THE BUSINESS OF ACCOUNTING
A Roundtable Discussion

THE Los Angeles Business Journal has once again turned to some of the leading accountants in the region to get their assessments regarding the current state of business accounting, economic variables, and the various trends that they have been observing, and in some cases, driving.

Below is a series of questions we posed to these financial stewards of Los Angeles and the unique responses they provided – offering a glimpse into the state of business accounting in 2016 – from the perspectives of those in the trenches delivering financial advice and leadership to the businesses of our region today.
Successful clients are faced with paying more taxes on federal, state and local levels. We have assisted our clients with effective strategies to reduce or eliminate California taxation. Clients who have significant taxable income can use techniques such as captive insurance companies, which offer significant tax deductions and other benefits. Many clients are able to reduce their taxes from research and development credits and perform cost segregation studies on their real estate. Other tax minimization techniques include deferrals of taxable income by using cash basis distribution companies to avoid being taxed on accounts receivable, disbursements to fiscal-year sales and marketing companies to defer income recognition, utilization of pension and profit sharing plans, and other techniques.’

DREW GREY

There are several new trends in the market place. The smaller businesses are utilizing technology to enhance their presence and bottom lines. This is resulting in increased investment in technology platforms resulting in growth in employment and revenues for the small businesses technology services providers. Social accountability is also very much expanding on the corporate side. Many companies are moving towards telecommuting options for their employees besides the flexible work arrangements to accommodate life needs.

KASH HUSSAIN

Have you been observing any new, positive business trends this year?

HUSSAIN: There are several new trends in the market place. The smaller businesses are utilizing technology to enhance their presence and bottom lines. This is resulting in increased investment in technology platforms resulting in growth in employment and revenues for the small businesses technology services providers. Social accountability is also very much expanding on the corporate side. Many companies are moving towards telecommuting options for their employees besides the flexible work arrangements to accommodate life needs.

DREW GREY

What industries do you feel are expanding and experiencing growth in LA?

MAZZA: Silicon Beach is fueling growth for the technology industry in Los Angeles. As major brands have joined the ranks of Silicon Beach, Los Angeles has legitimately staked a claim on being the second-largest tech hub in the world.

HUSSAIN: We are seeing an increase in Healthcare, Biotech, Alternative Energy, Alternative Finance and Hybrid Media & Technology platforms in the LA market. Real Estate is also continuously expanding in its reach and we see a great amount of new activity in industrial sector in the inland empire.

Grey: Successful clients are faced with paying more taxes on federal, state and local levels. We have assisted our clients with effective strategies to reduce or eliminate California taxation. Clients who have significant taxable income can use techniques such as captive insurance companies, which offer significant tax deductions and other benefits. Many clients are able to reduce their taxes from research and development credits and perform cost segregation studies on their real estate. Other tax minimization techniques include deferrals of taxable income by using cash basis distribution companies to avoid being taxed on accounts receivable, disbursements to fiscal-year sales and marketing companies to defer income recognition, utilization of pension and profit sharing plans, and other techniques. We study each client to determine the optimal strategy that meets specific goals. Paying less in federal, state and local taxes provides more cash flow for business or investment.

MAZZA: The only significant change in the current year is the tax on investment income under section 1411, which is a tax on individuals not a tax on businesses. Our clients have been negatively affected by this additional tax to finance the Affordable Care Act. All additional government benefits have a price to be paid, and unfortunately, taxpayers bear that burden.

What other federal or state regulations are having the most significant impact on your clients’ business? Why?

MAZZA: The compliance regulations under the Affordable Care Act are burdensome to businesses and create additional administrative costs. It’s a consequence of every new government-sponsored program that carries with it new regulations.

What are some of the top concerns of middle market CFOs in 2016 — and how do you help them?

HUSSAIN: For 2016 it is the uncertainty around the political landscape and resulting future legislation changes which may impact the business. The credit market is fairly open to exploitation and interest rates are very low. However, cross border trade is creating issues with respect to the strong U.S. dollar for the companies exporting their products. There are reservations on spending on capital expenditures due to the election year. Further, there is an enhanced regulatory burden, which is challenging for the CFOs to manage. Minimum wage hike over the next few years is a concern and may have implications for the Companies and their expansion strategies.

GREY: CFOs are concerned with many issues; however one of their primary issues is having sufficient debt or equity to fund their business. We actively assist our clients in the preparation of detailed financial projections to plan for their needs. We have developed strategic relationships with conventional and non-conventional financing sources that can provide the debt needed to expand their businesses. We have strategies that separate the financial statements from the income tax returns thus enabling our clients to pay less tax while not impacting the financial statements. Commercial lenders make borrowing decisions based on the company’s compiled reviewed or audited financial statement. Therefore our clients are able to increase their cash flow through paying less in income taxes and are able to obtain the maximum amounts available from lending sources.

MAZZA: Our research based on the RSM Middle Market Leadership Council (MMMLC) survey of 700 U.S. executives shows the middle market continues to experience generally positive economic conditions with forward expectations of higher net earnings and gross revenues. Moreover, survey participants expect to increase capital expenditures during the next six months and increase hiring. The major takeaway from the survey is that, for the middle market, talk of the U.S. economy falling into recession is premature at best and overblown at worst.

How do your clients handle the challenge of increasing their credit facilities while minimizing the taxes they pay the government?
BDO provides assurance, tax, advisory and consulting services to a wide range of publicly traded and privately held companies. We offer a sophisticated array of services and the resources and capabilities of the BDO global network, combined with the personal attention of experienced professionals.

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“Not just global resources. Credibility with the regulators.”
People who know, know BDO.”
ACCOUNTING ROUNDTABLE

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GREY: Clients preparing financial statements for financial institutions must find the balance between reducing federal and state taxes, and reporting strong earnings to the financial institutions that have provided credit facilities. We have strategies that emanate the clients’ financial statements from their tax reporting. How do we do this? Financial institutions require an accrual-based financial statement, while tax law differs significantly from accrual accounting. This difference can yield lower taxable income without impacting the accrual-based EBITDA of the company. We evaluate each company to identify areas where the financial statement and tax reporting can be separated by applying different year-ends and methods of accounting. At SRG, we use the GAAP and tax rules to our clients’ advantage, while maintaining integrity in all aspects of our reporting. This is another example of our creative, value-added approach to solving our clients’ problems.

Are there any recent trends you’ve noticed in terms of how your clients manage their finances?

HUSSAIN: We are seeing an increasing focus on outsourcing internal operations and partnerships/IJs on projects to diversify risk. Finding competent and able workforce continues to be a challenge. There is also a significant push by our clients to structure transactions to maximize on all available federal and state tax incentives such as R&D credits.

What is the biggest difference you’ve noticed between the accounting professions today compared to when you first became licensed?

GREY: The most significant change is the amount of new financial statement and income tax changes in the rules that impact the clients and our firm. Our services have evolved to meet the changing landscape of business operations today. We are active in strategic financial consulting, and act at a level of a Chief Financial Officer and, in some cases, as the Chief Executive Officer. Many of our partners and professional staff have been controllers, CFOs, or CEOs. This level of seasoned experience gives our firm a unique ability to meet our clients’ needs. We are actively involved in the Merger and Acquisition activities from the buy and sell side, selecting the appropriate investment banker, and assisting with long-term planning for tax minimization and succession planning. We have developed effective strategies to eliminate or substantially reduce estate taxes and regular taxes from the sale. Asset protection is another benefit that flows from an effective structure. Our firm has become global to meet the needs our clients who cover the world.

Are there any additional services that you offer today that perhaps were not offered in the past?

MAZZA: As the economy has continued to improve, we have found that companies invest more in consulting services, particularly in the areas of technology and management, risk advisory and financial advisory. Cybersecurity is a hot topic that is top of mind at many companies, and we have several experts in that field.

GREY: Our firm has developed value-oriented services that increase our clients’ net after-tax cash flow. We provide tax strategies that reduce taxable income and do not impact the financial statements that commercial banks rely upon to provide credit facilities. We separate tax planning from financial reporting in a responsibly creative manner. We are trusted advisors serving at top levels in management. Our expertise as Controllers, CFOs and CEOs offers our clients knowledge and experience, which other CPA firms do not possess. Our services have evolved to meet the changing landscape of business operations today. We are active in strategic financial consulting, and act at a level of a Chief Financial Officer and, in some cases, as the Chief Executive Officer. Many of our partners and professional staff have been controllers, CFOs, or CEOs. This level of seasoned experience gives our firm a unique ability to meet our clients’ needs.

How important is private equity in terms of keeping businesses thriving?

HUSSAIN: The value of the dollar against other major currencies is very strong and thus creating opportunities for our clients who are in the import businesses. On the other side, the US exporters are seeing a slowdown due to this issue. Currency hedging is happening rather frequently at our clients now and there is a great deal of concern on volatility in other currencies at present.

MAZZA: We find that Los Angeles companies are acquiring more of their foreign distributors and contract manufacturers. Also, we see increased inbound investment, including foreign companies opening shops in LA. There are fewer Greenfield versus acquisition expansion into China. And, more companies are looking to export products.

How has international commerce impacted your local client businesses?

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JOE MAZZA

JUNE 6, 2016

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Thinking about your business is a big part of ours.

PUT OUR TAILORED INSIGHTS TO WORK FOR YOU.

To make confident decisions about the future, middle market leaders need a different kind of advisor. One who starts by understanding where you want to go and then brings the ideas and insights of an experienced global team to help get you there.

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Our clients continue to face challenges with running a business in LA County. Within LA, the minimum wage is scheduled to increase to $15 an hour by 2020 (other cities within the county have also adopted similar plans), and the LA City Council recently approved increasing the minimum paid sick leave policy for all employers from three days to six days, including small businesses. Additionally, the LA Business Tax continues to prove burdensome for our clients. Inconsistant tax audit results and outdated guidance drafted for an economy of the past continue to leave taxpayers confused and often shocked by the tax. While there are many geographical advantages of operating a business within the county, our clients are now questioning whether it makes economic sense to remain here.

JOE MAZZA

What are some of the biggest mistakes companies make when it comes to managing their finances?

HUSSAIN: Some of the key mistakes companies make include:

a) Not planning for growth late in the economic cycle. The current cycle has been on for 7 years and there is a likelihood that we may see some pull-back;

b) Not being ready to capitalize on early expansion in the start of the economic cycle. This requires to prepare early and deploy when leading indicators point to on-coming growth;

c) Not managing budgets to actual or having a robust budgeting process;

d) Not paying attention to competitors and supply chain, and

e) Not paying attention to customers and reacting to economic changes.

GREY: Companies need to better plan for their financing needs, and more effectively project their covenant performance. This planning helps to confirm and maintain compliance and the conditions required to increase their credit facilities. Companies also need to communicate more frequently with their lenders regarding both positive and negative situations. The biggest mistake companies make is that they try to reduce their tax obligation in the same entity that they are using to borrow from the bank. Tax minimization and financial statement optimization are mutually exclusive, and cannot be achieved in the same entity. The SRG Advantage is the emancipation of the financial statements from the tax returns, yielding our clients optimal results. Lower income taxes are paid and the financial statements are fairly stated; this enables the company to obtain the maximum amount of available financing.

What role can smart accounting play when it comes to helping a company grow its business these days?

GREY: The CPA firm needs to identify growth opportunities and help clients implement strategies to optimize their market share. Short term, mid-term and long-term planning contributes to achieving these goals. Once a comprehensive business plan is developed, our firm will introduce lending institutions, private equity firms or private sources to achieve the goals. The accounting firm is an active partner with its clients in reaching their goals. Continual monitoring of results is a critical contribution of the accounting firm. The business plan and forecast should be monitored and revised regularly to properly plan for the company’s success.

What keeps your clients up at night in 2016?

HUSSAIN: Some of the things clients worry about most include:

a) Expected slow-down in demand;

b) Increased regulatory burden;

c) Volatility in capital markets;

d) Volatility in political landscape;

e) Technology evolving too fast in changing market conditions and the inability to react to those changes; and

f) Expectations from the owners on growth curves.

What's the biggest piece of advice you give your clients when it comes to planning for the future?

GREY: Clients need to adapt to continually changing circumstances. We meet regularly with our clients to review their goals and desires, and ensure that we are providing them with the maximum value possible. We recommend that our clients who own businesses plan their exit strategy well in advance, as they may need to transition family members or key employees into a succession plan. Exits can be costly; we have ways of reducing costs substantially. Our income tax and estate tax methods achieve the transfer while offering our clients maximum control and cash. Many clients want to maximize their entity value and then exit through a sale. We can assist with the sale. We recommend that exit strategy planning be done many years before it is executed. Having a well-seasoned plan can ensure proper capital gains treatment, avoid inclusion in the client’s taxable estate, and often help avoid paying taxes to the state of California.

HUSSAIN: There are a few things I recommend:

• Have a vision and a plan that your key management and employees believe in;

• Ensure that the right support is provided to the team;

• Obtain regular inputs from your customer base and supply chain;

• Assign and monitor tasks objectively on a regular basis; and

• Know that plan will change based on changing market conditions. Implement a process to monitor trends and establish protocols to update the plan in a timely fashion.
THE SRG ADVANTAGE™
Some clients see us as excellent CPAs who are great business advisors. Others see us as trusted business advisors who happen to be great accountants. Either way, SRG is a unique team of professionals with one goal in mind: helping clients plan for and achieve their financial goals. We call this the SRG Advantage™.

We strive to increase our clients’ net worth by retaining more cash to invest. Our strategies seek ways to reduce taxes without impacting the financial statement income and transfer of wealth, thereby reducing estate taxes and protecting assets from creditors as a result of the proper structure.

Whether you are a large and established corporation, a fast growing start up, or a highly successful individual, let us show you how the SRG Advantage™ can help provide the financial strategies and solutions you need to succeed.

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“Your business is more than just numbers. That’s why we’re more than just accountants.”
Drew Grey, CPA
Partner, SRG, LLP
When and How to Sell a Business

By SCOTT ROUSE

W ords a wave of consolidation hits an industry, an independent owner is forced into some choices. You can sell, and join the trend, or you can maintain your independence — and face stiffer competition than ever before. The consolidation has access to more plentiful and more inexpensive capital, and they benefit from economies of scale. They can drive prices down when they choose to seek market share. It can be advantageous to be the first in your region to sell to the consolidator. You might get a higher price, and you might be chosen as a “flagship” for the area. Other acquisitions made in the region would then come under your management — and you might enjoy acquiring other businesses with someone else’s money. If you delay, your profits might be reduced by the impact of new competition, and you would have a less robust business to sell.

The best advice is to be prepared. A company making several acquisitions in an industry is comparing managements. Many well-run and highly profitable businesses function perfectly well without a business plan, but professional managers in public companies have such plans, and today you can acquire software to help you accomplish the task for about $100. Documentation, like a business plan, allows a prospective buyer to evaluate a business more readily. The buyer’s focus is about $100. well-run and highly profitable businesses function perfectly well without a business plan, but professional managers in public companies have such plans, and today you can acquire software to help you accomplish the task for about $100. Documentation, like a business plan, allows a prospective buyer to evaluate a business more readily. The buyer’s focus is on expected profits, and a business plan is where you tabulate these projections. It means less disruption of your business if much of the evaluation of your business can be accomplished off-site. And disruption of your business can unsettle employees and customers, and it can threaten its value. Financial statements are central to any discussion of selling a business. They become more important than ever, and professional presentation will impress the buyer and allow the transaction to proceed quickly. Audited or certified statements would allow you to make the best possible impression, and might allow you to demand more in cash at the closing (because the audited statements reduce the buyer’s risk).

MISTAKES SELLERS MAKE

Overconfidence is the first mistake commonly made. Buyers know the subtleties of mergers and acquisitions for sellers it is usually all new. It is not an even match. So sellers should consult lawyers and accountants early to understand the tax and other issues that recur. You can sell the assets of your business, or you can sell the shares of your corporation, and the tax consequences are quite different. Buyers typically prefer to buy assets, and sellers typically prefer to sell shares. You must consult professionals to understand, in advance, how much money it is at stake. You need to know the tax treatment of payments for a consulting agreement, or a non-compete agreement. The buyer is likely to suggest that part of the price be attributed to such agreements, but the taxes on these payments are higher than the capital gains rates that usually apply to the sale of the business. Timidity can be another problem. Sellers don’t ask buyers enough questions, especially about the financing. Buyers often want to borrow part of the purchase price from someone — usually a bank, or the seller, or both. Notes owed to sellers are almost always subordinated to bank debt, and the unsuspecting seller does not discover this until final papers are being reviewed. A seller who expects to be owed money by the buyer after the closing — for notes, payments under a non-compete agreement, or a consulting agreement — should understand the buyer’s proposed balance sheet for the day after the closing. Few sellers ask enough questions about the planned financing.

NEGOTIATIONS

If you want to sell your business, you strive to get an offer in writing. It is a key milestone towards the target. But too early it is a problem. An offer in writing routinely asks the seller to accept within about two weeks, and it routinely asks the seller to stop talking to other buyers. A seller should not accept an offer before developing a sense of what other buyers might be willing to pay — and this takes time. Take time to understand an offer thoroughly — is the buyer going to assume the debts in your business, or expecting you to pay them off out of the price? The best weapon of a seller in negotiations is a good, credible alternative, another buyer or a decision to keep the business. The smartest sellers keep the buyer guessing — guessing about how interested they are in making the deal, and at what price. They know that getting too friendly too early (this is tempting, and a natural instinct in these circumstances) can be costly — buyers won’t stretch to the top end of their price range if the deal appears “in the bag.” Negotiations for the sale of a business extend beyond one day, and they often last several weeks. After a handshake on the price, the buyer investigates the business, the due diligence. The buyer can often point to some new information and say this is a reason to decrease the price. The seller is now weaker than the buyer — the buyer can walk away without stigma, the seller, on the other hand, may be considered “soiled goods” if the deal is not completed. This underscores the importance of doing your homework about the buyer, and talking to others that have dealt with them, before you shake hands on a deal. The stakes are high, financially and emotionally. The best price usually comes when the seller agrees to run the business for the new owner for a few years. Then price is not the seller’s only concern. The working environment could cause extraordinary stress, and exact a price of its own.

Scott Rouse is a freelance writer and merger/acquisition specialist.
New Survey: Half of Americans Expect Identity Theft to Cause Them a Financial Loss in the Next Year

AICPA's National CPA Financial Literacy Commission Provides Tips to Prevent Americans from Being Victimized by Financial Schemes

June 6, 2016

The good news is that the vast majority of Americans (93 percent) have suffered identity theft or attempted identity theft. The news is not so good: The vast majority of Americans (93 percent) affected by identity theft (93 percent) affected by identity theft took action to fix it; approximately three in four (72 percent) contacted their credit or debit card company to set up additional protection; and half (50 percent) used cash or checks because they knew the fraudster (10 percent) used their debit card to set up additional protection; and one in 10 (10 percent) used internet fraught with financial fraud schemes that have the potential to cause major financial harm. A basic rule for any investment is that it seems too good to be true – it probably is.

“Being proactive can help mitigate the threat of a financial loss resulting from identity theft. Helping to prevent losses from investment fraud requires a similar approach – and a healthy dose of skepticism. Since investment fraud involves an active decision to put money at risk, often times with friends or family, reporting it can seem like a difficult decision. In fact, six in 10 U.S. adults who were victims of investment fraud (59 percent) did not report it to the authorities. Among those who didn’t, more than four in 10 (41 percent) did not report it because they didn’t know who to contact (25 percent). Another one in five (18 percent) cited embarrassment as the reason they did not report the investment fraud.

“Americans who are victimized by investment fraud or identity theft should alert the proper authorities, regardless of the circumstances,” added Anton. “By reporting the crimes, they are increasing the chance that the scammers will be brought to justice and reducing the risk that they will target others in the future.” The survey found that almost one in five (19 percent) Americans have been victimized by investment fraud.

The scams most often cited were Ponzi or pyramid schemes (six percent); closely followed by a fraudulent IRS tax return or refund scam, unrealistically high guaranteed investment returns, collectibles, get rich quick seminars (four percent each), and email requests for money (three percent).

The AICPA’s National CPA Financial Literacy Commission offers the following tips to prevent or mitigate the effects of identity theft and investment fraud and information on who to contact if you are victimized.

IDENTITY THEFT
1. Check your credit report free annually, even for your children
2. Get free identity theft protection from your credit or debit card company
3. Check account balances daily with apps
4. Use solid passwords and change them frequently
5. If you are a victim of identity theft, report it immediately to the Federal Trade Commission, your local police department, and credit reporting agencies

INVESTMENT FRAUD
1. Be careful if it sounds “too good to be true”
2. All aspects of the transaction should be transparent; ask questions
3. The risk vs. reward should be reasonable
4. Resist pressure to invest or act quickly
5. Report fraud or suspicious activity to the Securities and Exchange Commission and Financial Industry Regulatory Authority

For more information on AICPA, visit www.aicpa.org.