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West Florida Chapter
ACCOUNTING CONFERENCE

June 17, 2011 • Pensacola

FICPA

New Conference!

2011 West Florida Chapter
Accounting Conference

Friday, June 17, 2011

8:10am-9:00am

Managing Risk.....1
Phillip S. Howell, J.D., CPA
Director/Galloway Johnson Tompkins Burr and Smith

9:00am-10:55am

Accounting & Auditing Update.....22
Robert T. Fahnestock, Ph. D., CPA
Chair and Professor/University of West Florida

10:55am-11:45am

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Gene B. Gaines, CPA
Senior Manager/Saltmarsh, Cleaveland & Gund, CPAs

12:45pm-1:35pm

Regional Economic Update: Is 2011 The Year for Recovery?.....36
Rick Harper, Ph.D.
Executive Director/ University of West Florida, Office of Economic Devlopment

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"When Good Leaders Lose Their Way".....48
Mark Whitacre, Ph. D
COO & President/Cypress Systems, Inc

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Betsy Bowers, CIA, CFE, CGFM, CIG
Associate VP /University of West Florida, Internal Auditing & Management Consulting

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Mary E. Wiggins, CISA, MCTS
Senior Manager/O'Sullivan Creel, LLP

Managing Risk

Phillip S. Howell, J.D., CPA

Phillip S. Howell

Director

Galloway Johnson Tompkins Burr and Smith

Phillip S. Howell (Director) practices in the area of commercial litigation with an emphasis on professional negligence defense, business and real estate disputes, construction liens and defects, and first-party insurance in federal and state courts. Phillip has represented diverse businesses to resolve their disputes through the most efficient means possible, from informal negotiations, mediation and arbitration, to litigation and trial. Phillip also handles appellate matters and has successfully argued before the Florida Supreme Court.

Phillip has represented attorneys, certified public accountants and other professionals in professional negligence litigation, and developers, design professionals, contractors, and materials manufacturers and suppliers in construction litigation in state and federal courts. He has presented seminars on Florida construction law and professional liability. Although Phillip's litigation practice has consisted primarily of commercial matters, he has defended personal injury and wrongful death claims in maritime, products liability and general negligence claims.

In addition to litigation matters, Phillip has handled a broad range of transactional matters, including business and commercial real property sales and purchases, re-financing, defeasance and foreclosures. He is well-versed in corporate formation, governance and tax matters. Before practicing law, Phillip practiced public accounting and continues to maintain his license as a Florida Certified Public Accountant, a designation he has held since 1991.

Phillip also is admitted to the United States Tax Court.

MANAGING RISK

Using Engagement Letters to Minimize the Risk of Professional Liability

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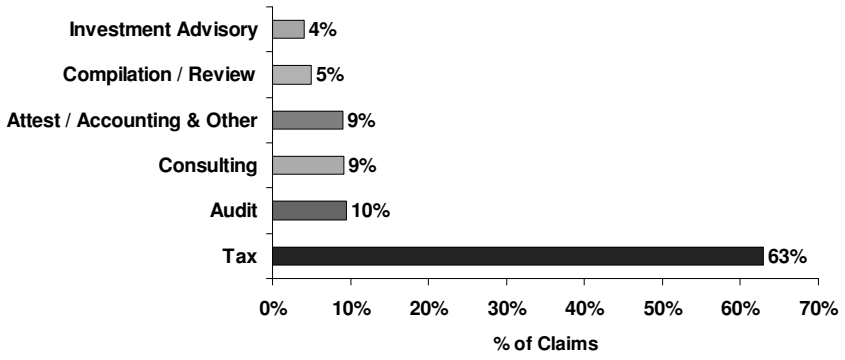
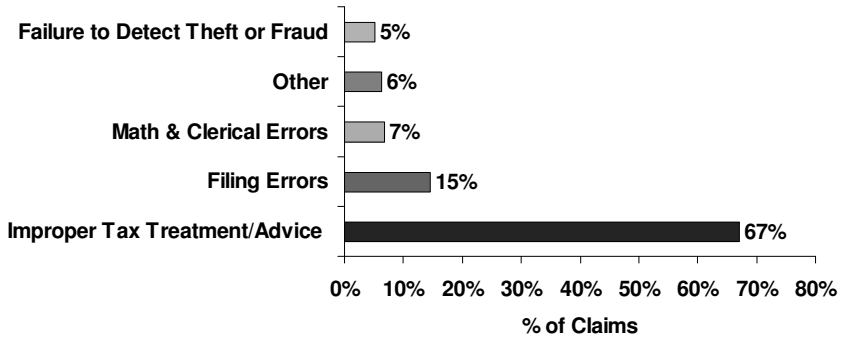
GALLOWAY JOHNSON TOMPKINS BURR AND SMITH
GJTBS

2010 Claims By Practice Area



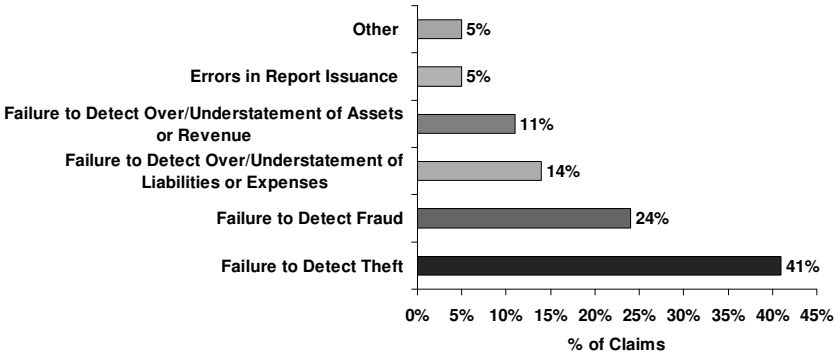
Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies

2010 Tax Causes of Loss



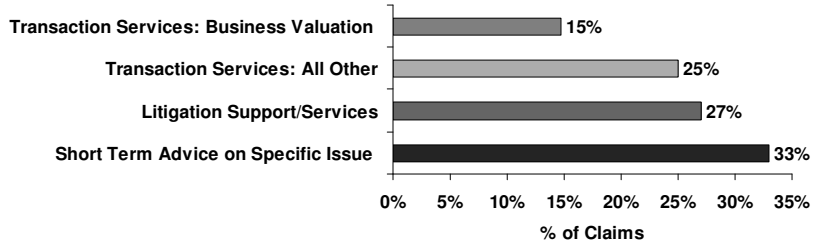
Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies

2010 Audit Causes of Loss



Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies

2010 Consulting Causes of Loss



Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies

Professional Standards

- Rule 201 of AICPA Code of Professional Conduct
  - (1) Professional Competence
  - (2) Exercise Due Care
- Professional Negligence - failure to comply is a breach of the standard care

http://www.aicpa.org/Research/Standards/CodeofConduct/Pages/default.aspx

Engagement Letters

The purpose is to establish an understanding

What should be included in an Engagement Letter?

- ✓ The parties to the engagement
- ✓ Services to be performed
- ✓ Responsibilities of the parties
- ✓ Termination of the engagement
- ✓ Limitations on liability and damages
- ✓ Fee arrangements

Parties to the Engagement

- Liability may hinge on a proper recitation of who is and who is not a party
- CPAs hired by attorneys
- Attorney-client privilege prohibits disclosure of the CPA's work prematurely

Scope of Services

Too much information

- Excessive detail may open CPA to charges that engagement was not completed in its entirety or that the conclusions are not properly supported

Too little information

- May result in misunderstandings and disputes with clients and third parties regarding the specific tasks to be performed

Responsibilities of the Parties

- Many CPAs have encountered a client who failed to disclose relevant information and documentation
- These failures could materially alter CPA's conclusions

Affirmative Duties on Client

- Prevents frustration and mistaken presumptions
- Client has duty to provide CPA with appropriate information
- Client is ultimately responsible for the submissions of the generated information or report

Identify the AICPA Professional Standards Applicable to the Engagement

These define and limit a CPA's responsibilities in different types of engagements

- A bookkeeping services engagement which will not include the compilation or review of a client's financial statements is governed only by the Code of Professional Conduct
- A consulting services engagement is governed by the Statements on Standards for Consulting Services
- A valuation engagement is governed by the Statements on Standards for Valuation Services.

Identify the AICPA Professional Standards Applicable to the Engagement

- A compilation or review engagement is governed by the Statements on Standards for Accounting and Review Services
- An audit engagement is governed by Statements on Auditing Standards

Best Practices – Tax

IRS Circular 230, Section 10.33

a. ***Best practices.*** Tax advisors should provide clients with the highest quality representation concerning Federal tax issues by adhering to best practices in providing advice and in preparing or assisting in the preparation of a submission to the Internal Revenue Service. In addition to compliance with the standards of practice provided elsewhere in this part, best practices include the following:

Best Practices – Tax

IRS Circular 230, Section 10.33 (Cont'd)

1. Communicating clearly with the client regarding the terms of the engagement. For example, the advisor should determine the client's expected purpose for and use of the tax advice and should have a clear understanding with the client of the form and scope of the advice or assistance to be rendered.

Best Practices – Tax

IRS Circular 230, Section 10.33 (Cont'd)

2. Establishing the facts, determining which facts are relevant, evaluating the reasonableness of any assumptions or representations, relating the applicable law (including potential applicable judicial doctrines) to the relevant facts, and arriving at a conclusion supported by the law and the facts.

Best Practices – Tax

IRS Circular 230, Section 10.33 (Cont'd)

3. Advising the client regarding the import of the conclusions reached, including, for example, whether a taxpayer may avoid accuracy related penalties under the Internal Revenue Code if a taxpayer acts in reliance on the advice.

SSARS 19

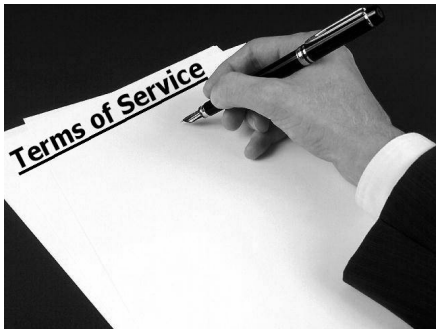
Changes to compilation and review standard

- Reviews
  - Previously, the SSARSs stated that it was preferable that the understanding be in writing
  - SSARS 19 now requires that the understanding be documented in writing
  - Effective for financial statements ending on or after December 15, 2010

Audits
Use of Engagement Letters

- Carefully define scope of services
- Consider intended users
- Define management's responsibilities

Terminating an Engagement



- Provide an option to withdraw from engagement
- List contingencies warranting the CPA's right to withdraw
  - Providing untruthful information
  - Being dishonest or uncooperative

Terminating an Engagement

- Bars client from alleging a CPA's withdrawal led to further damages
  - Demise of client's business
  - Loss of business opportunities

Limiting Liability & Damages

- Hold harmless provisions may
  - Limit the liability of the CPA
  - Limit the amount of damages
    - Consequential
    - Incidental
    - Punitive
  - Provide for indemnification or contribution

Limitations on Liability Provisions are Strictly Construed

- Courts will not enforce unless the language is clear and unequivocal

Courts often look for ways to find limitation of liability language unconscionable or unenforceable, especially when there is significant exposure at issue (i.e., clause limits losses to $100,000 in fees paid to the CPA when the potential loss is $10M)

Example of an Indemnification Provision That Was Disallowed

[Client] hereby indemnifies [auditors] and its partners and employees and holds them harmless from all claims, liabilities, losses, and costs arising in circumstances where there has been a knowing misrepresentation by a member of [client's] management, regardless of whether such person was acting in [client's] best interest. This indemnification will survive termination of this letter.

Fee Arrangements

- Fixed Fee
- Time and expenses
- Contingency

Contingent Fees

- Some engagements lend themselves to a contingent fee arrangement
- For example, the engagements involving the recent BP oil spill claims
- Juries may frown upon contingent fee arrangements

Contingent Fees

- Each state has its own specific rules regarding fee arrangements for performing a professional service
- Conduct careful research regarding the state's individualized rules and regulations before charging a contingent fee

AICPA Code of Professional Conduct

- Rule 302 prohibits contingent fees for certain services:
  - Audits or reviews of financial statements
  - Compilation of a financial statement that CPA reasonably expects third party to rely on and the compilation report does not disclose a lack of independence
  - Examining prospective financial information
  - Preparation of a tax return or refund claim not subject to substantive review

Florida's Rules

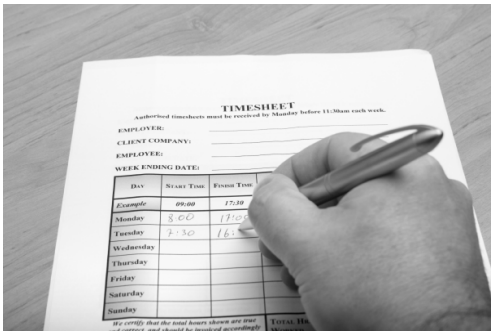
- Florida Administrative Code, Rules 61H1-21.003 and 61H1-21.005, prohibits contingent fees for:
  - Audits
  - Review or compilation services
  - Services for prospective financial data
  - Tax filings, unless that taxing authority has begun an audit on a tax filing

Florida Statute § 473.302(8)(a)

- CPAs are prohibited from accepting a contingent fee in connection with the following services:
  - Preparing an opinion on financial statements
  - Attesting as an expert to the reliability of financial information

Defending Fees

- Under any arrangement, ALWAYS document in your working papers the time incurred in performing the services
- Consider promissory notes, personal guarantees or other forms of security



Fee Arrangements for Experts

- Judge determines whether an expert is qualified to testify
- Judge determines whether CPA has the minimum qualifications in area CPA is expected to testify:
  - Special knowledge
  - Special skill
  - Special experience
  - Special training
  - Special education

Protecting "Unqualified" Experts

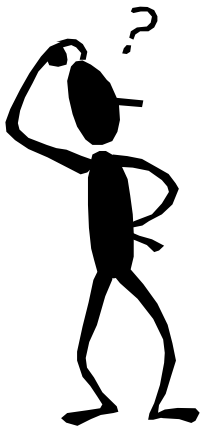
- Some clients will not pay CPA if judge determines that CPA is unqualified to testify
- Protecting against this attack:
  - (1) Attach curriculum vitae (CV) to engagement letter so client does not later claim lack of knowledge
  - (2) Include provision that CPA is still entitled to payment despite a judge's determination that CPA is unqualified to render testimony in case

Accept only those engagements in which you have sufficient competence and experience to complete the engagement with due professional care, and decline other engagements

AND

Use a properly crafted engagement letter to minimize risk, avoid misunderstandings with clients, and ensure timely payment.

Questions?



Accounting & Auditing Update

Robert T. Fahnestock, Ph. D., CPA

Bob Fahnestock

Professor and Chair
Department of Accounting and Finance at the
University of West Florida

Bob is Professor and Chair of the Department of Accounting and Finance at the University of West Florida. He has been at UWF for 37 years. He is also a native of Pensacola. He has a B.S. degree and Master of Accounting degree from Florida State University. His Ph.D. is from the School of Accountancy at the University of Mississippi. Bob received his Florida CPA Certificate in 1972.

Bob has given numerous professional and academic presentations and published in a variety of journals and periodicals. He is a member of the FICPA, AICPA, and American Accounting Association. His primary area of expertise is in the area of financial accounting and reporting.

Retirement & Benefits Update

Gene “Benny” Gaines, CPA

Benny Gaines, CPA

Senior Manager

Saltmarsh, Cleaveland & Gund

Benny is in charge of the Employee Benefit Plan practice at Saltmarsh, Cleaveland & Gund in Pensacola, Florida. He joined the firm in 2010 after having worked with employee benefit plans at Deloitte & Touche for over 16 years. He began his specialization in the employee benefit plan industry after college while working with an Employee Benefits Consulting Firm in Nashville, Tennessee, which focused exclusively on Taft-Hartley Pension and Welfare benefit plans (Collectively Bargained Union Plans).

In addition to the employee benefit plans practice, Benny maintains a broad range of tax experience with large and small businesses.

Benny received his Bachelors degree in Accounting from the University of Alabama. He maintains his CPA license in Tennessee and is in the process of receiving his Florida CPA license. He is a member of the American Institute of Certified Public Accountants and serves on a national employee benefit plan industry committee with PKF North America.

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Current Developments in Employee Benefit Plans

Presented by:
Benny Gaines, CPA
Saltmarsh, Cleaveland & Gund
June 17, 2011

Current Developments

Government Regulators

- **DOL/PBGC**
  - Fiduciary Standards
  - Financial Accounting Standards
  - Advocate for Participant Rights
  - Guaranty of DB pension benefit
- **IRS**
  - Monitor tax benefits to Sponsor and Participants
  - Enforcement by plan exams
  - EPCRS-Corrections Program

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Current Developments

DOL Update

- Regulatory
- Audit Quality
- Reporting Compliance Initiatives
- EFAST2

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Current Developments

Regulatory Update

- Disclosures, disclosures, disclosures
- Employee Deferrals
- Fiduciary Project

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Current Developments

Audit Quality Update

(EB Plan Audits-From 2008 Form 5500 Database)

- Estimated 9,500 CPA Firms
- Approximately 77,000 Plan Audits
- 64% were Limited Scope Audits

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Current Developments

Audit Quality Update

- Enforcement Focus
  - Firms performing the most audits
  - Firms performing the fewest audits
  - Multi-employer plan audits
  - ESOP audits
  - Health and Welfare plan audits

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Current Developments

Audit Quality Update

- Commitment to Quality at Executive Level
- Importance of EBP Audit Practice
- Internal Inspection Programs

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Current Developments

Reporting Compliance Initiatives

- Stop Filer Program
- Late Filer Program
- Filings with missing IQPA Reports
- Filings with missing Schedule C and Schedule C data

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Current Developments

Reporting Compliance Initiatives

- 403b Plan Filings
- From 5500-SF Eligibility
- Small Plan Audit Waiver Eligibility
- Black-Out Notice Rules

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Current Developments

EFAST 2

- #1 Filing Error***-STOP I-104 Message***
- Amended Filings
- SSA Data-Form 8955
- DFVC Program

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Current Developments

IRS Update

Employee Plans Strategies

- 401k Compliance Issues
- Abusive Transactions & Emerging Issues
- New 403b programs
- EPCRS

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Current Developments

401k Compliance issues

- 401k Compliance Questionnaire EPCU Project
- Top 401k Errors
- Common Errors

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Current Developments

Abusive Transactions

- Plan Exams
- Emerging Issues
- EPCU & supplemental exams

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Current Developments

403(b) Programs

- Develop Pre-approved 403(b) program
- Develop 403(b) Fix-It Guide

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Current Developments

EPCRS

- Self-Correction Program (SCP)
- Voluntary Correction Program (VCP)
- Closing Agreement Program (CAP)

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Current Developments

Online Help

- IRS- www.irs.gov "Retirement Plans Community" tab
- DOL- www.dol.gov/ebsa/
- AICPA- www.aicpa.org "Employee Benefit Plan Audit Quality Center"
- Numerous law firms and industry emails

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Current Developments

Questions?

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Current Developments

Benny Gaines, CPA

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Current Developments

This presentation and the related discussion contain general information only, and the speaker or their firms are not, by means of this presentation and discussion, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services.

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Current Developments

Some of the developments noted in this presentation were compiled from the sessions presented at the AICPA's National Conference on Employee Benefit Plans held May 1–3, 2011.

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Regional Economic Update: Is 2011 The Year for Recovery?

Rick Harper, Ph.D.

Rick Harper, Ph. D

Executive Director

University of West Florida,

Office of Economic Development and Engagement

Rick Harper's career as an economist began in 1979 at the Research Triangle Institute in North Carolina, where he was involved in all phases of various funded research projects. Rick received his Ph.D. in Economics from Duke University in 1989 and joined the UWF faculty that same year. He received his bachelor's degree from Guilford College in North Carolina. Rick directs UWF's new Office of Economic Development and Engagement. He served on Governor Jeb Bush's Council of Economic Advisors from 2001 – 2006. He supported the economic analysis work of the Florida Senate on a variety of issues and has done extensive work on the economic impact of the BP oil spill.

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FLCPA West Florida Chapter

Regional Economic Update: Is 2011 the Year for Recovery?

UWF Office of Economic Development and Engagement
The University of West Florida
Rick Harper, Ph.D., Director

June 17, 2011

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Economic Drivers in the National Picture

- Decent economic growth (domestic CapEx needed)
- Job weakness continues (Timing lags, GDP structural deficit)
- Housing market weak (Need formation of new households)
- Monetary policy (Fed has tools necessary to unwind QE)
- Fiscal policy ($1,540,000,000,000 deficit)
- Energy prices / inflation (oil $100+, some commodity inflation)
- Dollar / inflation ($ sideways, inflation expectations anchored)
- Growth abroad picks up (esp. SE Asia, helps US exports)

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National Outlook 2011:

- Housing purchase prices more affordable
- Economic activity well up from recession levels
- Economic growth trajectory suffering from debt overhang
- Unemployment flat, and remains above 8%
- Residential real estate market recovery awaits economic recovery
- 10 year Treasury yield wobbles with continued economic uncertainty
- Homebuyer tax credit expired
- Large banks prosper, community banks fail
- Budget crisis continues until economy resumes strong growth
- Health care cost trajectory unsustainable

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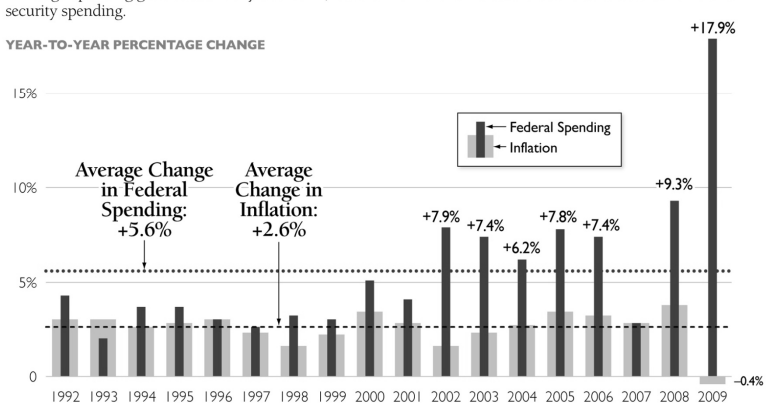
Federal Spending Is Outpacing Inflation

Prices normally rise year to year, but federal spending has risen even faster, making it more costly than ever. Although spending grew substantially after 9/11, less than half of the increase is due to defense and homeland security spending.

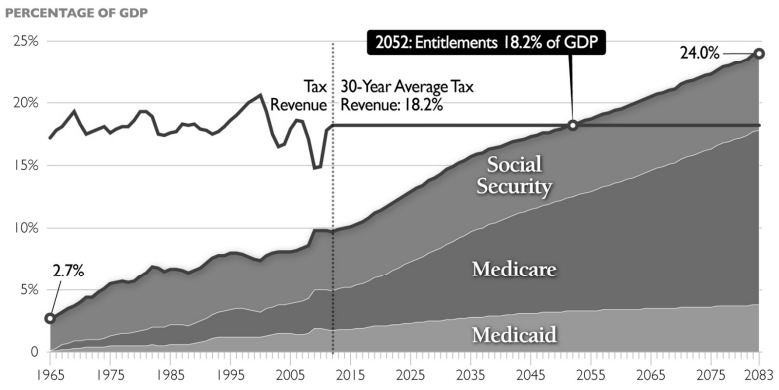


Source: White House Office of Management and Budget and Bureau of Labor Statistics.

Federal Spending Chart 5 • 2010 Budget Chart Book ☎ heritage.org

Entitlements Will Consume All Tax Revenues by 2052

If future taxes are held at the historical average, spending on Medicare, Medicaid, and Social Security will consume all revenues by 2052. Because entitlement spending is funded on autopilot, no revenue will be left to pay for other government spending, including constitutional functions such as defense.



Source: Congressional Budget Office.

Entitlements Chart 1 • 2010 Budget Chart Book ☎ heritage.org

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Florida: Recovery Lags the Nation

- Massive housing inventory being slowly absorbed – at falling prices. Adverse wealth effects.
- Unemployment hovers at 11% . Structural issues.
- Population growth remains weak.
- Local government budget stresses.

✓ Investment Incentives Will Provide Short-Term Boost.
✓ Impediments to Productivity Growth Must Be Addressed.

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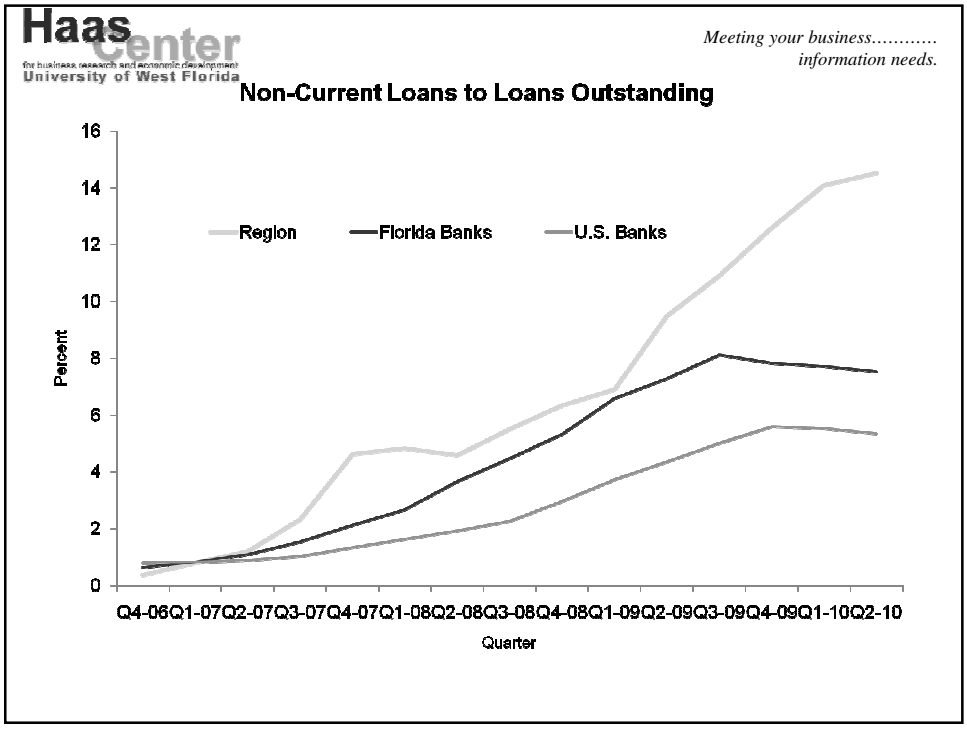

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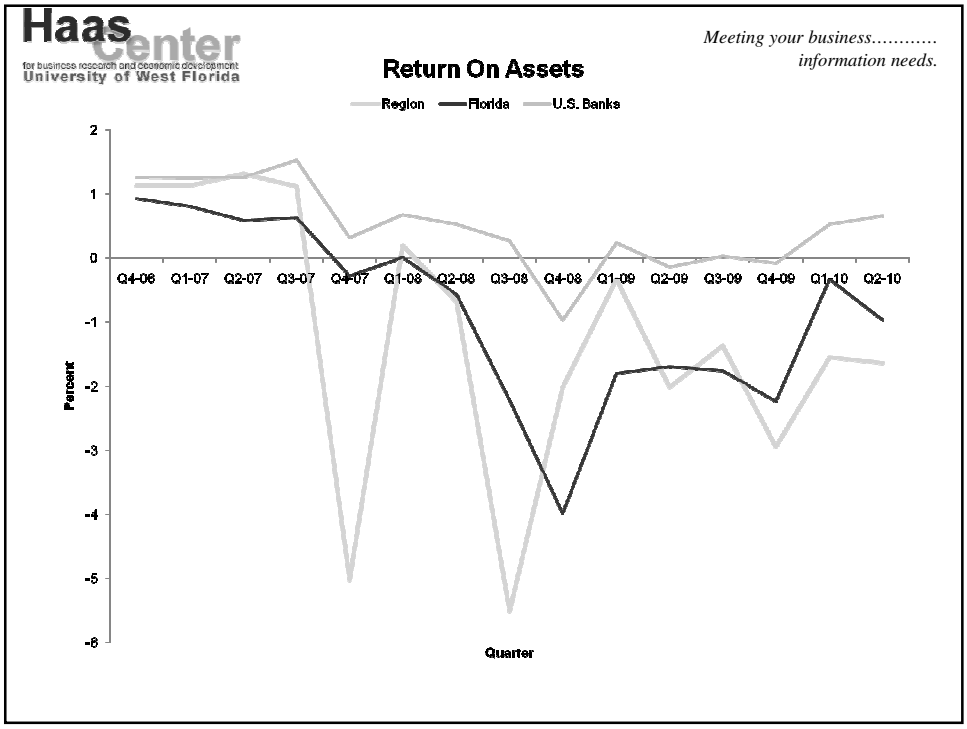

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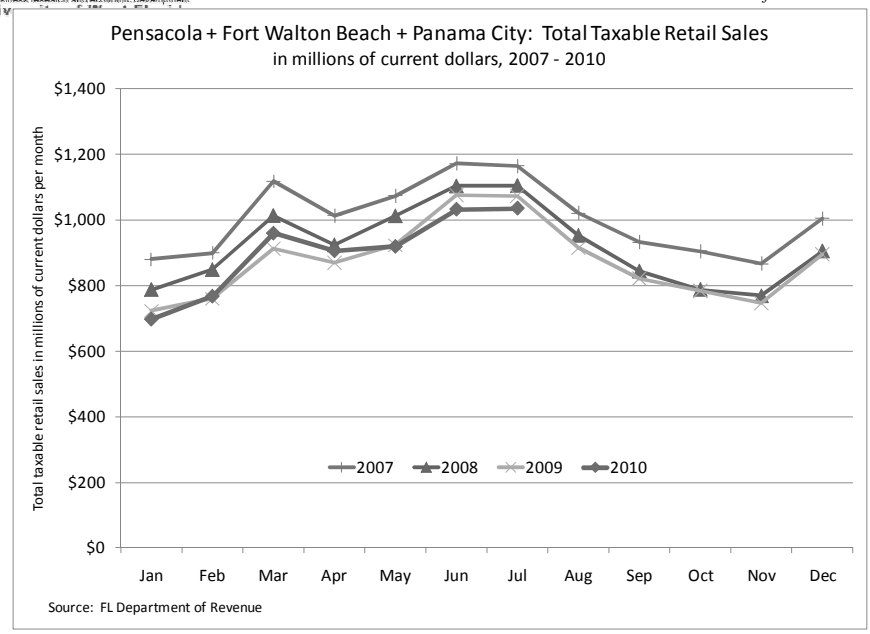

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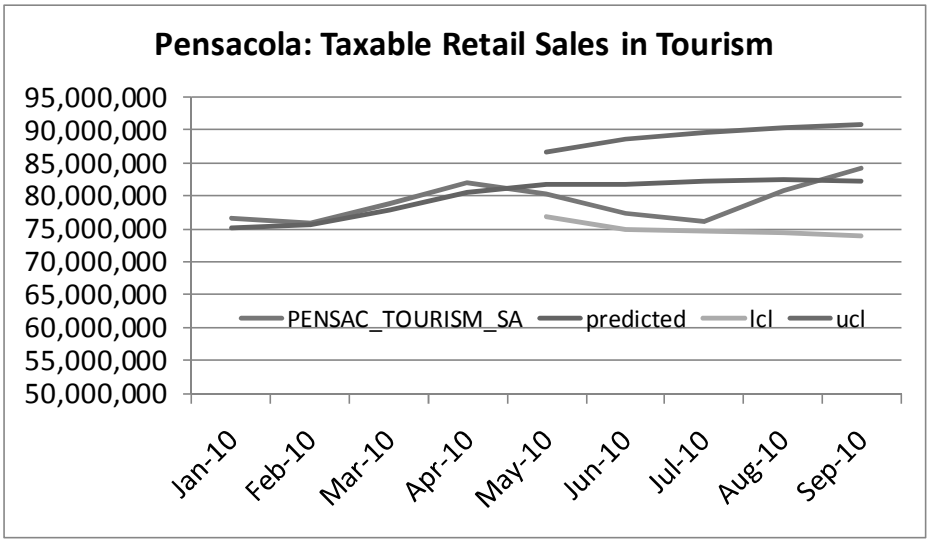

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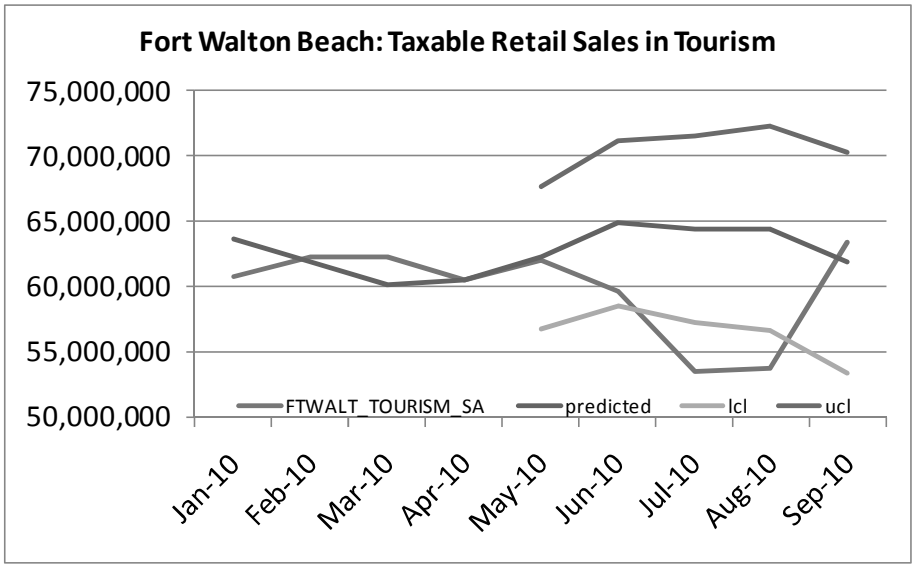

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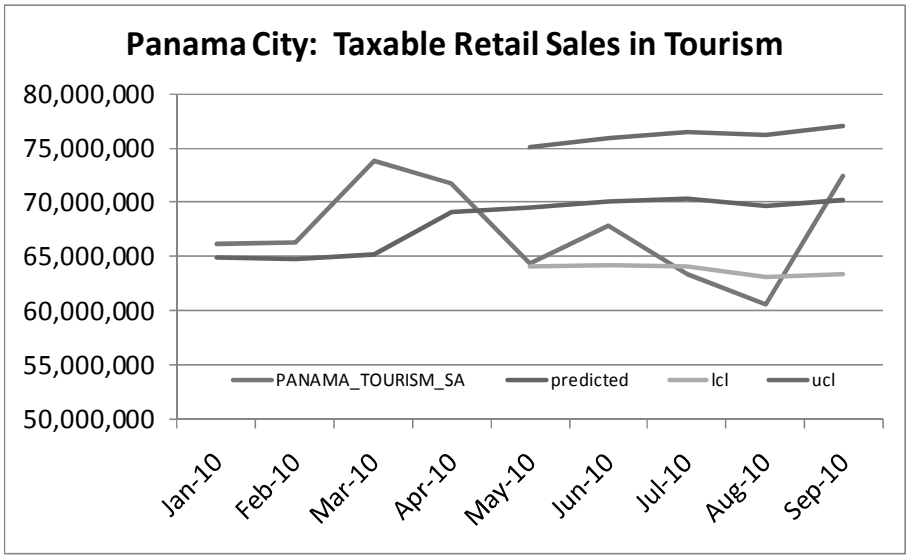

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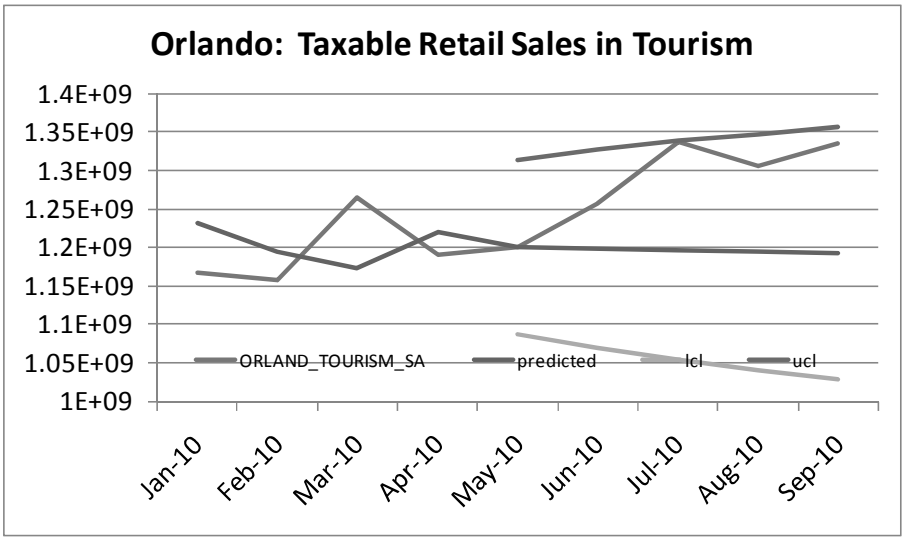

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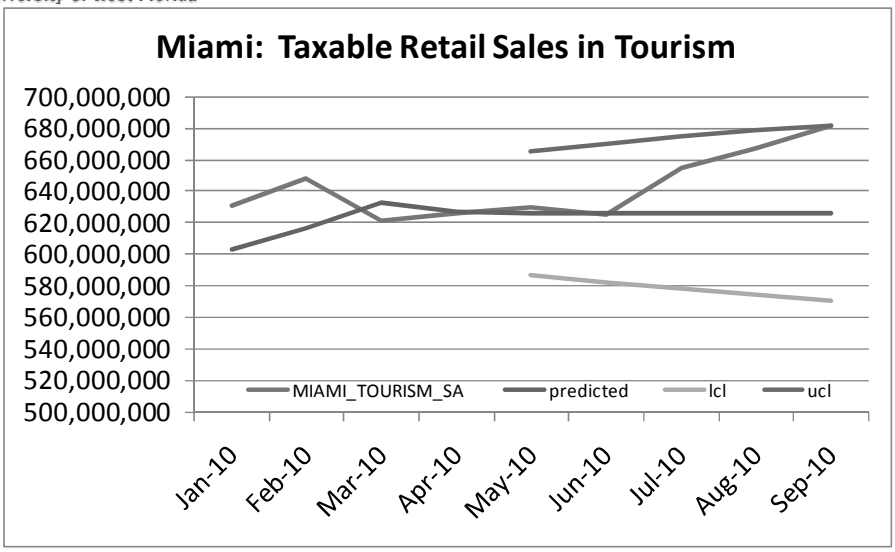

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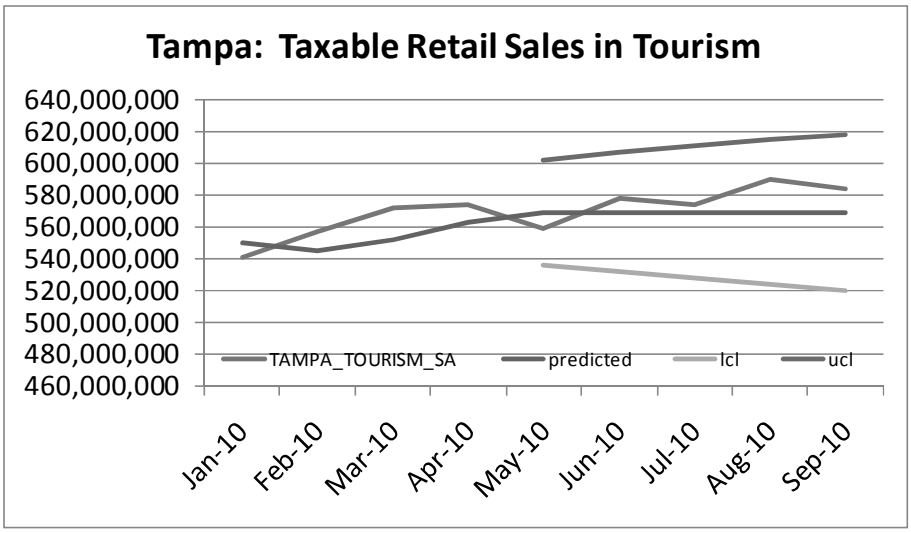

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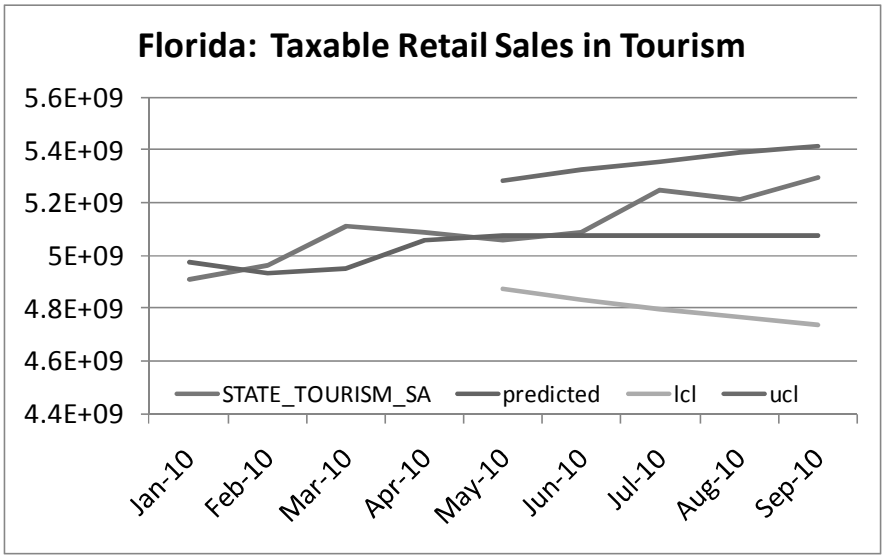

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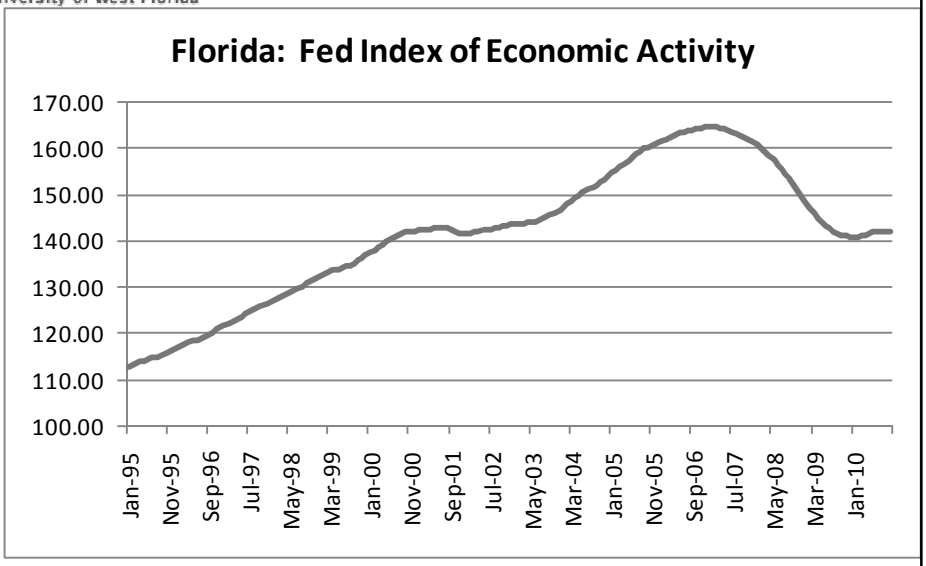

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What are the bright spots?

- Home price drop helps FL competitiveness
- NW FL with less than average housing overstock
- Miles of National Seashore/AFB limited coastal speculation
- The big 3: military payrolls, drive-to tourism, healthcare
- Pilot training, Special Ops, Weapons RDTE look safe
- JSF & 7th SF arrive
- NW FL entered recession earlier than FL, recovers earlier
- Longer-term baby boom demographics are good

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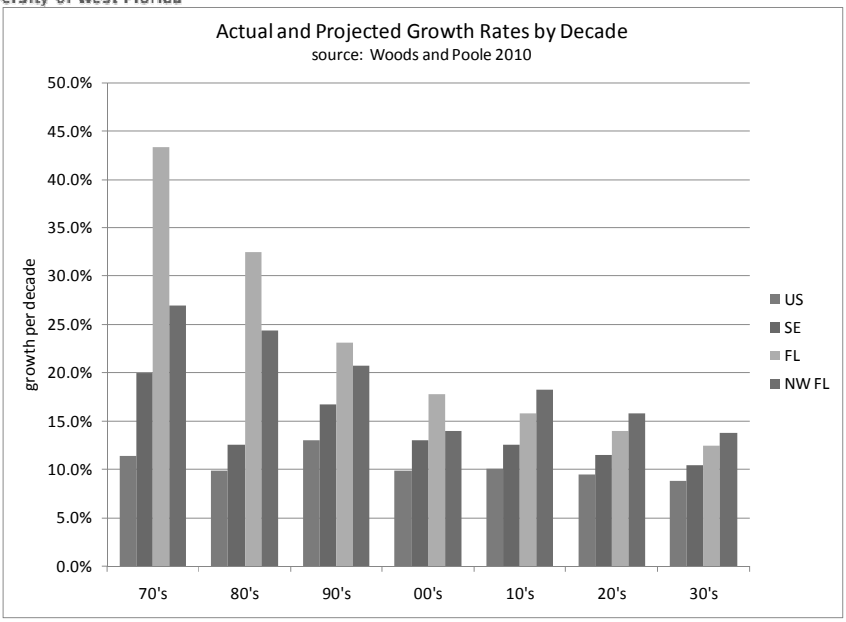
information needs.



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Meeting your business.....
information needs.

FLCPA West Florida Chapter

Regional Economic Update: Is 2011 the Year for Recovery?

Questions?

UWF Office of Economic Development and Engagement

The University of West Florida

Rick Harper, Ph.D., Director

June 17, 2011

"When Good Leaders Lose Their Way"

Mark Whitacre, Ph.D

Mark Whitacre

COO & President

Cypress Systems, Inc

Presentation Topic: "When Good Leaders Lose Their Way".

The ultimate lesson in personal and business ethics…but is also a story of Hope, Family Commitment, Redemption & Second Chances, and a real-life example of Overcoming Extreme Adversity, against all odds.

Bio

Mark Whitacre is the subject of the recent book, "***Mark Whitacre Against all Odds"***. This new book highlights Mark's redemption and second chance. In addition, a new feature film is currently in early development, titled "***The Harvest King***" to highlight the inspirational story about how Mark and Ginger Whitacre survived against all odds, and Mark's redemption and comeback in the business world. Mark Whitacre was also the subject of the *Warner Brothers* 2009 feature film, ***"The Informant"***, starring Matt Damon as Mark Whitacre, and the recent *Discovery Channel* TV-documentary, ***"Undercover"***.

Mark Whitacre is an Ivy League Ph.D. and was the highest-level executive of a Fortune 500 company to become a whistleblower in US history. After blowing the whistle in 1992, Mark then worked undercover with the FBI for 3 years wearing a wire everyday in one of the largest price-fixing cases in history. Working undercover for such a long period of time took a tremendous psychological toll on Mark in the mid-1990s. After his undercover tenure was completed, Mark went to federal prison for eight and a half years for white-collar crimes (fraud) that occurred during his undercover tenure. What was remarkable, he was able to keep his marriage to his high school sweetheart and family completely intact. Today, the FBI agents, whom were involved with Whitacre's case, tout Whitacre publicly as a "national hero" for his substantial assistance with one of the most important white-collar cases in history. And four FBI agents -along with a former federal prosecutor involved with Mark's case- are lobbying for a Presidential Pardon for Mark.

His story is an important personal and business ethics lesson about "doing the right thing". But it is also a story of hope, family commitment, how to overcome extreme adversity, and a story of how redemption and second chances really do exist in America. After Mark's decade-long prison sentence was completed, he rejoined his loving family and was quickly hired as an executive back to his roots in the biotechnology industry. After a few years, he was promoted to COO and President. Further information about Mark Whitacre is at his official website, www.markwhitacre.com , and **http://www.jpw3.org/missionpossible-markwhitacre.html .**

When Good Leaders Lose Their Way

Under pressure living two lives

Archer Daniels Midland

Moral Compass

FBI Agent Brian Shepard

Think about it!!! What would you have done?

Three Paradigms

-Short Term vs. Long-term

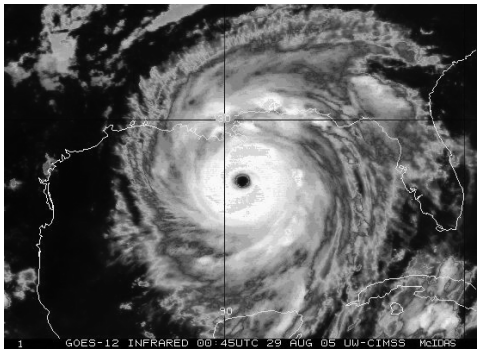
-Individual vs. Community

-Loyalty vs. Truth

Good leaders can lose their way

Know Your Value System

If unclear, then decisions can be tough



Background

Solid midwestern roots

Any hints of criminality ?

Background

- Not one to take shortcuts which is often associated with criminal activity

What is life like working undercover?

It is a double life

Life undercover and wearing a wire everyday

International Cartel

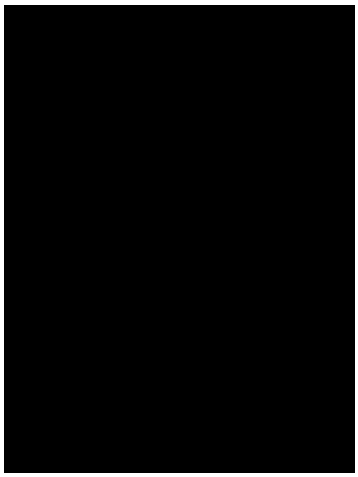
- Illegal meetings were around the globe:
  Hong Kong, Japan, Mexico City, Paris
  Vancouver, Switzerland

Life as an Informant

Life as an Informant

Life as an Informant

"Mark, an executive is blocking our video camera view"



Life as an Informant

Actual tape recorder used in Japan

Changing tapes in Japan

Prosecutors needed me to get cartel members to say…

Life as an Informant

- Atlanta meeting helped to seal their fate

From Whistleblower to Target

Let's Discuss

How were the frauds done?

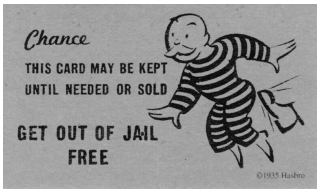
How was the price fixing done?

How were both undetected?

What was I thinking?

- The Deal of a Lifetime!

  Lawyer James Epstein



- Take home message:

  Listen to the professionals you hire

From that to this!!!

White collar crime: More people going to jail than ever before

Fraud and unethical activities happen in every industry

Corporations

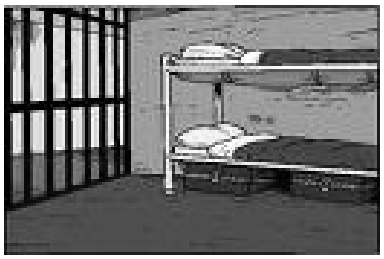
Non-profit organizations

Government

Churches

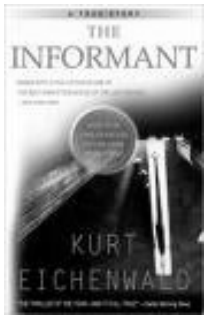
Schools

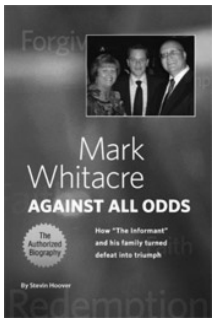
The Prison Years

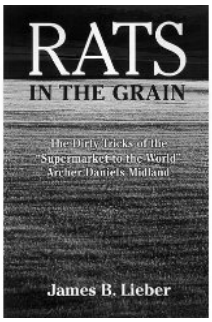


Over 8 ½ years in federal prison

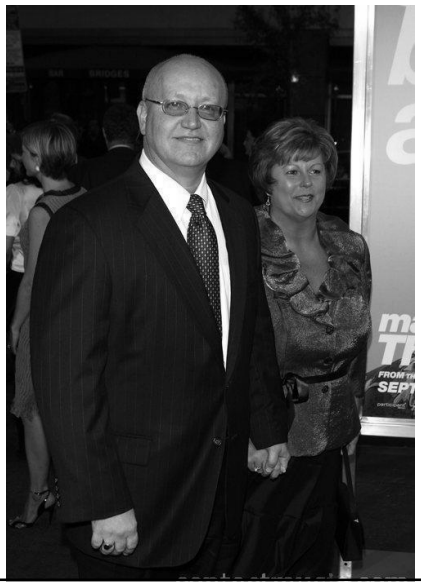
Better not Bitter-You can overcome extreme adversity!!!







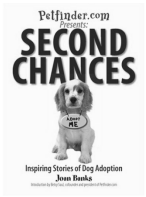
Movie Premiere



Movie Premiere

It was not worth it!!!

-with my Family…



-with Food Companies (the victims)

-with FBI & Prosecutors…

-with my Career..Cypress Systems, Inc

HealthWarehouse.com

SM

OTC=HEWA

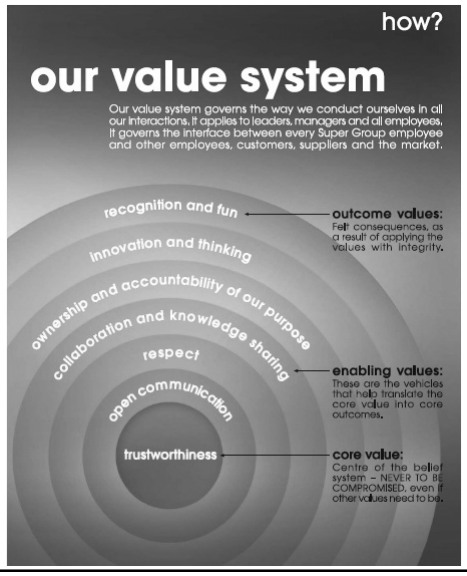
.

A 2-minute news clip by the FBI is embedded here, and will be played **at the June 17th conference**

Preventive Measures

- Keep your life balanced, not all work…

Know Your Value System



Corporate Conscience

It's not just about "shareholder value"!

We need to shift our thinking towards

"PURPOSE"

Ethical Fitness

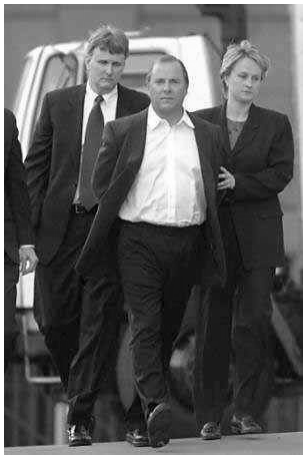
Like physical fitness, it is not a passive exercise

www.globalethics.org

Reflections

- Never deviate from what is the right thing to do!!!

Do Not Become One of These Scandals



Every person is the architect of their own character

Always think long-term

Live your life assuming the green lamp is always with you

Let's Discuss

How were the frauds done?

How was the price fixing done?

How were both undetected?

Internal Controls and Expense Reimbursement Schemes

Betsy Bowers, CIA, CFE, CGFM, CIG

Betsy Bowers

Associate Vice President for Internal Auditing & Management Consulting

University of West Florida

Betsy Bowers is the Associate Vice President for Internal Auditing & Management Consulting at the University of West Florida (UWF), where she has directed internal auditing since 1993. She is also adjunct professor at UWF, teaching an upper-division course on White Collar Crime.

Ms. Bowers has worked in higher education for more than 25 years, as a grant accountant, internal auditor, and internal audit director/chief audit executive. Prior to coming to Florida, she worked in Tennessee at East Tennessee State University and Northeast State Technical Community College (NSTCC), where she launched the internal auditing function at NSTCC.

Ms. Bowers received her BBA in Accounting and her MBA from East Tennessee State University. She holds Certified Internal Auditor (CIA), Certified Fraud Examiner (CFE), Certified Government Financial Manager (CGFM), and Certified Inspector General (CIG) designations.

A past president of Institute of Internal Auditors (IIA) chapters in Tennessee and Florida, Ms. Bowers serves on the Board for the Northwest Florida Chapter and is an instructor for IIA seminars. In 2008, the Northwest Florida chapter established the *Betsy Bowers Scholarship* with the University of West Florida for students desiring to pursue internal auditing careers. Two $500 scholarships are given each Fall Semester. Ms. Bowers is immediate past president of the Northwest Florida chapter of the Association of Certified Fraud Examiners (ACFE) and serves now as the chapter secretary. She is a member of the Steering Committee for the Northwest Florida InfraGard chapter, sponsored by the Federal Bureau of Investigation's National Infrastructure Protection Center. Ms. Bowers is a past national president of the Association of College & University Auditors (ACUA).

Recently, Ms. Bowers led the university's financial recovery for the Deepwater Horizon Oil Spill, which affected the beaches of Pensacola, Fl. From 2005 to 2008, in addition to internal auditing, Ms. Bowers led hurricane financial recovery for the University of West Florida. As a result, she was appointed to the Florida Board of Governors' Emergency Preparedness Taskforce, and has spoken on disaster recovery at national conferences for ACUA, IIA, National Association of College and University Business Officers (NACUBO), Society for College and University Planning, Council of Higher Education Management, and Health and Educational Facilities Finance Associations.

Expense Reimbursement Schemes

Betsy Bowers, CIA, CFE, CGFM, CIG
Associate Vice President, Internal Auditing
University of West Florida
June 17, 2011

Learning Objectives

- Explain what constitutes expense reimbursement fraud.
- Discuss the data on expense reimbursement fraud from the *2010 National Fraud Survey*.
- Understand how mischaracterized expense reimbursement schemes are -committed.
- Be familiar with the controls identified for preventing and -detecting mischaracterized expense schemes.
- Identify the methods employees use to overstate otherwise legitimate -expenses on their expense reports.
- Understand controls that can be used to prevent and detect overstated -expense schemes.

Learning Objectives

- Explain what a fictitious expense reimbursement scheme is and differentiate it from other forms of expense reimbursement fraud.
- Identify red flags that are commonly associated with fictitious expense schemes.
- Discuss what a multiple reimbursement scheme is and how this kind of fraud is committed.
- Discuss the controls identified in this chapter for preventing and detecting multiple reimbursement schemes.
- Be familiar with proactive audit tests that can be used to detect various forms of expense reimbursement fraud.

3

What Is Expense Reimbursement Fraud?

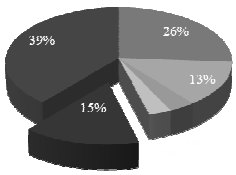
- Employees overstate business expenses to generate inflated reimbursements
- Very common type of fraud
- Difficult to detect

http://www.youtube.com/watch?v=UNt46Xj7aMU

Expense Reimbursement Schemes

- Mischaracterized Expenses
- Overstated Expenses
- Fictitious Expenses
- Multiple Reimbursements

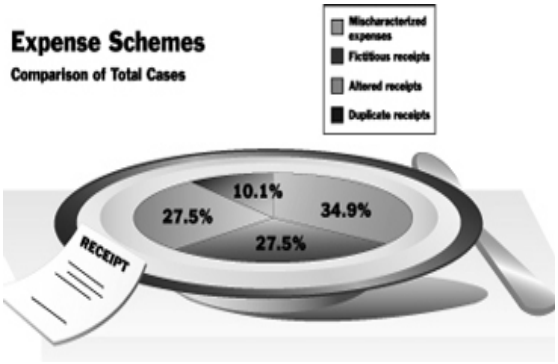
Expense Reimbursement Schemes



278 expense reimbursement schemes were reported, with a median loss of $33,000.

Source:
ACFE Report to the Nation 2010

Expense Reimbursements – Breakdown of Cases



Mischaracterized expenses were the most common scheme, followed by fictitious and altered expenses.

Mischaracterized Expenses

Employee claims reimbursement for non-business expenses by classifying them as business-related

- Personal travel, vacations
- Personal meals
- Dates, etc.

search ID: ghm470
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Mischaracterized Expenses – Countermeasures

- Clearly communicate company policy on reimbursable expenses
- Require detailed expense reports with date, time, purpose for expense
  - Independently spot-check with customers
- Compare dates and times of expenses with employee's work schedule

Mischaracterized Expenses – Countermeasures

- Compare expense reimbursements to budgeted levels and to prior years
- Analyze expense reimbursements per employee
- Require all expense reports to be approved by a supervisor

Overstated Expenses

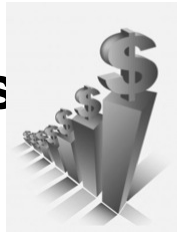
Employee pads reimbursement by overstating actual business expenses.

- Common way to funnel $ to slush funds
- Common scenarios:
  - No support required for reimbursements
  - Employee alters receipts

http://www.youtube.com/watch?v=AkiIp0dNq6c

http://www.bbc.co.uk/news/uk-politics-13006446

Overstated Expenses



"Overpurchasing"

- Variation of overstated expenses scheme:
  - Buy two plane tickets,
  - One cheap, one very expensive
  - Fly on the cheap ticket
  - Return expensive ticket, keep receipt for expense report

Overstated Expenses – Countermeasures

- Require original support for all reimbursements – no photocopies
- Obtain vendor records to verify questionable expenses
- Compare the cost of similar expenses incurred by different employees (e.g., A & B both fly to Atlanta; A's ticket $400 more)
- Look for department-wide trends of excessive reimbursements – indicator of slush fund

Fictitious Expenses

Employee submits nonexistent expenses

- Produce fictitious receipts
- Obtain copies of blank receipts from restaurants, bars, etc.
- Claim expenses paid by clients or other parties

Fictitious Expenses - Countermeasures

- Track expense reimbursements per employee; look for:
  - Expenses that consistently rounded off, ending with “0” or “5”
  - Expenses consistently for same amount
  - Expenses that tend to fall just below reimbursement limit
  - Employees who pay cash for high-dollar items (no audit trail)

Fictitious Expenses - Countermeasures

- Compare credit card statements to employee expense reports
- Look for counterfeit receipts – poor quality, no phone or address, no logo, etc.
- Compare mileage claims to travel actually incurred
- Look for consecutively numbered receipts in support of expenses

Multiple Reimbursements

Employee requests more than one reimbursement for the same expenses

- Submit several types of support for same expense (e.g., travel agency invoice and airline ticket stub for same flight)
- Submit several copies of the same support through different departments or budgets
- Submit expense, wait a month, submit it again

Multiple Reimbursements – Countermeasures

- Do not accept photocopies as support
- Run reimbursement reports per employee, look for duplicate amounts, support, etc.
- Do not reimburse old expenses (e.g., 60 day limit)
- Investigate expense reports approved by supervisors outside requestor's department

Multiple Reimbursement Schemes

- A single expense item is submitted several times to receive multiple reimbursements
  - Example: Airline ticket stub and travel agency's invoice
- Submit the credit card receipt for items charged to the company's credit card account
- Submitting the same expenses to different budgets

Preventing and Detecting Multiple Reimbursement Schemes

- Enforce a policy against accepting photocopies
- If photocopies are accepted, the accounting system should have an edit for duplicates
- Establish clearly what types of support documentation are acceptable
- Scrutinize expense reports that are approved by supervisors outside the requestor's department
- Require expense reimbursements be approved by the employee's direct supervisor
- Establish a policy that expenses must be submitted by a certain time limit

Expense Reimbursement Controls

- Expense reports should require the following information:
  - Original support documentation
  - Explanation of business purpose
  - Time and date
  - Place of expenditure
  - Amount

- Any deviations require independent verification

Safeguards to Prevent Expense Fraud

- **1. Maintain a travel reimbursement policy or guidelines**
  2. Require original documentation
  3. Initiate a formal review process
  4. Routinely question expenditures
  5. Have all disbursements made in a formal manner
  6. Implement the use of corporate charge cards
  7. Receive credit activity reports on a monthly basis
  8. Annually audit a sample of employees' expense reports
  9. Treat reimbursement activities consistently
  10. Prosecute offenders

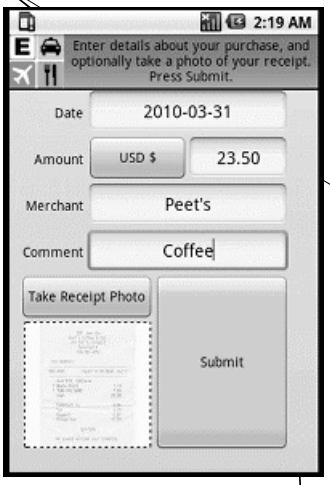
Expense Reimbursement Controls

- Detailed review of all expenses by a supervisor
- Regular comparison of expenses with historical and budgeted amounts
- Spot-check expenses with employee work schedule, client records, service provider, etc.
- Data mining by auditors

Paperless Environment

•Pages per employee is increasing at 10% per year
• Organizations now maintain **30 times more** data than in 1999 (Gartner)
• The U.S. annually spends $25-35B filing, storing and retrieving paper.
• The number of pages consumed in the U.S. offices is going up at the rate of **20% per year**.
• Typical office workers spend 40% of their time looking for information.
• **Professionals spend over 500 hours annually reviewing & routing files, and another 150 hours looking for incorrectly filed documents.**
• A Gartner Study reveals the average document is copied 9 times
• It is estimated that 80% of information is still retained on paper even though more than 80% of the documents we work with are already in a computer somewhere. (CAP Venture Group)

Expense Reimbursements Paperless



Cost of Mishandling Paper:

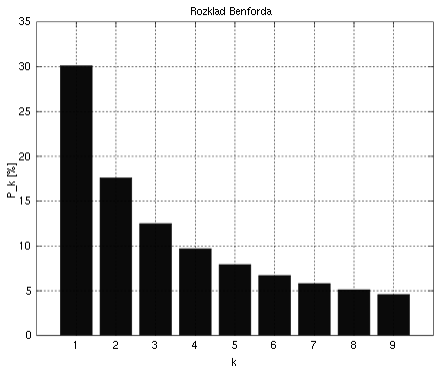
•$20 to file a document.

•$120 to search for a misfiled document, that is if you can find it.

•$250 to recreate a lost document.

•*Source: INC magazine*

Benford's Law



- http://videos.kirix.com/data-and-the-web/2008-07-22-benfords-law/2008-07-22-benfords-law.htm

Data mining for expense fraud

Unauthorized Suppliers/Vendors

	SUPPNO	SUPPNAME	SUPP_COUNTRY
1	10229	A J FORSYTH & CO LTD	NIGERIA
2	10500	AASMAN DESIGN INC	BARBADOS
3	10656	ACCPAC INTERNATIONAL, INC.	BARBADOS
4	10900	ACKLANDS - GRAINGER INC	BULGARIA
5	11173	ADDISON WESLEY LONGMAN LTD.	BULGARIA
6	11400	AG JOYERIA	ARGENTINA
7	11810	AISES PUBLISHING INC	BARBADOS
8	12203	ANKE KRUSE ORGANICS INC	CANADA
9	13007	AON REED STENHOUSE INC	CANADA
10	13214	ARC ACCOUNTS RECOVERY CORPORAT	BARBADOS
11	16093	ARCTIC STAR PRINTING INC	SAUDIA ARABIA
12	16796	AROGA TECHNOLOGIES LTD.	SAUDIA ARABIA
13	17974	ARROW ELECTRONICS, INC.	SCOTLAND
14	18147	ASSANTE CAPITAL MGMT LTD.	SCOTLAND
15	18152	AVIDA HEALTHWEAR INC.	SCOTLAND
16	18197	AXENT TECHNOLOGIES, INC.	BARBADOS

Begin with a master supplier or vendor database.

This will be compared with purchasing records.

Data mining for expense fraud

Unauthorized Suppliers/Vendors

- The master supplier file is "joined" with the purchase file based on the supplier number (SUPPNO) in both databases. Note the absence of a supplier for record #11.

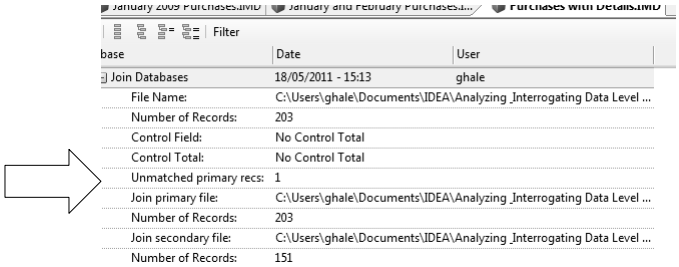
January 2009 Purchases.IMD | January and February Purchases.I... | **Purchases with Details.IMD**

	SUPPNO	ORDER_DATE	PURCH_ORDER	PRODUCT	QTY_ORDER	AMOUNT	SUPPNO1	SUPPNAME	SUPP_COUNTRY
7	11810	1/21/2009	100080200	240517	100	599.90	11810	AISES PUBLISHING INC	BARBADOS
8	11810	2/11/2009	100090400	163686	283	3,352.59	11810	AISES PUBLISHING INC	BARBADOS
9	12203	1/12/2009	100080300	207144	83	497.75	12203	ANKE KRUSE ORGANICS INC	CANADA
10	12203	2/23/2009	100090500	203807	256	8,488.38	12203	ANKE KRUSE ORGANICS INC	CANADA
11	12204	2/20/2009	100090600	238071	406	8,215.54			
12	20028	1/22/2009	100082800	238434	36	216.32	20028	BETONSTEIN GMBH	GERMANY
13	20028	2/4/2009	100090700	138304	275	9,856.81	20028	BETONSTEIN GMBH	GERMANY
14	20041	1/19/2009	100080900	198924	1740	10,438.63	20041	BIJOUTERIE CARMEN	FRANCE
15	20041	2/4/2009	100090800	133627	116	1,629.40	20041	BIJOUTERIE CARMEN	FRANCE
16	20129	1/5/2009	100082500	183521	383	2,297.44	20129	BILEVICH BOEDO	MEXICO

Data mining for expense fraud

Unauthorized Suppliers/Vendors

- After performing IDEA's "Join Database" function, the database history shows the number of unmatched records.

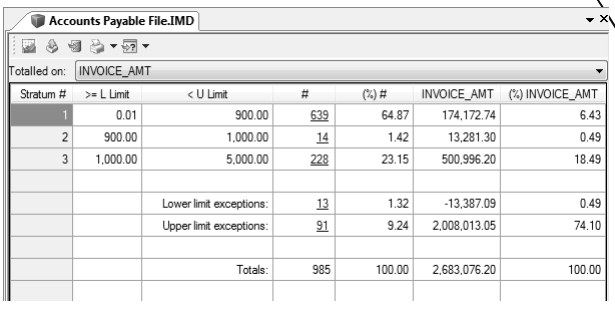


base	Date	User
Join Databases	18/05/2011 - 15:13	ghale
File Name:	C:\Users\ghale\Documents\IDEA\Analyzing _Interrogating Data Level ...	
Number of Records:	203	
Control Field:	No Control Total	
Control Total:	No Control Total	
Unmatched primary recs:	1	
Join primary file:	C:\Users\ghale\Documents\IDEA\Analyzing _Interrogating Data Level ...	
Number of Records:	203	
Join secondary file:	C:\Users\ghale\Documents\IDEA\Analyzing _Interrogating Data Level ...	
Number of Records:	151	

Data mining for expense fraud

Stratification

- Data can be stratified to isolate expenses that fall slightly below certain limits (e.g. the reimbursement limit).



Accounts Payable File.IMD

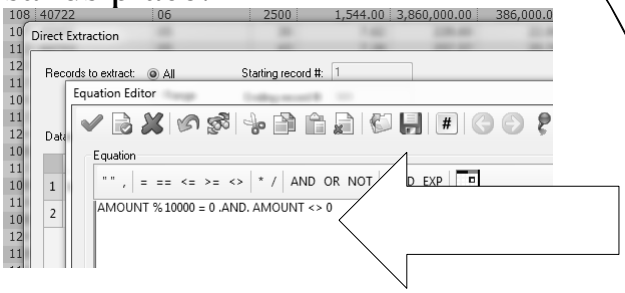
Totalled on: INVOICE_AMT

Stratum #	>= L Limit	< U Limit	#	(%) #	INVOICE_AMT	(%) INVOICE_AMT
1	0.01	900.00	639	64.87	174,172.74	6.43
2	900.00	1,000.00	14	1.42	13,281.30	0.49
3	1,000.00	5,000.00	228	23.15	500,996.20	18.49
		Lower limit exceptions:	13	1.32	-13,387.09	0.49
		Upper limit exceptions:	91	9.24	2,008,013.05	74.10
		Totals:	985	100.00	2,683,076.20	100.00

Data mining for expense fraud

Direct Extraction—Rounded Numbers

- Databases can be queried to extract records based on formulas—such as this, which will extract dollar amounts rounded to the ten-thousands place.



Data mining for expense fraud

Direct Extraction—Rounded Numbers

- The resulting extraction lists records with amounts in multiples of $10,000.

	INV_NO	INV_DATE	SALESREP	CUSTOMER_NO	PROD_CODE	QTY	UNIT_PRICE	AMOUNT	SALES_TAX	TOTAL_SALE
1	1000006	1/4/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
2	1000011	1/10/2008	108	40722	06	2500	1,544.00	3,860,000.00	386,000.00	4,246,000.00
3	1000011	1/13/2008	108	40722	06	2500	1,544.00	3,860,000.00	386,000.00	4,246,000.00
4	1000006	2/4/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
5	1000006	3/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
6	1000006	4/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
7	1000006	5/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
8	1000006	6/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
9	1000006	7/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00
10	1000006	8/3/2008	999	11111	05	1000	10.00	10,000.00	1,000.00	11,000.00

Data mining for expense fraud

Duplicate Key Detection

- Duplicate Key Detection identifies duplicate documents. The INV_NUM column shows possible attempts made to mask the duplicate number.

DUP VEND MOD INVOICE DATE ...

	VND_NUM	INV_NUM	MOD_INV_NUM	INVOICE_DATE	CV
10	CAHNERS	UK343181	UK343181	12/4/2007	C125
11	CAHNERS	Uk-343-181	UK343181	12/4/2007	C125
12	HIGGINS	INV26928	INV26928	8/5/2008	C127
13	HIGGINS	INV*26928	INV26928	8/5/2008	C127
14	MT PRDT	0065/AUG00	0065AUG00	1/22/2008	C125
15	MT PRDT	0065-Aug00	0065AUG00	1/22/2008	C125
16	MURRAY	567481	567481	4/24/2008	C126
17	MURRAY	567481	567481	4/24/2008	C126
18	ONETIME	14/4/00	14400	9/13/2007	C124
19	ONETIME	14.4.00	14400	9/13/2007	C124
20	ONETIME	14-Apr-00	14APR00	9/13/2007	C124

Data mining for expense fraud

Duplicate Key Detection

- Duplicate Key Detection identifies duplicate documents. The INV_NUM column shows possible attempts made to mask the duplicate number.

DUP VEND MOD INVOICE DATE ...

	VND_NUM	INV_NUM	MOD_INV_NUM	INVOICE_DATE	CV
10	CAHNERS	UK343181	UK343181	12/4/2007	C125
11	CAHNERS	Uk-343-181	UK343181	12/4/2007	C125
12	HIGGINS	INV26928	INV26928	8/5/2008	C127
13	HIGGINS	INV*26928	INV26928	8/5/2008	C127
14	MT PRDT	0065/AUG00	0065AUG00	1/22/2008	C125
15	MT PRDT	0065-Aug00	0065AUG00	1/22/2008	C125
16	MURRAY	567481	567481	4/24/2008	C126
17	MURRAY	567481	567481	4/24/2008	C126
18	ONETIME	14/4/00	14400	9/13/2007	C124
19	ONETIME	14.4.00	14400	9/13/2007	C124
20	ONETIME	14-Apr-00	14APR00	9/13/2007	C124

Group Exercises

1. **What would have prevented the fraud?**
2. **How could the fraud have been detected?**
3. **What audit steps/tests should be employed to detect this type of fraud?**
4. **What should they do to prevent this in the future?**

Questions

Contact information

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Migrating from SAS 70 to SSAE 16, Overview and New Reporting Requirements

Mary E. Wiggins, CISA, MCTS

Mary Wiggins, CISA, MCTS

Senior Manager

O'Sullivan Creel, LLP

Mary Wiggins, CISA, MCTS is a Senior Manager of the firm's Consulting Services division, located in the Pensacola office. Mary's specialization is in accounting system implementation and training. She has been with the Firm since 1992, and has over twenty years of industry experience as a network engineer and consultant. Mary has a BSBA from the University of West Florida, graduating cum laude, and a Masters of Accountancy. She is an Intuit ProAdvisor, a Microsoft Certified Technical Specialist (MCTS) for Microsoft Great Plains Dynamics, and a Certified Information Systems Auditor (CISA).

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(MEMBER NAME) can be reached by telephone at _____(PHONE NUMBER)____, or via e-mail at _____(E-MAIL ADDRESS)_____.

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