

# KAKIMOTO & NAGASHIMA LLP

CERTIFIED PUBLIC ACCOUNTANTS  
CONSULTANTS

## NEWSLETTER

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### 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.

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## Summary of Articles

### Keys to Lowering Professional Fees

Due to the additional compliance required under the Sarbanes-Oxley Act\*, "Big Four" accounting firms are in a position to raise audit and review fees. In the past, smaller to medium-sized companies found it easier and convenient to obtain all of its accounting and tax needs from one accounting firm. As most companies are under increasing pressure to raise profits or reduce losses, many are pursuing other alternatives to lower their professional fees. In addition to the fees, quality of the work provided by the CPA firm must be carefully considered. Through careful review of the company's requirements and the capabilities of the CPA in delivering "quality work", substantial savings may be realized.

\* The Sarbanes-Oxley Act was signed into law on July 30, 2002, and introduced significant legislative changes to financial practice and corporate governance regulation. It introduced stringent new rules with the stated objective: "to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws".

### Disagree with an IRS Notice?

An IRS notice arrives regarding your corporate or individual tax return that you have filed some time ago. Even if it is a notice of refund, you may still want to confirm the amount of the refund, but what should you do if there is additional tax due? If you disagree with the adjustment(s) proposed by the IRS, you have the option to appeal. In this issue, we will cover the procedures taxpayers may follow when they dispute an IRS assessment.

### IT Projects: Hints for Success

It is said that in the year 2003 only approximately 30% of IT projects are successfully completed in the U.S. and Japan. Implementing an IT project is a difficult road to navigate and requires technical knowledge, understanding of business operations, and management ability. However, there are some factors, to consider in order to avoid having your project fall within the majority. We can learn from the numerous cases of publicized failed IT projects and move forward to successful completions of IT projects in the future.

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## Reducing Professional Fees

### Professional Fee Trend - Big Four Accounting Firms

During 2003 all "Big Four" accounting firms lost more public company audit clients than they gained, according to Auditor-Trak as reported in the March 2004 issue of the Practical Accountant. Smaller firms gained 21% of the clients lost by the large firms.

As problems surround the aggressive style of the Big Four firms and with the increase in audit compliance required under the Sarbanes-Oxley Act, the **large firms are geared to raising fees** on top of the currently high fees they charge. Even for the non-public smaller companies in the US requiring audits, additional audit procedures are now required.

### Alternative to Using Large Firms

Most companies are under severe pressures to increase profits or reduce losses. One way is to **consider an alternative to using the Big Four** with their high costs. Companies should consider using different professional firms for different projects to **minimize the overall costs** of professional fees. (see table below for an example.)

### Quality of Smaller Firms

One concern that companies may have is the quality of the work. Although not all firms are the same, smaller firms who are members of the American Institute of Certified Public Accountants (AICPA) must **undergo a quality control audit (peer review)** every 3 years conducted by an independent and outside CPA. The peer review program has been developed and overseen by the AICPA and is administered by 41 state CPA societies across the country.

Firms who are not members of the AICPA are not required to undergo the peer review. You may wish to ask your accounting firm if they have undergone a peer review, and if so, what report (unqualified or qualified) they received.

### Coordination with the Parent Company Auditing Firm

If the parent company is a public company in Japan, a consolidated audited report must be submitted to the Japan Securities and Exchange Commission. The subsidiary company's audited report will generally be required. Coordination with the parent company's auditing firm will be necessary and the due date must be met so that the consolidation can be processed timely.

Smaller firms can meet all of the requirements that the parent company's auditing firm requests. As long as the **quality, timely reporting, and communication requirements** are met, our experiences have shown that the parent company's auditing firm does not have a problem.



### Selecting a Smaller Firm

When considering a smaller firm to provide services, the following points should be addressed:

- Size of the firm – generally better to have at least 20 professionals.
- Ability to perform work in various states.
- Experience with the required work.
- Experience of the senior management and staff personnel.
- Experience working with the Japan CPA firms.
- If the firm undergoes peer review, and if so, what report was issued previously.
- Standard rate schedule.
- Ability to meet the deadlines.

### Conclusion

The next time you are considering having accounting and tax work done, significant fees may be saved by considering smaller firms. **By carefully making the right selection, the attention to details, the requisite quality, improved communications, considering the needs of the company, and savings on the fees are very feasible.**◆

#### Smaller Accounting Firm

- Payroll work
- Accounting and tax out-sourcing work
- Audit and review of financial statements for small to medium sized companies
- Corporate income tax returns
- Individual tax returns
- Transfer pricing work for small to medium sized companies
- PC based IT consulting

#### Large Accounting Firm

- Large M&A projects
- Projects requiring many professional staff
- Audit and review of financial statements for large companies with many locations
- Very difficult tax projects
- Large IT projects
- Transfer pricing work for large companies

## Appealing to the IRS

Individuals and business entities are required to file tax returns with the federal government on an annual basis. Once filed, the Internal Revenue Service (IRS) examines the accuracy of the reported figures. If the IRS disagrees with amount(s) reported on the tax return, a written notice is issued with the findings and proposed changes (resulting in additional tax due or refund). If the taxpayer agrees with the IRS findings, the tax case will be closed once the deficiency is paid or when the taxpayer receives the refund. What happens, however, if there is a disagreement with the proposed change? The following will explain the process the taxpayer can take when making an appeal to the IRS.

### A. Conference with a Tax Examiner and/or Examiner's Supervisor

First, a conference with the tax examiner and/or the examiner's supervisor can be requested. They will provide a detailed explanation of the proposed change. In response, the taxpayer is given the opportunity to explain his position and interpretation of tax laws supporting his treatment. The parties will discuss the issues in an attempt to reach an agreement.

### B. Requesting Fast Track Mediation

If a satisfactory result is not obtained in process (A), the taxpayer may ask for a new conference with the tax examiner and/or supervisor and request that a mediator from the Appeals Office attend. The Appeals Office is a department separate from, and independent of, the IRS Office. The Appeals Officer is trained in mediation and facilitates the communication between the taxpayer and the IRS representative to help reach a mutually satisfactory resolution that is consistent with the applicable law.

### C. Filing a Written Protest

In the event that the parties continue to have a dispute, subsequent to steps (A) and (B), the IRS will send the taxpayer a copy of the examination report explaining the examiner's proposed changes, along with a letter (known as a "30-day letter"). The taxpayer can appeal the case to the Appeals Office of the IRS. In general, taxpayers have 30 days from the date of the 30-day letter to appeal; however, in most cases, the tax authorities will approve an additional 30-day extension.

When preparing a written protest, the following should be included:

1. A statement requesting to appeal the IRS findings to the Appeals Office.
2. Taxpayer's name, address, telephone number, and tax identification number (Social Security Number or Employer Identification Number).
3. The date of the 30-day letter and case number.
4. The tax year(s) in question.
5. A list of item(s) in disagreement and the reasons for the disagreement.
6. The description of facts supporting the taxpayer's position for item(s) in disagreement.
7. The law or authority supporting the taxpayer's position, if any.
8. A signature, attesting that all statements are true, under penalties of perjury.

It may be difficult, for certain companies, such as those conducting business activities internationally, to gather all documents required to file a written protest by the due date. If the company files an incomplete claim, the protest may be returned to the company for completion and resubmission. In addition, if new facts are presented with the appeal, the Appeals Officer may investigate the validity of the information. Conferences with the Appeals Office are held to provide an opportunity for the taxpayer and Appeals Officer to discuss disputed issues and settle the differences in a timely manner. Conferences with the Appeals Office are held in an informal manner. Generally, the role of the Appeals Officer is to take a justifiable and fair position to settle the differences without costly court trials. The Appeals Officer has the authority to settle the matter even if the IRS and the taxpayer have a considerable amount of differences. Appeals Officers are required to consider the issues in an objective way; however, it does not mean that they must resolve all disagreements.

### D. Notice of Deficiency and Filing a Petition with the Tax Court

If there is still a disagreement after procedure (C), or if the taxpayer fails to respond to the 30-day letter and does not pay the amount due, the IRS will send a 90-day letter, also known as a *Notice of Deficiency*. The taxpayer has 90 days (150 days for taxpayers residing outside the United States) from the date of the notice to file a petition with the Tax Court or pay the deficiency. The 90-day period (or 150 day period, if applicable) may not be extended. When filing a petition, the taxpayer must strictly follow certain procedural and jurisdictional requirements and consultation with an attorney is highly recommended at this point.

### E. District Court and Court of Federal Claims

As stated above, the taxpayer must file a petition with the Tax Court or pay the amount due when a 90-day letter arrives. A taxpayer, however, can still appeal at a later date even in cases where a petition was not filed or when the amount due was paid. The taxpayer generally must file the claim within three years after filing the original tax return or two years after the deficiency is paid, whichever is later. If the appeal remains unresolved, the taxpayer can take the case to the United States District Court or to the United States Court of Federal Claims. Similar to cases heard at the Tax Court level, the process requires careful attention to laws and regulations and consultation with an attorney is again highly recommended.

### Summary

Dealing with the IRS can be frustrating and time consuming. At times, if the proper procedures and processes are not followed, unfavorable outcomes may result. With an understanding of the general process for the appeals process, taxpayers may be able to resolve the issues directly or, if the work is outsourced, can better judge the work of the CPA or other professionals.

For most appeals process, we do recommend retaining a qualified professional. However, even though you may outsource the work, the important thing to remember is to be involved and get an understanding of what is going on. ♦

## Preventing IT Project Failures

A recent survey conducted by Nikkei Computer Magazine investigating the condition of information technology in 2003 revealed “only 26.7% of IT system development attained successful levels (1,746 participants).” Projects were deemed a **“success” if it met the originally intended quality, cost, and time frames.** The results of the survey show that 75 % of the companies felt they did not obtain the anticipated result.

Was there a clearly defined understanding of the **“anticipated result”** between the company and IT service provider at the commencement of the project? It may be possible that the successful level did not reach 30% because of the ambiguity of the initial agreement.

It is not unusual to hear about failures in the construction of IT systems or IT projects being cancelled before completion. IT systems are an integral part of everyday business and it can **offer many new benefits**, but in consideration of the difficulties of systems implementation, management needs to understand the risks involved. Fortunately, we have the advantage of past experiences that have taught us **critical factors that divide successful projects from disappointing ones.**

We have listed several key factors that should be considered before the onset of a system implementation. We recommend anyone who is currently thinking about a new IT system to consider these points to prevent costly failures.

### Assigning an appropriate project manager

- The project manager should have the technical knowledge, business skills, and managerial ability to effectively oversee the project and there should be enough support to supplement the areas of weaknesses such as technical knowledge and/or skills.

### Service provider/vendor that fits the company’s needs

- Be aware that the provider/vendor may specialize only in their specific technology or products they promote and do not always make efforts to search for more effective alternatives.
- Consider the quality and background of the provider/vendor team members. There can be a lack of personnel capable of monitoring and supervising team members.
- Monitor and evaluate provider/vendor performances. Be cautious of lip services and take appropriate measure if you question the work.

### Setting realistic due dates

- Consult the opinions of staff members working on site and make sure they are reflected in the original plans.
- Analyze the time needed to be spent in each stage of a project and be sure to examine any big differences in actual time versus originally scheduled time. Also, be prepared for changes in the timeline of the project.
- Create a culture of open communication with project staff members to enable prompt identification of delays, unfavorable or unforeseen problems.

### Constant communication

- Be sure system-user opinions are reflected in the project.
- There should be open communication between operations personnel and IT specialists.

- There should be constant communication including written status and progress reports between the project manager and staff members working on site.

### Involvement of top management

- Top company management involvement is necessary for any reconstruction of business processes; this should include the coordination of inter-departmental cooperation.
- Having an understanding of each project in order to set realistic goals.

### Project is managed based on limited experience or instinct

- Prepare proper documentation at each stage of the project.
- Standardize processes so that technicians will perform duties in a uniform fashion.
- Create sufficient test procedures and management controls; verify test results.

### Communicating the definition of a successful project

- Project planning and development should focus on actual business operations.
- Project members should include company personnel who can consider the project from a business operations standpoint and have the opportunity to make comments.
- Each member should have a clear concept of cost vs. benefit.
- Project manager has clearly relayed the project objectives so that every staff member understands his/her respective role in the IT project.

Even in the U.S., where project management is advanced, the success rate of IT projects is said to be about 30%. In addition to the points noted above, Japanese companies located in the U.S. also need to overcome the “language barrier” to successfully implement IT systems. Recently, even in Japan, increasing discussion regarding the importance of IT project management has been noted due to the heightened awareness of the difficulties involved in managing IT projects to successful completion; companies will need to implement important measures to prevent costly failures. Within the key points to success, **a clear understanding of the “anticipated result”** must be communicated from the initiation to completion of the project between the parties. In this way, even if the company discovers a need for improvement in some area, there is a high chance that the project will **reach the “anticipated result”**.

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