

The Business of Accounting*



**A ROUNDTABLE
DISCUSSION**



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Business of Accounting Roundtable

As our roller-coaster of an economy continues to see its climbs and dips, the Los Angeles Business Journal turned to some of the leading accountants in the greater Los Angeles area to get their assessments regarding the current state of business accounting in Los Angeles and the various trends that they have been observing, and in some cases, driving. Below is a series of questions the Business Journal posed to these financial stewards of Los Angeles County and the unique responses they provided – offering a glimpse into the state of business accounting in 2011 – from the perspectives of those in the trenches delivering financial advice and leadership to the businesses of our region today.

ROUNDTABLE PARTICIPANTS:

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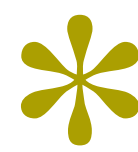
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How has the slump in the economy affected your clients and what advice have you given to help them?

LEAPER: Over the last few years our economy has seen the most severe recession in quite some time. Are we at a bottom yet and when can we expect the economy to improve? Are current economic conditions the new normal? These are questions clients ask as they struggle to structure their organizations to get back to profitability and position themselves for growth.

Economic conditions continue to be challenging for middle market companies. Most have seen a decline in revenue which is not rebounding, are experiencing difficulty managing cash flow, and find bank credit more difficult to obtain.

Since this sector is the main engine of job growth in our economy, and our economy will not rebound until people have jobs, the recovery is largely dependent on the ability of banks to provide

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lending to middle market companies.

Given these facts, companies need to adjust expectations and form strategies for the new normal. Many companies have cut costs to adjust to revenue declines but find it is not enough. To survive and thrive in the new normal, companies should focus on a few key areas:

- Growing revenue in highly profitable categories or lines of business and shedding less profitable activities
- Creating operating efficiencies (rethinking or re-engineering business processes)
- Maximizing cash flow by reducing receivable balances and inventory balances, or in the case of service companies, increasing employee utilization.

You may have a certain group of products or services that have a higher gross profit margin, or it may be a group of customers. Conversely, you may have products where margins are very thin. Identifying these groups and then taking action to pursue growth in the areas where you have higher margins is a time investment that will have positive results. Additionally, you could consider extending your geographical reach by selling products via the internet.

Another area that may yield cost savings is looking at all of your operating processes to see if there are any opportunities to make them more efficient. A method of doing this is work process

mapping where you walk through a process step-by-step and document the results. I have participated in this process many times and it always seems to yield improvements through efficiencies. The key is to be creative in your thinking and not accept "this is the way we have always done it."

Improving profitability is an element to increasing your cash balances but focusing on improving your cash flow velocity will raise the balance as well. Two key areas to focus on to increase cash flow are inventory and accounts receivable (AR). The faster they turn, the more cash you will have - it's as simple as that. To manage inventory you will need good information from both the production planning side (orders coming in) and your current inventory levels.

Common elements to all of these objectives are the need for good information, creativity and a strategic focus to frame smart business decisions. Focus on investing time to create sound practices in your business and you will be better able to weather the current storm.

GRIFFITH: Enough has been said about the severity of this most recent economic down-turn. As a tax advisor, my advice is to focus on the fundamentals and work hard to remain a *taxpayer* (profitable with positive cash-flow).

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THOMAS LEAPER



Have you seen a change in the way your clients monitor cash flow and what are some examples you can share?

SACHS: Yes, particularly in the areas of customer credit, inventory control, and the review and evaluation of overhead expenses. Conservatism seems to be the rule of the day. Depending on the industry, we have seen tightening of days outstanding, pushing reductions of 10 to 15 percent, development of more efficient re-order points for inventories, and logistics optimization to gain benefits of consolidation and aggregation of the movement of goods.

We see many of our clients placing extra focus on their monthly budgets and cash flow projections. They are monitoring budget-to-actual results in a more timely manner and are adjusting their operations as needed. Further, we see higher levels of executive management and owners taking control of cash disbursements and slowing down the disbursement timeline.

Our clients are conserving their cash so that they can weather this storm and

be better prepared to seize the strategic opportunities that are available. One of our clients, for example, made immediate reductions in their cost structure at the end of 2008 and early 2009. Not only did this allow them to achieve profitability in 2009, but it also provided them sufficient capital reserves and overall financial strength to make an acquisition of a struggling competitor.

KRAJANOWSKI: "Cash is King" has never been a truer statement. I advocate clients using detailed rolling 13 week cash projections to closely monitor cash, accounts receivable, and purchase commitments. I see clients implementing more deposit/retainer strategies when selling, as well as an increased use of progress billings. Clients are self-financing more than ever and using credit lines less, in order to truly have an emergency fund available.

'Cash is King' has never been a truer statement ... Clients are self-financing more than ever and using credit lines less, in order to truly have an emergency fund available.

DAVID KRAJANOWSKI



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whether the
economy has
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How has going green impacted your practice and your clients' businesses?

DUBAN: What is interesting is that in accounting firms, which were previously paper driven, going green has actually not only helped save the planet but it saves money. For a very small change in systems and little or no investment, reams of paper can be saved by reducing client copies of papers kept in files and instead saving them electronically; forwarding tax returns in electronic form rather than paper; sending invoices electronically; saving supporting documents and retaining source documents similarly. This saves not only paper, but the money for labor to copy documents, toner, wear and tear on machines, and most importantly the real estate required to store all the files. Other forms of going green, for example recycling; green kitchen practices and 4 day work weeks have increased morale, reduced waste and provided opportunities for employees to participate in management decision and brain storming as we continue to look for new opportunities. For clients, our reduced costs and overhead have helped keep fees in check at a time when increases were difficult to justify. It has also increased efficiency and turnaround time as documents saved electronically can be sent electronically, thus providing immediate response to client's requests. And since we are respected by our clients, I think we have an opportunity to set a good example of how going green can benefit the small business owner and I believe that we have often inspired our clients to follow similar practices.

SACHS: Many of our clients have made significant investments in "going green" because they believe it's the right thing to do, environmentally and economically. For example, a client spent \$1.5 million on solar panels at its Anaheim facility. It was an environmentally sound decision because the panels generate about 85 percent of the electricity they need, but it is also a bottom line savings, as they have received both Federal and state tax credits. Further, our client has received substantial positive press and praise within their industry for taking a leadership role in dealing with environmental issues. We have several "green" tax specialists who are working to help our clients understand the maze of Federal and State tax incentives to maximize the cash flow effect of green strategies.

On the less severe end, our clients are thinking more about things like eliminating plastic water bottles and providing reusable water bottles, adding energy-efficient vehicles to their employee fleet, going paperless, and retrofitting their lighting systems. We've been able to support their efforts by making them aware of the tax credits and accelerated depreciation available and by introducing them to some of our strategic relationships, such as Cohn Logistics, which can make their shipping expenditures more rewarding by consolidating environmental and economic resources. On many levels, "going green" is a win-win.

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SCOTT SACHS



How has the use of technology impacted how your clients run their businesses – are they willing to make the investment in this economy?

KRAJANOWSKI: Clients, though somewhat reluctant, are open to investing in technology for their businesses. Detailed cost/benefit analysis is the rule. If justified, clients are spending dollars to maintain or increase their competitive advantages. Favorable tax laws are helping to create the cash to implement their strategies.

DUBAN: Clients now realize, particularly the younger generation, that technology can only benefit them, make them more competitive and help them in the short and long term. They have all had to "step up" in order to "keep up." They have had to continually upgrade technology, which seems to change daily and we have found our small businesses to be on the cutting edge of new technological advancements, particularly those in southern California, which is extremely competitive com-

pared to other areas. I feel that clients do not think they have a choice about making these investments, they must do so in order to survive in the long term. They have had to dedicate significant resources to continually upgrade their information technology systems. And this has impacted the bottom line sometimes in the short term. However, recently, with very aggressive bonus depreciation legislation and special depreciation income tax allowances, some of which started as far back as 9-11, clients have found that the tax benefits can, in fact, offset the required investment and that if we as their trusted advisors share that upside potential benefit, they are then ready to make the investments readily and can reduce income taxes as well, thus creating cash flows while they simultaneously upgrade their businesses.

Clients now realize ... that technology can only benefit them, make them more competitive and help them in the short and long term. They have all had to 'step up' in order to 'keep up.'

DENNIS DUBAN

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 What is the best success story you have seen and what have you learned from it?

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LEAPER: An RBZ client was engaged to provide goods and services to the South Korean Government through a U.S.-based consulting firm. The services were to be provided both in the U.S. and South Korea, and the goods were to come from all over the world. Two days before signing the agreement, they decided to send a copy to us – alerting us to the deal. We immediately spoke with our resident International Tax expert who advised our client to divide the Agreement into three separate contracts in order to avoid the potential of paying South Korean tax on the goods and the portion of services to be provided in the U.S.


We got on a conference call with our client, their attorney and communicated our suggested changes to the Consulting Firm. Everyone agreed to our approach and the contract was split into three documents. There were a few more details that had to be worked. This included confirming

everything with our JHI Affiliate in South Korea (JHI is an international affiliation of accounting firms). It took several calls to iron out all the contract details but the bottom line is we saved our client from a potential 24.2% foreign tax, which may not have all been creditable in the U.S., on over \$10 million of income. So the moral of the story is, before signing the contract, involve your accountant as early as possible.

GRIFFITH: The best success story has nothing to do with business and everything to do with the primacy of integrity and character. While every business school teaches that all business enterprises have an obligation to make a profit (i.e., the “end” result), what is not always clear is that the “end does not justify the means” when the means involve illegal, unethical, or otherwise destructive actions or activities.

The best success story has nothing to do with business and everything to do with the primacy of integrity and character.

ALAN GRIFFITH

 What are common difficulties that you are observing and what have you learned from them?

DUBAN: The two biggest challenges that our clients face are obtaining sufficient capital to operate or expand their businesses and obtaining new high quality employees to manage and operate their businesses. Bank financing is challenging to say the least and even though there is increased unemployment, extraordinary employees are difficult to find. In terms of financing we have learned to be patient with banks, to provide ALL of the information that they request as efficiently as possible and to work closely with them to insure financing becomes available. We offer to meet with them personally, to continually follow up on requests, show more information than was required previously and understand that they are also in business to make a profit so there is a price to pay for expansion capital. Further we have learned to operate in a new regulatory environ-

ment, understand the banks' point of view and provide information that will assist them in compiling their files and satisfying their board and auditors. Finally, we have learned how important it is to retain quality employees by offering significant benefits and compensation knowing that they are in demand and that it is an extremely competitive time for employers to attract quality employees. This has been a challenge with often decreasing revenues, but clients and customers appreciate consistency in service and the compensation may just need to come from the bottom line initially in order to remain competitive. High quality employees that interact well with customers and client help them to feel safe in a very difficult environment. This might be considered counterproductive to cash flow and budget constraints, but it is of paramount importance.

 How has international commerce impacted your local client businesses?

ANIK: International commerce has become an increasingly important area for our clients' growth. While international expansion has historically been a big-company dominated strategy, we are seeing more small and mid-sized companies expanding operations outside the U.S. Many foreign markets have experienced higher growth than the U.S. over the past five years, and with the weak U.S. dollar, products manufactured domestically continue to be attractive to foreign companies. Additionally, we've seen clients establish their own manufacturing or distribution activities abroad to take advantage of consumer buying power. Over the last two decades, low cost labor was a major factor driving


companies overseas, with most or all of their production re-exported back to the U.S. Now, companies are looking to sell their products in the foreign markets, creating new challenges and opportunities for U.S. management.

GRIFFITH: If a business is not involved in international commerce – get involved! If a business is involved with international commerce - get more involved!

Becoming multi-national involves many “moving parts,” but a properly trained and experienced CPA will help overcome obstacles and maximize positive results by, for example, making introductions to local-jurisdiction advisors, advising on the proper legal entity struc-

Over the last two decades, low cost labor was a major factor driving companies overseas ... Now, companies are looking to sell their products in the foreign markets, creating new challenges.

JOEL ANIK



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ture, and assisting with recurring issues - like transfer pricing and proper reporting.

VAN DER WELL: We are routinely seeing companies in the local marketplace being impacted by the world economies whether that is through sourcing of products, establishment of manufacturing facilities or the distribution of their products. This has created enormous complexities for our clients in terms of the impact of establishing residency in foreign countries, the ability to obtain financing for foreign operations, developing a plan to move profits across country borders, and setting up tax structures that will minimize their overall tax burden across all countries. This complexity has required us to develop an international organization that is seamless in the delivery of client service to our customers, expand our understanding of how to establish businesses in many of the major economies of the world and to understand the impact of international operations to the domestic tax and business operations of our clients.

LEAPER: RBZ has been servicing the local Los Angeles community for well over 35 years, but it has really been only in the past five to ten years that international commerce has significantly affected our clients. This has affected the way we service them.

As one example of how things have changed, RBZ was founded as a firm catering to the real estate business, and to this day real estate represents a large percentage of our client base. However, until recently, international commerce

really didn't affect this group of clients at all; they invested in local real estate, with local investors, and worked with local financial institutions.

As the world's information has become easier and inexpensive to gather, real estate investment opportunities for our clients have expanded significantly. Even smaller real estate investors have benefitted. Now it is common for our mid-size real estate clients to work actively with foreign investors and financial institutions to hold properties locally and abroad.

But it isn't just our real estate clients or even our larger clients who have benefitted from this internationalization of business; our smaller clients have as well. It used to be that the cost of doing business internationally made doing business cross border unaffordable for smaller companies. However, the cost of international travel and communication (does anyone remember how much per minute it used to cost to dial overseas?) has become affordable. A small local business can easily open and operate a subsidiary in Colombia, source product from China, or buy a rental property in Belgium.

With opportunities like these there come complexities and challenges. We now have a dedicated group of professionals within RBZ who assist not only our larger international businesses and the people who run them, but also our long-standing clients who wish to take advantage of international opportunities out there without getting held back by any of the tax or accounting issues surrounding them.

We are routinely seeing companies in the local marketplace being impacted by the world economies ... This has created enormous complexities for our clients.

TODD VAN DER WELL

 **What are you doing to prepare your clients for the IFRS* and how do you think it will affect their businesses?**

GRIFFITH: Educating and translating. IFRS is the "future language" of business and clients must attain fluency.

VAN DER WELL: Within our client base, we have been dealing with the adoption of IFRS since 2003 and have a team of experts who routinely deal with the IFRS and US GAAP differences. Through this knowledge base, Moss Adams is IFRS-ready and, as we've done for many clients, we can help companies successfully transition from U.S. GAAP. Our international specialists work closely with our clients to examine all the ramifications IFRS can have on our client's financial reports, from vendor contracts to employee benefit plans to incentive compensation.

ANIK: Many of our clients are asking for guidance on how they should move forward given the uncertainty surrounding IFRS. The decision of how they move forward really depends on

how proactive the client chooses to be. We educate clients on the aspects of IFRS that they need to consider so that they can take steps now to make the process more manageable in the future. For example, if a client is preparing for an accounting system change, it's worth the extra time to consider whether or not this system will work for both U.S. GAAP and IFRS. But even companies that are less proactive are focused on how the FASB and IASB's convergence projects related to leasing, revenue recognition and other key areas may impact their business. Both U.S. GAAP and IFRS convergence projects and full conversion to IFRS will result in vast organizational changes for companies. This is true not only in the application of accounting standards, but also relating to critical accounting processes, the control environment, software and system needs, training and resource needs, and contractual obligations.

International Financial Reporting Standards is the 'future language' of business and clients must attain fluency.

ALAN GRIFFITH

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Joe Torre

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 What Federal/State regulations have the most significant impact on your clients' businesses? Why?

GRIFFITH: All regulatory efforts share the goal of "righting" a perceived wrong. Query whether it is most effective to fight it, or to find ways to work (profitability) with it.

DUBAN: As we are primarily a tax practice, our experience is from the point of view of income, franchise, payroll, sales, property, city business and other tax regulations. The tax structure continues to become more complicated and it garners a greater share of a company's resources as new ways to raise revenue are implemented. As income taxes continue to take more resources, our clients are forced to look at all possible ways to reduce the

burdens and they rely on us to keep up with new reporting regulations and opportunities. City business taxes that are based on *gross* revenues and not *net* income do not help when a client is already losing money and is still forced to pay a significant portion of his revenues to do business in Los Angeles. New State Board of Equalization enforcement of use taxes on out of state purchases and increased enforcement of foreign account reporting have considerable impact on clients and not only can increase tax burdens increase, but they can also increase the dollars clients must dedicate to us in fulfilling their tax reporting requirements.

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DENNIS DUBAN

 What issues keep your clients up at night?

KRAJANOWSKI Issues keeping clients up at night include California's economic recovery. As the unemployment rate remains especially high for non-skilled labor, and across the board in certain industries like construction, this has a direct impact on consumer spending.

Another issue clients are concerned with is State and Municipalities' rules, regulations and fees. As governmental agencies scramble to post results to justify their current staffing levels, budgets, and in some cases their existence, clients are left with the daunting task of navigating through these tough times with little empathy from government.

SACHS: Our clients are fearful of what they don't know. Have they made the best strategic decisions to weather the next phase of the economy? If there is a second dip, do they need to make more drastic changes? How do they find new

markets or products to increase margin? Where do they get the capital to invest in new technology or necessary capital expenditures? Where are interest rates going? And for many business owners trying to solidify their short- and mid-range strategic succession plans, how will capital gains and ordinary tax rates change? And what will the estate rules look like in 2013 and beyond?

Many are fearful of relying on credit. We've seen clients with exceptional credit performance not be able to take advantage of extraordinary financing opportunities because of the impact of regulation on business credit. There is significant liquidity in the market but the cost of non-bank capital is high, forcing clients to work harder for less return. With the abundance of Federal and State regulations pending, including healthcare, there is still significant uncertainty, and it's causing paralysis at all levels.

Our clients are fearful of what they don't know. Have they made the best strategic decisions to weather the next phase of the economy?
SCOTT SACHS

 What do you anticipate is the next big compliance-driven event?

SACHS: Beyond IFRS, which has enormous impact, compliance relating to the proposed lease capitalization, financial statement presentation, and other accounting rules will require concentrated client support. Individually or combined, these rules will recast the way financial statements are presented and will have a significant impact on accounting systems design, reporting, financial contracts, and taxes.

 How does a company plan for tax changes given the state's political landscape?

KRAJANOWSKI: Planning for tax changes in today's political environment can be tricky. With a mounting state deficit, the California legislature generally will look to either raising taxes or cutting back on state employees and/or their benefits. The latter is more difficult due to the influence of labor unions. Therefore, businesses should plan for an increase in taxes either at the business and/or individual level. In fact, a significant amount of businesses operate through pass through entities such as partnerships

(including LLC's) and S corporations in which the individual pays the tax on the profits of the business. Businesses can pay the increased taxes as a cost of doing business in the state or look to alternatives such as moving the business to a friendlier state, converting a pass through entity into a C Corporation (assuming the tax rate at the corporate level is less than the individual level which is currently the case) and/or outsource part of its operations to countries with an educated workforce that are business friendly such as

Success usually comes
to those who are **too busy** to notice.



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India and the Philippines. There are costs associated with any decision, however, as California is one of the highest taxing states in the nation, the cost of change becomes less than the cost of doing nothing.

ANIK: Companies benefiting from California Enterprise Zone hiring credits should think about accelerating the vouchering process to perfect the credit from prior years. Governor Brown has proposed significant limits to vouchering on a lookback basis. Also, companies should watch for potential mandatory single sales factor apportionment for California income tax purposes. An effort is underway to take away the single sales factor election in favor of requiring all taxpayers to use that method.

DUBAN: Typically, a company tried to plan for increased taxes by considering tax reduction opportunities, prudent tax planning and by taking advantage of legislated tax benefits. Now, with significant economic issues and government budget deficits in California threatening the economy and warranting tax increases, businesses must look at whether it is feasible to remain in California or relocate to a state with a more favorable tax structure. The costs of moving are no longer as prohibitive as the taxes of remaining, and although moving was not formerly in the vocabulary of business owners and advisors, it is now, with so many states offering incentives that outweigh the costs of relocating businesses. If taxes continue to increase exponentially, businesses must be prepared to move.

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JOEL ANIK



How should companies evaluate their accounting firms?

ANIK: With the recent economic conditions and increased capacity within the accounting profession, there has been a focus on fee reduction that has had many companies using price as a primary (and sometimes sole) criteria for selecting a firm. While competitive fees are important, companies would be well served to consider additional criteria that ultimately contribute to value such as: cultural fit, growth stage, business complexity and industry.

An entrepreneurial company won't necessarily be well served by a firm that focuses on working with mature well established organizations. A company considering an exit strategy should seek to work with a firm that enjoys a strong reputation in the capital markets. Complex international issues are best addressed by a firm capable of coordinating consistent service delivery in the geographies where a company is operating or looking to expand. When a firm has deep experience in an industry, they not only know how to address a company's unique accounting issues but will bring additional ideas and recommendations based on the industry best practices.

When a firm is a solid match for a company and is committed to delivering quality service, clients receive much more than basic compliance services, they have a trusted advisor on their side. A good fit makes for a more efficient approach to service delivery and reduces the time and stress on the company's staff. With relevant and current experience dealing with the issues, companies can expect very prompt and reliable answers to their toughest questions.

Beyond all of this, the right firm will be perceived as a resource for a client's

success and not simply another overhead item. Commonly stated, Benefits - Cost = Value. From this perspective, price becomes a fraction of the value equation.

LEAPER: The services provided by accounting firms are often viewed as commodities. Your accounting firm could, and should, be much more than that. To get the most out of this essential business relationship, look to your accounting firm's industry expertise, professional relationships, and its people to gauge the value you receive.

Rather than engaging a firm that wants to be everything to everybody, emphasis should be placed on retaining a firm that has identified specific industry niches where their knowledge and experience runs deep. Firms of this nature will be able to provide valuable advice as it relates to your business, and ultimately your bottom line.

Your accounting firm should have well developed networks of professionals and specialists to call on when the need arises. It may sound cliché, but business is all about who you know. Access to sound relationships is a valuable asset that a reputable accounting firm can provide to your company.

As for people, let's face it, accounting, along with most businesses rely heavily on human capital. Companies should attribute value to their relationships with their Firm's partners and engagement team. Check out the culture of your accounting firm. Is turnover high? Does it attract quality professionals? Does this impact the client service you receive? You'd be surprised how much value this adds to your engagement.

The services provided by accounting firms are often viewed as commodities. Your accounting firm could, and should, be much more than that. To get the most out of this essential business relationship, look to your accounting firm's industry expertise, professional relationships, and its people to gauge the value you receive.

THOMAS LEAPER

Thanks to all the participants!



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