

# THE AMPER review



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## SOX 404 DELAYED AGAIN FOR NON-ACCELERATED FILERS

Public companies that are non-accelerated filers felt some breathing room when the Securities and Exchange Commission (SEC) voted to delay, for an additional year, the compliance date for Section 404 of Sarbanes-Oxley at its September 21 meeting. The delay includes foreign private issuers that are not accelerated.

As stated in the SEC Advisory Committee resolution, this third delay was issued for a number of reasons, including the overall cost of compliance, complexity of the process, and new guidance. The Public Company Accounting Oversight Board (PCAOB) and SEC's releases guide companies through the Section 404 process based on the first year process and the Committee of Sponsoring Organizations of the Treadway Commission

is expected to release additional guidance in the future.

During May 2005, the PCAOB issued a Policy Statement and Staff Questions and Answers, discussing some of the issues raised during the first year of auditor's implementation of PCAOB's Auditing Standard No. 2. Many of the issues addressed were raised at the SEC's Roundtable on Implementation of Internal Control Reporting Provisions, held during April 2005.

The Policy Statement considered the auditing practices used in the first year of implementation that may be ineffective or inefficient in meeting the objectives of Auditing Standard No. 2 and issued guidance to make audits of internal controls more effective and cost-efficient through inspections of registered public accounting firms. At the Roundtable, investors expressed strong support for Section 404 goals but companies found the requirements costly and demanding. They also questioned if the benefits are worth the cost. At the conclusion, the PCAOB board decided to issue additional staff questions and answers to clarify provisions in the standard to reduce costs. Specifically, auditors should:

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## WEIGHING YOUR ENTITY OPTIONS

One of the most important decisions a new business owner will make is under what form of legal entity their business will be conducted. The term “Choice of Entity” is what a lawyer refers to when deciding on the legal form of a new business. Most new business owners are aware of corporations (C-corporations) and partnerships as the two most traditional legal entities. However, over the years, the list has grown longer to include limited partnerships, limited liability companies and Subchapter-S corporations.

With the exception of a regular (or general) partnership, all of the mentioned entity choices share a common goal: to help the owner limit personal liability exposure. Why is this so important?...because, depending on the choice of entity, an owner can be liable for tortious (think slip and fall) injuries caused by the business. Keep in mind that no type of liability-limiting entity can protect an owner’s personal assets from liabilities related to his or her own professional errors and omissions or tortious acts.

In addition to liability issues, business owners want to minimize their taxes. The differences among the entities can yield significantly different tax results. This article will deal with some of the more significant considerations in choosing the type of entity in which to conduct one’s business.

### C-Corporation

A C-corporation is an independent legal entity, existing apart from its shareholders, officers and directors. With a C-corporation, you do not get the “flow-through” tax benefits that all other small business entities enjoy. What this means is that the profits and

losses of the company are taxed at the entity level, not at the shareholder’s level. The C-corporation will have to file a tax return and pay taxes on the income it receives. Then, if there are any dividends to be paid to the owners, those owners will have to pay taxes again on the money received as dividends. This is the double taxation of corporations that so many shareholders grumble about. There are ways, however, for small corporations to avoid the double taxation of income. Often, a small corporation will pay its owners salaries rather than pay dividends, so the corporation gets a deduction for the amount paid to shareholders. But the IRS watches such salary payments very closely and considers unreasonable compensation as non-deductible dividends. Not surprisingly, startup businesses rarely adopt the traditional corporate format.

### S-Corporation

An S-corporation is a hybrid between partnerships and C-corporations. S-corps are formed exactly like a C-corp and have a very similar structure. There are shareholders, by-laws, articles, stock, etc., just like a C-corp. But the tax treatment of the S-corp is markedly different from that of the C-corp. Unlike a C-corp, income and losses of an S-Corp are generally attributed pro rata to the owners. This means that there is no “double taxation” of corporate income like there is with a C-corp. Another advantage to

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“A careful choice of entity analysis at the outset will help avoid costly problems later.”



## ENTITY OPTIONS

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an S-corp is the lower tax rates. That is, when an S-corp's income is distributed, it will be taxed at the rate of the individual owners, rather than the higher rate applicable to C-corps.

### General & Limited Partnerships

Partnerships consist of two or more partners. Each partner in a general partnership carries unlimited personal liability for the obligations of the partnership. Each partner has complete and equal managerial control over partnership affairs unless there is a partnership agreement stating otherwise. Partnerships are often cheaper to maintain than corporations. Partnerships do not have to take minutes detailing their actions like corporations, nor do partnerships pay taxes (the partners pay taxes individually on the income they receive from the partnership). There are no directors, officers, etc., just the partners. That's the good news. The bad news---each general partner in a general partnership has personal liability for all of the partnership debts. In addition, general partners are jointly and severally liable for the tortious acts of co-partners who are acting within the scope of the partnership business.

A special type of partnership is the limited partnership. Limited partnerships have one very large advantage over the general partnership: limited partners do not take on personal liability for the obligations of the partnerships; they are only liable to the extent of the money contributed to the partnerships. The general partner in the limited partnership, however, retains all of the personal liability for partnership debts that one finds in the general partnership entity.

Why use it? The limited liability partnership is often attractive to entrepreneurs because they can retain control of the business by acting as the general partner, while still being

able to offer limited partner investors the tax benefits of a tax flow-through entity. But with Limited Liability Companies offering the same benefits without requiring a general partner, limited partnerships are becoming less common.

### LLC

The main advantages of Limited Liability Companies ("LLC") are the protection the LLC owners receive from business creditors and the fact that, unlike a limited partnership, the owners (referred to as members) can still participate in the management of the business. The LLC has one very large advantage over the general partnership: members of an LLC do not take on any personal liability for the obligations of the LLC and they are only liable for debts of the LLC to the extent of their investment in the LLC. Additionally, there is no requirement that there be a general partner who retains personal liability for the LLC debts that one finds in limited partnership entities.


The LLC enjoys the same "flow-through" tax treatment that partnerships and S-corporations do. The rules concerning capital accounts, contributions and other basic partnership taxation principles apply to LLCs as well. In short, this means that although LLCs (other than single member LLCs) must file a tax return, the LLC owners report income and pay the taxes owed on such income using their personal tax rates. A downside is that, unlike a C-corporation, an LLC (like partnerships and S-corps) cannot retain earnings without the owners of the business having to pay income taxes on those earnings.

### State Taxes

You should also be aware that some states impose a tax and/or fees on each of the above types of entities. You should check with your tax advisor to make sure you

minimize your company's overall tax liabilities.

### Summary

This general information just scratches the surface regarding this topic. It is important to coordinate these matters with your accountant and attorney when deciding your business entity type. Have your professional team compare each entity form's pluses and minuses, paying special attention to different industries, which may also affect the choice. Doing a careful "choice of entity" analysis and taking the appropriate steps at the outset will help avoid costly problems later. Many factors influence these decisions including both federal and state tax considerations. 

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## PLANNING & FINANCIAL CONCERNS OF DIVORCING COUPLES

**W**hy is it important for you to understand the basics of divorce law?

While divorce is certainly a time of emotional turmoil, it's a time of financial upheaval as well. The financial change brought about by divorce can be particularly devastating to families with children and to older couples who have assigned the career duties to one spouse and the homemaking duties to the other.

When seeking a divorce, you should become familiar with the major topics: marital property versus separate property, alimony, investments, debt, retirement plans, property settlement, taxation, budgeting, legal fees, and, if you have children, child custody and child support. You should also consider risk management, and, if you're older, Social Security.

By becoming knowledgeable about these areas, you can provide your attorney (if any) with a complete and accurate outline of your wishes regarding the divorce settlement, and you will be able to make an informed decision before signing your divorce agreement.

property may be classified as either separate property or marital property, but again, these definitions will vary depending on your state. Therefore, it's important for you to know how your state classifies property. For example, one state may mandate that separate property consist of gifts, inheritances, and property owned prior to the marriage, and that such items will not be divided between the spouses in the event of a divorce. Another state may proclaim that all property owned by the couple is marital property, subject to division at divorce--it doesn't matter who inherited what.

### **What should you know about child custody, child support, and alimony?**

When parents separate and divorce, one of the most emotionally charged issues involves the decision regarding who will live with the children. Determining the extent of child support, and possibly the necessity for enforcement of child support payments, is also cause for stress.

Child custody is based on a number of factors. Most judges place primary importance on the best interests of the children. Custody may be classified as physical or legal, and can be awarded to one or both parents.

Most states have child support guidelines for determining the amount of child support to be paid. Child support orders can be modified when there's a substantial change in circumstances, and most states provide a number of methods for collecting unpaid support.

Alimony is also an important topic. Alimony is based on one party's need and the other's

### **How is property classified for divorce purposes?**

Assets are divided in accordance with state law, so it makes a difference whether you live in a community property state or an equitable division state. Within these two categories of states,



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# DIVORCING COUPLES

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ability to pay. Deciding whether a spouse should receive alimony (and, if so, how much) is based on certain criteria, which can vary from state to state.

## What should you know about property division?

Property division is a complex area, encompassing such subtopics as the marital residence, debt, and retirement plans and Qualified Domestic Relations Orders (QDROs.)

It also involves a number of other areas as well, including: classification and valuation of property, hidden assets, family businesses, and structuring property settlements. The Property Settlement at the conclusion of the divorce will dictate how the assets and liabilities will be divided.

## What should you know about taxation?

If you're legally separated or divorced, it's important to become familiar with the applicable tax rules regarding filing status, dependent children, alimony, and property disposition. Indeed, understanding the tax implications of your initial preferences regarding child custody and property settlement may alter or influence your final decisions.

## What should you know about budgeting and finances?

During the divorce process, both spouses must determine and disclose their monthly income and expense needs. Claims for support (based on need and an evaluation of the other party's ability to pay) often originate from this financial disclosure. It's not uncommon in a marriage for one spouse to assume primary responsibility for the family budget. For some couples, bills are paid when due, but neither party tries to stick to a budget. When two households are

created incident to a divorce, cash becomes tighter and it becomes necessary to develop a budget. A number of tools can be used for this purpose.

We have also found it important to assist one or both spouses in creating a new financial planning framework to make important financial decisions easier after the divorce. Again, it is not uncommon that one spouse to assume primary responsibility for the investment decisions for the family. Given the new situation after the divorce, it is advisable for both spouses to seek the guidance of experienced professional financial advisors.

## What do you need to know about legal fees & professional services?

When seeking a divorce, you'll want to always consider hiring an attorney. Depending on the complexity, you may want to also consider whether an accountant should be hired. If you wish to hire an attorney, you should note that divorce attorneys typically charge hourly rates and require you to submit retainers (lump sums) up front. These fees can be less expensive or more expensive, depending on the complexity of the case, the reputation and experience of the divorce attorney, and the geographic location.


If you're a financially dependent spouse (such as a homemaker), it's possible for a court to award sufficient legal/accounting fees and costs to enable you to retain competent counsel. Upon your submission of an appropriate motion to the court, a judge could order your spouse to subsidize your legal fees for the divorce.

You should also consider the deductibility of divorce expenses. In general, most legal/accounting fees and court costs for obtaining a divorce are considered personal expenses and aren't deductible for income tax purposes. However, you may deduct as a

miscellaneous deduction on IRS Schedule A, subject to the 2 percent floor, any money paid for advice related to the tax consequences of your divorce or securing income. Specifically, deductible items include fees for advice on securing and collecting alimony and the tax consequences of property and payments received. On your legal bill, your attorney should make a reasonable allocation of the legal expenses between tax-related (deductible) and non-tax-related (nondeductible) advice.

## Do you need to know about risk management and Social Security?

Risk management should certainly be considered when a divorce seems likely. The selection of beneficiaries for your life insurance policy will probably be revised, and, in some cases, your health insurance coverage may terminate. Often, for example, one spouse participates in a group health insurance plan at work that provides coverage for both spouses. When a divorce occurs, coverage for the non-employee spouse may end. You need to know what your health insurance options are and how life, disability, and property insurance should factor into your divorce agreement.

Social Security may be an issue if you're an older individual seeking a divorce after a long-term marriage. Be aware that, if you've been married to your spouse for at least 10 years, you may (in certain cases) be able to qualify as a dependent for Social Security purposes. Thus, you might be entitled to benefits, even if you never worked. 



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“Retirement is wonderful. It’s doing nothing without worrying about being caught while doing so.”

## TAX NOW OR LATER: IS THE ROTH 401(K) RIGHT FOR YOU?

The humorist Gene Perret once said, “Retirement is wonderful. It’s doing nothing without worrying about being caught while doing so.” If that is the case, why is it that so many people choose to put off saving for this blissful, Utopian stage of their lives?

The thought of saving for retirement can be daunting, but for most it is inevitable. Experts unanimously agree that retirement should become a primary consideration immediately, given that nearly one-third of all employees feel they will need to accumulate at least \$500,000 in order to live comfortably throughout their retirement. The question that then presents itself is, what vehicle should I invest in in order to offer me the greatest benefit given my particular situation? The answer could lie in the new Roth 401(k) being introduced January 1, 2006.

First, a little background on the subject. The Taxpayer Relief Act of 1997 created the original Roth IRA account. The Roth IRA allows investors to contribute after-tax dollars to the account and allows them to withdraw those funds, tax-free, at retirement. However, the annual contribution limits of the Roth IRA in 2005 are \$4,000 and \$4,500

(the latter for those over 50) and the full benefits of this type of after-tax retirement account are only available to single-filers making up to \$95,000 and married couples making a combined maximum of

\$150,000 annually. Alternatively, the 401(k) retirement account was created by Congress in 1981 and gets its name from, you guessed it, the investment vehicle’s corresponding section in the Internal Revenue Code ... who said accountants weren’t creative? The 401(k) has long-been hailed as the best retirement strategy because it offers the most beneficial tax advantages. This accolade is due to the fact that employees can contribute to this plan through pre-tax dollars, allow their dividends, interest and capital gains to compound throughout their working career, and then pay tax on the full amount at the time of retirement. For better or worse, some intuitive thinking will allow you to see that many people will find themselves in a much higher tax bracket at age 65, as opposed to age 30 or 40, and therefore will be forced to hand over a hefty percentage to Uncle Sam at retirement. Although both investment accounts are prudent and advantageous, they also have their own pros and cons.

In 2006, Congress will implement the new Roth 401(k) provision enacted by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). This plan is formulated to combine the advantages of both aforementioned accounts in order to provide employees with another option. Put most simply, the Roth 401(k) will basically be a traditional 401(k) account that is not bound by income thresholds (as is a Roth IRA), allows for greater annual contributions (also known as “elective deferrals”), and is supplemented with the Roth IRA benefits of tax-free growth and withdrawals. However, this plan will only be available for a limited time; tentatively, the provisions are designed to “sunset” in 2010. This means that your previous Roth 401(k) contributions can

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remain in the plan, but no further after-tax Roth 401(k) contributions could be made after that time. Roth IRA's are not affected by the EGTRRA "sunset rule." Of course, as is the case with many new provisions, Congress could extend this plan at some time in the future if it becomes increasingly popular among individuals and corporations. The Roth 401(k) is open to all employees who qualify for a traditional 401(k), which is a windfall for highly compensated individuals who would otherwise be excluded from holding a Roth IRA account due to income limitations. The maximum aggregate elective deferrals allowed in 2006 will be \$15,000 (\$20,000 for employees age 50 or older). Aggregate elective deferrals include contributions to both traditional 401(k) and Roth 401(k) plans. Money can be withdrawn tax and penalty-free as long as the holder is at least 59 ½ and has held the account for five years.

It is difficult to gauge whether the new Roth 401(k) will catch on among employers. As it stands, employees who work for companies that offer Roth 401(k)'s will have the option of contributing to traditional and/or Roth 401(k)'s, and they will decide what percentage of their total contribution goes into each account. Employers may offer matching contributions in traditional and/or Roth 401(k) plans, but these contributions will continue to be treated as pre-tax contributions subject to taxation when distributed. Many employers have already expressed hesitation about amending their current plans to provide for the new Roth plan due to the perceived headache the additional accounting will cause. Despite the additional costs, if the right marketing campaign was implemented, employees would be persuaded to increase demand for the Roth 401(k) and employers and plan sponsors will undoubtedly feel the pressure to adopt the provision.

So is the Roth 401(k) right for you? It depends. Do you want to pay taxes now or later? The traditional and Roth 401(k) accounts have the ability to yield the same amount at retirement as long as your tax bracket stays the same; however, the Roth option yields a higher return if your tax rate rises throughout your working career, while

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- integrate their audits;
- exercise judgment to tailor audit plans to the risks facing individual audit clients;
- use a top-down approach;
- use the work of others;
- engage in direct and timely communication with audit clients.

According to the PCAOB, using these approaches should provide for improvements in the process and cost reductions in the future. The Q&A portion, issued separately, provides the staff's opinions on the related implementation issues discussed in the Policy Statement. The PCAOB Policy Statement and Q&A can be found at [www.pcaobus.org](http://www.pcaobus.org).

The SEC guidance is from the Division of Corporate Finance and is a staff statement on management's report on internal control over financial reporting. The statement is the staff's views on issues raised in the implementation of Section 404, which was discussed during the Roundtable discussions. The statement addresses the following areas:

- the purpose of internal control over financial reporting;
- reasonable assurance, risk-based approach, and scope of testing and assessment;
- evaluating internal control deficiencies;
- disclosures about material weaknesses;
- information technology issues;


the traditional accounts will have a better pay off if your tax rate declines. Regardless of whether you view having money as more important now or later in life, it is crucial not to underestimate your future needs due to neglect or shortsightedness. Taking a hard look at your retirement planning options is a necessity. 

- communications with auditors;
- issues related to small business and foreign private issuers.

The SEC makes it clear that the principle of the guidance is the responsibility of management to determine the scope and assessment and to test accordingly. The full document can be found at the following site:

<http://sec.gov/info/accountants/staffcreproting.htm>

COSO is continuing to develop an internal control framework for smaller companies. A new framework initially scheduled for release and comments in August, was first delayed until September, but is now delayed until further notice.

Many non-accelerated filers, at a minimum, began the process of assessing internal controls before the delay. For companies that haven't started implementation, begin the process soon. Developing a long-term plan with a top-down risk-based approach will limit the number of controls tested minimizing the cost. For success, the two most critical factors of the project are that senior management, specifically the CEO, is involved and sets the proper tone at the top, and that the company designates, trains and commits qualified resources. The struggle in the first year will be compliance, understanding the requirements, and committing the resources necessary to get the job done. 



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## NEW OFFICERS

Amper, Politziner & Mattia is pleased to announce **new Officers**, Neal Godt and Ed Phillips to the firm.

**Neal K. Godt** CPA is an Officer in the Public Companies Group in the New York office of Amper. Neal has over 20 years of experience in public accounting. He has assisted publicly-held clients with all aspects of SEC reporting, compliance and filings. He has also assisted clients with transactions such as private placements, debt financings and 144A debt offerings. Among the industry sectors Neal has served are fabricated manufacturing, distribution, chemicals, oil & gas, textiles, consumer products, retail, for-profit trade schools, automotive supply and professional services firms. He also has significant experience with US multi-national companies, as well as those based in Sweden, Italy, UK, Japan, Hong Kong, Austria and Switzerland. Neal received his BA in Economics and Accounting from the University of Michigan.



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**Edward A. Phillips** CPA, CIRA, CFE is an Officer in the Insolvency and Asset Recovery Group with over 17 years of professional experience. He provides a wide array of financial advisory and forensic accounting services to clients with a focus on bankruptcy, financial restructurings and liquidations, both in and out of court. Mr. Phillips has represented debtors, creditors' committees, secured lenders and trustees. Additionally, he has acted as a liquidating trustee and a receiver. He is a Certified Public Accountant, Certified Insolvency and Restructuring Advisor and a Certified Fraud Examiner. He is a member of the American Bankruptcy Institute, the Turnaround Management Association, the Association of Insolvency and Restructuring Advisors and the American and Pennsylvania Institute of Certified Public Accountants. 



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