Resisting Pressure from Start to Finish

Gary Leeman, CPA/ABV, CFF, CGMA, CMC
Cendrowski Corporate Advisors

September 23, 2016
I Do What I Do
and
Won’t What I Don’t
Overview

- Industry Characteristics
- Industry Accountants vs. IT Professionals
- Pressures
- Conceptual Framework
- Integrity and Objectivity
- Conflicts of Interest
- Standards & Principles
- Acts Discreditable
- Confidentiality
- Skepticism
- Cases
Industry Characteristics

• Key External Income Drivers
• Characteristics for Success
• Competition
• Entrance Barriers
• Volatility
• Regulation
# Industry Characteristics

<table>
<thead>
<tr>
<th>Key External Drivers</th>
<th>Health</th>
<th>Life</th>
<th>Property &amp; Casualty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Health Expenditure</td>
<td>Number of Employees</td>
<td>Number of Employees</td>
<td>Number of Vehicles Registrations</td>
</tr>
<tr>
<td>Number of Employees</td>
<td>Median Age of Population</td>
<td>Median Age of Population</td>
<td>Home Ownership Rates</td>
</tr>
<tr>
<td>Median Age of Population</td>
<td>Number of Physician Visits</td>
<td>Per Capita Disposable Income</td>
<td>Yield of 10 Year Treasuries</td>
</tr>
<tr>
<td>Number of Physician Visits</td>
<td>Per Capita Disposable Income</td>
<td>Yield of 10 Year Treasuries</td>
<td>S &amp; P 500</td>
</tr>
<tr>
<td>Per Capita Disposable Income</td>
<td>Yield of 10 Year Treasuries</td>
<td>Yield of 10 Year Treasuries</td>
<td>National Disaster Index</td>
</tr>
<tr>
<td></td>
<td>S &amp; P 500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mature</td>
<td>Industry Consolidation</td>
<td>Industry Consolidation</td>
<td>Industry Consolidation</td>
</tr>
<tr>
<td>Industry Consolidation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Concentration</td>
<td>Medium</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Top 4 Market Share</td>
<td>34.77%</td>
<td>13.61%</td>
<td>31.8%</td>
</tr>
<tr>
<td>Success Factors</td>
<td>Extensive Distribution Networks</td>
<td>Extensive Distribution Networks</td>
<td>Cost Effective Distribution System</td>
</tr>
<tr>
<td></td>
<td>Reputation</td>
<td>Compliance with Government Regulations</td>
<td>Manage Risk</td>
</tr>
<tr>
<td></td>
<td>Ability to Pass on Cost Increases</td>
<td>Effective Cost Controls</td>
<td>Range of Procedures</td>
</tr>
<tr>
<td></td>
<td>Handling Government Regulation</td>
<td>Effective Asset Management</td>
<td>Management of Asset Portfolio</td>
</tr>
<tr>
<td></td>
<td>Cost Controls</td>
<td></td>
<td>Disciplined Underwriting</td>
</tr>
<tr>
<td></td>
<td>Additional Revenue from Additional Sources</td>
<td></td>
<td>Accurate Information</td>
</tr>
</tbody>
</table>

Source: IBIS World Data
<table>
<thead>
<tr>
<th>Industry Characteristics</th>
<th>Health</th>
<th>Life</th>
<th>Property &amp; Casualty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Competition</td>
<td>High</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Barriers to Entry</td>
<td>High</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Violations</td>
<td>Medium</td>
<td>Medium</td>
<td>Low</td>
</tr>
<tr>
<td>Regulations</td>
<td>High - Increasing</td>
<td>High - Increasing</td>
<td>High - Steady</td>
</tr>
<tr>
<td>Revenue Increase: 2021 vs 2016</td>
<td>10.73%</td>
<td>13.29%</td>
<td>9.06%</td>
</tr>
<tr>
<td>Avg. Annual Increase</td>
<td>2.15%</td>
<td>2.67%</td>
<td>1.81%</td>
</tr>
</tbody>
</table>

Source: IBIS World Data
Industry Accountants vs. IT Professionals

• Comparisons
• Chart
<table>
<thead>
<tr>
<th>AICPA</th>
<th>ISACA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Integrity</td>
<td></td>
</tr>
<tr>
<td>Objectivity</td>
<td>Objectivity</td>
</tr>
<tr>
<td>Conflict of Interest</td>
<td></td>
</tr>
<tr>
<td>Subordination of Interest</td>
<td></td>
</tr>
<tr>
<td>Intellectual Honesty</td>
<td></td>
</tr>
<tr>
<td>Professional Competence</td>
<td>Competency</td>
</tr>
<tr>
<td>Due Professional Care</td>
<td>Due Professional Care</td>
</tr>
<tr>
<td>Planning and Supervision</td>
<td></td>
</tr>
<tr>
<td>Sufficient Relevant Data</td>
<td>Disclosure of Facts</td>
</tr>
<tr>
<td>Comply With Standards</td>
<td>Compliance With Standards</td>
</tr>
<tr>
<td>Confidentiality</td>
<td>Confidentiality</td>
</tr>
</tbody>
</table>
Pressures

- Relationships
- Circumstances
- Goals
- Requirements
- Time
- Needs
Conceptual Framework

- **Threats**
  - Relationships or Circumstances Compromising Compliance with Rules

- **Safeguards**
  - Actions Eliminating or Reducing Threats to Acceptable Levels

- **Acceptable Level**
  - Third Party Expected to Conclude Compliance with Rules Not Compromised
Conceptual Framework

• Process
  – Identify Threat
  – Determine if Significant
    • Is it acceptable?
    • Should it be eliminated?
    • Does it affect objectivity?
    • Does it compromise compliance?
  – Safeguards
    • Identify
    • Apply
Threat Categories

• Adverse Interest Threat
  – Employee Interest Adverse to Organization
  – Lawsuit Between Parties
  – Immediate Family Relationship Outside Organization
Threat Categories

• Advocacy Threat
  – Employee Promotes Organization to Point Objectivity Compromised
  – Obtaining Financing to Business Plan: Issues of Items Included or Excluded
  – Knowingly, Information Provided Will Influence Third Party
Threat Categories

• Familiarity Threat
  – Long-Term Relationship with Person in Entity
  – Family Member a Supplier
  – No Review of New Work Because of Past Work Product
  – Family Member a Subordinate
  – Gifts from Vendors or Customers
• Self Interest Threat
  – Employee Benefits from Interest in Relationship or Employee Organization
  – Family has Financial Interest
  – Value of Family Interest in Organization Affected by Decision
  – Bonuses
Threat Categories

• Self Review Threat
  – Evaluation of Previous Service or Decision-and Relied Upon on a Later Service
  – Internal Audit Procedures: Performed Previously in a Different Position
  – Accepts Previously Performed Work as a Basis for Future Work
Threat Categories

• Undue Influence Threat
  – Subordinates Judgment to Individual in Entity or Third Party
  – Results From: Position, Reputation, Expertise, Personality, Coercion
  – Examples: Provide Misleading Information, Deviate from Company Policy, Change Conclusion, Hire Unqualified Individual
Safeguards

• Eliminate or Reduce Threats
• Reduced Threats – Must Be to an Acceptable Level
• Categories
  – By Profession, Legislation, or Regulation
  – By Employee Organization
Safeguards

• Effectiveness
  – Proper Threat Identification
  – Design of Safeguard
  – Who Affected
  – How Applied
  – Applicability to Another Category
Safeguards

• Examples:
  – Profession, Legislation, Regulation
    • Education
    • Professional Standards
    • Licensing
  – Employee Organization
    • Ethical Conduct
    • Commitment to Compliance
    • Internal Policies
    • Awareness of Fraud Potential
Integrity and Objectivity

• Maintain Integrity and Objectivity
• Free of Conflicts of Interest
• No Known Misrepresentation
• No Subordination of Judgment
• Relationship to Conceptual Framework
  – Apply When Can’t Find Other Solutions
  – Violation: When Can’t Demonstrate Safeguards at Acceptable Level
  – Seek Guidance When Obstacles – Could Even be Legal Standards
Conflicts of Interest

- Question if a Reasonable, Informed, Third Party Aware of the Information Would Conclude There is a Conflict
- Creates Adverse Interest
  - Service Involves Two Parties at Same Time With Different Intents
  - Employee has Interest Different Than Party Being Served
Conflicts of Interest

• Situation
  – Two Employees at Same Time
  – Two Partners in a Partnership Dispute
  – Financial Information Prepared for Only Part of Managers in a Dispute
  – Family Member on One Side
  – Board of Employer Making Investment
Conflicts of Interest

• Identify
• Evaluate: If Exists Can it be Acceptable?
• Disclosure
• Document
• Seek Guidance: Entity, Professional Standards
• Known Misrepresentation, Subordination of Judgment
General Standards

• Professional Competence
• Due Professional Care
• Planning and Supervision
• Sufficient Relevant Data
• Questions
  – Any Threats to Above?
  – Are Safeguards Needed?
  – Any Conflicts to Adherence?
Compliance With Standards

• Professional Promulgations
• Government Agencies
• Financial Reporting Frameworks
Accounting Principles

- GAAP: Can Only State No Departure
- Consider Treats and Safeguards
- May Be Required to Deal With Conflicts
- Departures
  - Justified
  - Unjustified
Acts Discreditable

• Prohibited
• Apply Conceptual Framework
• Pressures
• Conflicts
• Discrimination & Harassment in Employment Practices
• For CPAs: Disclosing CPA Exam Questions & Answers
Acts Discreditable

• Failure to File Tax Return or Pay Taxes
• Negligence Preparing Financial Statements or Records
  – Making, Permitting, Directing Someone Else To
  – Failure Correcting
  – Signing, Permitting, or Directing to Sign Document
Acts Discreditable

- Governmental Bodies, Commission, or Regulatory Agencies
  - Follow Standards, Guides, Rules, Regulations
  - Appropriate Reporting Framework
  - Material Departure an Act Discreditable
    Unless Disclosed and Why
Acts Discreditable

• Indemnification & Limitation of Liability Provisions
  – May Be Prohibited by Banking Regulations, State Insurance Commissions, SEC
Confidentiality

- Applicable to Employer and Volunteer Organizations
- Any Proprietary Information
- Inadvertent Disclosure
- Outside Advisors: Notify Confidentiality
- Subsequent Employer: No, Can Only Use Experience and Expertise
Confidentiality

• OK to Disclose if Legal or Professional Responsibility
  – Valid Subpoenas
  – Violation of Law
  – Defend Self
Confidentiality

• Additional Permitted Disclosure
  – Financing
  – Vendors
  – External CPAs
  – Attorneys
  – Regulators
Promoting & Marketing Services

• Must not be False, Misleading, or Deceptive

• CPA Credential Use
  – Subject to Jurisdiction
Skepticism

- Public Company Accounting Oversight Board

“An attitude that includes a questioning mind and a critical assessment of audit evidence”
Skepticism

• AICPA
  – Located issue addressed in professional standard pronouncements approximately 40 times
  – Auditing
    • Explanatory material in obtaining reasonable assurance
    • GAAS requires auditor exercised professional judgement and maintain professional skepticism
  – Ethics
    • Discusses breach of independence affecting skepticism
  – Management Discussions and Analysis
Skepticism

• PPC
  – Cautions Avoiding Manipulating Projections Potential Provision Regarding Valuation
  – Cautions Effects in Litigation

• Standards of Fieldwork
  – Competency
  – Due care
  – Supervision
  – Sufficient Relevant Data

• Sufficient Relevant Data is Our Evidence
• Assistance to Reasonable Certainty
Cases
Case 1
Fast Funds Agency

The Fast Funds Insurance Agency submitted a forged application to a premium finance company. The agency used client information to obtain funds for both business and personal interests. The agency received both a direct premium payment from its’ client and funds from the finance company. The agency followed up by financing a policy that did not exist. The insurance carrier had no idea the transaction took place. The agency continued the aforementioned procedures multiple times. The activities caused the lapse of policy coverages. Insurers failed to receive premium remittances.

Discuss how insurers can safeguard against these practices.
Case 2
The Phantom Commissions

An insurance agent disputed the amount of commissions owed to him. It turned out the CFO short-changed the commission owed by purposely posting the commission due as income to the agency.

The owner of the agency hired an outside third party to review the situation. However, the outside accountant was given instructions to exclude certain funds received required to be entered as accrued commissions, to consider them as revenues.

*Discuss the ethical issues surrounding the situation and how the reporting can be corrected.*
The High Equality Insurance Company is preparing its request for approval of an increase in its premium rates. The company has been financially successful resulting from a combination of cost controls including the ability to pass on cost increases, handling government regulations, and generating additional revenues from new sources. Senior management recognizes the financial statements indicate excellent financial results, potentially limiting the approval of rate increases. The company’s Board has asked its CFO to provide projections indicating a need for higher rates beyond what any evidence indicates.

Discuss the ethical issues surrounding this scenario.
Case 4
Provider Punishment

A healthcare service provider’s policy is immediate payment by its patients. The provider when obtaining a payment does not provide an actual receipt. It indicates the amount paid on a copy of the detailed patient visit sheet. The amount collected is usually in excess of the amount shown on the subsequently issued Explanation of Benefits form.

The patient is required to call if an adjustment is needed. The patient is thanked for the call and told if the patient hadn’t called, the patient would receive no refund. The patient is told due to the volume of patients, no refund will be issued for eight weeks.

The refund was not sent. The patient calls again after 9 weeks and a check is sent.

Discuss what the role of the insurance carrier should be.
Case 5
1, 2, 3, Kick

An insurance carrier’s policy holder had a car accident. The policy holder had a preference to have the car fixed at the car dealership where it was purchased. The insurance carrier representative (middleman) advised that the dealership was not a “preferred vendor” and repairs would not be guaranteed. The middleman received a commission and the “preferred vendor” paid a 5% fee to the insurance carrier.

Discuss the ethical issues related to:

1. The middleman’s representation
2. The insurance carrier receiving a 5% “referral fee”
3. Disclosure to the policy holder
4. The recording of the financial transaction
Wrongful death and wrongful termination cases can be located in the federal court system. The U.S. code allows for punitive damages to be assessed against companies in these matters. The concept includes that the defendant company can be assessed damages to the extent the company will be deterred from acting in the same way again and it can get penalized financially but not to the extent it could be forced into bankruptcy.

*Discuss the provisions your carrier has in its policies to refuse payment for those punitive damages.*

*Discuss the procedures for disclosing any liability for punitive damages in your financial statements.*
Insurance adjusters are part of the underwriting costs. In certain instances they may seek specialized laboratories to determine values of material. For example, there is one laboratory for carpeting.

Carpeting professionals may disagree with the lab. Carpets may differ as to thickness, durability, softness, touch, moisture retention, etc.... There are differences in padding as well.

Given the aforementioned, how would the CFO recognize potential liability for these types of claims on a financial statement?
The IT professionals are routinely involved with the security, accuracy, and efficiency of information systems. Information systems design, implementation, or integration services performed need to adhere to ethical standards.

Discuss how you as an IT professional can illustrate how you deal with the issues of:

1. Objectivity
2. Due professional care
3. Disclosure of facts
4. Compliance with standards
Accountants and IT professionals are frequently requested to perform various tasks. Some of these tasks may have never been previously performed.

Discuss your process in determining why you may be able to perform the task, why you could perform it, and finally, if you were to complete the project, how you were able to do it competently.
Accountants and IT professionals frequently have access to proprietary information. They may also obtain access to proprietary information performing voluntary activities.

**Discuss:**

1. **The differences, if any, in the disclosure of confidential information from either an employer or volunteer organization.**

2. **What and to whom it is appropriate to disclose confidential information.**