



# ARKANSAS SOCIETY OF ACCOUNTANTS

RESPECTED ACCOUNTING PROFESSIONALS SERVING OUR COMMUNITIES

## Monthly Newsletter

November 2006

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### • FROM YOUR PRESIDENT'S PEN •



Dear Members,

I am writing this article after completing the 1040 extended filing season. I must confess I didn't do as well this year as in years past. Since the automatic extension form extended the filing deadline to October 16, I fell into the trap of waiting longer than usual to begin filing the extensions. I think the problem was that without that additional extension we previously had to file by August 15, I had no incentive to begin completing the extensions earlier. In the past I would "catch the wave" about July 10 and begin completing as many automatic extensions as I possibly could by August 15. I would usually complete at least two-thirds of my extensions. Then about September 10, haunted by the fact that October 15 was fast approaching I would dive into completing the additional extensions. This year I failed to "catch the wave" in July and you know the rest of the story. I wonder if I am the only one who fell into this trap. By the way, I took the final extended tax return down to the wire. Taxpayers got their information to me in mid-afternoon on the 16th and I completed it at 8:00 pm on the 16th, got the taxpayers' signatures on forms 8453 and AR8453, and transmitted the return at 8:15 pm. Believe it or not, the taxpayers had a refund coming. Just think, they could have already received that refund if they had gotten their information to me during the regular filing season, and I would have gotten

home by 5:00 pm (well, maybe 6:00 pm).

I've already devised a plan to avoid the onslaught of preparing those extended returns in such a short time next year. I'm thinking that I'll select a month between April 15 and August 15 and prepare two-thirds of my extended returns. Then, about September 10, I will begin completing the remainder of the extensions. Wait a minute, that sounds like the old plan. Maybe the old plan wasn't so bad after all.

With the 2005 filing season behind us it's now time to get ready for the 2006 filing season. It's time to get into the "tax mode" before the filing season begins. One of the best ways to get into the "tax mode" is to attend a Gear Up 1040 tax seminar. If you want to get into the mode early, you can attend the seminar in Little Rock on November 16 and 17 at the Little Rock Hilton. If you want a few more days before getting into the mode, you can attend the seminar in Springdale on November 30 and December 1 at the Holiday Inn.

Select one of those seminars and join the "elite crowd" of tax practitioners for the fast approaching 2006 tax filing season.

Have a happy Thanksgiving. We have much to be thankful for.

Ronny Woods, PA  
President, ASA

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## Significant Developments in Tax Preparer Cases

An Everett, Washington tax fraud promoter was sentenced to 35 months in prison, the Justice Department and Internal Revenue Service (IRS) recently announced.

In other cases, a federal court in Arizona permanently barred a preparer from promoting a tax scheme that used business trusts and LLCs to disguise personal expenses as business expenses. And in the sixth injunction obtained against preparers

claiming the so-called mariner's deduction, a Louisiana court barred a couple from preparing tax returns asserting unrealistic positions.

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## Inside the IRS

Refund opportunity. There's an amended return opportunity to get a refund of tax paid on awards for damages for personal, non-physical injuries. A recent decision in the US Court of Appeals for the District of Columbia (Marrita Murphy, No. 05-5139) held that damages received for emotional distress and injury to personal reputation are not subject to income tax, and that Section 104(a)(2) of the Tax Code, which makes these damages taxable, is unconstitutional. Money damages received for loss of earnings or punitive damages are still taxable. Caution: The IRS is expected to appeal this case, but amended tax returns should be filed to protect the right to receive a refund.

**Private collection agencies.** Now that the IRS has outsourced a portion of its collection work, a private debt collector may contact one of your clients. Limits: These collection agencies can only negotiate installment payment agreements of up to \$25,000 and 36 months. Good news: A private collection agency cannot

issue a summons for financial information and cannot make third-party contacts – with your bank, employer, or neighbors for example. Strategy: You may have an easier time getting an agreeable installment plan with a private collection agency since they're paid a commission on anything they collect, whereas the typical IRS collection employee has no financial incentive to let you pay off your liability over time.

Note: If you can't or won't accept an agreement with the private agency, your case gets sent back to the IRS, which will then pursue collection in the normal manner.

What special agents want to know when they contact a tax preparer. One of the most important witnesses in a criminal case against a taxpayer is the person who prepared the tax return. The preparer generally has in his/her possession work-paper files that contain originals or copies of financial documents and handwritten notes. The special agents will summons these to obtain evidence of criminal conduct, looking for proof of intent to evade the payment of tax by underreporting income or hiding assets. Advise for tax preparers. Before agreeing to talk to a special agent, as for a summons for the requested information. If the IRS issues a summons, review it with your attorney before making any statements to the IRS. You want to be sure that you have not been complicit in your client's wrongdoing.

## **Giving Your Business Clients Things They Need And Things You Can Provide**

*How to Use Written Financial Analysis to Serve You Clients Better*

By Brian Hamilton, CEO, ProfitCents

When you go out to dinner, you are usually hungry. When you buy water, you are thirsty. When you buy a winter jacket, you want to stay warm. In these individual cases, the value exchange between buyer and seller is clear and there is a definite need and solution set.

In accounting, less certain is that we are giving clients what they need. Sometimes, we don't know what they need, which is born of the fact that either we don't ask them or they don't tell us. Clients are sometimes intimidated by their accountants or by accounting and sometimes clients don't quite know where their pain points are, at least with respect to accounting and finance. By the time the pain points become obvious (i.e. a client runs out of cash) it is too late.

Often, clients don't know enough about our knowledge pool to tap into what we might provide and what they need. Let's examine two broad challenges that people face each day in running a business:

1. They typically have at least some sense of isolation or separateness that

comes from being on their own. It is lonely running a business for many reasons that reach beyond the scope of this article. For most of our lives starting from grade school, we are conditioned to be part of a structure or a group. I believe that the largest deterrent to starting a business is the sense of fright that comes from the realization of starting a detachment.

2. They need good advice and information to help them run their businesses. Many businesses suffer from a lack of adequate information and advice. The reason that business people need advice is that they are not competent in all the operating areas of a business.

As accounting professionals, wouldn't it be nice to intersect the things that we are very good at with the highest and most acute needs of the client? The best professionals can combine "1" and "2" above by reaching out to clients and helping them by giving them appropriate advice and information. So, how can we intersect what we know with the needs that clients have? The accountant needs to hold a line between trying to help out without moving too far into areas at which they are uncomfortable.

People who run businesses are typically very good at either selling or getting products and services delivered well. In the food chain of needs, selling a product is probably the highest need. Entrepreneurs

are not very good at making financial decisions. In fact, they are terrible at finance and have no interest in it. What does this mean? It means that they typically ignore finance and accounting.

As a result, what happens in companies where the people running them have little financial knowledge? (Please note that we are ignoring "sick" companies, those that have products or services that don't meet market needs, where the companies are doomed to fail sooner or later):

1. Founders or principals are such good salespeople that they can make up with great sales volume what they miss in financial inefficiency. In general, this scenario is not such a bad outcome. If clients can generate super sales volume where marginal revenue excels marginal costs, then good things happen. Did you ever have a client that infuriated you at some inner level because, despite their obvious indifference to finance and accounting, they still do well? In these very rare cases, this dynamic can make you feel unnecessary.

2. Founders or principals are really super operational people and fairly good salespeople. They can sell pretty well because they know the product really well and because they flat out know how to make things happen and get out great products and services. The need for reasonable financial skills in these cases is lower as well. These

companies can do fine even though they may not have great accounting and financial skills. These cases, too, are less than common.

3. Founders or principals are pretty good at pushing out good products and services. Yet, these above average skills cannot overcome both the inclination for poor financial management and the lack of interest in it. This is where many people businesspeople fail, since most of us are good at some things but not super performers in anything. These types of businesses and people can and do struggle. The people running these businesses need your help.

Most business people can benefit from understanding their financial condition and making better decisions. Why? Because financial numbers tell a story of a business by helping your customers understand the financial picture of the business. Take a simple case. Suppose a business has a low gross margin that is slipping over time. (Sales less cost of sales/sales)? What are the ONLY possibilities here relevant to the business?

1. The company is not controlling inventory or direct costs. Managers need to get unit costs under control. Perhaps direct labor is out of line. Perhaps people are not being managed efficiently. Maybe new suppliers are needed.

2. Prices need to be boosted. If prices cannot be boosted, then managers need to

assess why. Maybe it is the market. More often, the company is not meeting the needs of clients and the marketplace.

The idea is simple- help your clients look at financial statements, understand what is going on, and make a plan to get better results. Here are some guidelines:

1. Sit down with clients once per quarter and go over their financial condition with them. Bring the financial statements of the client and bring some written analysis to help them understand their statements in plain language (Don't throw a bunch of financial numbers at them that they will never understand). There are excellent technologies available that take hard-to-understand numbers and convert them to easy-to-understand plain language.

2. Be sure to set the right tone in these meetings. Don't talk down to clients. Ask questions. Listen carefully. Go over the numbers carefully. Try to look at the important numbers – the key performance indicators.

3. Put all the numbers into practice and action. Make a plan. Financial numbers come alive when they are understood and acted upon. Give the owner some simple things that he/she can do to improve performance.

By providing useful analysis, an accounting professional can become a confidant to the business owner and can help the business

owner with tangible things to become successful. Accountants are more than compliance professionals; they are in a unique position to build a great relationship with people who need friends and who need information.

**About the Author:**

Brian Hamilton is the chief executive officer and leader of the management team for Sageworks, Inc., which develops ProfitCents, an application that aids accountants in communicating with clients. Brian can be reached at brian.hamilton@sageworksinc.com or 919.851.7474 (x501).

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**Misuse of Trusts**

For years, unscrupulous promoters have falsely sold trusts as tax-avoidance devices – and they continue to do so.

Sometimes promoters claim that by paying wage or investment income into a trust, an individual escapes the duty to pay income taxes on it. Other scammers claim that by putting your home and other assets into a trust you own or control, you become able to deduct payments made to the trust or use of the house or assets. The scammer can claim anything that might be believed by a victim.

Trusts can serve many good, legal purposes, but tax evasion is not one of them. Generally, income earned in a trust continues to be taxable to you if you continue to control and use the trust assets. If you truly give away the assets within the trust, the income earned on them will be taxed to the trust itself or its owner, so tax payments will remain due.

It is true that there are particular types of trusts approved by the Tax Code and IRS that can reduce taxes under specific circumstances.

If you think you are obtaining one of these legitimate trusts, have it reviewed by an independent expert such as a tax lawyer or CPA, don't rely on the word of the person selling it.

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**HAVE A NICE DAY AND SEE**

**YOU AT THE 1040 GEAR UP SEMINAR**

**LITTLE ROCK OR SPRINGALE**

**TAKE YOUR PICK!**



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Name of Firm \_\_\_\_\_ Number of Employees \_\_\_\_\_

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Are you a Licensed, Registered or Certified Public Accountant? \_\_\_\_\_ If yes, give License# \_\_\_\_\_

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Do you hold an Associate or Baccalaureate degree with a minimum of 24 semester hours in Accounting? Yes \_\_\_\_\_ No \_\_\_\_\_

Are you engaged in any other trade or profession? \_\_\_\_\_ If yes, please describe \_\_\_\_\_

Please list other accounting organizations in which you hold membership: \_\_\_\_\_

I hereby state that the accompanying statements are correct to the best of my knowledge and belief. I further state that I will abide by the Constitution and By-Laws of the Society and will practice in strict conformity with the Code of Ethics and Rules of Professional conduct adopted by the Society.

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