A Carnival of Information

27th Annual Accounting Show

September 19-21, 2012
Broward County Convention Center / Ft. Lauderdale
27th Annual Accounting Show
September 19, 2012
Ft. Lauderdale

1:45pm-5:15pm

Malpractice Risks: Navigating the New Frontier
Steven M. Platau, CPA
Professor of Accounting/University of Tampa

2011 - 2012 Accounting Shows Committee

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Malpractice Risks: Navigating the New Frontier

Steven M. Platau, CPA
Steve Platau is Professor of Accounting where he has served in the faculty since 1984. His works have been published in the Journal of Accountancy, Practical Accountant, CPA Journal, Real Estate Review, The Practicing CPA, Employee Benefits Journal and Florida CPA Today among others. Steve is a principal consultant to the CNA Insurance Companies providing loss control programs to CPA firms nationally. His professional involvement includes service as a member of the Florida Institute of CPA's Board of Governors and on various FICPA and AICPA committees including an award as Outstanding Committee Chairman for his work in chairing the FICPA's Professional Liability Committee. Mr. Platau's business experience includes time with two of the "Big 5" international accounting firms, private law practice and industry accounting along with financial interests in several hospitality businesses. He has been an arbitrator serving on the American Arbitration Association's National Panel of Arbitrators since 1985, he began training arbitrators in 1995. His mediation experience includes certification by the Florida Supreme Court as a Circuit Court Mediator since 1991. Dual training in both accounting and law provide Mr. Platau with a unique and varied perspective on issues facing the accounting profession.
Accountants Liability: No Good Deed Goes Unpunished
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Seminar Objectives

• Provide practical information on:
  - Accountants professional liability risk exposures
  - Risk control tools and techniques
Accountants Liability: No Good Deed Goes Unpunished
AICPA Professional Liability Insurance Program

Agenda

• Claim statistics
• Tax services
• Evolution of a claim
• Accounting and audit services
• Practice management
• Consulting and financial advisory services
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AICPA Professional Liability Insurance Program

Claim Statistics
2011 Claims by Area of Practice

- Compilation and Review: 2%
- Investment Advisory: 5%
- Consulting: 7%
- Audit: 9%
- Accounting, Attestation, and Other: 12%
- Tax: 65%

Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies
2011 Tax Claims by Cause of Loss

- **Failure to Detect Theft or Fraud**: 2%
- **Other**: 6%
- **Unauthorized or Improper Practices**: 9%
- **Math and Clerical Errors**: 10%
- **Filing Errors**: 14%
- **Improper Tax Treatment/Advice**: 60%

Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies
2011 Audit Claims by Cause of Loss

- Failure to Perform Compliance Testing or Reporting: 6%
- Failure to Disclose Related Party Transactions: 6%
- Errors in Report Issuance: 13%
- Failure to Detect Theft: 13%
- Failure to Detect Misstatement in Financial statements: 23%
- Failure to Detect Fraud: 26%

Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies
2011 Consulting Claims by Area of Practice

- **IT Consulting**: 5%
- **Transaction Services: Business Valuation**: 9%
- **Transaction Services: All Other**: 23%
- **Short Term Advice on Specific Issue**: 23%
- **Litigation Support/Service**: 41%

Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies
2011 Theft and Fraud Claims

- Consulting: 3%
- Investment Advisory: 9%
- Review/Compilation: 13%
- Tax: 13%
- Accounting/Other AOP: 25%
- Audit: 38%

Source: AICPA Professional Liability Insurance Program
Underwritten by CNA Insurance Companies
Tax Services
Preparer Responsibilities

- Examples of claims from failure to exercise due diligence
  - Failure to make an election
  - Reliance on incorrect advice/opinion of others
  - Failure to inquire about client’s foreign accounts/assets/interests
- Cir. 230 - §10.22, Diligence as to accuracy
  - Skepticism, e.g., inconsistent client information
  - Scrutinize advice/opinion of others
### Preparer Responsibilities

<table>
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<th>Claim</th>
<th>Examples of Risk Control</th>
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| Failure to make an election                                           | • Sufficient knowledge of the client  
|                                                                       | • Adequate training  
|                                                                       | • Supervision                                                                             |
| Reliance on incorrect advice/opinion of others                       | • Use reasonable care in engaging others  
|                                                                       | • Evaluate adequacy and accuracy of their advice                                          |
| Failure to inquire about client’s foreign accounts/assets/interests | • Make reasonable inquiries if information implies possible participation in foreign transactions/accounts or possession of foreign assets/interests |
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**Tax Advice**

- Tax advice claims
  - Incorrect tax advice
  - Failure to give tax advice
Risk Control – Tax Advice Claims

• Incorrect tax advice
  - Understand the purpose of the engagement
    • Ask questions to put the request in proper context
  - Know the tax professional standards
    • Circular 230
      - §10.33, Best practices for tax advisors
      - §10.35, Requirements for covered opinions
      - §10.37, Requirements for other written advice
    • Statements on Standards for Tax Services (SSTS) Nos. 1 & 7
      - Provide all advice in writing
Risk Control – Tax Advice Claims

• Incorrect tax advice, cont.
  – Cir. 230 §10.33, Best practices for tax advisors
    • Communicate the engagement scope, limitations, and terms clearly
    • Establish the relevant facts
    • Evaluate reasonableness of assumptions or representations
    • Apply law to the relevant facts
    • Support conclusions with the law and the facts
    • Advise client of risks and consequences of the conclusions
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Risk Control – Tax Advice Claims

• Failure to advise
  - Engagement letter
    • Specify
      - Services to be provided
      - Scope limitations
      - Client responsibilities
      - Client should only rely on written advice
      - Fee structure
Risk Control – Tax Advice Claims

• Failure to advise, cont.
  - Sufficient knowledge of the client
    • Inform client of other tax issues
      - Opportunity for additional services
    • Maintain contact throughout the year
      - “What’s new with the business?”
    • Be alert of other tax/financial implications
  - Document discussions
Risk Control – Tax Advice Claims

• Failure to advise, cont.
  – Sufficient knowledge of the issue
    • Obtain knowledge in particular tax area to recognize issues
    • Seek advice from specialist
  – Requests for participation in client meetings
    • “Why am I here?”
    • Third party reliance on advice to client
  – Information requests
    • Understand client’s purpose
    • Within scope of engagement
Tax Compliance Claims

• Examples of tax compliance claims
  - Errors related to new client’s prior year returns (SSTS No.6)
    • Failure to identify errors and prepare amended returns
    • Errors due to reliance on inaccurate carry forward information
  - Filing errors
  - Computational errors
  - Missed elections or incorrect elections made
  - Failure to recognize book/tax differences
Risk Control - Tax Compliance Claims

- Promote tax quality control policies and monitor compliance
- Invest in pre-tax season preparation
  - Check PTIN registration for return preparers
  - Perform risk assessment on existing clients
  - Prepare and issue engagement letters
  - Identify staffing needs and provide staff training
    - Last minute tax law changes
    - Firm quality control policies and procedures
  - Perform necessary updates to tax software
Risk Control - Tax Compliance Claims

• Examples of tax season quality control:
  - Assign staffing based on experience and training
  - Monitor progress, provide adequate supervision and review
  - Check supporting records and workpapers of new client PY returns
  - Use docket systems or electronic workflow applications to track progress
    • Monitor chain of custody of returns
    • Include all returns
    • Identify bottlenecks, reassign work as needed
  - E-filing documentation
    • Proof of e-file submission acceptance, certified mail receipts
      - Last-minute returns
      - Inform clients in advance if extensions are needed
Other Tax Claims

- Examples of other claims
  - Failure to detect theft
    - Write-up and bank reconciliation services
  - Mishandling of client documents
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Risk Control - Other Tax Claims

• Failure to detect theft
  - Define scope limitations in engagement letter
    • Tax services are not designed to detect fraud or theft
    • Preparer will not audit or verify information/representations provided by the client
  - Inform client in writing regarding any suspicious or unusual activity
Risk Control - Other Tax Claims

• Mishandling of client documents
  - Safeguard originals and return to client immediately
  - Obtain consents before disclosure or use of client information
• AICPA Code of Professional Conduct, Rule 301, Confidential Client Information
• IRC §7216 – Disclosure or Use of Information by Preparers of Returns
• State board of accountancy rules
Estate and Gift Tax Claims

• Inexperience/inadequate training
  - Lack of knowledge in current federal and state tax laws

• Improper tax planning advice
  - Didn’t advise client that only certain trusts (e.g., QSST, ESBT) can be shareholders of S Corp.

• Responsibilities undefined
  - Preparation of 706, 709, 1041, state estate or transfer tax returns
    • Attorney or CPA?
    - Poor communication

• Large late filing and payment penalties
Estate Tax Claim Scenario

- CPA had a long-time client who owned a business
- Assisted with succession and estate planning
- Met several times with client’s attorney, investment advisor, and financial planner
- Asked to prepare estate tax return for the first time after client died
- Unable to gather all the information in time
- Did not obtain an extension of time to file or pay
- Did not think of filing an estimated return
- Sued by estate to recover large late filing and late payment penalties and interest
Risk Control - Tax Compliance Claims

• Examples of tax season quality control:
  - Assign staffing based on experience and training
  - Monitor progress, provide adequate supervision and review
  - Check supporting records and workpapers of new client PY returns
  - Use docket systems or electronic workflow applications to track progress
    • Monitor chain of custody of returns
    • Include all returns
    • Identify bottlenecks, reassign work as needed
  - E-filing documentation
    • Proof of e-file submission acceptance, certified mail receipts
      - Last-minute returns
      - Inform clients in advance if extensions are needed
Gift Tax Claim Scenario

• Client created GST trusts for grandchildren and made gifts each year
• CPA prepared client’s gift tax, individual and trust income tax returns
• CPA failed to make the Section 2632(c) election to automatically allocate donor’s unused GST exemption
• Client’s attorney discovered the error upon client’s death
• Potential GST tax liability of over $5 million
• Estate sued CPA alleging negligence and failure to exercise due care
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Tax Audits and Collections Claims

• Dissatisfaction with settlement terms and consequences
  - Inexperience
    • Unfamiliar with tax authority practice and procedures
  - Poor communication and documentation
    • Did not inform client or obtain client’s approval before settlement
  - Complexity of issues
    • Accepts less favorable settlement due to inadequate analysis
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Tax Audits and Collections Claims

- Criminal exposure
  - Fails to ask agent if audit was part of a criminal investigation
  - Fails to advise client to consult with attorney upon learning facts with criminal implications
Risk Control - Representing Clients in Tax Audits and Collections

- Existing client
  - Review prior year returns for
    - Errors
    - Improper advice on tax positions
      - Lacks a reasonable basis (Cir. 230 §10.33)
      - Did not meet higher standard as required
    - Report to insurer as potential claims
  - Conflict of interest
    - Advice challenged by tax authority
Prospective client
- Contact predecessor
  - Assess client’s integrity
  - Did the client follow predecessor’s advice?
- Review prior year returns before accepting engagement
- Obtain retainer
Risk Control - Representing Clients in Tax Audits and Collections

• Documentation
  - Engagement letter
    • Power of Attorney does not substitute
  - Communication of significant matters
  - Efforts to work with un-cooperative clients
  - Settlement discussions and approvals from client
Evolution of a Claim
Accounting and Audit Services
Compilation and Review Claims

• Failure to detect theft
• Failure to exercise due care
• Inadequate disclosure
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Compilation Claim Scenario

• CPA prepared compiled financial statements for client
• CPA noticed that current-year expenses were unusually high
• CPA inquired of the bookkeeper, but did not verify the answer
• Client discovered that the bookkeeper was running his personal expenses through the business
• CPA is sued by the client for failure to detect theft
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Review Claim Scenario

• CPA performed a review
• Review procedures identified inventory was not turning over quickly, but no additional procedures were performed to test valuation
• Review report was given to bank by management in order to obtain financing
• Inventory was over-valued, thus assets were overstated and bank collateral was nonexistent
• Company went out of business and CPA was sued
Compilation and Review Claims

• Issues
  - Expectation gaps
  - Engagement creep
    • Long-time accountant is seen as de facto CFO
      - Responsibility for management decisions
  - Privity
    • Communications with third parties on client’s behalf
Compilations and Reviews

• SSARS 19
  - Engagement letters required for both compilations and reviews
  - Enhanced documentation requirements
    • Compilations – document significant findings or issues
    • Reviews – document management’s response to inquires for analytical procedures and significant matters
  - Performance standards for reviews
  - Independence
    • Allowed to disclose reason for lack of independence in compilation report but must disclose ALL reasons
Risk Control – Compilation and Review

• Define scope of services in engagement letter
  - Specify client responsibilities & scope limitations
• Keep adequate documentation
  - Inform client about suspicions of theft or fraud
  - Maintain professional skepticism and document follow up discussions
  - Communicate significant matters, e.g., poor internal controls
Risk Control – Compilation and Review

• Going Concern
  - Ask management about possible effects on financial statements
  - Evaluate management’s response
  - Include going concern paragraph

• Resist client pressure to
  - Delay report issuance
  - Exclude going concern paragraph
Risk Control – Compilation and Review

• Subsequent events
  - Becoming aware of events during compilation or review
  - Becoming aware of events after report date, but before report release date
  - Evaluate management’s response on effects to financial statements and disclosures
  - If financial statements are not revised
    • Consider modifying report or withdrawing from engagement
    • Consult SSARS for guidance
Risk Control – Compilation and Review

• Subsequent discovery of facts existing at the date of the report
  - Consult with legal counsel
  - Inform management or those charge with governance
  - In a compilation
    • Obtain additional or revised information
  - In a review
    • Perform additional procedures
Risk Control – Compilation and Review

- Subsequent discovery of facts existing at the date of the report, cont.
  - Previously-issued report can no longer be used
    - Advise client to adequately disclose the facts and impact on financial statements to users
  - Ensure that adequate disclosures have been made
  - Inform highest level personnel if management refuses
  - Notify known users in writing to prevent further use or reliance
  - Consult with an attorney prior to sending notifications
  - Consult with SSARS for detailed guidance
Audit Claims

- High-severity claims
- Examples of audit claims
  - Failure to detect theft or fraud
  - Reliance on materially misstated financial statements
- Common plaintiff assertions
  - Non-compliance with professional standards
    - Inadequate planning
    - Inappropriate staffing
  - Did not address PY internal audit deficiencies in current year audit
  - Did not exercise professional skepticism
Risk Control – Audit Claims

• AICPA Statements on Quality Control Standards
  - Firm-wide quality control documentation
  - Written quality control policies and procedures
    - Evidence of regular reviews and updates of quality control policies and procedures
  - Firm-wide quality control training and attendance
  - Link between quality control policies and professional development
Risk Control – Audit Claims

• Client and engagement quality control documentation
  - Client acceptance and continuance
  - Independence
  - Staff qualifications and training
  - Appropriate supervision and review
Risk Control – Audit Claims

• Key engagement quality control issues
  - Management integrity
  - Independence
  - Audit staff and supervision
  - Audit procedures
Risk Control – Audit Claims

• Audit Planning Process
  - Assess management integrity
  - Evaluate independence and conflicts of interest
  - Develop audit strategy and plan
  - Identify audit team and specialists
    • Document each team member training and qualifications
  - Risk assessment
    • Discuss current year significant events with management
Risk Control – Audit Claims

• Audit Planning Process, cont.
  - Determine audit procedures
    • Consider prior year internal control deficiencies and audit adjustments
    • Perform critical review of checklists and modify pre-populated audit programs for current engagement
  - Document the planning process, including discussion from brainstorming session
Audit - Specific Risk Issues

- Consent to use auditor reports
- Restatements
- State and local government audits
- Service organization control reports
- Changes in accounting standards
Audit - Specific Risk Issues

- Consent to use auditor reports
  - No legal or professional obligation to grant consent
  - Before firm provides consent, consider
    - Resources and expertise
    - Subsequent events
    - Public offerings subject to PCAOB standards and SEC reporting requirements
      - Consider if firm can perform services if not PCAOB registered
        » Comply with PCAOB standards
        » Consider subsequent events
Audit - Specific Risk Issues

• Report restatements as potential claim if due to prior errors
• Misstatement of earnings
  – Tax provisions
• Consult professional standards
  – Disclosure and notification requirements
Audit - Specific Risk Issues

• Risk Control - Restatements
  - Audit quality control
  - Use of specialists
  - Adequate training and supervision
State and Local Governments Audits

• State of the economy
  - Municipalities may
    • Declare bankruptcy if allowed under state law
    • Default on bond obligations
• Possible claimants
  - Clients
  - Bondholders/bond insurers
  - Investors
  - Pension plan participants
  - Vendors and creditors
Risk Control - State and Local Governments Audits

- Not just “summer work”
- Perform thorough client and engagement acceptance and continuance procedures
  - Review indemnification language in procurement bid packets
- Provide adequate staff training
- Requires specialized knowledge
  - GAGAS vs. GAAS
    - Independence requirements
  - Specialized audits if federal funding (e.g. Circular A-133)
Risk Control - State and Local Governments Audits

• Plan ahead before attending board meetings
  – Send only experienced CPAs
  – Establish an understanding of the purpose of the CPAs’ participation before the meeting
  – Be the first item on the agenda
  – Leave immediately after presentation
  – Minutes should reflect the CPA’s exit

• Document communication with board and/or audit committee

• Consider additional procedures and testing due to poor internal controls
  – Exercise professional skepticism
Service Organization Control Reports

- Attestation Engagements
  - SOC 1 (can be Type 1 or Type 2 – SSAE 16)
    - Report on controls at service organization that likely are relevant to an audit of a customer’s financial statements
  - SOC 2 (can be Type 1 or Type 2 – AT 101)
    - Specifically addresses one or more of Trust Services principles (security, availability, processing integrity, confidentiality and privacy)
  - SOC 3 (AT 101)
    - Similar to SOC 2 and available for public use
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Service Organization Control Reports

• Do not misconstrue or misrepresent service as consulting engagements

• Key risks
  – Clients don’t understand differences
  – Intended for third-party use
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Risk Control - Service Organization Control Reports

• Communications with client
  - Discuss purpose and users
  - Describe reporting options
• Engagement letters
  - Define service scope and limitations, intended users
• Staff training and supervision
  - Monitor changes in standards
Changes in Standards and Frameworks

• Changes in accounting standards
  – Convergence of IFRS and GAAP
    • Monitor progress and prepare for convergence
  – Private company financial reporting
    • Monitor activities of the FAF and the Blue Ribbon Panel on Standard Setting for Private Companies
• COSO Internal Control – Integrated Framework
Practice Management
Privacy and Data Security

• Potential Breach Scenarios
  - A CPA’s laptop or flash drive containing unencrypted information is lost or stolen
  - A paper copy of a client’s tax return is found in an opened envelope in a semi-public hallway
  - Client’s tax return is sent in an unencrypted file to the wrong e-mail address
  - A company is hired to shred confidential information offsite that does not properly destroy confidential documents
  - CPA notices signs of forced entry to her office, files appear to have been moved
  - A firm employee sends confidential client information to his personal e-mail address to work on the file over the weekend
  - The company which hosts the CPA firm’s online customer portal reports that a hacker may have accessed client data
Privacy and Data Security Compliance

- Gramm-Leach-Bliley Act
  - FTC Financial Privacy Rule
    - Non-CPA tax return preparers must provide annual privacy policy notices
  - FTC Safeguards Rule
    - Accountants significantly engaged in providing financial products or services must develop and implement a written information security plan
- SEC Regulation S-P
  - Applies to SEC registered investment advisers, brokers
Privacy and Data Security Compliance

• State privacy and security breach notification laws
• HIPAA and HITECH Acts
  – “Business Associates” with access to private health information must comply
• IRC 7216 prohibits knowing or reckless disclosure or use of tax return information
  – Treasury Regulations 301.7216-1, 301.7216-2 and 301.7216-3
• AICPA Rule 301
  – Rule 301- Confidential Client Information
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Risk Control - Privacy and Data Security

• Secure and control access to office and data storage
  - Including paper and electronic storage
• Encrypt electronic data when
  - Required by law
  - Practicable or advisable
• Password protection
  - Use strong passwords
  - Change regularly
  - Do not share
  - Protect both system access and transmitted files
• Monitor law and regulation governing data security
• Firm policies regarding data security and confidential information
Privacy Breach Response

- Investigate and prevent further damage
  - Consult with technology experts
- Preserve relevant data
Privacy Breach Response

• If breach has occurred
  - Determine corrective response
  - Consider notification issues
  - Consult with attorney on breach response
    • Review privacy and data security laws and regulations
    • Consider legal obligations or recommendations to:
      - Obtain credit reports
      - Initiate fraud alerts or security freeze on credit reports
      - Notify state and federal
    • Have attorney assist in drafting notification letter
  - Consult with insurance agent and carrier
Privacy Breach Costs

- Investigation
- Consultation with expert and attorney
- Remediation
- Compliance with privacy breach notification laws
  - Notification letters
  - Credit monitoring services
- Claims or lawsuits
  - Identity theft
  - Loss of trade secrets
- Regulators/agencies investigations
- Consult with insurance agent about coverage
Privacy and Data Security

- Privacy and data security resources
  - AICPA website at www.aicpa.org
    - Data privacy and security resources housed on the Privacy and Data Protection page in the IT Center
  - FTC website at www.ftc.gov
    - “Protecting Personal Information: A Guide for Business”
  - HHS website at www.hhs.gov
    - See HITECH ACT Rulemaking and Implementation Update
  - State breach notification requirements at www.ncsl.org
Social Media Use

- Employee posting of
  - Confidential information
  - Embarrassing information
  - Information detrimental to lawsuit defense

- Potential for
  - Loss of business
  - Professional liability claim or board complaint
  - Defamation claims
  - Employment practices claims
Risk Control - Social Media Use

• Implement written social media policy
• Monitor “on the job” compliance with policy
• Before discussing inappropriate postings
  – Consult with employment practices attorney
Conflicts of Interest and Confidentiality

- CPA provides tax services to husband and wife (H and W)
  - Divorcing
  - Both have Schedule C income
  - H has a business and files a business tax return
    - Can CPA provide both tax returns to W?
    - Can CPA provide tax planning advice to both?
    - Does CPA have a potential or actual conflict?
      - If so, can it be waived?
Engagement Management

• Characteristics of high-risk client relationships, including
  - Do not pay invoices timely
  - History of disputes with professionals or others
  - Integrity issues
  - Refuse to sign and return engagement letters
  - Disregard advice
  - Difficult, uncooperative, abusive
  - Poor recordkeeping
Engagement Management

• Risk control
  - Client acceptance and continuance
  - Bill and collect frequently
    • Require retainers
  - Use engagement letters on all engagements
    • Including non-traditional, non-repeating engagements
    • Engagement letter provisions
      - Client responsibilities
      - Scope and responsibility limitations
        » Dissemination of CPA work product
      - Suspension of work and withdrawal
    - Client termination
Consulting and Financial Advisory Services
Types of Financial and Investment Advisory Services

- Financial planner
- Investment adviser
- Registered representative (stock broker)
Licensing and Registration

- Financial planning, pension consulting or investment advice for a fee
  - Subject to state or federal licensing/registration requirements
  - Rules are complex
    - Investment Advisers Act of 1940
    - Consult with expert
Licensing and Registration

• The CPA’s Guide to Investment Adviser Registration
• Other resources available in Personal Financial Planning (PFP) section of AICPA web site
  – www.aicpa.org
De Minimis Exceptions to Licensing and Registration

- Limited and subject to both federal and state law
  - Exception to investment adviser definition under Investment Advisers Act of 1940
  - States have varying and specific laws on exceptions
  - Federal and state law subject to change
    - Dodd-Frank Act
      - Changes to federal licensing and registration requirements
    - Review available AICPA resources and consult with expert
What is a Financial Planner?

• Provide services in interrelated financial areas:
  - Risk management and insurance planning
  - Budgeting, savings and cash flow planning
  - Tax planning
  - Investment planning
  - Retirement planning
  - Wealth transfer and estate planning
Financial Planner

• AICPA Statements on Responsibilities in Personal Financial Planning Practice
• Professional credentials
• Fiduciary duty determined under state law
  - Act in a client’s best interest
  - Perform with loyalty and good faith
  - Fully disclose all pertinent information
Financial Planning Claims

• Claim allegations
  - Unsuitable plan
  - Failure to monitor or update plan
Risk Control - Financial Planning

• Engagement letter
  - Specify scope limitations and client responsibilities
  - Include caveats such as need to regularly update
  - Specify responsibility for implementation and monitoring
Risk Control - Financial Planning

• Questionnaire
  - Assess client’s financial situation and goals
  - Discuss profile with client
  - Develop financial plan based on profile

• Discuss financial plan

• When recommending investment professionals, investigate and provide alternatives
  - Consider including disclaimer regarding supervision
Accountants Liability: No Good Deed Goes Unpunished
AICPA Professional Liability Insurance Program

**Investment Adviser**

- Registration or licensing requirements
  - Register with SEC or state
  - All states except Wyoming require registration
  - Series 65 license required
- Record keeping
- Custody
- Disclosure
- Subject to fiduciary standard
Investment Adviser Claims

• Failure to advise regarding diversification of assets
• Failure to advise in accordance with client’s financial goals
Risk Control - Investment Adviser

• Ask client to complete investment risk profile questionnaire
• Make recommendations based on client’s investment goals and other pertinent client criteria
• Perform due diligence prior to recommending investment managers
  – Including funds they manage, recommend or invest in
Risk Control - Investment Adviser

• Know your client
  - Effectively service client accounts
  - Act in accordance with instructions
  - Obtain authority to act on behalf of account holder
  - Comply with industry laws, rules and regulations
Registered Representative

- Sells securities for a commission
- Also called account executive or stockbroker
- Registration with FINRA usually linked to a particular broker dealer
- Activities may be excluded from coverage under professional liability insurance policies
  - Consult with insurance agent
- Monitor laws and regulations
- Know your client
Registered Representative Claims

- Churning
- Unsuitable investments
- Improper execution of trades
- Pricing violations
- Bad investment advice
Registered Representative – Risk Control

- Risk control considerations
- Consider suitability of investments based on age, employment, investment objectives, financial situation, needs, investment experience, etc,
- Monitor Dodd-Frank Act and related regulations
- Exercise due diligence in execution of trades
- Insurance coverage issue
Fiduciary Services - Duty

• Highest standard of care

• Legal duty to
  - Act in client’s best interests
  - Perform with loyalty and good faith
  - Fully disclose all pertinent information to client

• Insurance coverage limitations
Case Study

• CPA provides tax and family office services to multi-generational extended family
  - Discusses investments with client on occasion
  - Becomes co-trustee of living trust along with beneficiary
    • Hires own firm to provide accounting, tax and financial-planning services
      - Provides tax and other services to multiple beneficiaries of the trust
      - Introduces beneficiaries to another client regarding a business opportunity
• What are the potential issues?
Business Valuation

• Scenarios
  - Married Filing Jointly 1040 client is going through a divorce and one spouse’s attorney requests CPA’s assistance in valuing marital property
  - Compilation client requests CPA’s assistance in providing a value of the company for a potential buyer
  - CPA performs tax and bookkeeping services for a two-member partnership; one member decides to retire, and the CPA is approached to assist in determining a buyout value for the retiring partner
  - Audit client requests a “back of the envelope” valuation of a segment of the client’s business, with the deliverable being a short letter addressed to the client
Accountants Liability: No Good Deed Goes Unpunished
AICPA Professional Liability Insurance Program

Business Valuation Claims

• Over/(under) statement of assets or liabilities
  - Inadequate data collected
  - Incorrect or unreasonable assumptions used
  - Use of incorrect methodology, or over-reliance on selected methodology
  - Reliance on “rules of thumb”
• Lack of appropriate qualifications/inexperience
  - Unfamiliar with industry or business
  - Hard to value assets
  - Complexity
• Conflict of interest or lack of independence and objectivity
• Alleged fraud
Risk Control - Business Valuation

• Familiarity with AICPA Statements on Standards for Valuation Services No. 1 (SSVS No. 1)

• Thorough client and engagement acceptance procedures
  – Even for existing clients

• Use of engagement letters
  – Define scope of engagement and intended users of deliverables

• Obtain waiver of conflict of interest

• Staff training and supervision
  – Obtain proper credentials
  – Remain current in a changing environment
AICPA Professional Liability Insurance Program
Reporting Matters

• Policy
  - Required notice
    • Potential claims
    • Actual claims
  - Optional
    • Subpoenas
    • Board complaints
    • Regulatory inquiries
Conclusion

- Final questions
- Evaluation form
- Sign-in sheet
- CPE Credit/Premium Credit form
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