in Mortgage Foreclosure Cases

By Stephen Matvey



The right to a jury trial in mortgage foreclosure proceedings remains a developing area of law in Pennsylvania. Generally, the question of whether a civil cause of action requires a jury trial is determined by a three prong test: 1) The court is to determine whether there is a statutory basis for a jury trial. 2) If no statutory basis exists, the next inquiry is whether the particular cause of action existed at the time the Pennsylvania Constitution was adopted. 3) If the cause of action and a right to jury existed at that time, then the inquiry is whether a common law basis existed for the claim. *Advanced Tel. Sys., Inc. v. Com-Net Prof'l Mobile Radio, LLC,* 846 A.2d 1264, 1275–76 (Pa. Super. 2004). However, there is no controlling Pennsylvania case law by either the Superior Court or Pennsylvania Supreme Court expressly prohibiting the right to a jury trial in mortgage foreclosure proceedings.

Attorneys may not be aware that this right exists, or assume it does not exist due to the general nature of foreclosure proceedings. For example, numerous foreclosure proceedings occur where the party being foreclosed upon does not have the resources to prepare and argue a defense involving issues of material facts. However, historically the cause of action identified as *scire facias sur mortgage* was created by the Act of 1705, and recognized that such actions were triable and tried before juries. The existence of jury trials in *scire facis sur mortgage* actions means that mortgage foreclosure actions were both triable and tried before juries when the first Pennsylvania Constitution was enacted in 1776. Moreover, the language of the Pennsylvania Constitution has preserved this right in successive constitutions, and several cases in the 1800's and 1900's discuss the waiver of a jury trial in a foreclosure proceeding. Irv Ackelsberg, *Residential Mortgage Foreclosure, Pennsylvania Law and Practice* (George T. Bisel. Co., I nc., 2d ed. 2014). Therefore, for the waiver of a jury trial in a foreclosure proceeding to be an issue, the right to said trial must exist.

To counter this position, attorneys representing the foreclosing party have made the argument that the Pennsylvania Rules of Civil Procedure would need to specifically set forth the right to a jury trial in a mortgage foreclosure action for the right to exist. However, this is incorrect. Pa. R.C.P. 1150 neither prohibits nor proscribes a jury trial in foreclosure actions because the rule is in fact silent. Instead, it states that when the parties waive the right to a jury trial, the resulting non-jury trial "shall be in accordance with Rule 1038." Therefore, the language of Rule 1150 clearly presumes and contemplates that foreclosure actions may be tried before juries.

Furthermore, the Court of Common Pleas of Allegheny County recently rejected a Motion to Strike Jury Trial in a mortgage foreclosure proceeding. On April 20, 2018 the Honorable John T. McVay, Jr. ruled "recognizing that the Pennsylvania Constitution preserved existing jury trial rights Pa. Constitution Act §6 providing 'trial by jury shall…remain inviolate', this court concludes that subsequent 1836 statutory references to mortgage foreclosures as actions in equity and the Pa. Rules of Civil Procedure's complete silence on the subject should not be construed to negate the right of a jury trial when issues of material facts are presented." *Nationstar Mortgage, LLC d/b/a Champion Mortgage Co. v. John Christofis,* No. MG-17-000189 (Allegheny Co. Ct. Com. Pl., April 20, 2018).

Overall, whether a mortgage foreclosure action involves a jury trial will be a fact specific inquiry, involving questions of whether there are material facts being disputed. However, the right itself is supported by case law, the Pennsylvania Rules of Civil Procedure and the Pennsylvania Constitution. ■

Stephen Matvey is an Associate Attorney at Very Law PLLC. His practice currently focuses on civil disputes, criminal defense, and consumer rights.

Civic Engagement by Tweet

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While an ecosystem of legal-related discussion, jokes, and memes can be found on many social media sites, Twitter's unique functionalities appear to give rise to a singularly thriving expanse. Without participation from Justices of the Supreme Court, it might seem unlikely that the judiciary would be significantly involved in the conversation. Yet, judges from around the country have found ways to engage the law-twitter community that are entertaining, while still being mindful of their responsibilities to the communities they serve.

Justice Beth Walker of the West Virginia Supreme Court of Appeals (@bethwalkr) is a relatively new addition to the law-twitter community but has quickly adapted to the nature of the loosely-knit social media group, often interacting with fellow appellate Judge Stephen Dillard of the Georgia Court of Appeals (@judgedillard). Judge Dillard, for his part, is an absolute must-follow for any aspiring law-twitter member. He can often be found granting 'motions' to take 'judicial notice' of law-twitter birthdays or complaining about unseasonably warm weather (an opinion in which Walker, J. concurred).

However, the discussions that take place on law-twitter are not all just for fun – sometimes they bring members from very different areas together to discuss common issues and brainstorm solutions. When an anonymous law-twitter member complained that rural courts should "Do. Uncontested. Motions. Better." apparently intending to release some steam from a long day of driving about his or her state, a rural judge and fellow law-twitter member from Alabama replied simply "how?" The ensuing conversation and contributions from other members centered around procedures that were generally agreed upon as being beneficial, and how those might be expanded to more courts, or what difficulties those could pose to courts with varying levels of resources at their disposal. Certainly, the original poster could not have foreseen that a tweet expressing some frustrations could lead to a conversation with judges who were interested in what he or she had to say, but those kinds of interactions appear to happen on a regular basis between members of law-twitter.

In a more recent exchange, a law professor from Case Western University (@jadler1969) noted that four federal courts of appeals live stream oral arguments before their courts, while "SCOTUS still refuses to release same-day audio" for the majority of its cases. Judge Dillard re-tweeted Professor Adler, opining that "The Supreme Court of the United States should live stream and archive its oral arguments." A reply came soon after from Chief Justice Bridget McCormack of the Michigan Supreme Court (@bridgetmarymc) noting her agreement with a simple "Preach." Justice Walker from West Virginia did not comment on the discussion but was seen elsewhere on law-twitter expressing her jealousy over the electronic voting system for preliminary votes on petitions boasted by the Texas Supreme Court's Justice Eva Guzman (@justiceguzman).

Perhaps it is not a surprise that judges at the trial and appellate levels who engage with other legal professionals on Twitter are generally in favor of increased utilization of technology. What may be surprising to young lawyers and law students approaching law-twitter for the first time is just how open many of these members of the judiciary are in their communication with colleagues and the general public about many of the issues facing the legal industry. A simple frustration with travelling to outlying counties that would have gone uttered to a friend or colleague without much note in previous generations can now be the catalyst for discussion about procedures in rural jurisdictions. Young attorneys who want to be a part of the conversation, or who at least want to see it while it unfolds in real time, may find law-twitter members such as the ones discussed above to be great resources in navigating a complicated industry. ■

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Submit an article for Point of Law, the YLD's ABA award-winning newsletter

YLD members are encouraged to write about the practice of law or any substantive legal issue of interest. Additionally, writers are encouraged to write responses to any article appearing in this issue. Featured authors will have their article – up to 1,000 words long – published along with a brief bio. Articles and inquiries may be submitted to *YLDCommunications@gmail.com.*

Destroyed Records:
The Next Battleground of Pennsylvania's Right-to-Know-Law

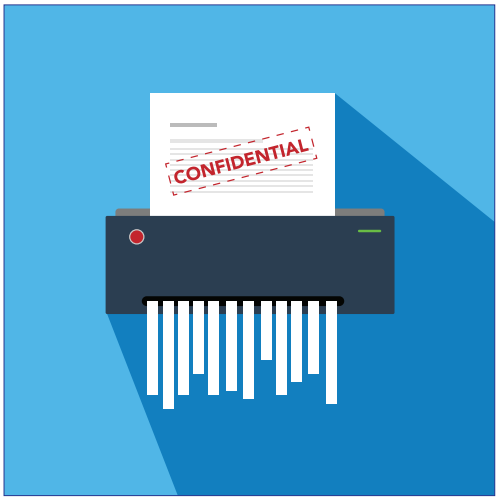
By Zachary N. Gordon

The Right-to-Know-Law ("RTKL"), 65 P.S. § 67.101 *et. seq.,* vastly improved the public's ability to monitor state and local government agencies in Pennsylvania. The basic framework of the RTKL also ensures that in simple cases records are provided promptly. Despite this significant progress, one area where the RTKL has not been successful is addressing records that government agencies have destroyed.

Under the RTKL, government records are deemed public unless a specific exemption applies. Requesting records under the RTKL is simple. A person submits a RTKL request for records from a Pennsylvania state or local agency. The agency has 5 business days to respond. The agency at its sole discretion may extend that 5-business day period for an additional 30 days.

If the agency fails to respond in the required timeframe or if the requester believes the agency's response is insufficient, the requester may pursue an administrative appeal. The administrative appeal is usually filed with the Office of Open Records ("OOR"), and must be decided within 30 days.

If the OOR or other administrative appeals officer does not decide the appeal in 30 days or a party does not agree with the decision, then the next step in the process is judicial review. If the agency is a local agency, then the requester or agency can seek judicial review in the Court of Common Pleas where the agency is located. An appeal from the Court of Common Pleas is heard by the Commonwealth Court. Judicial review of state agencies, however, proceed immediately to the Commonwealth Court.



While the process may sound daunting, it is relatively quick and inexpensive until judicial review is sought. The OOR has published simple 1-page forms for both RTKL requests and administrative appeals. (*https://www.openrecords.pa.gov/RTKL/Forms.cfm*) Further, most government agencies now list the open records officer – the person designated to accept RTKL requests – on the agency's website. The OOR also has a database of those officers and their contact information on its website. (*https://www.openrecords.pa.gov/RTKL/AOROSearch.cfm*) Thus, drafting a request and finding the correct person to send it to can be accomplished in minutes for basic requests.

While the RTKL works well to expand access to government records, two of its provisions limit the RTKL's effectiveness. First, the RTKL imposes no obligation for agencies to preserve records. 65 P.S. § 67.507. Second, the RTKL does not require agencies to provide records that are not in its possession. 65 P.S. § 67.705. These two provisions when combined have been used to deny access to records that are deleted.

In one instance, the Philadelphia Inquirer sought the texts of the mayor of Philadelphia related to his duties as mayor. The mayor, however, had deleted his texts. The request was denied by the mayor's office. The OOR affirmed the denial since the records did not exist. *Vargas v. City of Philadelphia,* AP-2019-0213 (OOR April 8, 2019) available at *https://www.openrecords.pa.gov/Documents/FinalDet/39803.pdf.*

Many agencies do have their own record retention policies. Unfortunately, there is usually no recourse for the public if a request is denied because the agency deleted the records, even if the agency's own record retention policy forbid the destruction. For instance, with the mayor of Philadelphia, the Philadelphia Inquirer argued that the mayor's correspondence was supposed to be maintained for years according to the city's own policies. *Id.* The RTKL, however, currently offers no relief for violations of an agency's record retention policy.

In contrast, if the records are deleted after the agency receives a request for records, courts are becoming far less forgiving. In a recent case in the Court of Common Pleas, the City of Scranton failed to preserve the records subject to a RTKL request. The Court found that the destruction was not intentional, but still sanctioned the agency for not ensuring the record was properly

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provided helpful tips and pointers on making good impressions on partners, managing a stressful caseload, and interacting positively with others.

Finally, the YLD was awarded the Comprehensive Award for the consistently excellent programming and service events that our members have dedicated their time and resources to put on year after year. One part of the YLD's submission for the Comprehensive Award was a project which had piloted in 2013, but was re-launched with new curriculum in 2018-2019: the Diverse Law Student Initiative. The Diverse Law Student Initiative seeks to engage young diverse leaders while they are in law school, expose them to the ACBA, and provide them with networking opportunities. The rigorous program requires students to earn points for their participation in various committee and section meetings, as well as participation in various young lawyer's division events. The goal of the program is for young diverse leaders to find jobs in Allegheny County and remain engaged with the ACBA.

It was a great honor to attend the 2019 ABA Annual Meeting with immediate past-Chair Lacee Ecker to receive these awards. While we certainly do not seek recognition in serving each other and our communities, I am proud to say that our efforts have again received national commendation. It is a testament to commitment and enthusiasm of our members that we are able to hold such wonderful events year-in and year-out. ■

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preserved. *Lockwood v. City of Scranton,* AP-2019-0279 available at *https://www.openrecords.pa.gov/Appeals/FinalDetRecord.cfm?docket=2019-0279* (containing the OOR's opinion and copies of the Court of Common Pleas pleadings and decisions).

If the public is interested in records that they believe may be deleted, they could continually request the most recent version of those records. If the agency deletes the records with an active request, it may be subject to sanctions.

Another way to remedy this situation, would be for the RTKL to be amended to allow requesters to contest whether an agency has complied with its own record retention policy. Currently, the RTKL only asks whether the record exists at the time of the request. If the record has been deleted before the request, the current law allows no remedy. Instead, the law should be amended to allow requesters to challenge the denial on the grounds that the record was deleted in violation of an agency's record retention policy. The agency should also be subject to sanctions for frustrating public access by violating its own policies.

Without such an amendment to the law, another approach could be to sue to compel compliance with the agency's record retention policy in a mandamus action. One such attempt, however, was not successful. *PG Pub. Co. v. Governor's Office of Admin.,* 120 A.3d 456, 458 (Pa. Cmwlth. Ct. 2015), *aff'd,* 135 A.3d 578 (Pa. 2016). It is unclear if a future challenge with more clear violations of the law would be successful.

Some other approaches to remedy this problem have included new laws related to record retention. California passed a requirement to preserve emails after learning that some agencies were routinely deleting emails. *https://www.courthousenews.com/email-transparency-bill-clears-california-state-assembly/*

Pennsylvania record retention policies vary widely by agency, so broader reform and modernization of record retention policies could also help further preserve records for future release. This is important because many of the record retention policies in Pennsylvania are subject to change by the agency itself. For instance, in *PG Pub. Co. v. Governor's Office of Admin* the agency argued that the agency could create a record retention policy that failed to preserve any records. *See* Frank and Gordon, Trump Wages War Against the Media While Pennsylvania State Agencies Wage a Behind the Scenes Cold War, 27 Widener Commonwealth L. Rev. 7, 26, fn. 116 (2018). A general record retention law would protect records if an agency decided to revise or abolish its current record retention policy.

The RTKL has been a great expansion of public access to government records. Destruction of records, however, remains one of the areas where public access can still be frustrated. With some minor changes, the law's laudable goals could be achieved on greater scale by ensuring that public records are not destroyed. ■

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AI Report:
Algorithm-Driven Machines are Here for Our Jobs

Here's a brief overview of what you need to know about the current status and implementation of AI Systems in the legal field.

By Ashley M. London and Dr. James Schreiber

The Artificial Intelligence systems we feared were coming from our jobs are already here.

Most of us are interacting with AI systems on a daily basis, so much so that revenue generated from the direct and indirect application of AI system software is estimated to grow to as much as $36.8 billion by 2025. As a subset, the global legal analytics market alone is expected to reach a staggering value of $1.8 billion by 2022.

For a profession that operates in a system based on the principle of *stare decisis et non quieta movere,* there exists a strong bias supporting the development and application of so-called machine learning in law and the legal field. A 2018 ABA study showed attorneys reporting saving time and increasing efficiency as the biggest advantage to the adoption of AI systems in law firms. Victoria Hudgins, *ABA Survey: Only 10 Percent of Law Firms are Currently Using AI,* LAW.COM (Jan. 11, 2019), *https://www.law.com/legaltechnews/2019/01/11/aba-survey-only-10-percent-of-law-firms-are-currently-using-ai/.*

Promoters of the disruption of technology in the legal field say in the short run that AI systems will lead to "greater legal transparency, more efficient dispute resolutions, improved access to justice… and lawyers will be empowered to work more efficiently." Benjamin Alarie et al., *How Artificial Intelligence Will Affect the Practice of Law,* SSRN (Nov. 29, 2017), *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3066816.* For example, the average human attorney can review a contract in 92 minutes, or approximately 15 billable increments of six (6) minutes each, while an AI system can perform the task in 26 seconds. That's not even one increment on an average billable-hour clock.

In 2017, the McKinsey Global Institute found that while nearly half of all law job tasks could be automated by current technology, only 5% of all jobs could be entirely automated. *See* James Manyika et al., Harnessing Automation for a Future that Works, McKinsey & Co. (Jan. 2017), *https://www.mckinsey.com/featured-insights/digital-disruption/harnessing-automation-for-a-future-that-works.* Applying its current definition of technology – widely available or being tested in a lab – McKinsey estimates that 23% of a lawyer's job can be automated. Studying the automation threat to the work being done by lawyers at big law firms, two professors at the University of North Carolina School of Law found that putting all new legal technology in place immediately would result in a 13% decline in lawyers' hours.

The idea that machines can become as powerful as an expensively trained advocate in the law is irresistibly seductive. For example, an AI system dubbed Lex Machina (Latin for "law machine") acquired by Lexis Nexis in 2015, is already on its 13th expansion of its legal analytics platform that began with a focus on Intellectual Property (IP) cases. The product mines litigation data to provide attorneys with information such as the average duration of a legal

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matter, damage awards, resolution, opposing counsel litigation history, and historic rulings from judges on motions and other decisions.

If profit is one of the biggest motives spurring law to look for ways to embrace AI systems, there are other identifiable factors at play in the sharp rise of legal technology applications including: a reduction in entry-level law jobs across the country; a recent slump in law school admissions figures; the expense of civil litigation; and, the need to try to close the ever-growing justice gap for low-income families in the United States.

Lawsuits are expensive, and so are the large white-collar law firms that appear to be the fastest adopters of AI system technology. The average civil lawsuit in America today costs between $45,000 and $1.1 million from complaint to verdict. It is little wonder then that according to the American Bar Association's (ABA) 2018 Legal Technology Survey Report found that AI system usage is greatest at law firms with over 100 attorneys. Hudgins, *supra.*

It is only recently that the legal profession is appearing to enter a recovery phase after a fairly serious depression - where legal jobs and people going to law school were in a decline- until a slight turn-around began in 2018. During the years of drought, legal services providers began developing technology that filled the void, including LegalZoom, LLC, which was founded in 2014, and is now valued at $2 billion. Since 2012, legal technology start-ups have raised $757 million in capital to develop new AI systems technology. That's a rapid power-up, one that even an improving legal job market cannot compete against. The Bureau of Labor Statistics in its most recent publication of the Occupational Outlook Handbook shows that the growth in law jobs is holding steady at 8% for the period of 2016-2026, which is as fast as average. For the first time in years law schools saw their numbers of applicants increase in 2018, at a rate of 11% higher than the admissions cycle for 2017-2018. So, while legal jobs and workforce numbers appear to be slowly creeping up, legal technology systems have already sprinted far ahead.

While many of us may feel threatened by the rapid adoption of AI systems, in many cases justifiably so, there is at least one potential upside in that this technology is enabling lawyers to close the justice gap. For example, the Legal Services Corporation (LSC), provides civil legal services to clients at or under the 125% poverty guideline, or those household of four that survive on $30,750 per year. In 2018, President Trump's cabinet proposed to eliminate funding completely for the LSC programming, which is now only funded by state and federal government sources to the tune of $480 million for 2018, which does not even closely track with inflation ($936 million, if tracked with inflation since 1980). So, it is no surprise then that the organizations providing civil legal services to economically vulnerable populations are turning toward technological advances to stretch funding dollars.

In 2015, the LSC reported employing more computer-powered services such as: created automated self-help forms for clients with legal needs of a limited scope; creating a state-specific legal portal as an automated triage process to guide clients to the specific support and services they need; and, a greater use of mobile technologies to reach clients more effectively. Duquesne University School of Law Professor Katherine Norton is working with Crivella Technologies Ltd. in Pittsburgh, Pennsylvania, to develop a program to assist pro se litigants with custody appeals using a decision tree-based algorithm. The project is currently in the application development process, and is being designed to assist litigants in articulating claims and drafting the basic documents necessary to initiate an appeal.

In its attempt to replace attorneys, AI will undoubtedly provide job opportunities for skilled advocates to test their mettle forging a new set of laws, regulations, and an ethical framework for governance and policing of this new technology.

The full text of this article will appear in the Duquesne Law Review's AI Symposium Edition. Vol. 58. ■

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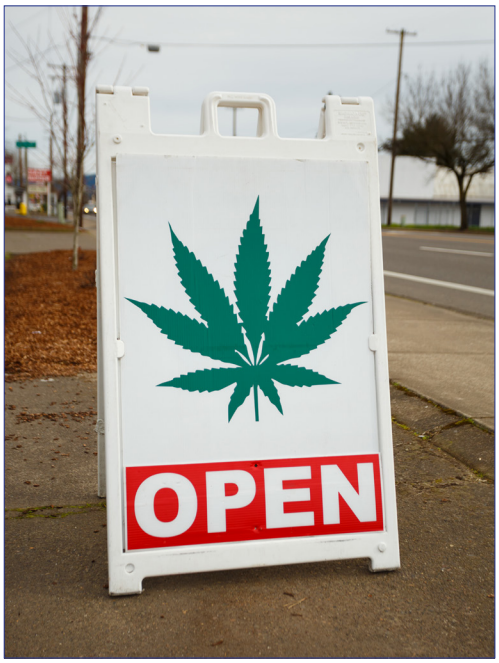
Federal Tax Issues Facing Cannabis Businesses

By Christine Green

Since the legalization of the medical use of cannabis in Pennsylvania in 2016, the legal community within Pennsylvania has seen a sharp increase in the number of clients seeking advice with respect to their cannabis businesses. Given that cannabis use remains fully illegal under federal law, these clients face unique legal challenges including special taxation issues. Unlike most businesses, cannabis businesses are prohibited from taking any federal tax deductions. Without proper planning and sound advice, this prohibition causes cannabis businesses a lot of grief.

Section 280E of the Internal Revenue Code disallows deductions and credits for amounts paid or incurred in carrying on any trade or business that consists of trafficking in Schedule I or Schedule II controlled substances (within the meaning of the Controlled Substances Act) which are prohibited by federal law or the law of any state in which the trade or business is conducted. Even though many states have legalized cannabis (whether for medical use or both medical and recreational use), Section 280E applies to cannabis businesses because cannabis is Schedule I controlled substance under federal law.

Congress enacted section 280E in response to a United States Tax Court memorandum decision permitting a taxpayer who was in the business of selling various illegal drugs to claim deductions. *See Edmondson v. Comm'r,* T.C.M. 1981-623 (1981). Many taxpayers have argued that section 280E's prohibition is unfair as applied to cannabis businesses because Congress could not have intended for state-legalized businesses to be subject



to Section 280E. *See, e.g., Alt. Healthcare Advocates v. Comm'r,* 151 T.C. No. 13, 135 (2018). To date, no taxpayer has been successful in making such arguments. In a recent case, a taxpayer came closer to prevailing than any others, but still lost, on the grounds that section 280E is unconstitutional as an excessive penalty provision, with some of the judges agreeing with the taxpayer in the concurring and dissenting opinions. *N. California Small Bus. Assistants Inc., v. Comm'r,* 153 T.C. No. 4, 44, 51 (2019) (Gustafson, J., concurring in part dissenting in part) (Copeland, J., concurring in part dissenting in part).

Aside from arguing that section 280E is unfair and unconstitutional, taxpayers have asserted that they have separate lines of business in addition to selling cannabis and that the separate business does not constitute the "trafficking" of cannabis. So far, the case law has been harsh toward taxpayers in this area with the IRS generally prevailing whether a business is a grower, processor, or dispensary. The seminal case in making this argument is *Californians Helping to Alleviate Medical Problems, Inc. v. Comm'r,* 128 T.C. 173 (2002) (*"CHAMP"*) where the taxpayer operated a community center for members with life-threatening diseases and also provided medical cannabis, or marijuana, to its members. The IRS took the position that the taxpayer operated a single business, which consisted of selling medical marijuana, subject to section 280E. However, the court agreed with the taxpayer that there were two businesses, the provision of caregiving services and a secondary business of supplying medical marijuana to members. The caregiving services provided were extensive: weekly support meetings, guest lectures, lunches for low-income members, and counseling. Ultimately, the taxpayer was permitted to allocate its business expenses among the two businesses. Section 280E only applied with respect to supplying medical marijuana. *Id.* at 183.

Other taxpayers have tried making similar arguments as the taxpayer in *CHAMP* but have normally failed. For example, in *Canna Care, Inc. v. Commissioner,* T.C. Memo 2015-206 (2015), a dispensary that also sold T-shirts, books, and other items was treated as a single business engaged in the sale of marijuana. *Id.* at *12. In *Patients Mutual Assistance Collective Corp. v. Commissioner,* 151 T.C. 176 (2018), one of the largest marijuana dispensaries in the United States argued that it had separate lines of business with only one being the sale of marijuana. The dispensary also sold branded clothing,

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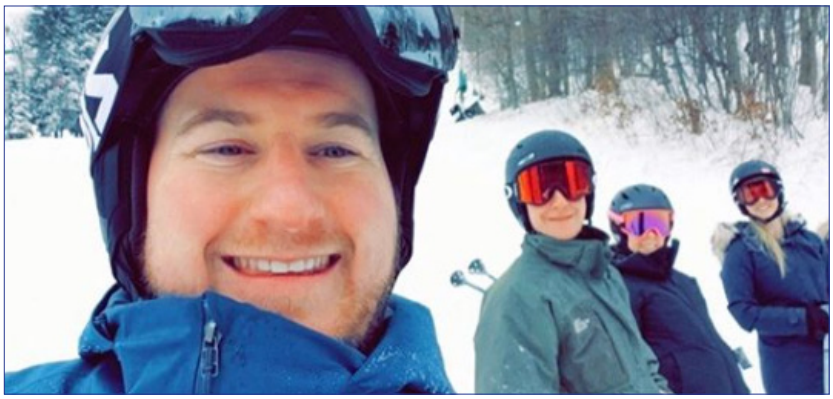
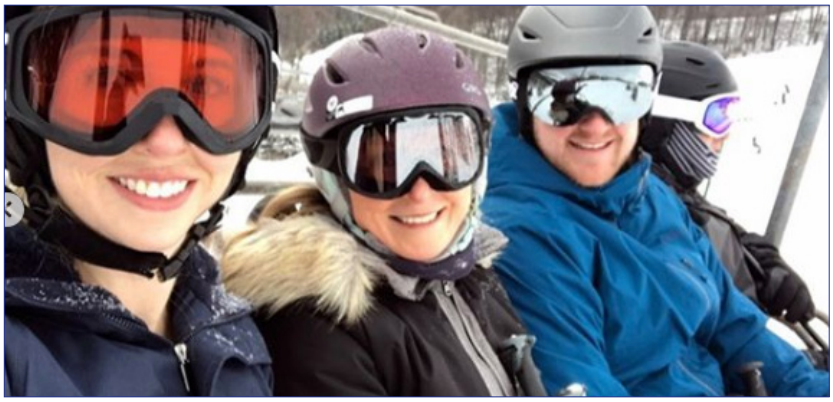
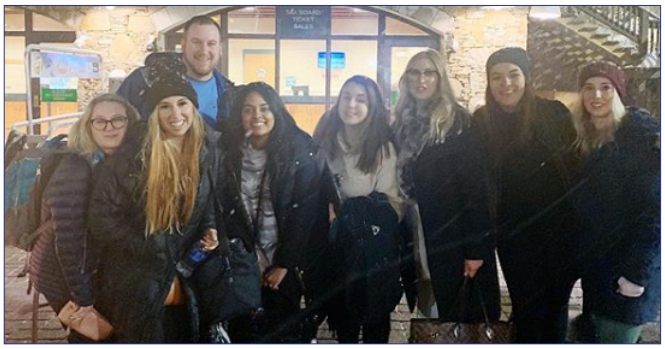
February 2020







Federal Tax Issues Facing Cannabis Businesses

Continued from page 9

hemp bags, and various marijuana paraphernalia. However, the sale of non-marijuana items accounted for only 0.5% of the dispensary's revenue and the items occupied only 25% of the sales floor. In addition, to access the sales floor, a customer had to present credentials showing that they were permitted to purchase marijuana. The court determined that the sale of the non-marijuana items was clearly incidental to the dispensary's sale of marijuana and not a separate trade or business. *Id.* at 113.

Although section 280E prohibits businesses that sell cannabis from claiming deductions, section 280E does not prevent such businesses from taking account of cost of goods sold ("COGS"). Taxpayers owe federal income tax on their gross income, not their gross receipts. Gross income generally means gross receipts less COGS. The law, though, does not permit converting otherwise disallowed deductions under section 280E into allowable COGS. Rather, cannabis businesses should carefully determine their COGS to make sure costs appropriately classified as COGS are not mistakenly treated as expenses for which deductions are impermissible.

Hiring skilled accountants familiar with section 280E and able to assist with tracking and appropriately categorizing costs is critical. There are different rules for determining COGS with respect to taxpayers treated as resellers versus producers. *See generally* I.R.C. § 471. The general consensus among practitioners is that for cannabis dispensaries, the amount of COGS is limited essentially to the price paid for the cannabis. For growers or processors, however, a wider range of costs (sometimes including indirect costs) can be included in COGS. ■

Christine Green is an Associate with Clark Hill PLC, in its Corporate practice group. Her practice focuses on federal tax matters. She also teaches corporate income tax as an adjunct faculty member at Duquesne University School of Law. She can be contacted at cgreen@clarkhill.com.

Recent Guidance from the IRS Regarding Cryptocurrency

By Jamie Drennen

On October 9th, 2019, the IRS released Revenue Ruling 2019-24, the agency's first official cryptocurrency guidance since 2014.

Cryptocurrency is a form of virtual cash that sends payment from one individual to another, without the use of ordinary financial institutions. *Blockchain Investment Trends in Review,* CB INSIGHTS, *https://www.cbinsights.com/research/report/blockchain-trends-opportunities* (last visited Oct. 31, 2019). Unlike traditional forms of payment, cryptocurrency is based on "blockchain" technology which records each and every transaction. *Cryptocurrency,* INVESTOPEDIA, *https://www.investopedia.com/terms/c/cryptocurrency.asp* (last visited Oct. 31, 2019). Blockchain is often considered to be safer than traditional means of money transfer because it documents and verifies the specific currency used. *Id.*

Cryptocurrency can be used as cash to buy and sell items online. However, cryptocurrency is in finite supply, so it is often used as a form of investment property rather than as the virtual cash it was intended to be. Matt O'Brien, *Bitcoin isn't the future of money – it's either a Ponzi scheme or a pyramid scheme,* WASHINGTON POST (Jun. 9, 2015), *https://www.washingtonpost.com/news/wonk/wp/2015/06/08/bitcoin-isnt-the-future-of-money-its-either-a-ponzi-scheme-or-a-pyramid-scheme/?utm_term=.d3c5de78684c.* To date, cryptocurrency has been largely unregulated because it is so unique, complex and difficult to define.

The most recent piece of cryptocurrency guidance from the IRS, Revenue Ruling 2019-24, deals specifically with a unique cryptocurrency

occurrence called a "hard fork." This occurs when a particular cryptocurrency "undergoes a protocol change resulting in a permanent diversion from the legacy or existing distributed ledger." Rev. Rul. 2019-24. In other words, the cryptocurrency has broken from the public ledger which once tracked its every move. The cryptocurrency's future transactions are now tracked on a new ledger. Rev. Rul. 2019-24.

In some instances when a "hard fork" occurs, those broken-off units of cryptocurrency are "air-dropped," or delivered, to users' online cryptocurrency "wallets." Rev. Rul. 2019-24. However, in some instances, such as when the "wallet" is managed by a cryptocurrency exchange that does not yet recognize the new cryptocurrency, a delay occurs. Rev. Rul. 2019-24. An everyday example of this delay is when funds are "pending" in a bank account after deposit. The funds are ultimately ours, but we don't have the ability to access the funds or move them around yet. Once the cryptocurrency exchange recognizes the new units of cryptocurrency, they will be accessible to the user. Rev. Rul. 2019-24. According to Rev. Rul. 2019-24, it is at this point that the taxpayer "has receipt" of the cryptocurrency, and, more importantly, realizes income.

Before Revenue Ruling 2019-24, the IRS mailed off thousands of warning letters to cryptocurrency holders in July of 2019. Laura Saunders and Britton O'Daly, *IRS Sending Warning Letters to More Than 10,000 Cryptocurrency Holders,* THE WALL STREET JOURNAL (July 26, 2019), *https://www.wsj.com/articles/irs-sending-warning-letters-to-more-than-10-000-cryptocurrency-holders-11564159523.* The effect of these letters, in popular opinion, was that the IRS intended to treat cryptocurrency as an investment rather than cash. This would mean that taxpayers would realize their "accession to wealth" when the cryptocurrency was sold, and the calculation of value would be determined by the taxpayer's basis in the cryptocurrency as well as its price when sold. *Commissioner v. Glenshaw Glass Co.,* 348 U.S. 426, 431 (1955).

Looking to the few pieces of guidance released by the IRS thus far, it would appear that appropriate tax treatment of cryptocurrency may vary depending on the circumstances in which it is used or acquired. Due to cryptocurrency's multi-faceted nature, further guidance from the IRS will be necessary for taxpayers to fully understand how to properly report cryptocurrency transactions.

If you practice tax law, be sure to stay current with the ever-evolving world of cryptocurrency to best counsel those of your clients who choose to dabble in this enigmatic currency. ■

Jamie Drennen is a Tax Analyst at Schneider Downs & Co., Inc. Her practice focuses on Estates and Trusts. She can be contacted at jdrennen@schneiderdowns.com.

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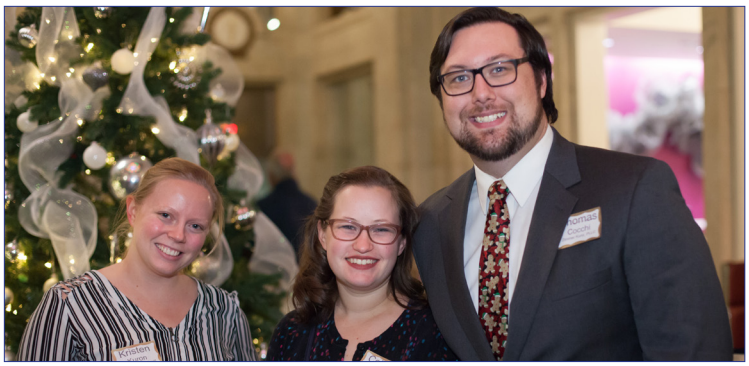
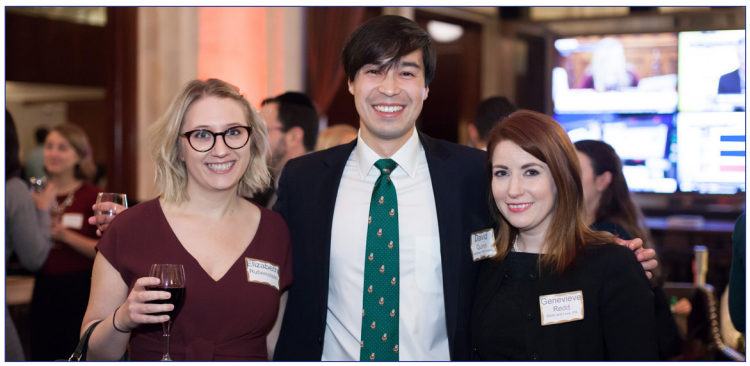
YLD HOLIDAY PARTY

December 2019



YLD CHILDREN'S GIFT DRIVE AND HOLIDAY PARTY

December 2019