

# KAKIMOTO & NAGASHIMA LLP

CERTIFIED PUBLIC ACCOUNTANTS  
CONSULTANTS

## NEWSLETTER

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### Inside this issue:

Summary of Articles	1
Reducing Costs. Improving Performance. Outsourcing: a Definite Option.	2
New Regulations for Submitting Form W-4 to the IRS	3,4
Will the Real John Doe Please Stand Up?	4



### Any Questions?

We are committed to providing our clients with quality and excellent services. If you have any questions or comments, please let us know by either e-mail or phone. Our company profile is available on the internet at:

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## Summary of Articles

### The Possibility of Outsourcing

Today, the demand for accurate and prompt financial information is enormous; both internal financial processes and external reporting requirements must be addressed. Big Four/large CPA firm fees are on the rise. Moreover, to survive in an intensely competitive market, a company must also focus on its strategic efforts which includes soliciting additional support from its finance department. How does a company cope with the added pressure? In this issue, we discuss outsourcing possibilities and the potential support a smaller CPA firm can provide.

### Form W-4 (Employee's Withholding Allowance Certificate)

New temporary regulations for submitting Form W-4 were issued on April 14, 2005. The temporary regulations eliminate the requirement that employers submit copies of potentially questionable Form W-4s. In this issue, we discuss Form W-4, the contents of temporary regulations, and commonly asked questions regarding form W-4.

### Identity Theft

Millions of Americans now have a new reason to dread the mailbox. In addition to the tried-and-true collection of Letters You Never Want to See -- the tax audit, the high cholesterol reading, the college rejection letter -- there is now the missive that reveals you are on the fast track to becoming a victim of identity theft. Someone may have taken possession of your credit card info, Social Security number, bank account or other personal data that would enable him or her to go on a permanent shopping spree -- leaving you to deal with the financial, legal and psychic bills.

The Internal Revenue Service and Treasury Department has announced that the optional standard mileage rates has been increased for the final four months of 2005. The rate increased to 48.5 cents a mile for all business miles driven between Sept. 1 and Dec. 31, 2005. This is an increase of 8 cents from the 40.5 cent rate in effect for the first eight months of 2005, as set forth in Rev. Proc. 2004-64.

## Reducing Costs. Improving Performance. Outsourcing: a Definite Option.

**T**oday, the demand for a company to balance and control its internal financial processes with external reporting requirements is enormous. Due to the transformation of the public accounting industry and related fee restructuring, it is imperative that a company evaluates alternatives to achieve lower overall professional fees and staffing costs. Whether a company is public or non-public, the "Big Four" and national/large firms conduct a significant number of audits. Although the Sarbanes Oxley Act (SOX) requirements are only required for public company audits, the whole accounting industry has been affected. Due to their reputation and recent notoriety, the Big Four and larger firms are subjected to increased amounts of scrutiny by just about everyone; strict compliance with recent regulations and policy changes are pushed down to all areas in their practices. In accordance with Big Four/large firm policy, certain "nonaudit" work once considered as part of the audit is being severely curtailed, while higher audit fees are being charged. Are your auditors not able to provide you with the same trusted services as before? Not enough financial and accounting staff to take on the new requirements and processing of information? Several of the new requirements can be intimidating and difficult to implement. Coupled with the loss of guidance and advice you have once received from your auditor, one may feel overwhelmed and confused. Bring in another CPA firm to deal with the overload. Many smaller CPA firms have the requisite expertise and knowledge to assist your company in these areas while streamlining your processes and charging lower fees.

SOX prohibits CPA firms from providing "nonaudit" services to their public company audit clients. Presently, nonaudit services consist of:

- bookkeeping or other services related to the accounting records or financial statements of the audit client
- financial information systems design and implementation
- appraisal or valuation services, fairness opinions, or contribution-in-kind reports
- actuarial services
- internal audit outsourcing services
- management functions or human resources
- broker or dealer, investment adviser, or investment banking services
- legal services and expert services unrelated to the audit

Since the SOX passage, fees charged by external auditors have continued to increase by double digit percentages. In 2004, a marked increase in audit fees was due to the implementation of SOX "Section 404" requirements (financial control audits). On top of that, a public company incurred substantial costs in other areas associated with Section 404 compliance. Before the enactment of SOX, audit fees were usually kept to a minimum because the auditing firm had the opportunity of securing other lucrative services from their audit clients. Public com-

pany audit fees are on the rise to compensate for the loss of higher margins related to the now prohibited nonaudit services.

The traditional relationship between public companies and their outside auditors has virtually disappeared. Because of the restrictions placed on outside auditors by SOX, the auditor/client relationship tends to be more adversarial and formal; public companies can no longer consider their outside auditors as trusted advisors.

Internally, financial and accounting staff workloads are increasing; companies may find themselves in a position of being understaffed. Companies should evaluate their internal financial operations structure and consider the possibility of outsourcing certain financial functions. Routine and traditional time-consuming tasks (receivables/credit, payables, fixed asset tracking, etc.) are excellent candidates for outsourcing. Areas that require judgment, strategic and policy-setting should be retained inside. Processes such as budgeting, management report processing and accounting/tax compliance areas can also be explored for outsourcing possibilities. If financial functions are outsourced effectively, companies will benefit from the streamlining of information and quality improvement in transaction processing while realizing cost savings in the long run. Value-added contributions provided by finance/accounting operations management and executives will increase because their time will not be occupied by the day-to-day administration of outsourced operations; management can focus on strategic business support activities.

As discussed in our article "Reducing Professional Fees" (*October, 2004*), to minimize overall professional fees and staffing costs, companies should consider the use of smaller firms to provide what their internal staff cannot undertake or outside auditors can no longer offer:

- Income tax provision preparation and/or calculations
- Transfer pricing studies
- Individual income tax services for executives
- SOX Section 404 compliance services
- Business valuations
- Audit workpaper schedule/reconciliation preparation
- Temporary/permanent finance/accounting staffing and consultation

The use of a smaller CPA firm for the company's staffing requirements and nonaudit services may lead to a reduction of overall professional fees, lower staffing costs and provide for more flexibility. Due to the number of different options and alternatives and varying degrees of service performance please feel free to contact us for further service details.♦

## New Regulations for Submitting Form W-4 to the IRS

**O**n April 14, 2005, the Internal Revenue Service (IRS) issued temporary regulations that provide guidance for employers and employees relating to Form W-4.

### What is Form W-4?

Form W-4 (Employee's Withholding Allowance Certificate) is a form completed by employees indicating the marital status and the number of personal allowances so the employer can withhold the correct federal income tax from the payroll. The employer must maintain the Form W-4 signed by the employee and have an updated form completed by the employee when a status change occurs. Form W-4 is also used by employees who claim exemption from withholding to inform the employer of this status. In order to claim exemption from withholding, the employee must have had no tax liability in the prior year and expect no tax liability in the current year. An exemption certificate is good for the calendar year and a new form must be completed by February 15<sup>th</sup> of the following year to renew the exemption claim.

### **The Purpose of the Temporary Regulations**

The temporary regulations eliminate the requirement that employers submit copies of potentially questionable Form W-4s to the IRS, unless directed to do so in a written notice. At the same time, the IRS has developed a process to use the information reported on W-2 wage statements to more effectively determine that the employees have enough federal income tax withheld from their paychecks.

### Temporary Regulations under Internal Revenue Code Section 3402(f)

Prior to the change, employers were required to submit to the IRS all Form W-4s filed by employees who claimed more than 10 allowances or claimed exemption from withholding while expecting to earn more than \$200 a week in wages. Effective April 14, 2005, employers must submit copies of Form W-4 to the IRS only when directed to do so in a written notice. If the IRS determines that an employee's withholding amount is insufficient, a "lock-in" letter that specifies the maximum number of personal allowances permitted for the employee may be issued. If the employee is still employed by the employer, the employer must give the employee copy of the lock-in letter provided by the IRS to the employee within ten business days of receipt. If the employee is no longer employed by the employer, the employer must notify the IRS in writing. The employer must withhold tax in accordance with the lock-in letter as of the date specified in the lock-in letter, which is no earlier than 45 days after the date of the letter. Before the lock-in rate becomes effective, the employee will have an opportunity to submit for approval to the IRS a new Form W-4 and a statement supporting the claims made on the Form W-4 that would decrease federal income tax withholding. An em-

ployer cannot decrease the withholding amount once a lock-in rate is effective. Employers will be subject to penalties if it fails to follow the IRS's lock-in instructions.

### Commonly Asked Questions Regarding Form W-4

#### **When does a Form W-4 become invalid?**

Any unauthorized change or addition to a Form W-4 will cause the form to be invalid. If an employer receives an invalid Form W-4, the employer must request another Form W-4 from the employee. Until the employee furnishes a valid W-4, the employer must withhold from the employee as from a single person claiming no exemptions unless a prior W-4 Form is in effect.

#### **What happens when the number of allowances changes during the year?**

When a change in the number of personal allowances occurs during the year due to events such as marriage or the birth of a child, the employee may file a new Form W-4. If the number of allowances decreases, a new Form W-4 must be provided to the employer within 10 days of the change.

#### **What happens when the employee submits a revised Form W-4 after the effective date of the "lock-in" letter from the IRS?**

If an employee submits a new Form W-4 that decreases the amount of withholding after the effective date of the lock-in letter, that Form W-4 must be disregarded. However, if the new Form W-4 claims a number of personal allowances less than the maximum number specified in the lock-in letter increasing the withholding, the employer must base the withholding on that W-4.

#### **What should the employer do if an employee submits a valid Form W-4 that appears to be claiming an incorrect number of personal allowances?**

The employer should withhold federal income taxes based on the number of personal allowances claimed on the Form W-4. However, the employer should inform the employee that the IRS may require the employer to withhold income tax for the employee at the proper rate if it determines that the withholding is not adequate. In addition, the employee should be advised that once this occurs, the employee will not be allowed to decrease the withholding without the approval of the IRS.

#### **State Implications of the New Federal Form W-4 Rules**

States have their own rules regarding withholding allowance certificates, so it is important to review the applicable state rules. In the case of California, employees must complete Form DE 4 (Employee's Withholding Allowance Certificate,) rather than Form W-4, if (1) the federal and state information differs for the marital status, number of regular allowances, or the additional dollar amount to be withheld for income tax, or

*(Continued on page 4)*

(Continued from page 3)

(2) additional state allowances are claimed for estimated deductions. An employer is required to send a copy of Form DE 4 to the state with Form DE 6 (Quarterly Wage and Withholding Report) if an employee claims more than ten withholding allowances on Form DE 4.

The effective date of the above change is April 14, 2005 and expires on or before April 11, 2008. ♦



## Will the Real John Doe Please Stand Up?

In the course of a busy day, you may write a check at the grocery store, charge tickets to a ball game, rent a car, mail your tax return, change cell phone providers or apply for a credit card. Chances are you don't give these everyday transactions a second thought. But an identity thief does. It's the fastest growing crime in America, costing \$53 billion last year. Some 50 million identities have been compromised or stolen in the last six months alone. So how can you protect yourself from these cunning thieves?

Over the past four years more than half a million identity theft victims have filed complaints with the Federal Trade Commission (FTC) indicating that they have a digital imposter. A recent study indicated that 9.3 million people were victims of the crime last year. In all, a number that averages out to one in every 23 consumers. These numbers are quite alarming because identity theft is a serious crime. People whose identities have been stolen can spend months or years - and their hard earned money - cleaning up the mess thieves have made of their good name and credit record. In the meantime, victims may lose job opportunities, be refused loans, education, housing or cars, or even get arrested for crimes they didn't commit.

Nearly all financial institutions now allow their customers to gain access to their accounts over the internet. And why not,

considering how easy it is to pay your bills with only a few mouse clicks? But it also puts vital personal information onto an easy-access medium. Gaining access to these services would be a dream come true for the hearty criminal. The days of "dumpster diving" have evolved to the technologically advanced method of hacking passwords over the internet in order to gain access to your personal information. Determined hackers and identity thieves are constantly probing for our names, dates of birth, credit cards, Social Security numbers, bank accounts, pin numbers and passwords.

An E-mail scam known as "Phishing" is proven to be another scheme the thieves would use. Disguising itself as a legitimate E-mail from known sources such as PayPal or Bank of America, it tricks the unsuspecting consumer to literally hand over login information for the websites of these institutions. You are sent to a bogus website, that almost identically mimics the genuine one, and asked to supply supposedly lost or outdated personal information. The thieves log this information and use it to their advantage.

Here are ways you can protect yourself:

- Use longer passwords and ones that combine numbers, letters and punctuation.
- Do not use the same user name and password for all your online needs. Mix it up a little and do not keep anything consistent.
- If you log into newspaper sites, recipe sites or other sites that don't have any kind of critical components, you should use a fake name and address.
- Remember that all financial institutions will **never** ask for your login information via E-mail.
- Do not use public computers when using these types of services.
- Being smart about who you give your personal information to is the best advice for all to use.

It may mean more work, trying to remember more passwords, but it will also lead to more protection for you and your identity. ♦

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