Before and After Disaster Strikes

Are you prepared for the next unexpected catastrophe?

BY JAMES D. KRICKETT

Regardless of how it happens, disasters have the ability to shut down for good any professional practice or business. A whopping 74% of organizations have experienced workplace data losses, and while 32% recover in a matter of a few days (usually at a hefty cost), 16% never recover.

Obviously, to be adequately prepared, disaster recovery planning should be done in advance so that when disaster strikes, the podiatry practice does not have to close its doors, temporarily or permanently. The immediate problem, however, is how to cope with the Coronavirus pandemic.

Coping With Disaster

Since no podiatry practice is immune from the effects of disaster, what happens after a disaster occurs may not be covered by the practice's emergency response plan—if one exists. What can a podiatrist or the practice's principals do to help their practice recover from this or any unexpected event?

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There are a number of logical and necessary steps that can be taken to help recover, including:

• Before and during the event, steps should be taken to ensure the physical safety of workers in the workplace.

• Obviously, if the practice's office has been forced to close, local authorities should be contacted for a timeline for a safe return.

• Any damaged equipment, materials, or items should be kept until the insurance adjustor has visited and documented the losses. If it is not possible to keep the items due to health or safety concerns, they should be photographed or videotaped prior to disposal.

• Look for your area to be declared a national disaster area either by the federal government or state officials, if it has not already been so labeled.

• Talk with the practice's creditors immediately.

• Current cash on hand should be reviewed along with emergency savings to begin the task of prioritizing all bills. Paying employees, insurance premiums, rent, and/or mortgage payments should be a priority.

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• If employee layoffs are necessary during the recovery or rebuilding process, certain steps must be taken with regard to notification and preparation to handle unemployment claims. Many creditors will work with the troubled practice or business to establish forbearance or some other type of reduced payment arrangement.

Financing the Recovery

Because even the very best disaster recovery plan will fail without the right level of financing, the most appropriate finance partners must be quickly identified. These partners can include a mix of existing lenders, the practice's suppliers, its creditors, and even personal funding.

Using personal or family funds to finance the recovery of a practice or business is called "Boot Strapping." Boot strapping can involve personal investment by the principals, partners, their family and friends, and/or shareholders. Unfortunately, our tax laws make self-funding a touchy and complex option.

Whenever a loan is made between related entities, or when a shareholder makes a loan to his or her incorporated practice or business, our tax laws require a fair-market rate of interest be included. If not, the IRS will step in and make adjustments to the below-market (interest) rate transaction in order to properly reflect "imputed" interest. How large the tax impact depends on the effect of added interest income to the lender and the bite of an offsetting interest expense deduction felt by the borrower.

Federal Disaster Funding

And, don't forget the role government funding can play in the recovery. The Small Business Administration (SBA) has, for instance, long provided financial help for those suffering from disasters, natural and man-made. Through the SBA's Office of Disaster Assistance, practices and businesses can apply for low-rate, long-term loans for physical damage caused by a declared disaster. Currently, eligible small professional practices and businesses may borrow up to $2 million for up to 30 years to repair and replace real property, machinery, and inventory at a 4% interest rate.

The SBA also offers an economic injury disaster loan that provides working capital up to $2 million. It can be used for operating expenses the practice could have paid if the disaster hadn't occurred, even if there isn't any physical damage. The current rate for a loan of up to 30 years is 4%.

The Rise of Really Alternative Financing

Applying for a loan at any time can be a daunting and unrewarding task especially for the principals or partners in a podiatry practice that has suffered any type of disaster loss. But fortunately, modern technology is providing an alternative. Crowdfunding allows those seeking money to post details of their need, plans, or project online and, hopefully, donations come flowing in.

Today, by advertising on websites, called "funding portals," those needing funds can reach out directly to investors. The Securities and Exchange Commission (SEC) recently approved new rules that allow professional practices, businesses, even start-ups, to more easily raise money from investors using crowdfunding sites.

The 2017 JOBS Act crowdfunding provision allows professional practices and businesses to use online resources to solicit investments from individuals without having to register their shares with the SEC, as long they raise less than $1 million a year. The amount that individuals can invest is restricted according to income.

Negotiating Recovery

When money is owed, the majority of banks and vendors would rather be repaid over time than take over the practice or business, or its assets, or force it into bankruptcy… provided, of course, they can be shown the benefit of a recovered operation.

That can mean providing an operational and financial recovery plan that exhibits the practice's viability and outlining a repayment plan and timetable. Protecting the lender's collateral is a priority and should be demonstrated in the recovery plan.

A Tax Loss

Our tax laws can help reduce the bite of many disaster losses, not merely those resulting from the pandemic. Although our tax rules are pretty straightforward in denying any tax write-off for lost profits, many other types of losses encountered by the average professional practice can be eased or lessened simply by taking advantage of several tax breaks.

Under our current tax rules, any loss sustained during the taxable year, and not covered or "made good" by insurance, can be claimed as a tax deduction. Would a refund of taxes paid by the practice in past, more profitable years help ease the pain of lingering losses this year?

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To help cushion losses suffered by professional practices and others from disasters, the tax laws contain a special rule for losses that the President of the United States has determined warrants assistance by the federal government under the Disaster Relief and Emergency Assistance Act. Podiatrists have the option of deciding whether their or their practice's loss would be most beneficial if used to offset the current year's tax bill or better employed to reduce the previous year's tax bill, generating a refund of previously paid taxes.

Another type of loss, Net Operating Losses (NOLs), are typically subject to a taxable income limitation and, until now, couldn't be carried back to reduce income in earlier tax years. The

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CARES Act, however, allows professional practices, businesses, and even some individuals to carry back NOLs from 2018, 2019 and 2020 for five years and temporarily remove the TCJA rule limiting losses to 80% of taxable income.

The new rules also modify loss limits for pass-through entities such as partnerships or S corporations and sole proprietors, which means that all practice losses can now be used to create badly-needed cash from refunds of taxes paid in earlier, hopefully, more profitable years.

One of the best ways to protect assets in the event of another disaster is to protect the data in your system.

Paybacks Can Be Expensive or Not

The forgiveness of many federal loans, loans that can be turned into non-repayable grants and debts forgiven by creditors, banks, other lenders, and even landlords, is ordinarily a taxable transaction.

Usually, when a debt is cancelled, forgiven, or discharged for less than the amount owed, the result is Cancellation of Debt (COD) income. Similar consequences occur when property secured by debt is taken in satisfaction of that debt and where the property is treated as having been sold.

However, as part of the Small Business Administration's (SBA's) debt relief efforts, SBA will pay the principal, interest, and fees of current 7(a), 504 and microloans issued prior to September 27, 2020. Best of all, the 6-month payment relief is not a deferment, but actual debt forgiveness.

What's more, thanks to the CARES Act, any loan forgiveness under the government's $350 billion small loan programs can be excluded from income for tax purposes. For both measures, a three-year look-back ensures that a professional practice or business cannot be broken up to come in under the $25 million threshold.

Disaster can strike at any time. Regardless of how it happens, natural disasters, mishaps, viruses, and other events all have the ability to shut down a practice or business for good if it is not prepared.

Planning for New Disasters

While the impact of the COVID-19 pandemic on the practice or business was severe, it is the property damage caused by a flood, a cyber/virus attack, physical damage from fire, flood, explosion or other natural disasters, damaged systems, equipment, power outages, workplace violence, hazardous spills, or the result of terrorism, where planning can help mitigate the damage. How the podiatry practice responds within the first few hours of the crisis can also make or break the operation.

Disaster planning can ensure the practice will be there for patients regardless of the situation, immediately rather than several weeks too late. One of the best ways to protect assets in the event of another disaster is to protect the data in your system. With cloud technology patient information can be accessed from anywhere.

When dealing with a crisis, many podiatrists overlook the critical continuity component. The way in which the practice communicates both during and after a disaster will directly affect how well that recovery goes. The plan should include contact information for all employees, banks, and insurance and leasing information that might be vital for operating the practice.

Communicating with patients can occur via multiple communication channels including:

• Social Media: Provide not only health tips on preparedness beforehand, but reassurance that the practice is available for assistance, and the many ways in which it can be contacted.

• Phone/email/text messages. Actively reaching out to patients who might be in distress and connecting with them demonstrates both compassion and concern. And, remember, during many types of events, patients may have to rely on mobile devices. A website accessible via a mobile application can keep the lines of communication open.

Protecting the assets of the practice's patients is the

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reason many podiatry practices exist. When the unexpected happens, patients may depend on the practice to be there safeguarding not only its own assets against any threats but also those of the patients.

Planning Disaster Strategies

Disasters can strike at any time, often with little or no warning. Yet, a recent study by the Travelers Insurance Group found that 48% of small businesses are operating without any type of continuity plan, although 95% indicated they felt prepared.

Although it is not possible to create a plan for every threat the podiatry practice could potentially face, the disaster plan could begin by addressing the highest risk likely to impact the practice. Obviously, developing a disaster preparedness plan is a critical first step as taking proactive steps before disaster strikes can help lessen the financial ramifications and help the practice recover faster.

Of course, even after taking precautions and with a comprehensive disaster plan, any practice can experience a crisis including thefts, accidents, or natural disasters such as storms or the COVID-19 pandemic. After all, any plan is only as good as the practice's ability to recover from them.

Back-up Plans

A back-up plan or so-called "business continuity plan" is a written document outlining how the practice will respond to a disaster. The coronavirus pandemic illustrated just how important, and controversial, insurance coverage for disaster losses can be. Many practices have insurance in case of a fire or a burst water pipe.

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Few, however, are protected in the event of an earthquake or flood. And who expected to need insurance from the effects of a pandemic?

So-called "business interruption" insurance often requires a special "rider" tacked onto the all-inclusive coverage offered by some insurance companies. Plus, it is currently controversial as evidenced by a number of lawsuits involving failure to pay for business interruptions resulting from the pandemic.

Carefully reading the practice's policy's fine print and understanding the coverage may uncover the need for a rider or a separate policy to cover losses from severe weather or events that aren't included in the existing insurance policy or policies.

Risk Mitigation

It may be too late now, but anticipating future risks, and mitigating them, can greatly ease recovery efforts. If computers play an important role in the practice, an alternate back-up that can be switched to should be included. Backing up all of the operation's vital financial information or keeping copies in another location is also vital.

Help

This is not the time to go it alone. Help from the operation's bank, the Small Business Administration, the local Chamber of Commerce, and other local sources can help with both disaster planning and recovery.

The operation's CPA should be able to help, at least with the numbers. Chances are he or she can also advise on many other aspects of the practice and, most likely, has a list of contacts that can advise on other recovery strategies. **PM**

James D. Krickett is a well-known tax and financial adviser whose columns are syndicated to more than 65 publications each week. His features routinely appear in the pages of leading trade magazines and professional journals.