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Certified Public Accountants Consultants

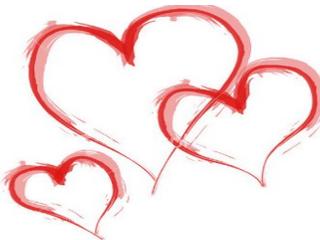
NEWSLETTER

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Any Questions?

We are committed to providing our clients with quality and excellent services.

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Summary of Articles

Classification of Deferred Income Taxes (ASU 2015-17)

In November 2015, the FASB issued ASU 2015-17, "Balance Sheet Classification of Deferred Taxes". Included as part of the FASB's simplification project on reducing the cost and complexity of U.S. GAAP, this ASU simplifies the classification of deferred income taxes by requiring an entity to present deferred tax assets/liabilities as noncurrent amounts on a classified balance sheet. Highlighted in this article are the new ASU's key provisions; companies will need to determine how much of an impact this and other new simplification accounting standards will have on its financial reporting and disclosure.

Protecting Americans from Tax Hikes Bill Now Law

Right before the end of 2015, Congress passed and President Obama signed into law, a tax extender bill, the Protecting Americans from Tax Hikes Act of 2015 (the PATH Act). Unlike typical tax extenders legislation seen in prior years, the PATH Act makes permanent over 20 key tax provisions. It also extends many other provisions for two or five years. This article mentions a few notable tax extenders that are available for taxpayers to utilize on 2015 tax returns.

Accelerate Your Financial Close

The financial statements are critical to management in their ability to understand the financial health of the organization and allow management the opportunity to make decisions in a timely manner. However, the process of generating reliable and timely financial statements provides challenge to most companies. Our article summarized the techniques in how to accelerate your closing process.

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We look forward to providing you with up-to-date accounting and tax information.

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Let's Simplify Matters – Changes in Deferred Tax Classification

On November 20, 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update 2015-17, “Balance Sheet Classification of Deferred Taxes” (“ASU 2015-17”). Included as part of the FASB’s simplification initiative launched in 2014, the ASU was issued in the spirit of improving or maintaining the usefulness of the information in financial statements while reducing the complexity and cost in financial reporting.

What’s the Difference?

Currently, an entity is required to separate deferred tax assets and liabilities into current and noncurrent amounts on a classified balance sheet. Classification of the deferred tax asset or liability is based on the classification of the related asset or liability. If a deferred tax asset or liability is not associated with a specific asset or liability (for instance, a tax credit or net operating loss), classification was usually based on the reversal date of the related temporary difference.

Based on stakeholder input, the FASB determined there was very little benefit to financial statement users from the current and noncurrent classification of deferred tax assets and liabilities. Stakeholders asserted that the timing of recovery and settlement of the deferred tax asset/liability was not always consistent with its current or noncurrent classification. In addition, entities incurred additional costs to properly categorize its deferred tax assets and liabilities.

To simplify balance sheet presentation, ASU 2015-17 will now require that deferred tax assets and liabilities be classified as noncurrent in a classified balance sheet. Consistent with the guidance under existing U.S. GAAP, entities will continue to address deferred tax assets and liabilities on a tax-paying component and tax jurisdiction basis for offsetting purposes. Valuation allowances will also be classified as noncurrent.

The guidance under ASU 2015-17 will align the balance sheet presentation of deferred tax assets and liabilities with International Financial Reporting Standards. IAS 1, “Presentation of Financial Statements”, requires entities to classify deferred tax assets and liabilities as noncurrent in a classified balance sheet.

Effective Date

For public entities, ASU 2015-17 will be effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods.

For all other entities, ASU 2015-17 will be effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15 2018.

Early adoption is permitted for all entities as of the beginning of any interim or annual reporting period and may be adopted as follows:

Prospective Basis

- Disclose the nature of and reason for the change in accounting principle
- Include a statement that prior periods were not retrospectively adjusted

Retrospective Basis

- Disclose the nature of and reason for the change in accounting principle
- Include quantitative information about the effects of the accounting change on prior periods

Looking Forward

This standard will have an eventual impact on all companies; in general, companies will likely have a reduction in working capital due to the decrease in deferred tax assets and liabilities. This could have a bearing on certain financial ratios and metrics which could impact certain agreements and contracts. Communication of this change in accounting to any stakeholders should also be considered and, if warranted, done in advance.

What’s Next?

As part of the FASB’s simplification initiative the following proposed accounting standards have been issued which could have a bearing on income tax accounting:

- Intra-Entity Asset Transfers (additional research/outreach is being performed)
- Improvements to Employee Share-Based Payment Accounting (ASU expected to be issued first quarter, 2016)

Completed and other FASB simplification initiative projects:

Completed

- Business Combinations: Simplifying the Accounting for Measurement-Period Adjustments (ASU 2015-16)
- Inventory: Simplifying the Measurement of Inventory (ASU 2015-11)
- Intangible – Goodwill and Other – Internal-Use Software: Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement (ASU 2015-05)
- Compensation – Retirement Benefits: Practical Expedient for the Measurement Date of an Employer’s Defined Benefit Obligation and Plan Assets (ASU 2015-04)
- Interest – Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03)
- Income Statement - Extraordinary Items and Unusual Items: Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items (ASU 2015-01)

Underway

- Balance Sheet Classification of Debt
- Equity Method of Accounting

Please consult us for further information on these accounting standards and/or to discuss the impact ASU 2015-17 may have on your Company’s future accounting and financial reporting. ♦

Correction of November 2015 Newsletter

New Due Dates for Certain Commonly Filed Federal Tax Returns

Beginning with the 2016 tax return, the extended due date for fiscal year-end corporate tax returns (other than those for a June 30 year-end) is the 15th day of the tenth month following the year end.

Protecting Americans from Tax Hikes Act of 2015

On December 18, 2015, President Obama signed into law a bill, the Protecting Americans from Tax Hikes (the PATH) Act. This Act retroactively extends a collection of key individual, business, and energy tax breaks that were originally scheduled to expire on December 31, 2014. Some provisions have been made permanent, while others have been temporarily extended through 2016 or 2019. With passage of this bill, taxpayers will be able to utilize the tax extenders on their 2015 tax returns.

The following table lists a few notable tax extenders that have been retroactively extended:

	Made Permanent	Extended through 2016	Extended through 2019
Individuals	<ul style="list-style-type: none"> Sales tax deduction 	<ul style="list-style-type: none"> COD principal residence exclusion Mortgage insurance premium deductible as interest 	
Businesses	<ul style="list-style-type: none"> R&D credit IRC §179 - enhanced 15-year recovery period 		<ul style="list-style-type: none"> Bonus depreciation – phases out

For Individuals

Made permanent

- Sales Tax Deduction – deduction for state and local general sales taxes in lieu of state and local income taxes.

Extended through 2016

- COD principal residence exclusion** – extends the provision for the discharge of debt on a qualified principal residence taxpayer can exclude from income up to \$2 million of debt discharged before Jan. 1, 2017 (includes debt discharged on or after Jan. 1, 2017 if the discharge is pursuant to a binding written agreement entered into prior to Jan. 1, 2017).
- Mortgage insurance premium deductible as interest** – extends the ability to deduct the cost of mortgage insurance on a qualified personal residence (the deduction is unavailable for a taxpayer with an Adjusted Gross Income in excess of \$109,000).

For Businesses

Made permanent

- R&D credit** – extends the Research Tax Credit for both the 20% traditional research tax credit and the 14% alternative simplified credit (modified after 2015)
 - Tax years beginning after December 31, 2015, a small business may claim one of the following credits:
 - Taxpayers (TP) with the average annual gross receipts for the 3 preceding taxable years is \$50 million or less can claim credit against Alternative Minimum Tax or
 - TP with less than \$5 million in gross receipts can claim credit up to \$250,000 against employer FICA (*OASDI tax liability only*).
- IRC §179- enhanced** – a taxpayer may immediately expense up to \$500,000 of Section 179 property (e.g., depreciable tangible property and qualified real property) annually, with a dollar for dollar phase-out of the maximum deductible amount for purchases in excess of \$2 million. The \$500,000 and \$2,000,000 amounts are indexed for inflation for taxable years beginning after 2015.
- 15-year straight-line recovery period** – extends and makes permanent the 15-year cost recovery period used for qualified leasehold improvements, qualified retail improvements and qualified restaurant property.

Extended through 2019

- Bonus depreciation** – extends 50% bonus depreciation to qualified property (e.g., original use of tangible property) purchased and placed in service before January 1, 2018 (bonus depreciation for qualified property placed in service in 2018 is 40% and qualified property placed in service in 2019 is 30%)

Individual Taxpayer Identification Numbers

The Act also makes the following provisions concerning Individual Taxpayer Identification Numbers (ITINs):

- An ITIN will expire if not used on a Federal income tax return for a period of three consecutive taxable years (expiring on December 31 of such third consecutive year).
- Any ITIN issued before 2013 will no longer be valid on a staggered schedule between 2017 and 2020, regardless of whether such ITIN has been used on Federal income tax returns. Individuals with ITINs issued before 2013 need to apply for a new ITIN (See table below for expiration dates).

Year ITIN Issued	Expires on
Pre-2008	January 1, 2017
2008	January 1, 2018
2009 or 2010	January 1, 2019
2011 or 2012	January 1, 2020

Please note that this article does not cover all the changes including all tax extenders that have been retroactively extended by the PATH Act of 2015. If you have any questions pertaining to the PATH Act, please contact the office of Kakimoto & Nagashima LLP at (310) 320-2700. ♦

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Make reasonable estimates

When determining the various reserve calculations that go into the close process, it is important to provide the appropriate level of precision in the underlying estimates. For example, consider the sales return reserve. At period end, a detailed analysis could be performed of all transactions, credit memos issued subsequent to month end could be reviewed, or other sophisticated techniques could be used to calculate this reserve with a high level of precision.

In many situations though, if sales returns are fairly constant over the year, a simple calculation involving reserving for a certain percentage of current months sales based on historical return rates will likely yield a result that is materially consistent with the more complex approaches.

If a number cannot be estimated with appropriate accuracy and reliability, it is imperative to take the time to get the numbers right. The information provided by the accounting department must be accurate enough to be the basis for informed decisions.

Minimize your journal entries

There are essentially two reasons why journal entries are recorded – they are either the correction of an error or they are made to record a non-routine transaction.

Run a report of all journal entries made during the last three closings, and investigate them for recurring trends. Are there certain errors that continue to be made month after month that require journal entries? Are there other transactions that can be recorded in a different module in the accounting system?

There are also certain entries that are known amounts throughout the year, such as deferred rent or amortization of prepaid expenses. Using the recurring journal entry function in the accounting system, these transactions can be uploaded once for future periods, and then posted on a monthly basis if there have been no changes in the underlying transaction during the year.

What are the benefits of a fast close?

- Companies get more time to analyze results
- Executives and managers obtain vital information sooner
- Finance department personnel are freed for other activities
- Overtime and related costs can be cut out or eliminated

What can we do?

The implementation of changes to a company's close process can yield substantial benefits but you may encounter numerous challenges. If you are considering making a change or need assistance in your close process our accountants from Kakimoto & Nagashima LLP can help. To learn more about the services we offer, call us at (310)-320-2700. You can also visit our website at www.knllp.com. ♦

Accelerate Your Financial Close

What is the importance of timely and accurate financial statements?

The financial statements are critical to management in their ability to understand the financial health of the organization and allow management the opportunity to make decisions in a timely manner. Thus, the goal of any organization should be the ability to produce timely and accurate financial statements within a reasonable period of time after the period has ended.

For many companies, the financial close process is just getting the books closed. While many companies continue to experience longer-than-necessary close cycles, inadequate analysis of results, duplication of efforts and overall process inefficiencies, few have the desire to undertake a focused improvement effort.

What are the challenges?

The long cycle time and inefficiencies are usually driven by unclear responsibilities as well as a lack of clarity in the close process and company timelines. The challenges include:

- Lack of oversight/monitoring
- No definite due dates
- Extensive reliance on manual processes
- Lack of understanding of the “big picture”
- Low-priority tasks in the critical path
- Inefficient use of resources

What are the techniques to accelerate the financial close?

Techniques are listed below that will help facilitate in reducing the overall time required to close the books, while at the same time leveling out the work load in the accounting department, making the close well thought out systematic process.

Develop a detailed timeline

This timeline will act as your roadmap and will help set expectations for all members in the department. It will outline when all of the significant events in the close process should be completed, culminating with the release of the statements to stakeholders. The first draft of the calendar should reflect the company’s current capability to close, as it will be used as a baseline to measure future improvement.

Identify the critical path

The most effective method to find the areas for improvement is to perform a critical path analysis. In the close process, an item on the critical path would be one that directly impacts the completion date of the close. That is to say that if that task is not finished on time, it would delay the close. With these tasks identified, the next step is to find ways to complete them earlier in the cycle.

Select one or two of the identified critical path items, and start to explore some potential solutions with your team. Employees are more familiar with their tasks than anyone else, and they are likely aware of procedures that are not working well.

It is critical that these discussions result in realistic changes that are obtainable. Improvements in the close process should not simply be a mandate from management that everything will be done one day earlier. It is about working together to change the process to achieve a goal of reducing the close time.

Take advantage of technology

Simple applications, such as Excel, Dropbox, etc. can be implemented and result in more efficiency for accumulating and sharing data and for reporting. Implementation of technology outside is also a consideration. Reach out to vendors, to request they send invoices electronically rather than on paper. This will result in better data for accruals, facilitates paying of invoices electronically, and saves time and money.

Reduce or eliminate manual processes

The automation of routine and repetitive tasks is a key to efficient accounting operations. Although Excel is an exceptionally useful tool to accountants, it is important to remember that it is not an automated pro-

cess. Review your close timeline and list out all of the reports that are generated in the department including those intended for internal reconciliations or management analysis. Frequently, a significant number of these reports are system generated and then manipulated in Excel to reformat or to add additional information.

In order to obtain higher levels of efficiency, preferences for formatting or particular methodologies must sometime take a backseat to practicality. If there is a way a system can automatically process a transaction and remove it from the world of Excel, it will typically result in substantial increased efficiency and it can be well worth the tradeoff.

Communicate with people involved in the transactions

Get the people involved in shortening the close by suggesting changes. Hold group staff meeting to identify areas that can change now, where training is needed, and where change is dependent on other departments. Outside of finance, talk with the operating areas that generate revenue and find out what financial information is important to them and would help them achieve better performance. Engage them in close-process improvements by sharing with them the direct benefits of a faster close: The faster they can see the results of how they performed last period, the better they can do next period.

Don’t passively wait on information

There are situations where companies are waiting on hard copy statements to be received in the mail which takes days or sometimes weeks to receive. These basic assumptions need to be challenged. While it might have been the case years ago that such information was not available electronically, situations change, and it is unlikely you are the only client of that vendor that wants that information sooner. A simple phone call or e-mail can sometimes yield tremendous results, but only if the query is actually made.

In situations where required information cannot be obtained in a timely manner, alternative approaches should be considered. An estimate of an account balance based on historical results can often yield materially correct results or the data can be derived from other sources. More drastic measures include changing to new more responsive vendors that are able to supply the information in a timely manner.

Start the close process before month end

Do not start your closing process on the first day of the following month. This traditional way of thinking needs to be eliminated by starting the close cycle several days before the end of the month.

Review the close timeline and consider what accounts can be finalized in advance. Here are a few examples of activities traditionally performed during the close that sometimes can be done before the end of the month:

- **Allowance for uncollectable accounts receivable** – Perform the analysis and determine the appropriate allowance balance in the week before the end of the month. This number would also include an estimate for the activity for the last few days of the month if deemed significant. If a significant event occurs during the close, that information could be used to revise the allowance, but in most companies such late changes are highly infrequent.
- **Depreciation expense** – Consider adopting a depreciation policy where assets acquired during the first half of the month receive a full month of depreciation and those in the second half do not start depreciating until the first day of the next month. If consistently followed, such a policy is GAAP compliant and does not produce results that materially differ from other acceptable policies, and will allow the posting of the monthly depreciation entry before the end of the month.
- **Inventory counts** – Consider moving from a traditional count of 100% of inventory at period end to cycle counts. This will spread the inventory count process over the reporting period and will eliminate a significant amount of work that occurs during the close. It can also eliminate significant month-end adjustments as those will be recorded in real time during the month.

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