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#### Fall 2011 - Volume 29 - Issue 3

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### **KEY TAX DATES**

### **OCTOBER**

Individuals. Last day for filing 2010 Form 1041 for calendar-year estates and trusts that obtained automatic six-month filing extension.

**Employers.** Employers of nonagricultural and nonhousehold employees must file return on Form 941 to report income tax withholding and FICA taxes for the third quarter of 2011.

### DECEMBER

Estimated Tax. Payment of last installment of 2011 estimated tax by calendar-year corporation.

See Page 5 for additional key dates

### IRS AUDITS OF U.S. WITHHOLDING AND REPORTING OF PAYMENTS TO FOREIGN PERSONS: TIPS FOR BEING PREPARED

by Cynthia J. Hoffman, Director - International Tax Advisory Services

Generally, a "U.S. person" (this includes individuals and businesses) making payments for certain income items to a "foreign person" may be required to withhold U.S. tax on such payments and report this income and the applicable withholding to the IRS. Payments and withholding taxes are reported on U.S. Form 1042 and Form 1042-S. The general U.S. income tax withholding rate for payments to foreign persons is 30%. This rate may be reduced, to zero in some cases, pursuant to an income tax treaty or an Internal Revenue Code section that exempts the payment from tax. Amounts need to be reported on Form 1042 series even if no amount is withheld from the payment due to the treaty-based position.

These requirements are now a Tier I issue for the IRS. (Although IRS examination of the issue is not required by an examiner, a taxpayer should anticipate that this might be raised under audit.) Here are some tips to assist you in understanding what the IRS is reviewing for a Form 1042 audit:

- Do deposits made and on file with the IRS agree to deposits reported on Form 1042? Sometimes, the IRS reallocates deposits between types of taxes, so your Form 1042 deposit might be showing as short.
- Do Form 1042 and the totals of Form 1042-S reconcile?
- Are reported payments to related parties on Forms 5471, 5472 and 8865 reported on Form 1042-S to such parties?
- Do Forms 1042 and 1042-S reflect the proper entity name and EIN?

- Are you obtaining and maintaining Form W-8 or Form 8233 to certify the payee's foreign status and U.S. taxpayer ID number, and to document reduced withholding rates, if applicable under a tax treaty? Does the documentation exist at the time of the payment, or was it obtained at a later date? If so, documentation to assist in the acceptance of a late Form W-8 or Form 8233 should be part of your files.
- Do you maintain operating manuals, flowcharts and other written documentation for processes and procedures relating to the fiduciary duty as a withholding agent? This can include internal audit reports for open years that pertain to these processes.
- Review files for conflicting information with respect to the processes and procedures, or with respect to specific payees, that is not consistent with the classification of payments, withholding taxes and reporting.

A taxpayer who is contacted for an IRS exam of Form 1042 can review Internal Revenue Manual 4.10.21 (U.S. Withholding Agent Examinations - Form 1042) to gain a detailed understanding of IRS exam procedures.



CYNTHIA J. HOFFMAN INTERNATIONAL TAX ADVISORY SERVICES Director

## TOPSTORY

### IFRS...ARE YOU READY? DO YOU NEED TO BE RIGHT NOW?

by Donald B. Applegarth, Assurance Shareholder

It isn't news that over the past few years the SEC has lived by its mantra that the investing community needs a single set of high-quality, global accounting standards. In 2010, it put forth its Workplan with a hard mark of June 2011 to make a decision on whether or not to require public registrants to adopt IFRS. That target date was slightly interrupted with the passage of the Dodd-Frank Act and the need for the SEC to rewrite volumes of its rules and regulations to comply. Another drag on the timeline has emerged, specifically the time it takes for two separate boards (the FASB and the IASB) to work together with the objective of achieving convergence on several high-priority projects such as leases, financial instruments, insurance and revenue recognition. With the FASB and IASB working feverishly on joint projects and the expectation that these will be wrapped up by the end of 2011, the SEC recently floated a balloon when announcing one possible approach to transitioning to IFRS. A blend of convergence and endorsement, the condorsement approach would allow the FASB and IASB to finish joint projects while newly issued or amended IFRS would be adopted into U.S. GAAP pursuant to an endorsement protocol. The endorsement protocol would give the SEC latitude to modify or supplement IFRS when it is in the public interest.

Even though it might seem as if the SEC's decision process and the FASB and IASB convergence initiatives are moving along at a snail's pace and that they may never reach agreement or conclusion, you should be

prepared for a definitive answer on IFRS by the end of this year followed by a flurry of new accounting releases or vice versa. In other words, it may feel like you are watching the

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stalemate of Congress's debate over raising the debt ceiling, but in this author's view, once a decision on IFRS has been made, things will begin to happen at a quicker pace. However, concerns over IFRS being sufficiently developed, maintaining the independence of the standardsetting process, investor understanding and education, effects on laws and regulations, the impact on companies' systems, contracts, governance, litigation contingencies, and the preparedness of auditor and financial statement preparers still loom and will likely make for a lengthy timeline for any required transition to IFRS.

Does it mean that you have to invest in evaluating the impact of all this right now? Some would have you believe that it does, but frankly, no it does not. There is time, and in a recent survey there has been a slight reversal in IFRS readiness gains, as professionals await progress on convergence. My advice is to be vigilant and aware of what is happening (especially revisions to U.S. GAAP on the horizon such as those related to revenue recognition, leases and financial instrument accounting), but don't push all the chips in just yet, especially if you're a privately held company.

No one really knows the impact of IFRS on private companies. In July of 2009, a financial reporting framework called IFRS for Small to Medium-Sized Entities was issued to address the concerns of smaller entities over the complexities and

> cost of transitioning to IFRS. However, at the AICPA's National Advanced Accounting and Auditing Technical Symposium held in July 2011, it was noted that this framework really

hasn't been embraced to the extent it was hoped. And the Blue Ribbon Panel on Private Company Financial Reporting (the Panel) is clearly headed down an entirely different path by recommending that a new separate board (other than the FASB) be created under the Financial Accounting Foundation, the parent of the FASB. After taking a close look at the users of private company financial statements, the Panel has acknowledged that private company users have very different needs than those of investors in public companies, and has recommended that a separate board be established for dealing with the needs of private company financial statement users. Perhaps there is finally some traction over the age-old debate over the need for "Little GAAP," separate from "Big GAAP."

In any event, what is important is to align your company with an accounting firm that stays current with the ever-changing world of accounting and financial reporting, and perhaps more importantly, one that has the ability to make sense out of it and relay timely advice that is practical. For questions related to this issue, please contact Don Applegarth, Assurance and Advisory Shareholder at dapplegarth@schneiderdowns.com.

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## FEATUREARTICLE

### **RAISING CAPITAL**

by Anthony J. Ventura, Director, Schneider Downs Corporate Finance, LP

Businesses have limited capital resources that must continuously be allocated by managers between the competing capital needs of the business and its shareholders. In some cases, new third-party capital can be used to achieve a combination of competing business and shareholder objectives. Examples of business capital needs include investments in working capital, capital assets or acquired growth, and examples of shareholder capital needs include the desire for enhanced returns or events of liquidity. There are an unlimited number of alternative capital structures beyond commercial bank loans, including alternative senior debt, mezzanine/ subordinated debt, and preferred/noncontrol equity structures.

#### The Decision to Raise Capital

Companies consider raising capital with the best interest of the common shareholders in mind. Considerations for raising new third-party capital often include the opportunities to:

- Enhance the return on common equity by refinancing existing tranches of senior debt, mezzanine/subordinated debt, and/or preferred/non-control equity at a lower cost;
- 2. Enhance the return on common equity by investing the proceeds of the new capital into the business at an expected rate of return greater than the expected cost of the new capital;
- 3. Reduce common equity at risk by financing a distribution to common equity shareholders that allows them to realize and subsequently diversify wealth:
- 4. Provide liquidity to one or more

- common equity shareholders to finance the capital requirement of a stock repurchase or redemption; and
- 5. Preserve the business as a going concern and protect common equity value by using new third-party capital to finance short-term, non-recurring losses or damages.

### Requirements and Considerations of Raising Capital

There are an infinite number of combinations of sources, structure and costs of capital. Successfully and efficiently raising capital requires expert financial analytical ability, knowledge of current capital market conditions and the ability to identify, screen and contact capital market participants. The

variation in potential outcomes can create or destroy millions of dollars of current/future common equity value.

The costs of capital include: (i) upfront fees paid to capital providers and the expense of

transaction-related services, (ii) the service requirements of invested capital, including interest expense and the cashflow effect of reductions of invested debt or equity principal, as well as any related administrative costs, and (iii) termination fees, performance fees and the cost of common equity dilution when applicable.

### The Intangible Costs and Qualitative Benefits of Raising Capital

Intangible costs and qualitative benefits are the result of the perceived level of success and efficiency a capital raise has had in achieving the desired business and/or shareholder objectives. Examples of the elements of a transaction that can add, relative to initial expectation, the presence of intangible cost or qualitative benefit include: (i) the duration of time required to close a capital raise, (ii) the time, involvement and commitment of shareholders and managers to participate in a capital raising process, (iii) the quality of the relationship between capital providers, managers and shareholders, and (iv) the constraints, restrictions or other considerations of the new capital that executives must recognize and consider in making day-to-day operating decisions.

### How Schneider Downs Corporate Finance, LP (SDCF) Can Help

SDCF has extensive corporate finance experience and global finance contacts. SDCF assists in identifying providers of senior debt, subordinated/mezzanine debt and equity. Our team can: (i) provide real-time market intelligence and comprehensive valuation guidance; (ii) develop a list of potential lenders, deal sponsors or investors; (iii) secure senior or junior debt placements, (iv) secure minority and majority equity placements on a selective basis; (v) assist in creating offering memoranda; (vi) manage the transaction process and interaction with lenders and investors; (vii) work with client's legal counsel in preparation of purchase offers; and (viii) facilitate lender and investor due diligence.



ANTHONY J. VENTURA
SCHNEIDER DOWNS CORPORATE
FINANCE, LP
Director

## N E W S Y O U N E E D

#### **CLOUD COMPUTING CONSIDERATIONS**

by Patrick B. Armknecht, Technology Advisors Senior Business Development Manager

If you ask five different people to explain cloud computing, it's more than likely you will receive five different answers. In a nutshell, cloud computing can be described as subscription-based or rented services that are accessed via the Internet. These services include business applications, file storage, disaster recovery and network capacity, among many others. There are benefits and risks that should be taken into consideration when deciding whether cloud-based computing is the right choice for you.

Benefits that can be realized from cloud computing include:

- Reduction in Hardware Costs
- Reductions in Annual Maintenance Costs/Fees
- Better Cash Flow
- Increased Scalability
- Mobility/Remote Access
- Redundancy/Disaster Recovery
- Faster Deployment
- Updates/Upgrade
- Flexibility

Risks associated with cloud computing include:

- Reliability of the Service Provider
- Data Security and Confidentiality
- Internet connection
- Location of Servers

To read this article in its entirety, visit <u>www.schneiderdowns.com/cloud-computing-considerations.</u>



PATRICK B. ARMKNECHT TECHNOLOGY ADVISORS Business Development Senior Manager

### 0 & A

### **Schneider Downs Wealth Management Advisors, LP** *Quarterly Column*

### Given the high level of volatility in the stock market, should I invest my assets in a guaranteed annuity product?

by Beth D. Lynch, Investment Relationship Manager, Schneider Downs Wealth Management Advisors, LP

As with any investment, buyers need to fully understand what they are investing their dollars in, what the underlying fees are and, most importantly, how the investment fits into their overall financial situation. Purchasing annuity products can be very complex due to the structure of the annuity – fixed or variable – and also due to the extra guarantees that are available.

Annuities come in two basic structures. A fixed annuity can be thought of as a type of savings account. The insurer agrees to pay a fixed interest rate on the balance in the account. The account value is not subject to the risks of the market, but the participant is limited to savings-account-like returns. You could think of this type of annuity as a self-funded pension plan because at some time in the future, perhaps at retirement, the insurer can pay you a set dollar amount for the remainder of your life.

The advantages of the fixed annuity are that the purchaser knows that a fixed amount of dollars will flow into the household regardless of what the market or the economy is doing as long as the purchaser is alive (and possibly during the life of a second individual such as a spouse). A second advantage that applies to both, fixed and variable, is that the income in the annuity is not taxed until the owner starts taking distributions.

So, what are the disadvantages? The interest rate paid by the annuity might



not keep up with the cost of living. If you need to take out money before turning 59.5, in addition to income tax on the deferred earnings, you can be subject to a 10% penalty on the earnings. Additionally, if you change your mind and exit the annuity in the first several years of ownership, you might be subject to a penalty by the insurance company called a "surrender charge." Lastly, if you die after the annuity is in payment mode, your heirs might not be entitled to the remaining account value, depending upon the method of distribution.

A variable annuity adds the ability to invest in a variety of investments, including equity-based assets. In this type of annuity, owners can participate in upward swings in the market while protecting their annuitization value if they purchase certain guarantees, or what the insurance company calls "riders." In addition to the tax and withdrawal penalties mentioned above, there are two major disadvantages to variable annuities. First, the costs of the guarantees/riders are very expensive and can erode gains and principal. Second, if you withdraw

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### **SDNEWS**

### IGAF POLARIS A Global Association of Independent Firms

#### **ANNUITIES** continued from Page 4

an amount that is higher than the insurance company's maximums, it can jeopardize the guarantees that you have purchased.

Lastly, from an estate planning perspective, a benefit of an annuity is that it avoids probate; however, there is no step-up in basis to your heirs on any growth within the annuity. Growth is always taxed as ordinary income. You may use an annuity to pass assets to your heirs that avoid estate taxes and create a legacy for your family. Special attention and careful setup are required to have this strategy work. You should consult your estate planning attorney on ways to use deferred annuities in your particular plan.

Our advice to those thinking about investing in an annuity is to compare different types of annuities, understand the pros and cons, and ask questions. Annuities can be another component of your financial toolbox to help you meet your goals. Finally, make sure your advisor understands your needs and goals before deciding to purchase an annuity.

#### **Around Schneider Downs**

Picnic time! Both Schneider Downs offices hosted annual picnics. The Pittsburgh office picnic was held at Kennywood, and the Columbus office picnic was held at the Columbus Zoo.



Gennaro DiBello gives a short speech while the line forms at the sundae bar.



Wow, that's a lot of orange! Employees pose for a picture on the overlook at the Columbus Zoo and Aquarium.



John Stafford, Technology Advisors
Shareholder, retired at the end of June. As
a parting gesture, his team gifted him with
technology, of course, in the form of an
iPad 2! A huge "thank you" to John for his
contributions to the firm!



The Nonprofit Services Industry Groups in both Pittsburgh and Columbus held a full-day seminar for clients and friends. Pittsburgh's event was held in July at the Marriott City Center, and the Columbus event was held in August at the Mid-Ohio Food Bank. Above: Jay Meglich, Audit Shareholder, starts the day in Columbus with a welcome and industry update.



The Pittsburgh
Construction and
Transportation Industry
Groups each hosted a
golf outing in August at
Nevillewood Country
Club. The weather was
absolutely beautiful for
both outings. Thanks to all
who attended!



Karl Kunkle, Wealth Management Shareholder, got his *second* career hole-in-one at an outing at Shannopin Country Club this summer!

### **New Hires**

Our people are our greatest strength. We welcome our April, May and June new hires:

Lindsay A. Brooks Veronica L. Bucci Heidi M. Kaufman

Kensey M. Lacy

Jonathan A. Spero

Jack B. Wolford

### **CALENDAR - BENEFIT PLAN DUE DATES**

Forms 5500, Annual Return/Report of Employee Benefit Plan.

Year-End	Due Date	With 5558 Extension
2/28	9/30/11	12/15/11
3/31	10/31/11	1/16/12
4/30	11/30/11	2/15/12

Processing of corrective distributions relative to failed 401(k) ADP/401(m) ACP discrimination testing, in order to avoid a 10% employer imposed excise tax.

Year-End	Due Date
6/30	9/15/11
7/31	10/17/11
8/31	11/15/11

### ONPOINT

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#### **Need CPE?**

Schneider Downs will be hosting two continuing professional education (CPE) events in December. Reserve your seat today.

#### Columbus

December 7, 1:00 p.m. - 5:00 p.m. Hilton Columbus at Easton rsvpcolumbus@schneiderdowns.com

#### Pittsburgh

December 8, 8:00 a.m. - 5:00 p.m. Westin Convention Center rsvppittsburgh@schneiderdowns.com



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### **PROFESSIONAL NEWS**

**Paul M. Matvey**, Tax Shareholder, was elected Vice President of the Board of Directors for the Pittsburgh Field Club.

**Cynthia D. Warsing**, Chief Financial Officer, was selected as a finalist for the 2011 CFO of the Year Awards presented by the *Pittsburgh Business Times*.

**Theodore M. Pettko**, Audit Shareholder, is currently participating in Leadership Pittsburgh XXVIII.

Melanie M. LaSota, Director of Estate and Trust Tax Services, attended the AICPA Advanced Estate Planning Conference in Boston in July. Melanie was also re-elected as Secretary of the Pittsburgh Youth Symphony Orchestra.

Angela M. Gillis, Internal Audit and Risk Advisory Manager, was elected the Correspondent Secretary for the Central Ohio Chapter of The Institute of Internal Auditors. She was also appointed Vice President of the Central Ohio Association for Government Accountants.

Eric M. Wright, Technology Advisors Shareholder, was elected Chair of the IT Assurance Committee for the PICPA.

Frank A. Wischart, Business Advisory Services Director, was published in the July/August 2011 edition of *The Value Examiner* with the article "Using the Weighted Average Cost of Taxation for Pass-Through Entities."

Cynthia J. Hoffman, International Tax Advisory Services Director, spoke at the teleconference "Form 1042 Compliance and Audit Strategies" in July. She was also appointed to the advisory board of Camp Mary Orton.

Meredith J. Christy, Audit Senior Manager, was appointed Chairman of the finance committee and a member of the executive committee of Armstrong County Memorial Hospital.

John R. Null, Audit Shareholder, presented at the AICPA National Advanced Accounting and Auditing Technical Symposium in Las Vegas in July.

Mary D. Richter, Tax Shareholder, was quoted in the August 19th *Pittsburgh Business Times* article "Firms Working to Take Bigger Spot on Global Stage."

Ron A. Kramer, Director of Specialized Tax Services, spoke to the Greater Pittsburgh Nonprofit Partnership/Forbes Fund regarding the fate of the charitable contribution.

Schneider Downs co-sponsored the 2011 EACUBO Workshop with EACUBO (Eastern Association of College and University Business Officers) in June. Charles A. Oshurak, Audit Senior Manger, served as Chair.

**Susan M. Kirsch,** Tax Shareholder, attended the AICPA Tax-Exempt Organization Technical Resource Panel Spring Meeting with the IRS.