



# Journal of the CPA Practitioner

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## UPDATE...FROM THE NCCPAP PRESIDENT



ANDREW L. HULT, CPA

This is my first message as your new president. I am humbled and challenged to be stepping into the very big shoes worn by NCCPAP’s past leaders. I promise to do my best for you, as they have done. But, as with my predecessors, that best will only be worthy of you if it is founded on your input, your ideas and your guidance. Talk to me so that I can act effectively for you.

In his book, *Good to Great*, Jim Collins advances the theory that great companies don’t start with great ideas. They start with great people, and a consensus emerges from their interface. I think that he’s right. And it seems to me that we should change the word “companies” to “associations.” Then we can see that he’s describing NCCPAP.

The proof is in the pudding. For example, on July 26, 2009, the New York State Board of Regents instituted retroactive competency rules that effectively disenfranchised thousands and thousands of CPAs including, I believe, a significant portion of NCCPAP’s New York membership. The disenfranchisement seemed to be unintended, but it also was real.

During the ensuing months, NCCPAP was closely involved in the effort to redress the unintended consequences of Board of Regents’ rule changes. At this juncture, the State Board of Accountancy has proposed changes that are essentially in line with NCCPAP’s suggested remedies, including acceptance of peer review as an alternative to one thousand or more hours of attest work and grandfathering, for a period of time, practitioners who were considered qualified to sign financial statements on July 25, 2009.

As I write this letter, these changes have not yet been accepted by the New York State Board of Education and the Board of Regents. NCCPAP is continuing to monitor, and facilitate as necessary, their progress. Many of us inadvertently had our livelihoods stripped away, and NCCPAP acted decisively and effectively to restore them. In the past months, and not for the first time, NCCPAP achieved greatness on your behalf and mine. And NCCPAP did it because of the selfless efforts of its volunteer Officers, its volunteer Directors, its volunteer Committee Chairs and volunteers from its Membership.

This competency issue does not just benefit New York members. While New York is the first state to institute such rules, it is felt that other states will follow. NCCPAP’s fight for New York should benefit members in others states in the future.

Framed by the foregoing comments, what I have to say next is especially troubling.

Even though NCCPAP provides unique and essential functions, membership has trended downward throughout the past decade. NCCPAP will disappear unless you and I enroll new members. ***Please bring a friend, or a whole lot of friends, to the next NCCPAP national and/or chapter meeting. Invite them to join our association.***

If you and I do not do this effectively starting now, NCCPAP will not be around to fight our future battles. I ask each of us to bring one new CPA per

*(Continued on page 2)*

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To Be Announced

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*Journal of the CPA Practitioner* is published by the National Conference of CPA Practitioners (NCCPAP), a not-for-profit New York association.  
 Editorial: Copy due the 10th of the month preceding publication.  
 Advertising: Camera-ready art due the 12th of the month preceding publication.  
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 Price per issue: \$2.50 ©2009 NCCPAP

quarter, at the minimum, to a chapter or a national meeting. Simply put, my first priority is serving you. I will be able to do this if you share your insights, problems and recommendations. My telephone number is 516-565-1702. Alternatively, you can e-mail me at [alhult@alhcompany.com](mailto:alhult@alhcompany.com) or contact one of the wonderful Officers, Directors and/or Committee Chairs that the Nominating Committee has provided. Don't be a stranger.

My second priority is membership growth. It will be a bootstraps project; we don't have the resources to mount a marketing campaign. Each of us needs to contact friends who will benefit from NCCPAP membership as much as we have.

*Andrew L. Hult, CPA*

**CONGRATULATIONS  
 Officers & Directors 2009-2010**

Elected & Installed at the NCCPAP Annual Meeting

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Three-year term	Harold Ogulnick, CPA
Three-year term	Jay I. Rosenbaum, CPA
Two-year term	David Rothfeld, CPA

To all of our 2008-2009  
 Officers, Committee Chairs and Directors

**NCCPAP Sends  
 A Big "THANK YOU"**

The membership of NCCPAP sends a heartfelt "THANK YOU" to each of our dedicated NCCPAP Officers, Directors and Committee Chairs for all the time and effort you expended on behalf of NCCPAP.

Some of you have moved on, others have moved up and some of you are carrying our torch for yet another year. NCCPAP could not have grown, or continued its mission and programs, without you.

Your attendance at a  
**NATIONAL ISSUES COMMITTEE and/or  
 TAX COMMITTEE MEETING**  
 during NCCPAP quarterly meetings qualifies you  
 for up to 2 CPE Credits per meeting.  
 Call the National Office for details.

## Remote Office Connections Convenient, But Not Without Risks

by Armando D'Accordo, CMIT Solutions of South Nassau

**M**ore people than ever are working from home, on the road, or accessing their office PC from client sites and hotels. According to WorldatWork, occasional telework has risen dramatically in just the past several years. My experience with the financial services industry shows that more and more accountants are using remote access from client sites to transfer files or access information back at the office. Some interesting and somewhat startling facts:

- The number of employee telecommuters in the United States increased 39%, from 12.4 million to 17.2 million, between 2006 and 2008.
- The sum of all teleworkers—employees, contractors and business owners—increased 43% from 2003 to 2008, reaching 33.7 million last year.
- Fewer people are teleworking full time; however, more people are working remotely at least once a month.
- The most common locations for remote work are home (87%), a customer's place of business (41%) and car (37%). Restaurants and libraries are becoming less common locations for telecommuting.

In a previous submission to this newsletter I wrote about some parameters for setting up a remote office. In this article I want to focus on a specific type of threat that can put your business at risk during a remote access session. The threat can do damage even if you have followed all the proper guidelines, such as setting up a VPN, creating a secure sharepoint portal, or an encrypted connection like Logmein. In all of these cases you still need to be aware of the security threat posed by keyloggers.

A keylogger is a piece of software that records every keystroke made on a computer. A hacker who installs a keylogger virus on your computer will be able to see everything you type

on your machine—which comes in handy when they want to steal passwords, credit card numbers, bank account numbers, or sensitive client data. (This is truly a business and compliance nightmare!!)

For years, cyber criminals have been installing keylogger viruses on easy-to-breach, publicly accessed machines, such as those used in libraries. But your worry as a remote user probably won't be whatever viruses are crawling all over a publicly used machine; as statistics show, you're almost definitely using your own computer or a company-provided one for business work. So what you have to beware of is a whole new round of viruses that can be downloaded to your own PC.

Remember that Conficker worm that was supposed to strike on April Fool's Day, and ended up exploding about a week later? One of its most devastating payloads was a keylogger virus.

So to protect yourself from keyloggers stealing your passwords, don't ever use public computers for any procedure that requires a login—that means everything from checking email to checking a bank balance. And before using your own computer, or when using a client computer to access your office, make sure the antivirus and antispayware definitions are up to date and that full system scans are run on a regular basis. (Many people halt system scans or just stop running them altogether because they take up so much processing power. The solution to this issue is to run them at night. They are absolutely essential.) Remember that the mere presence of Anti Virus and Anti Spyware software does not guarantee that a PC is clean. The software and the PC require regular and automated updates and maintenance.

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September 29, 2009

Dear NCCPAP Member:

Your right to practice may be at risk. Here's, why, and what NCCPAP has done to protect your right to practice your chosen profession in New York State:

### What happened?

A new Accounting Reform Law was signed by Governor Patterson on January 27, 2009, which became effective on July 26, 2009. The law made significant changes to the professional practice law in New York State.

The New York State Board of Regents adopted regulations in accordance with the Accountancy Reform Act by amending Paragraph 13 of Section 29.10 of the Rules of the Board of Regents effective July 26, 2009.

**The new regulations offer a new definition as to who is "competent" to perform the attest function in New York State.** NCCPAP believes that it was not the intent of the new regulations to adversely affect current licensees, but that is what has happened. As a result, your NCCPAP leaders have been intimately involved in having the regulations rewritten.

These new competency requirements are:

- During the five year period prior to the date a CPA performs the attest function on or after July 26, 2009 a CPA must be able to demonstrate that he or she has devoted at least 1,000 hours in attest work; **and**
- During the three year period prior to the date a CPA performs the attest function on or after July 26, 2009, a CPA must have earned at least 40 hours of targeted continuing professional education in the area of accounting, auditing or other attest activities.

### What's the problem?

If you are like many NCCPAP members, you have a number of important clients. You provide attest, tax, and other services for them. If you do not meet the new, retroactive competency requirements at the time you perform the attest function, you have to tell these clients that you no longer are competent to report on their financial statements. One can imagine that this will not only force you to forego the attest work; it also might put you at risk of losing all of the tax and other services that you perform for that client.

## LETTER FROM NCCPAP TO ALL MEMBERS

### What has NCCPAP done in response?

A special subcommittee of the Issues Committee, led by Bob Goldfarb, formulated alternative proposals to redress the adverse impact of the law on all practitioners while accomplishing the ultimate goal of protecting the public. Among these alternatives is the suggestion that licensed practitioners be "grandfathered" for a period of time to allow the CPA to bring himself or herself into compliance with the new standards.

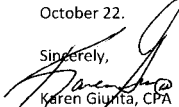
Additionally, on Wednesday, September 16 (one day after the September 15 tax deadlines and with sales tax return filings looming), NCCPAP leaders including Karen Giunta, Donald Ingram, and Bruce Berkowitz attended a New York State Board of Accountancy meeting in Albany. Donald spoke. He stressed the fact that the new rules, as they now stand, adversely affect the practices of thousands and thousands of CPAs.

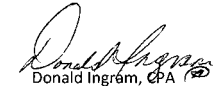
In addition to our attendance at this meeting, leadership of NCCPAP has been actively engaged during the last several months in ongoing conversations with state officials. We are fighting on your behalf to make sure that they understand the ramifications of what has taken place. We have presented them with what we consider thoughtful and appropriate alternative approaches to achieving their goals while protecting the livelihood of all licensed practicing CPAs.

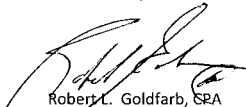
Please note that this issue has not yet been resolved. NCCPAP's involvement will continue, as we fight for the rights of all practitioners whose ability to provide attest services to their client has been put in jeopardy. As we continue our fight, we will be sending you updates as developments occur. In the weeks to come we will be speaking to members of the accounting media to make sure that everyone in the field understands what has been done, and why it must be challenged. This has happened in New York State; it could as easily occur in others that follow New York's lead in establishing competency standards.

As you know NCCPAP was founded to provide the practicing CPA with the ability to be represented and heard when necessary. This is clearly one of those times. NCCPAP has faced and successfully fought many similar challenges in the past, including the XYZ and Cognitor misadventures. We will continue to do so now and in the future on your behalf.

If you have any questions about these new regulations, and/or the status of proposed changes to them, please call one of us. You are also invited to join us for an update at the next National Issues Committee meeting in Pearl River, New York at 2:00 p.m. on October 22.

Sincerely,  
  
Karen Giunta, CPA  
President, NCCPAP National

  
Donald Ingram, CPA  
President, NCCPAP Nassau/Suffolk

  
Robert L. Goldfarb, CPA  
Chairman, Issues Committee

NCCPAP



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August 21, 2009

Hon. Douglas Shulman, Commissioner  
Internal Revenue Service  
1111 Constitutional Avenue, N.W.  
Washington, DC 20224

RE: Internal Revenue Service Public Forum on Tax Return Preparer Review

Dear Commissioner Shulman:

On behalf of the National Conference of CPA Practitioners (NCCPAP) I am writing to inform you of our position and concerns regarding the registration and/or licensure of tax return preparers. We appreciate the opportunity to inform you of our thoughts and concerns regarding the public forum on tax return preparers. NCCPAP is a national organization comprised of only practicing Certified Public Accountants. Our membership consists primarily of CPA *firms* rather than individual Certified Public Accountants. As the nation's professional organization comprised solely of practicing Certified Public Accountants, most of which prepare tax returns for clients every single day of the year, one of our primary goals is to make the tax system fairer and easier to administer. You will recall that our Nassau/Suffolk (New York) Chapter produces the Long Island Tax Practitioner Symposium of which the Internal Revenue Service is a co-sponsor.

**Registration of Tax Preparers**

NCCPAP supports the development of a single database of all **paid** tax return preparers. We believe that this database should also be posted on the IRS website for the public to view. The database should be searchable, as well.

We also endorse the **registration** of all paid tax return preparers. The registration of the tax return preparers should include: identification of the individual preparer, the identification of the individual's firm, if any, and should grant the IRS the right to suspend a preparer who does not comply with the CPE requirement (such requirement is discussed later). Additionally, all paid preparers should be required to confirm to the IRS that they are substantially in compliance with their own federal income tax filing obligations. This affirmation should include all owners, members and shareholders of the firm in which the individual practices as well as for their business entity.

In order to make this process easier for the IRS and easier for the tax practitioner, we believe that the IRS should utilize the Practitioner Identification Number (PTIN)

**LETTER FROM NCCPAP  
TO THE  
COMMISSIONER  
OF THE IRS**

Please note that we further believe that taxpayers who do not engage a registered tax return preparer should not be eligible for penalty abatement, except in situations where there is clearly a reasonable cause for the abatement of the assessed penalty(ies). NCCPAP recognizes that the IRS would have to engage in a significant public relations effort to enlighten the public as to who are registered tax return preparers and how to find out who is a registered tax return preparer.

**Continuing Professional Education**

Whereas NCCPAP **does not** support the idea of licensure by the IRS, we do support the requirement for continuing education for all registered tax return preparers to ensure competence with respect to basic tax knowledge. We believe that all paid tax return preparers should have a minimum of 24 hours of CPE training/updating annually **for all tax return preparers**. The courses must meet the standards set by NASBA and/or the IRS.

**Office of Professional Responsibilities**

As we indicated above, NCCPAP does not believe that licensure of tax return preparers is either necessary or appropriate. However, we do believe that the IRS's Office of Professional Responsibilities (OPR), which enforces Circular 230 governing the practice of CPAs, attorneys and enrolled agents before the service, should be given with the oversight responsibilities for *all tax return preparers*.

**Deduction of Tax Return Preparation Fees in Arriving At AGI**

NCCPAP believes that the deduction for tax preparation and representation fees should be deductible on Page 1 of Form 1040 as an adjustment to Adjusted Gross Income (AGI), with the requirement that the preparers' ID number (SSN, EIN, PTIN) be listed in order to allow the deduction. This will generate a direct reduction to AGI and taxpayers will not lose the tax benefit. NCCPAP believes that more taxpayers would insist on deducting the fees if they were certain that there would be a tax benefit. Furthermore, unlicensed tax preparers would be more likely to sign returns and report the fee income. The requirement of an ID number of the prior year's preparer would provide a mechanism for the IRS to register and control unlicensed preparers.

Thank you very much for the opportunity to explain our position and concerns in this area. We would be happy to meet with you to discuss our thoughts in more detail if you so wish.

Sincerely,

President

Chair, Issues Committee



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August 27, 2009

Mr. Daniel Dustin
Executive Secretary
State Board for Accountancy
State Education Building - 2nd Floor
Albany, New York 12234

Dear Mr. Dustin:

On behalf of the National Conference of CPA Practitioners (NCCPAP) we are writing to inform of our position and concerns regarding the new rules and regulations covering CPAs authorized to perform the attest function in New York State.

Recently the Board of Regents adopted regulations in accordance with the Accountancy Reform Act that was signed into law earlier this year. We are aware that with the changes in the law, new competency requirements to practice in the attest area have been put in place.

We agree that the public needs to be protected in part by having competent practitioners in the attest area, and that with the new requirements for licensure, a licensee newly licensed may not have the competency in that area.

Our concerns are contained in two provisions of the regulations, both of which are contained in the "competency" definition under paragraph 13.

(ii) Competency: Any licensee that performs the services prescribed in subparagraph (i) of this paragraph shall have the following competencies:

(a) at least 1,000 hours of experience within the last five years in the preparation or review of financial statements or reports on financial statements gained through employment in government, private industry, public practice or an educational institution; and

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competency requirement be met at the time of registration or at the time of licensee renewal.

There are two additional thoughts that we believe should also be considered. First, many of our members are already participants in the peer review program for various reasons. We believe that there is value in the peer review program and it does, in fact, make our members better accountants and auditors.

Another thought that our members proposed is the idea of increasing the CPE requirement as the number of attest engagements decreases. For example, if the CPA has 10 or more attest engagements then the CPE requirement would be 40 credits in the three-year period (as per your current regulations).

NCCPAP would also like clarification as to what is meant under Paragraph 13, subsection (ii)(a) as to what actually constitutes "an hour of experience."

Additionally, we believe that clarification is also needed as to what content must be included in the continuing education seminars in order to qualify as an hour of professional continuing education to meet the standards established under Paragraph 13, subsection (ii)(b).

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FROM NCCPAP TO THE EXECUTIVE SECRETARY OF THE NEW YORK STATE BOARD FOR ACCOUNTANCY

(b) at least 40 hours of continuing education in the area of accounting, auditing or attest during the three years immediately prior to the performance of such services; and ..."

First, we would like to address the provision requiring "1,000 hours of experience within the last five years in the preparation or review of financial statements or reports on financial statements gained..." We endorse this concept and believe that this experience requirement does, in fact, assist in protecting the public interest.

Secondly, whereas NCCPAP also endorses the new continuing professional education requirement we wish to express that this new requirement does pose a significant financial burden on practicing CPAs. Whereas at least 40 hours of professional education during the three years immediately prior to the performance of the attest function is also a provision we can accept, we do believe that the 40 hour requirement should be reduced to 24 hours, especially in light of the need to still meet the general 120-hour requirement.

As you can see, we have some concerns regarding the new competency requirements as stated above. However, our biggest concern is that these regulations, effective for all financial statements signed on or after July 26, 2009, changed the rules and regulations under which CPAs have been performing services for decades. We understand that the rules needed to be changed, and as indicated above, we agree with the concepts. We are concerned, however, that these rules may prevent some practitioners from performing the attest function who were in full compliance with the law prior to July 27, 2009.

We also believe that consideration should be given to modifying the provision requiring the competency requirement be met "during the three years immediately prior to the performance of such services..." We would like this rule modified such that the

2

Additionally, we believe that clarification is also needed as to what content must be included in the continuing education seminars in order to qualify as an hour of professional continuing education to meet the standards established under Paragraph 13, subsection (ii)(b).

On behalf of our New York State members, NCCPAP respectfully requests that the State Board for Public Accountancy, amend the "competency" requirements to grandfather current licensees and permit them to meet the new competency requirements on a prospective basis as discussed above.

Thank you for your time in considering our thoughts and concerns. We appreciate the opportunity to submit this letter for your review. Please do not hesitate to call us if you wish to discuss the contents of this letter in more detail.

Sincerely,

Karep Giunta, CPA
President

President

4

Robert L. Goldfarb, CPA
Chair, Issues Committee

Chair, Issues Committee

20%  
or 1%

e-filed returns have a 1% error rate  
compared to 20% for paper.

You do the math.

[IRS.gov/efile](https://www.irs.gov/efile)



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*How about your client's businesses?*

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## Financial Planning Designed for CPAs

### Death of Diversification Not Likely

by Jesse Mackey, NNA

The performance (or non-performance) of financial markets over the last two years has many financial media sources hailing the “death of diversification” and the end of Modern Portfolio Theory (MPT). In truth, portfolios built using a strategic asset allocation methodology that focuses on the inclusion of various historically low correlation assets have fared little better over the last two years than portfolios built using alternative methods (although they did slightly better). While MPT portfolios generally dropped in value less than their non-MPT counterparts, it is not much consolation to clients that their portfolios only dropped 45% in value rather than 50%. Part of the reason for this “failure” of MPT during the last two years is a much higher degree of short term correlation of historically non-correlated assets. This is not the only time it has happened.

A recent whitepaper from Morningstar Investment Services, Inc., “The Demise of Diversification?”, stated that “In the past, there have been several short-term episodes in which supposedly lowly correlated assets moved far South in tandem, but they usually did not affect as many major asset classes at the same time (as they have recently). In the subsequent periods, those high correlations tend to diminish as different economic factors such as interest rates, inflations, labor-costs, and industry/sector concentrations in different regions/countries affect asset classes’ returns differently. Last year’s high asset correlations echo market behavior in 1974. For both 2008 and 1974, a majority of major asset classes moved down sharply. At that time, as like today, it was reasonable that people questioned whether correlations between those asset classes were going to stay elevated, and that diversification might be dead.”

For anyone around the industry from 1975 to 2007, it is clear that despite pronouncements in 1974 of the “death of diversification,” MPT came back quite strong for the ensuing period as a return to relative normalcy in the financial system occurred. Based on history, it would be fair to expect a similar change following our current financial/economic crisis. If and when the return to financial normalcy occurs (if it hasn’t already), there will still be a persistent Achilles heel to MPT. Nowhere in the library of research on the subject is it claimed that MPT has the capacity to manage financial systemic (or “systematic”) risk, either in theory or in practice. In fact, the theory specifically states it cannot reduce these risks, and that one can only diversify away “non-systematic” risk. MPT has its limitations, but as of yet no one has come up with a statistically proven better alternative. So for the majority of your clients assets, it still makes sense to utilize the MPT methodology, either in its traditionally applied form or otherwise, by itself or in combination with alternative philosophies. Diversification is not dead. Contrarily, the theory is living and rapidly evolving.

*Jesse Mackey is the President of National Network of Accountants Investment Advisors, Inc. (NNAIA), an investment management firm that works exclusively with CPA firms and their clients. He can be reached at [jmackey@nnaplan.com](mailto:jmackey@nnaplan.com).*

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# Benefits Compliance FAQ

by Todd Bellistri, August Benefits, Inc.

**QUESTION: How long can a temporary employee be considered as a “temporary” worker for benefit purposes?**

**ANSWER:** It is permissible to exclude temporary employees from benefits, as a temporary classification is a bona fide employment classification. However, there would be a risk to misclassifying an individual as temporary for an extended period of time if the goal was to exclude them from benefits.

In *Herman v. Time Warner Inc.*, 56 F. Supp. 2d 411, (S.D.N.Y. 1999), the DOL sued Time Warner. The complaint alleged that Time Warner and its subsidiaries misclassified workers as either “temporary employees” or “independent contractors” to prevent them from participating in certain employee benefit plans. It was considered a breach of fiduciary duty under ERISA. While there is no federal definition of a temporary employee, the DOL proved that there was intent to exclude the workers from benefits, which resulted in a settlement being reached for \$5.5 million.

Anytime an employer uses a temporary classification, it should be based upon the employer’s business needs and the work assigned to the individual. The classification should never be used with the sole intention of excluding someone from benefits. Again, there is no specific number of months for which an employee can be classified as temporary. It would be determined on a case-by-case basis dependent upon the specific details of the situation. Typically, employers do not employ temporary employees for more than six months. In some extreme cases, they may be employed for one year.

Additionally, a 401(k) plan cannot exclude temporary, part-time or seasonal employees from the definition of eligible employees. However, the plan may exclude employees who do not satisfy minimum hours and service requirements (in most situations, a maximum of 12 months and 1,000 hours), but this would be outlined in the eligibility section of the plan document.

Best practices indicate that a temporary classification should be defined by the employer and included in the employee handbook. When hiring a temporary employee, the employer should be able to prove that the job is expected to be temporary in nature and is project-based. Also, any benefit plan documents should indicate whether or not that classification is eligible for employee benefits.

**QUESTION: What records should I keep for our retirement plan and how long should I keep them?**

**ANSWER:** Plan documents should never be discarded. This includes basic plan documents, adoption agreements, amendments and summary plan descriptions.

Annual filing reports should be maintained for at least six years. This includes 5500s, supporting materials for contributions, testing results, plan audits, summary annual reports, and distribution records.

Participant records should be retained during the participant’s employment and at least six years after the participant’s termination. This includes enrollment forms, beneficiary forms and distribution forms. Loan records should be maintained at least six years after the loan is paid off.

Whenever possible, use your plan vendor or actuary to maintain these items on your behalf.

Keep the things you need and store them so you can find them easily. Your goal should be to have the ability to locate quickly any plan information requested by a participant, auditor, or Department of Labor (DOL) agent.

*For further information, contact Todd Bellistri at [www.augustbenefits.com](http://www.augustbenefits.com)*

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## “2+2 = Autosum”

### An Article on the Decline of Use of Analytical Thought During the Audit Process

by Alex Buchholz, CPA, MBA

The other day, a colleague and I were talking about how young staff coming into the workplace today do not have a true sense of what it means to “analyze” or “think analytically.” They are too dependent on the computer to do their thinking for them and are not able to use the basic principles of logic in their ability to audit the information as presented by the client. This is a disturbing thought since analytical procedures play an important role in the audit process. This article will attempt to explore the role of analytical procedures and present some examples where analytical procedures helped in discovering significant deficiencies in the internal control of the client and, in one particular instance, caused a restatement to the client’s financial statements. The article will then conclude with a suggestion on how the analytical skills of younger staff can be improved so as to make them valuable assets as auditors.

SAS 96, “Analytical Procedures” states the following:

Analytical procedures are an important part of the audit process and consist of evaluations of financial information made by a study of plausible relationships among both financial and nonfinancial data. Analytical procedures range from simple comparisons to the use of complex models involving many relationships and elements of data. A basic premise underlying the application of analytical procedures is that plausible relationships among data may reasonably be expected to exist and continue in the absence of known conditions to the contrary. Particular conditions that can cause variations in these relationships include, for example, specific unusual transactions or events, accounting changes, business changes, random fluctuations, or misstatements.

Analytical procedures are required to be used in the planning phase of the audit as well as the final review stages. Analytical procedures can also be used during the audit as well as a substantive test. This is merely recommended and not required, as are the other two items mentioned above. However, if used in a proper fashion, this can be an excellent tool to reduce excessive substantive testing. Reduction in time leads to higher realization rates for audit firms, which is not a bad thing to have in this current economic state. In addition, analytical procedures can yield the same conclusion, as does substantive testing of details.

Now that we have a background of what analytical procedures are, let us examine two situations and see how the use of analytical procedures was lacking on the part of the audit staff.

Client A is a non-profit consulting group who provides medical guidance to other hospitals on various medical issues that arise. The setting for this example lies with the young staff, or “juniors,” coming down to audit the bank reconciliations. They obtained the bank statement account and performed the procedures as delineated in the audit program. Everything was referenced properly and the analysis itself was complicit in all

aspects contained in SAS 103, Audit Documentation. While reviewing the analysis the staff referenced an amount for dividend income. The amount itself was approximately \$5,000 for the entire fiscal year under audit. Initially, the amount was deemed immaterial and I moved onto the next workpaper to continue the review. However, after the second analysis and a quick review of the trial balance, it was noticed that there were no investments on the books. Therefore, how could the audit staff trace to an amount of dividends and not question the source? After having a discussion with Client A, it was discovered that investments were donated to the corporation several years back when the insurance company they had been using went public. As part of going public, they donated some shares to Client A. This error was material and did require a restatement to the financials as well as giving the client a new source of cash flows that they were unaware they had prior to this discovery. By simply looking, thinking, and analyzing the above scenario, analytical procedures were able to satisfy and discover a material misstatement. Had the juniors been less “robotic” in their thinking, they may have picked up on this as well.

We turn now to Client B, a non-profit day care center operator located in an economically poor area. They provide services to children such as education, snacks, and cultural enrichment programs. While the City reimburses the client for a majority of funds, there is a certain portion that parents pay, oftentimes in cash, called hereafter “parental fees.” These parental fees are paid to the various centers directly, deposited in the banks by the centers themselves and a record is given to the main accounting office for purposes of recordkeeping and reporting to the City. One of the tests performed for Client B was to see if the dollars/child appeared reasonable. The data was gathered from each of the four day care centers, and the “juniors” placed it on an Excel spreadsheet. They formatted the sheet and made it look presentable and covered all attributes from SAS 103. However, site #3 seemed to show a pattern that did not look consistent with the other three centers. The conclusion written by the juniors was that it was immaterial and somewhat consistent with the prior year. This was immaterial dollarwise—but did it really represent something more? Upon further inquiry of Client B, they did notify the auditors that site #3 did have a situation whereby the program director was misappropriating funds as they were coming into the center. The client was aware of this and was going to put additional internal controls in place to monitor this collection on a prospective basis. However, the use of analytical procedures by the junior staff did not detect this situation from the substantive testing they did. While immaterial at first, how do auditors have assurance that this will not rise to the level of a significant deficiency or even a material weakness forcing the financial statements to be materially misstated?

The key is to educate the younger staff in the proper usage

of analytical procedures. It is important to start with our accounting and auditing classes in both the undergraduate and graduate levels. Students need to be given practical examples using computer software to try and get them to think critically. Students need to have those various financial ratios explained to them in terms of what they mean analytically. One can find students who can recite the “current ratio” at the drop of a hat, but when told that a company has a current ratio of 0.32, a blank expression comes over their faces. This is unacceptable, as the world of auditing is getting more and more complex with each passing day. Blame resides not only at the educational level but at the professional level as well. As professionals, we must educate our junior staff on how analytical procedures need to be done as a way to reduce our expanded substantive testing where possible. We need to explain to them that analytical thinking is the strongest tool an auditor has and is used as a way to find those material misstatements if they exist. A great concern in the profession is that one day we shall say to juniors, “What is 2+2?” and they will respond, “Autosum.”

I leave you with this quote from B.F. Skinner: “The real question is not whether machines think but whether men do.” (Contingencies of Reinforcement, 1969). The rest I now leave up to you.

*Alex Buchholz, CPA, MBA is an audit supervisor with an audit firm specializing in the non-profit and healthcare sector. He is also an adjunct assistant professor at Brooklyn College of the City University of New York.*

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# Why Do Deals Fall Apart?

by Anthony J. Citrolo, CPA, CVA

**I**n many cases, the buyer and seller reach a tentative agreement on the sale of the business, only to have it fall apart. Once the reasons are understood, many of the worst deal-smashers can be avoided. Understanding is key. Both the buyer and the seller must develop an awareness of what the sale involves—and such awareness should include facing potential problems before they swell into floodwaters and “sink” the sale.

What keeps a sale from closing successfully? In a survey of business intermediaries across the United States, similar reasons were cited so often that a pattern of causality began to emerge.

**The Seller Fails To Reveal Problems.** When a seller is not upfront about problems of the business, this does not mean the problems will go away. They are bound to turn up later, usually some time after a tentative agreement has been reached. The buyer then gets cold feet—hardly anyone in this situation likes surprises—and the deal promptly falls apart. Even though it’s tough, sellers must be as open about the minuses of their business as they are about the pluses. Again and again, business intermediaries surveyed said: “We can handle most problems... if we know about them at the start of the selling process.

**The Buyer Has Second Thoughts About the Price.** In some cases, the buyer agrees on a price, only to discover that the business will not, in his or her opinion, support that price. Whether this “discovery” is based on gut reaction or a second look at the figures, it impacts seriously on the transaction at hand. The deal is in serious jeopardy when the seller wants more than the buyer feels the business is worth. It is of prime importance that the business be fairly priced. Once that price has been established, the documentation must support the seller’s claims so that buyers can see the “real” facts for themselves.

**Both Buyer and Seller Grow Impatient.** During the course of the selling process, it’s easy—in the case of both parties—for impatience to set in. Buyers continue to want increasing varieties and volumes of information, and sellers grow weary of it all. Both sides need to understand that the closing process takes time. However, it shouldn’t take so much time that the deal is endangered. It is important that both parties, if they are using outside professionals, should use only those knowledgeable in the business closing process. Most are not. A business intermediary is aware of most of the competent outside professionals in a given business area, and these should be given strong consideration in putting together the “team.” Seller and buyer may be inclined to use an attorney or accountant with whom they are familiar, but these people may not have the experience to bring the sale to a successful conclusion.

**Buyer and Seller Are Not (Never Were) in Agreement.** How does this situation happen? Unfortunately, there are business sale transactions wherein the buyer and the seller realize belatedly that they have not been in agreement all along—they just thought they were. Cases of communications failure are

often fatal to the successful closing. A professional business broker is skilled in making sure that both sides know exactly what the deal entails, and can reduce the chance that such misunderstandings will occur.

**Seller Doesn’t Really Want To Sell.** In all too many instances; the seller does not really want to sell the business. The idea had sounded so good at the outset, but now that things have come down to the wire, the fire to sell has all but gone out. Selling a business has many emotional ramifications; a business often represents the seller’s life work. Therefore, it is key that prospective sellers make a firm decision to sell prior to going to market with the business. If there are doubts, these should be addressed and resolved. Some sellers enter the marketplace just to test the waters; to see if they could get their “price,” should they ever get really serious. This type of seller is the bane of intermediaries/brokers and buyers alike. Business intermediaries generally can tell when they encounter the casual (as opposed to serious) category of seller. However, an inexperienced buyer may not recognize the difference until it’s too late. Most business brokers agree: a willing seller is a good seller.

**Or...The Buyer Doesn’t Really Want To Buy.** What is true for the mixed-emotion seller can be applied to the buyer as well. Buyers can enter the sale process full of excitement and optimism, and then begin to drag their feet as they draw closer to signing on the dotted line. This is especially true today, with many displaced corporate executives entering the market. Buying and owning a business is still the American dream—and for many it becomes a profitable reality. However, the entrepreneurial reality also includes risk, a lot of hard work, and long intense hours. Sometimes this is too much reality for a prospective buyer to handle.

**And None of the Above.** The above situations are the main reasons why deals fall apart. However, there can be problems beyond anyone’s control, such as Acts of God, and unforeseen environmental problems. However, many potential deal-breakers can be handled or dealt with prior to the marketing of the business, to help ensure that the sale will close successfully.

## A Final Note

Remember these components of a successful business sale:

- Good chemistry between the parties involved.
- Mutual understanding of the agreement.
- Mutual understanding of both buyer’s and seller’s emotions
- The belief, on the part of both buyer and seller, that they are involved in a good deal

*Anthony J. Citrolo, CPA, CVA is a principal of NYBB-Certified Business Intermediaries. He specializes in the valuation, merger, acquisition and confidential sale of privately held businesses with annual revenue up to \$20 million. Anthony can be contacted in his Melville office at 1-631-390-9650 or anthony@nybbinc.com*

**Eli Mason, one of the founders of NCCPAP, recently passed away at the age of 88.**

*Eli addressed the NCCPAP National Board and committee members in January 2005 at lunch during a quarterly meeting in Florida, where he spoke about some of his early experiences in our profession and of his love of auditing and being a CPA.*

*Eli presented NCCPAP with a copy of his Credo for a CPA, which we would like to share with you.*

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# ***En Banc* First Circuit Decision in Textron**

## **Tax Accrual Workpapers Are Not Protected by Work Product... Next Stop—The Supreme Court?**

*by Glenn Burdi, CPA*

**O**n August 13, 2009, a divided *en banc* (the entire court) U.S. Court of Appeals for the First Circuit reversed a January ruling by a smaller panel of judges on the same court holding 3-2 that the Textron tax accrual work papers were “independently required by statutory and audit requirements and that the work product privilege does not apply”. *United States v. Textron Inc.* No. 07-2631. This First Circuit *en banc* majority believes its’ decision takes a direct precedent to its’ own in *Maine v. U.S. Dept. of Interior*, 298 F.3d (First Cir. 2002) which stated that work product protection does not extend to “documents that are prepared in the ordinary course of business or that would have been created in essentially similar form irrespective of the litigation.” The *en banc* dissenting judges believe the majority blatantly ignored case precedent and “conducted a new analysis of the history of the work product doctrine and concluded that documents must be prepared for any litigation or trial and must be “use for” in litigation in order to be protected.”

History regarding the dispute over tax accrual work papers of the Textron litigation can be found in prior issues of *NCCPAP News & Views* (Aug. /Sept. 2008) and *Journal of the CPA Practitioner* (June/July 2009).

To summarize, the IRS brought an enforcement action in federal district court in Rhode Island. (See 26 U.S.S. Section 7604(a) (2006) requesting “all the Tax Accrual Workpapers” for Textron’s tax year ending on December 2001. Textron challenged the summons as lacking legitimate purpose and also asserted the attorney-client and tax practitioner privileges and the qualified privilege available for litigation (prospect of litigation with the IRS) materials under the work product doctrine. In August 2007, the U.S. District Court for the District of Rhode Island held that the work papers were protected by the work product privilege, which was derived from *Hickman v. Taylor*, 329 U.S. 495 (1947), and is now embodied in Rule 26(b)(3) of the Federal Civil Procedure. In January 2009, a panel of the U.S. Court of Appeals for the First Circuit affirmed that decision stating that, “the need to estimate the likelihood of success in litigation was a result of the need to set up a reserve fund to cover tax positions for which Textron could foresee disputes with the IRS.” In addition the First Circuit’s opinion was, “dual purpose documents created because of the prospect of litigation are protected even though they were also prepared for a business purpose.” In March 2009, the First Circuit vacated its ruling that the company’s tax accrual work papers are protected from IRS discovery and on June 2, 2009, the *en banc* panel of five judges for the First Circuit heard oral arguments from both Textron and the government resulting in the August 13, 2009 decision.

The question facing this *en banc* panel was “whether the attorney work product doctrine shields from an IRS summons

‘tax accrual work papers’ prepared by lawyers and others in Textron’s Tax Department to support Textron’s calculation of tax reserves for its audited corporate financial statements.” In this case the First Circuit needed to apply the 1970 Supreme Court rule which codified the work product privilege in Rule 26(b)(3) where it described the privilege as extending to documents and other tangible things that “are prepared in anticipation of litigation or for trial.”

The *en banc* panel focused on Textron’s motive of preparing the work papers and stated, “the purpose of the work papers was to make book entries, prepare financial statements and obtain a clean audit and without the possibly of litigation, no tax reserves or audit papers would have been necessary.” The *en banc* panel stressed the fact that, “it is not enough to trigger work product protection that the subject matter of a document relates to a subject that might conceivably be litigated. Rather, as the Supreme Court explained, “the literal language of Rule 26(b) (3) protects materials prepared for any litigation or trial as long as they were prepared by or for a party to the subsequent litigation.” The *en banc* panel believed that the tax accrual work papers prepared by Textron was not work done in anticipation of or for trial and were nothing more than work papers prepared in the ordinary course of business needed for public requirements to bring its financial books into conformity with generally accepted auditing principles, unrelated to litigation, and, therefore, not privileged.

Interestingly the *en banc* panel applied the “you know it when you see it” test to the lawyers who took part in the review (preparation) of the tax accrual work papers. They stated, “No one with experience of lawsuits would talk about tax accrual work papers in those terms. A set of tax reserve figures, calculated for purpose of accurately stating a company’s financial figures, has in ordinary parlance only that purpose: to support a financial statement and the independent audit of it.” The *en banc* panel found “no evidence in this case that the work papers were prepared for such use or would in fact serve any useful purpose for Textron in conducting litigation if it arose.”

A key statement that the *en banc* panel made that I believe was the ultimate reason why a reversal decision was made and as practitioners we should be concerned is, “The practical problems confronting the IRS in discovering under-reporting of corporate taxes, which is likely endemic, are serious. Textron’s return is massive, constituting more than 4,000 pages, and the IRS requested the work papers only after finding a specific type of transaction that had been shown to be abused by taxpayers. It is because the collection of revenues is essential to government that administrative discovery, along with many other comparatively unusual tolls, are furnished to the IRS.” It is this statement and the reasoning of the *en banc* panel that will embolden the IRS to secure taxpayer’s work papers even if they serve a

dual purpose, prepared in order to issue financial statements and anticipation of litigation. If the IRS can gain access to a taxpayer's tax accrual work papers, which to many reflect the "soft spots" on the tax return, the work papers will become the "IRS audit roadmap" revealing how much the taxpayer anticipates to settle each item for and calculate for the IRS their own tax assessment.

This decision is not the end for this issue. The *en banc* panel's dissenting opinion is quite compelling for the Supreme Court to grant a petition for certiorari. "The time is ripe for the Supreme Court to intervene and set the circuits straight on this issue which is essential to the daily practice of litigators across the country." The dissenting opinion specifically points out that even though the majority's decision allows discovery of a taxpayer's tax accrual work papers as a major resource to combat fraud, "this decision will be viewed as a dangerous aberration in the law of a well-established and important evidentiary

doctrine." The dissent outlines where the majority's decision "ignores precedents from circuit courts and contravenes much of the principles underlying the work product specifically in *Maine 298, F 3d* and *U.S. v. Adlman, 134 F. 3d*."

A spokesperson for Textron said that the company is reviewing the decision and that the company is considering filing a petition, which is due on October 12, 2009. It will be an important issue for the Supreme Court to address since the *en banc* panel's Textron decision is not limited to the discovery of taxpayer tax accrual work papers, but may apply to other documents outside of the tax arena and will have wide ramifications. The dissenting judges state, "Corporate attorneys preparing such analysis should now be aware that their work product is not protected in this circuit." We await anxiously for Textron's next move and the implications it will have in creating new law.

## Year-End Planning Ideas for 2009

by Debra A. Kinsler, CPA; Gruver, Zweifel & Scott, LLP

It is that time of year again when many are wondering how to minimize their impending tax burden while simultaneously meeting specific business needs. The recently enacted "American Recovery and Reinvestment Act of 2009" (the "Act") offers some business tax breaks in addition to other planning techniques described below.

Businesses were allowed in 2008 to deduct fixed asset acquisition costs by immediately writing off an unlimited, 50% of the total cost of new property. This was called "**bonus depreciation.**" As long as the recovery period wasn't more than 20 years, almost every type of tangible, depreciable property qualified, including certain building improvements. The remaining 50% could be depreciated over the useful life until completely written off. Under the new Act, Congress extended bonus depreciation through 2009. But it's necessary to act fast since the acquisition must be placed into service before 2010.

In addition, businesses can choose to immediately write off the entire cost of many types of fixed assets, or as much of the cost as needed to reduce income to a desired result. This is possible under the expensing election commonly known in the business world as "**Section 179.**" Last year, the maximum amount businesses could write off was increased to \$250,000. The new Act extends this through 2009. The acquisition can be either new or used tangible property. For family-owned businesses, a husband and wife are treated as one taxpayer and are allowed only one \$250,000 limit. For 2010, the old limit of \$125,000 is expected to be reinstated.

Although not part of the Act, another useful strategy is the "**0% capital gain rate.**" This is how it works. The top tax rate on most long-term capital gains and corporate dividends is 15%, at least for now. But instead, this 0% rate will apply for 2009 and 2010, and applies to gains from sales of capital assets held over a year, and to qualifying corporate dividends received,

which can come from the corporation you own. To take advantage and pay no tax on this income, you must end up in one of the two lowest tax brackets, as follows.

Businesses have many ways of reducing income when targeting a lower bracket. The above-mentioned depreciation techniques are an excellent way of doing that. Other ways can include contributing to retirement plans to defer income, or IRAs if deductible; utilizing a home office; converting taxable investments to nontaxable, such as municipals; determining which year is better to pay state estimated taxes, or bunching up other deductions like medical or charitable in certain years, if you itemize; paying for long-term care and/or health insurance, and/or contributing to a Health Savings Account if you qualify; prepaying some expenses if you're on the cash basis; or even paying your kids a reasonable wage before year end.

*This written advice is not intended or written to be used, and it cannot be used by you or any taxpayer for purposes of avoiding penalties that may be imposed on the taxpayer by the IRS or any applicable state or local tax authority.*

Sources: 2009 Thomson Reuters/RIA;  
Quickfinder Handbook.

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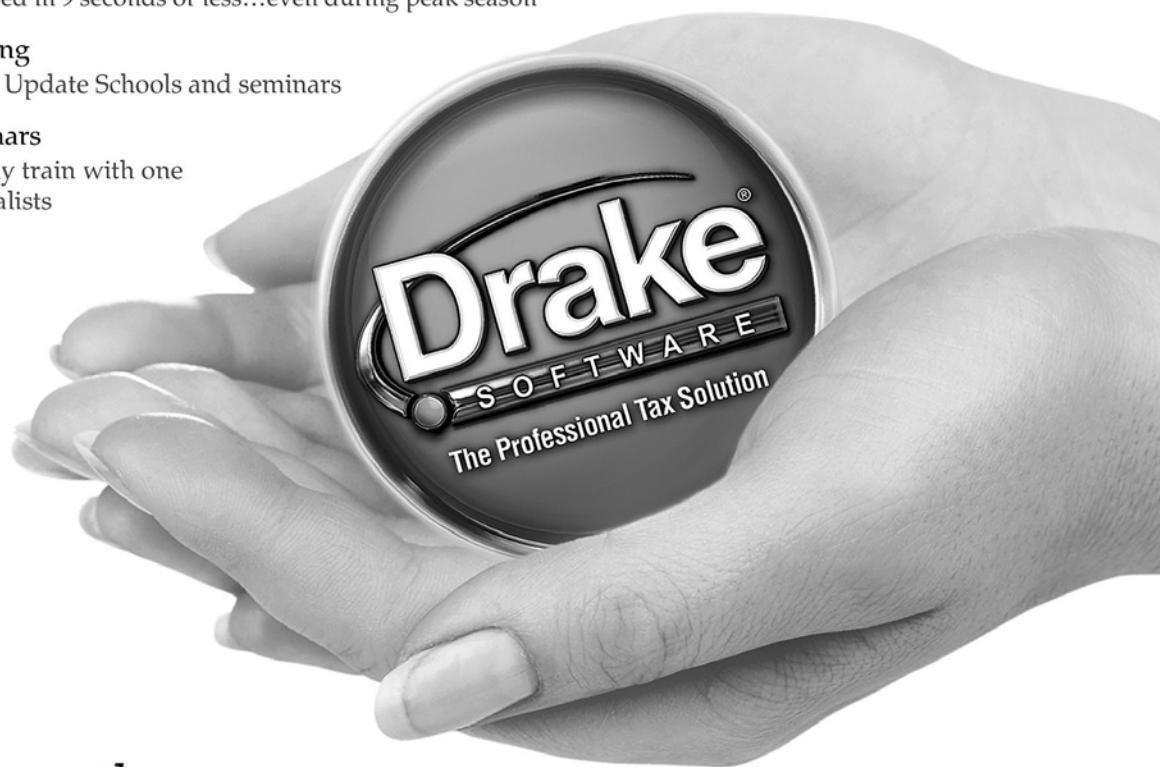
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**CHAPTERS' CALENDAR OF EVENTS****NOVEMBER / DECEMBER 2009 & JANUARY 2010****NASSAU/SUFFOLK, NEW YORK**

Contact: Chapter Office (516) 997-9500  
 Chapter Meeting; Reg./Buffet Dinner 5:30 p.m.;  
 Seminar 7:00 p.m. – Holiday Inn of Plainview, 215 Sunnyside  
 Blvd., Plainview, N.Y. (exit 46 off the L.I.E.), except as noted

*November 18, 19 & 20, 2009*

**2009 LONG ISLAND TAX PRACTITIONER SYMPOSIUM**

Crest Hollow Country Club, Woodbury, N.Y.  
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*Thursday, December 3, Chapter Meeting*

**1041 PREPARATIONS – 2 CPE (Tax) Credits**

*Thursday, January 21, Chapter Meeting*

**SOCIAL SECURITY – 2 CPE Credits**

**LONG ISLAND EAST, NEW YORK**

Contact: Chuck Pegler, CPA (631) 582-9090  
 E-mail: Chuck@PeglerCPA.com

Call for information.

**NEW YORK CITY, NEW YORK**

Contact: NYC Chapter Office (212) 946-4718  
 Call to confirm as topics, times, and locations are subject to  
 change due to attendance, speakers' preference, etc.

*November: to be announced.*

*Tuesday, December 22, 8:30–10:30 a.m.*

**NY STATE UPDATE – 2 CPE Credits**

Support Center for Non-Profit Management  
 305 Seventh Avenue (27th Street), New York City

*January: to be announced.*

**WESTCHESTER / ROCKLAND, NEW YORK**

Contact: Chapter Office (914) 708-9404  
 Doubletree Hotel, 455 S. Broadway, Tarrytown, N.Y.  
 (except where noted)

*Tuesday, November 24, 9 a.m. – 5 p.m.*

**CORPORATIONS, LLCs & PARTNERSHIPS**

– 8 CPE Credits

*Saturday, December 5, 8 a.m. – 4 p.m.*

**INDIVIDUAL UPDATE – 8 CPE Credits**

Westchester Broadway Theatre, 75 Clearbrook Road,  
 Elmsford, N.Y.

*Tuesday, December 8, 11 a.m. – 5:30 p.m.*

**TRI STATE UPDATE – 6 CPE Credits**

*(continued)* **WESTCHESTER / ROCKLAND, NEW YORK**

*Tuesday, January 26, Time to be announced*

**IRS TAX UPDATE – CPE Credits to be announced**

**NEW JERSEY**

Contact: Fred Bachmann, CPA (973) 377-2009

E-mail: bachmanncpa@msn.com

All meetings at Victor's Maywood Inn, 122-124 West Pleasant  
 Avenue, Maywood

Phone (201) 843-8022/ E-mail: www.maywoodinn.com

6–8:30 p.m. — Dinner and Seminar

*Monday, November 2*

**NJ TAX UPDATE – 2 CPE Credits**

*Monday, December 7*

**FEDERAL TAX UPDATE – 2 CPE Credits**

*Monday, January 11*

**NY STATE TAX UPDATE – 2 CPE Credits**

**FLORIDA**

Contact: Neil Fishman (561) 369-3228

All meetings at Comerica Bank, 1037 State Road 7, #117,  
 Wellington, Fla. Wellington Reserve, north of Forest Hill Blvd.  
 8:30– 10:30 a.m., Registration at 8 a.m.

*Thursday, November 5, 8:30–10:30 a.m.*

**9 SECRET TIPS TO INCREASING PROFITS**

– 2 CPE Credits

*Thursday, December 3, 8:30–10:30 a.m.*

**THE FINANCIAL ARCHITECTURE OF  
 CONTECTUAL TRANSITIONS PLANNING**

– 2 CPE Credits

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**NATIONAL MEETING** at the PGA Resort in Palm Beach  
 Gardens, Fla. Come One, Come All!!

**MASSACHUSETTS**

Contact: Ronald Tockman, CPA (781) 341-2400

*Tuesday, November 17, 7:30–9:30 a.m.*

**NEW TAX LAW WITH YEAR END PLANNING**

– 2 CPE Credits

Sheraton Needham, 100 Cabot Street, Needham, Mass.

*December & January: to be announced.*

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