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# FINANCIAL NOTES

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—  
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## Tax Planning??? This Year???

By Harvey McCown, CPA  
Firm Principal

This may be a good year (unfortunately) to consider some tax planning concepts that you may not have considered.

**HARVEST TAX LOSSES** – With the decline in the stock market, you may have some paper losses that could be converted into tax deductions. Price out your portfolio against your tax basis (not the high values of recent times). The loss securities can be sold to generate tax deductions. Those losses can offset capital gains and an additional \$3,000 of regular income each year. Do you have some loss stocks you want to sell anyway? Do you have some gain stocks you would like to sell but are afraid of the capital gains? Harvesting tax losses may help your tax bill and diversify your portfolio. Watch the wash sale rules for loss sales – you cannot buy back the same stock for 60 days – 30 before the loss sale and 30 after. This rule does not apply to sales for gains.

**BUY DEPRECIABLE BUSINESS EQUIPMENT** — Are you considering buying equipment sometime in the next 6 months or so? Consider buying it this year. You can write off up to \$24,000 of the cost on all equipment purchases, plus 30% of the remaining cost, plus the regular depreciation on the balance – all in this year. A \$100,000 purchase could generate a \$58,000 deduction in the first year or a tax savings of \$23,000 (at 40% tax rate). And you do not have to have paid for the equipment this year.

**NET OPERATING LOSSES** – Is your business going to have a loss this year? Could you make it larger by postponing income to next year and accelerating deductions to this year (easiest with cash basis accounting)? If yes, then you can carry that loss back 5 years, deduct it in that earlier year, and get a REFUND!

**GIFT DEPRESSED STOCKS** – You can make gifts to your children measured by the current price and not the potential value (or what it was a year ago and what you think – hope – it will be in the future). Each taxpayer can give \$11,000 (used to be \$10,000) per person per year. The value on the date of the gift is the measure of that \$11,000. Thus, a gift of depressed stocks can pack more future value into that same \$11,000. Watch the tax basis. It is given along with the stock. If you have a capital gain problem (even though the stock is depressed), then you are giving that to your kids also. If the kids sell the stock for a loss, they cannot use your old basis but must use the value on the date of the gift. A depressed gift can lose the loss potential.

**LOW INTEREST RATES** – Consider sales or loans to your children. The interest rates can be locked at today's very low rates. Hopefully your children can use the assets or loan proceeds to make much more than the low interest rates. This additional value will be theirs and not included in your estate.

**ESTATE TAX PLANNING** – Most commentators do not expect congress to ever let the estate tax die. Consider gifting techniques now while values and interest rates are low. Keep in mind the tax basis – a gift gives away your old (low?) basis. Passing it through your estate gets a new basis as of that date.

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# Shoring up Investor Confidence: Corporate Accounting Reform

America's financial markets stand on a foundation of trust in the integrity of reported corporate earnings. When news of fraudulent activities at certain large companies greatly weakened investor confidence this year, Congress and the President responded with a corporate accounting reform law — the Sarbanes-Oxley Act of 2002 (the “2002 Act”) — which was signed into law on July 30, 2002.

## Impact on Business Owners

The requirements of the 2002 Act apply to companies that issue publicly traded securities, their executives, and auditors. Therefore, *privately owned* companies generally are not affected. The new corporate accounting reform does not in any way disturb the relationship between privately owned companies and their accountants. Thus, as long as your business does not issue (and has not registered to issue) publicly traded securities, we can continue to provide you with the same range of services — both audit and non-audit — that we have been providing until now, even if your company has several shareholders.

## New Rules for Public Corporations

Under the 2002 Act, chief executive officers and chief financial officers must certify (based on each executive's knowledge) that each annual or quarterly financial report issued is not misleading and that it fairly presents the company's financial condition and results of operations as of and for the reported periods. Additional certifications regarding the evaluation of internal controls and disclosure of significant deficiencies in those controls also are required.

Companies will have to disclose any material changes in their condition more quickly than previously required. The 2002 Act requires stricter disclosures of transactions between companies and their directors, officers, and principal stockholders. Personal loans to executive officers and directors are prohibited, although a loan existing on July 30, 2002, is “grandfathered” as long as it is not materially modified or renewed on or after that date.

In addition to these changes, the new law provides that each member of a public company's audit committee must be a director of the company and must be “independent.” Essentially, this means an audit committee member may receive only “board-related” compensation and may not be an “affiliated person” of the corporation (such as a company executive).

## New Rules for Accounting Standards and Oversight

The 2002 Act establishes a new five-member oversight board under the jurisdiction of the Securities and Exchange Commission that will regulate the auditing of public companies subject to the securities laws. Only accounting firms that register with the board will be able to prepare or issue audit reports on publicly traded companies. The board will establish auditing standards for the registered firms and conduct periodic inspections of the firms.

During the period when auditing services are being performed for a client company, registered firms will not be allowed to provide the client with certain non-audit services. Among others, these services include: bookkeeping or other

accounting or financial statement services, financial information systems design and implementation, appraisal or valuation services and fairness opinions, actuarial services, and management functions or human resources. Tax services may be provided only if approved by the company's audit committee.

## New Rules To Limit Securities Analyst Conflicts and Provide Notice of Pension Blackouts

The 2002 Act contains provisions intended to prevent conflicts of interests for securities analysts whose firms also conduct investment banking business with a publicly traded company. Additional provisions of the 2002 Act require defined contribution retirement plans to provide participants with advance notice of “blackout” periods — periods of more than three consecutive business days during which their ability to direct or diversify their plan investments will be suspended or restricted. Directors and



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# Staff News

*Welcome!*



**Thomas Hong** joined the firm in August as a Staff Accountant. Thomas graduated from California Polytechnic State University, San Luis Obispo with a bachelors degree in accounting.



**Michael Olivares** joined the firm in September as a Staff Accountant. Michael graduated from the University of California Santa Barbara with a bachelors degree in accounting.

Congratulations to Andrea Hill and her husband Brian on the birth of their daughter Allison Taylor Hill. She arrived on September 9th. Allison has a big brother...8-year old Bobby.



## *The CPA Exam Results:*

Congratulations to **Jaclyn Hall!** She passed all 4 parts!

## 2002 Governmental Client Continuing Professional Education Day

On August 30, 2002 Burt Armstrong, CPA and firm principal, kicked off the 4th annual continuing professional education day. Clients, staff and interested organizations joined the firm for an 8 hour session. Burt first introduced guest speaker



Frank Crawford, CPA. Frank is a Certified Public Accountant practicing governmental accounting out of Oklahoma City, Oklahoma. He led the group through several hurdles of GASB 34 and covered three case studies to show how financial statements become transformed after implementing the new pronouncement.

In the afternoon, Rosalva Flores, CPA - Senior Accountant and Rebecca Thomas, CPA - Senior

Accountant discussed all of the new Governmental Accounting Standards Board pronouncements. Julie Auvil, CPA - Senior Accountant discussed Management Discussion and Analysis and how to include this new section into governmental financial statements. Later Eric Xin, CPA - Audit Manager gave everyone an overview of the Yellow Book updates.

The day was wrapped up with Burt Armstrong's talk on Corporate Governance and the changes in audit standards. With the rise and fall of Enron and communications giant Worldcom, it has meant many new bills being passed into law to assist with controlling fraudulent accounting practices.



**Brown Armstrong Speakers**  
(From the left; Rosalva Flores, Rebecca Thomas, Burt Armstrong, Julie Auvil and Eric Xin)

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## Shoring Up Investor Confidence

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officers will not be able to purchase or sell company stock during blackout periods in which at least half of a plan's participants are suspended from purchasing or selling the stock.

## New Penalties and Safeguards

The 2002 Act increases the penalties for corporate financial fraud and violations of the pension law. Moreover, the new law contains measures designed to protect employees of publicly traded companies who lawfully provide information or assist in an investigation regarding violations of the securities laws or fraud against shareholders. Under the Act, it is against the law to fire, demote, suspend, harass, or threaten such employees.

## Unchanging Commitment

The significant corporate accounting reforms summarized above were enacted in response to the misguided actions of certain individuals in a few firms. You can be confident that throughout this troublesome period, neither our commitment to the highest professional standards nor our tradition of trustworthy client service has changed. You also can be sure that we will continue to provide accounting, auditing, tax, and business consulting services with integrity and the highest regard for your trust in our firm.

## Tax Planning ???

*(Continued from cover)*

### ESTATE PLANNING – MINORITY INTEREST VALUATIONS

– If you own less than 50% of an asset or business, your interest is worth less because of the lack of control and lack of marketability. The IRS is now trying to combine diverse interests to get you over the 50% barrier. A surviving spouse may own 35% of the family business. The marital QTIP trust may own 35% also. Should the two 35% interests be added together to break the 50% barrier and preclude the valuation adjustments for lack of control and lack of marketability? That is the position the IRS is taking and the tax court has agreed. All situations where you have a power of appointment or other control over property or a trust should be reviewed for this concern.

For further information, or if you have questions regarding this article, please feel free to contact one of our professionals at (661) 324-4971.