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This month’s cover story is our annual tax software survey. For 14 years, authors Susan Anders and Carol Fischer have asked NYSSCPA members and tax practitioners about what kinds of tax preparation and tax research software they use and how satisfied they are with it. The comprehensive results, presented here in the Journal, should provide readers with a wealth of information about the experience of their peers and colleagues. Anyone in the market or considering a change in provider should pore over the results before making a decision.

Also this month, author David Crawford decries the lack of unity in the accounting profession’s leadership ranks, which he believes has led to external forces exercising undue control over the accounting curriculum and future shape of the profession. Many may disagree with his conclusions, but practitioners and educators alike should be aware of the issues and get involved with the collaborative efforts under way.

Our celebration of our 85th anniversary also continues this year: One of our feature articles looks back to World War II and the noteworthy contributions made by high-level CPA talent at the predecessors of the firm now known as Deloitte. And in News & Views, we open our archives to reminisce about the technology applied to accounting and tax practices 50, 75, and even more than a century ago. The times may have changed, but CPAs have always seen the challenges that technology presents to traditional methods and sought to leverage the opportunities they can bring to their clients’ operations and their own businesses.
In 2015, New York State CPAs continued to report satisfaction with tax preparation and commercial tax research packages: overall ratings generally increased. But the challenges of the 2015 tax season appear to have created greater difficulties for tax professionals. The majority of respondents experienced complications from tax law changes under the ACA. More than one-quarter of survey respondents reported significant problems related to late or incorrect Forms 1099 or Schedules K-1. In addition, many participants faced identity theft issues.

The United States’ entry into World War II marked the start of the largest business undertaking in the nation’s history, and accountants were needed to keep track of records and act as auditors—but public accounting firm staffs were decimated by enlistments and the draft. Although all CPA firms made contributions to the war effort, it was the predecessors of the firm now known as Deloitte that arguably supplied the most high-level talent. Their efforts helped ensure victory and led to innovations in accounting and auditing.
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Consider how the world of finance today is so vastly different from what it was just seven years ago. We were unsure if our entire financial system was about to collapse: there were budget cuts, failing businesses, high unemployment. Anyone with a reliable job could only hope it would remain that way. You hunkered down and worked hard, eager to prove your value.

Thankfully, those days are behind us. The economy has recovered, the job freeze has thawed, and even though we have been busy muddling through a slow recovery from a long recession, technology has continued its exponentially progressive forward march. As a result, what NYSSCPA members needed from their professional association just a few years ago may be vastly different from what they need today. With this in mind, the NYSSCPA will in January launch a long-overdue membership survey that will be used to inform our programs, technology, and content. Every Society member for whom we have an e-mail address will receive the survey—so if you haven’t recently updated your current record with us, please contact the NYSSCPA within the next month so your voice can be heard.

I often write and talk to accounting groups about how critical it is that firms prepare for the future; the business environment is no longer “business as usual,” and firm owners who think it is are in for a shock. Technology is not only changing the accounting profession’s playbook; it is also changing the entire playing field. Firms’ ability to adapt will determine who gets to play and who gets benched. With the results of this survey, the NYSSCPA can help its members make the cut.

Meeting the Needs of the Next Generation

About four years ago, we launched the NYSSCPA’s NextGen program because two-thirds of the membership was over 50 years old. We value these members, their leadership and contributions, and how much they in turn value their membership—but anyone looking at our membership numbers could see that the NYSSCPA was not meeting the needs of the next generation. So we set out to change that. We have made significant progress in increasing the number of students on our membership rolls, but almost equally as important is that we have expanded our NextGen programming based on what the next generation of accountants needs, not what we think they need. The same goes for baby boomers making assumptions about what millennials should be, how they should learn, and how they should reach their career goals.

The survey results will be rich in data that will allow us to better serve the needs of all of our members. We are giving special consideration to the responses of our NextGen members, since the survey will be gathering most of its data from an already engaged and vocal segment of our membership. We need to be the organization that the next generation not only wants to belong to, but also wants to engage with and lead some day. If we don’t meet this challenge, we risk becoming an organization that exists in an echo chamber, listening to ourselves talk about what the next generation needs instead of listening to what they have to say. We need to create value for all of members, not just the generation nearing retirement.

I hope you will help us reach this goal by completing the survey when it arrives in your inbox in January 2016. We’ll be using the ideas and suggestions that you share with us to write a new playbook for the NYSSCPA, instead of relegating ourselves to the bench.

Joanne S. Barry, CAE
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The lack of professional unity in the accounting profession has led to external influence over the shape of accounting education. Unified leadership would better serve both the profession and the public interest. The Pathways Commission, the body currently charged with developing strategy and making recommendations regarding the future of accounting education, has proposed a way to revitalize such efforts. This article examines the longstanding divide between accounting practitioners and educators, considers the results of a Pathways Commission report on the state of accounting education, and explores its recommendations for renewed cooperation among practitioners and educators.

The Report
In July 2012, the American Accounting Association (AAA) and the AICPA Pathways Commission issued a report on the future structure of higher education for the accounting profession (“Charting a National Strategy for the Next Generation of Accountants,” July 2012, http://commons.aaahq.org/posts/a3470e7ffa). The formation of this working group stemmed from a 2008 report from the Advisory Committee on the Auditing Profession (ACAP) to the U.S. Department of the Treasury. Based on suggestions from this quasi-governmental body, the Pathways Commission issued seven noteworthy recommendations regarding many issues affecting human capital in accounting education and practice. Equally important, though, is what it chose not to address. The ACAP had asked that the commission “consider a postgraduate professional school model to enhance the quality and sustainability of a vibrant accounting and auditing profession” (U.S. Department of the Treasury, “Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury,” pt. VI, p. 27, October 2008).

In response to that charge, the Pathways Commission “felt it was premature to address this issue without addressing the underlying issues currently impacting accounting education and the profession. Further study of this issue is suggested as a part of the ongoing implementation activities” (Pathways, p. 18).

The Pathways Commission chose to sidestep a much-debated issue of graduate education for the accounting profession, and instead opted to help create a malleable framework of accounting education for the next generation of accountants. The response is justified, given the “inflexibility of academic environments and the long standing disconnect between academe and practice” (Robert Bloom, “Perspectives on the Pathways Commission Report: An Analysis of the Proposals,” The CPA Journal, August 2013, pp. 10-14).” Apparently, the commission recognized the insurmountable chal-
lenges of gaining consensus for graduate education from multifaceted stakeholders and took a more prudent path in recommending further deliberation on this issue.

Although added education requirements cannot guarantee a higher level of performance and integrity in practice, one might imagine that major educational issues in accounting have diminished now that all states require 150 hours of higher education to obtain licensure as a CPA. The ACAP call to consider postgraduate education suggests otherwise, citing ongoing failures in the financial sector that mark the importance of an accounting and auditing profession bolstered by considerable education and experience for healthy, functioning U.S. capital markets (Department of the Treasury, 2008).

**Competing Claims for Authority**

The author’s own study regarding the accounting curriculum investigated and compared preferences of accounting educators and practitioners under the premise that there is a divide in the opinions of the two groups. An overall finding indicated significant differences between the ratings of practitioners and educators with regard to the authority to prescribe accounting curriculum of five stakeholder groups: 1) accounting educators, 2) accounting practitioners, 3) accountants in industry, 4) state boards of accountancy, and 5) accrediting bodies. This 2007 survey, which preceded the 2008 ACAP report by only months, lends credibility to the notion that differences between practitioners and educators existed at the time. For example:

- Practitioners and educators each rated themselves highest among the five stakeholder groups regarding prescriptive authority over the accounting curriculum.
- There were significant differences between practitioners and educators, but little support from either group in granting authority to any other stakeholders.

The gulf between the two groups lends support to the historical claim of competition for authority over matters in accounting education. As suggested by ACAP, a professional working group was needed to demonstrate cooperative efforts related to accounting educational reform. Subsequently, the Pathways Commission was formed in anticipation of doing just that.

**A Profession Lacking Unity**

Accountants have never been able to unify in a way that could have benefited them politically. As one author notes, “the relationship between the accounting profession and accounting higher education and government in the United States is convoluted and involves shifting alliances” (Glenn Van Wyhe, “A History of U.S. Higher Education in Accounting, Part II: Reforming Accounting,” *Issues in Accounting Education*, vol. 22, no. 3, 2007, p. 497).

Sentiments that have proven difficult to define have likely limited compromise and stymied attempts at change. This complex relationship appears to have pushed accountants into a reactionary corner more than once in the past decade. Specific examples include the National Association of State Boards of Accountancy (NASBA) 2005 proposal for curricular changes and the aforementioned 2008 ACAP report (NASBA, “Exposure Draft: Uniform Accountancy Act Rules 5-1 and 5-2,” February 2005). For a profession that has relinquished considerable self-regulation in the areas of financial accounting and auditing, any attempt by other entities to influence accounting activities should be taken seriously.


Public accounting has long been considered “professional” accounting, and correspondingly it has been the province of large CPA firms, which have had a significant formative impact on accounting education. Many academics resent this influence and oppose the exclusion of managerial accounting, internal corporate accounting, and internal auditing from the definition of professional accounting. Some academics have argued for various educational tracks in accounting, which ultimately resulted in the differentiation of managerial accounting and financial accounting at the curriculum level (Van Wyhe 2007).

These differences have also advanced the notion of obtaining special certification examinations for the areas of managerial accounting and internal auditing. The AICPA has implemented a certification process—i.e., the Chartered Global Management Accountant (CGMA) qualification—for CPAs meeting certain requirements in the area of management accounting. Decades ago, one author recommended a unique logical method of organizing the profession and astutely predicted that special certifications would likely be divisive rather than unifying (J. W. Partillo, “Unity in the Accounting Profession,” *Journal of Accountancy*, vol. 138, no. 1, 1974, pp. 50–58).

This recommendation failed to take root, just as many other recommendations have failed over the years. Now, the Path-
ways Commission has decided to be all-inclusive by defining the profession broadly and embracing almost anyone working in the accounting community as part of the profession.

Accounting has been likened to the legal profession, and although the legal profession includes both paraprofessionals and attorneys, it is unclear how being all-inclusive might affect the commission’s efforts at building a learned profession. Traditional learned professions (i.e., medicine, law, clergy) rely on both rigorous signature pedagogy and postgraduate degrees as marks of distinction, so it is uncertain whether the comparison is entirely appropriate. At one time, the CPA designation might have served as a sufficient mark of excellence for accountants, but the brand seems to have become less distinguished given the proliferation of various certifications and the trend towards postgraduate academic credentials in other professions.

**Reward Structures and Accreditation**

In their 1978 report (AICPA, “The Commission on Auditor’s Responsibilities: Report, Conclusions, and Recommendations,” 1978), authors Patten and Williams noted that the reward structure under which faculty labor in business schools contributes to the split between the research that practitioners and academicians view as important. For example, quantitative accounting research geared towards the financial markets is popular among accounting scholars because it adds to their academic credentials, but the topics often prove to be of limited value to the practice of auditing or public accounting. Comments in the Pathways Commission’s 2012 report indicate a dearth of meaningful links between practitioners and educators, causing the widest research divide the profession has experienced. The commission recommended modifying the reward structure for faculty by placing teaching on an equal level with research, but this recommendation will likely face stiff opposition from academicians who have benefited under the current system.

Some educators will assert that the current theoretical research agenda has garnered respect for accounting as an academic discipline by promoting the analytical rigor and abstraction that is valued in the academy. This vision is supported by the proposition that, in a professional field, educational preparation must be fundamentally academic to gain prestige and legitimacy (A. Colby, J. Dolle, T. Ehrlich, W. M. Sullivan, *Rethinking Undergraduate Business Education: Liberal Learning for the Profession*, Jossey-Bass, 2011). In accounting, the contradiction between academic theory and the pragmatism of practice has not been reconciled to the degree necessary to promote a mutually beneficial relationship.

An additional consideration is that while most other professions are accredited via organizations closely aligned with their professional practicing membership, accounting is not. The premier accreditation for an accounting program is awarded by the Association to Advance Collegiate Schools of Business International (AACSB). While AACSB accreditation of business schools is widely accepted and respected, secondary accreditation of professional accounting programs by that same body can be challenged on the grounds that it is not representative of the accounting profession.

Accreditation of accounting education should be of concern for the profession, because an outside body largely disconnected from practice is conferring this status. Many notable academicians are involved in the accreditation process, but there is little representation of the professional practice arm. For example, the current makeup of the Accounting Accreditation Committee (AAC) includes 13 members, 12 of whom are from higher education—predominantly administrators from AACSB schools—with only one representative from public accounting (AACSB, “Accounting Accreditation Committee,” 2015, http://www.aacsb.edu/). By contrast, the American Bar Association Council—the oversight body of law school accreditation—is made up of 21 members and limits deans and faculty to 10 members, with the balance consisting of judges, practicing attorneys, a law student, and three public representatives (ABA, “The Law School Accreditation Process,” 2013, http://www.americanbar.org/legal).

The accounting literature supports the notion that individuals most influential in accounting education are, and ought to be, accounting practitioners and accounting educators (Flaherty 1979; Rumble 1998). This seems reasonable, considering the influence other professions have over their own educational structure, content, and accreditation.

Accreditation might also be viewed as problematic because AACSB data from 2013 shows that only 495 schools in the U.S. with AACSB business accreditation can aspire to achieve this separate level of accreditation; secondly, only 169 of the 439 accounting programs in that category (38.5%) have separate accounting accreditation (AACSB, Schools Accredited in Accounting, 2013, http://www.aacsb.edu). This is a curiously low percentage, considering the number of schools that apparently have reputable business programs, but are either unable or unwilling to secure top accreditation for an accounting program. College deans influence accounting education through AACSB International (Colby et al. 2011; W. H. Black, “The Activities of the Pathways Commission and Historical Context for Changes in Accounting Education,” *Issues in Accounting Education*, vol. 27, no. 3, 2012, pp. 601–625). While their intentions are good, college deans and other administrators frequently have limited background in accounting, which means they make decisions based largely on the mission or financial considerations of the business school. In this way, the accounting profession has forfeited their ability to influence the educational experience of the very individuals they hire. Accreditation of accounting programs by the profession itself could have provided unity and helped to define the profession, but, as Van Wyhe stated, “accounting academicians did not feel the loyalty to the profession that academicians in the other professions apparently felt” (p. 497).
The ACAP’s proposal of considering a postgraduate professional school model separate from the business schools is not a new idea. This concept was put forth in the 1970s with limited success, at a time when several schools of accountancy were formed around the country despite the protest of business school deans. The Federation of Schools of Accountancy was formed in 1977 with the intention of separate schools of accountancy, whether independent of or within the schools of business (Glenn Van Wyhe, The Struggle for Status: A History of Accounting Education, Garland Publishing, 1994). While the AAA and AICPA initially cooperated to begin development of accreditation standards, the tone was changed by the AACSB’s sudden interest, which stemmed from the desire of business school deans to keep control of accounting programs (Van Wyhe, 2007). Shortly thereafter, the joint accounting group recognized it had insufficient support and terminated its accreditation efforts while the AACSB moved forward with little intervention (Wallace E. Olson, The Accounting Profession, Years of Trial: 1969–1980, AICPA).

Thus, the ACAP proposal calls for the reexamination of issues not fully resolved some 40 years ago. Perhaps separate postgraduate schools of accountancy are not needed, but an accrediting body for accounting programs with equal representation from those in practice and academia should be open for deliberation. The Pathways Commission appears to be logically poised to consider such a compromise, thereby adding clarity as to who really has authority for prescriptive changes in accounting education. Accordingly, the commission should seek input from its constituents regarding this issue.

**A Unified and Learned Profession**

While it cannot be inferred that differences between accounting practitioners and educators have resulted in a defective educational structure, future discord could prove to be hazardous for an academy and a profession under continuous scrutiny by many stakeholders. Perhaps the biggest threat to accounting as a sustainable profession is not the direct risk of divisiveness between the two groups, but the indirect and unintended consequences of surrendering to other groups a certain amount of unwarranted authority over educational issues. Without a sense of professional unity between the parties most influential in accounting education, external interests will continue to be able to use discord to their own advantage. Forging an enhanced educational framework that supports a viable accounting profession is a joint privilege held by accounting practitioners and educators that need not be relinquished to others.

The Pathways Commission, a body representing both practitioners and educators, is currently taking a thoughtful and deliberative approach to many of the issues confronting accounting education. After two years of implementation efforts, the goal of improving the educational process appears to be progressing. Building a learned profession by encouraging better integration of professionally oriented faculty into the academic arena, urging academic journals to publish on practice-oriented issues, and encouraging practitioner journals to promote awareness and use of academic research are all proposals that should further unity among a profession long divided (“Implementing the Recommendations of the Pathways Commission: Year Two,” August 2014).

Three working groups charged with the task of determining curriculum models and connecting those models to alternate career paths are currently organized around defining a common body of knowledge, developing signature pedagogy, and determining appropriate technology for the accounting generalist (AAA, “Update from the Pedagogy Task Force of the Pathways Commission, Accounting Education News, vol. 42, no. 1, 2014, pp. 6–7).”

While still in the early phases, efforts by the Pathways Commission to build “a learned profession through greater connectivity between the academic and practice elements of the profession” is unprecedented. Educators, public practitioners, and accountants in industry alike all seek to participate in a respected and vibrant profession that executes responsible authority over its own affairs. A working group that seeks input from multiple stakeholders is a realistic approach to embrace when confronted with the alternative of change imposed by groups less concerned with the sustainability of the accounting profession.

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Putting the Decades-Long ‘Plain Paper’ Debate to Rest

Will SSARS 21 Be the Final Resolution?

By Howard B. Levy

Driven largely by CPAs’ increased use of computers in preparing their clients’ financial statements, Statement on Standards for Accounting and Review Services (SSARS) 8, Amendment to Statement on Standards for Accounting and Review Services No. 1, Compilation and Review of Financial Statements—issued in October 2000—was thought to have ended 20 years of controversial discussions about CPAs’ association with unaudited, so-called “plain paper” financial statements. For the first time, SSARS 8 permitted CPAs to prepare and submit (without an accompanying report) financial statements not intended for third parties to members of client management who have knowledge of the company and who understand the limitations of the financial information. (See G. R. Young, J. R. Madray, “An End to the Plain-Paper Debate?” Journal of Accountancy, Jan. 2001.)

The debate intensified after SSARS 8 was issued, however, and in 2012 it escalated to the level of the AICPA’s Accounting and Review Services Committee (ARSC), the applicable standards-setting body. Three successive proposals were exposed for public comment before SSARS 21 was finally issued in October 2014 amidst a flurry of continued controversy. (For additional historical detail, see M. P. Glynn, “How SSARS No. 21 Became a Standard,” Journal of Accountancy, Oct. 28, 2014; M. Glynn, Ellen Goria, “Proposed Revisions Clarify Responsibilities for Preparers,” Journal of Accountancy, Aug. 2012; D. S. Conant, J. R. Madray, “A New Approach to Compilations,” Journal of Accountancy, Apr. 2000.)

SSARS 21 supersedes substantially all of its predecessor standards and resulted in a complete recodification. (Specific paragraphs are referenced herein to the recodification as AR-C section numbers.) SSARS 21, and the resultant recodification, will be effective for calendar year 2015 financial statements; however, early application is encouraged. (Note that SSARS standards apply only to privately held entities, not to interim reviews performed for SEC issuers.)

Preparation Services

In all practical respects, the newly authorized preparation service is a nonattest alternative to a compilation. As discussed above, this new service level was created after decades of debate among practitioners, standards setters, and other interested parties to create a bright line between accounting services (i.e., preparation) and reporting services (compilation, which is regarded as an attest service despite the absence of any assurance provided). SSARS 21 does not suggest in any way that CPAs need to restrict the use of prepared financial statements by any third-party users of the financial statements, although restriction in not prohibited. Moreover, a preparation does not require all the documentation necessary in a compilation (AR-C section 70.21), but it is, nevertheless, regarded as a professional service, subject to all applicable ethical requirements (AR-C section 60.08), and the performance requirements discussed below are otherwise substantially the same.

Because preparation is defined as a nonattest service, CPAs need not consider if they are independent. Independence is neither required nor implied, nor is it asserted, such as in a heading that might appear on an accompanying disclaimer of assurance— if one is issued (see next paragraph). If, however, other services requiring the accountant to be independent are performed or even contemplated in the future for the same client or one of its affiliates, care should be taken to preserve independence when performing preparation services.

The standard does not require any form of report for a preparation service engagement, provided a prescribed statement or legend is placed on each page that effectively conveys the message that no assurance is provided. It is particularly important to note that, even when third-party use of CPA-prepared financial statements is expected, it is not necessary under SSARS 21 that such a legend identify the preparing accountant. Enabling the anonymity of the preparing CPA is probably the most radical departure from prior professional standards embodied in SSARS 21. If, at management’s discretion, no legend is placed on each page, an alternative separate disclaimer (never referred to as a “report”) which clarifies that no assurance is provided on the financial statements and makes identification of the accountant or firm necessary (AR-C sections 70.14 and .A11) would be required.

According to the principal drafters of SSARS 21 (Michael Brand, ARSC chair, and Michael P. Glynn, AICPA senior technical manager and staff liaison to the ARSC), the main message to be taken from its issuance is that the objective of the engagement, as embodied in the CPA’s understanding with the client, will determine whether the new standard for preparation services is to apply or if the revised compilation standard will apply. Accordingly, CPAs must consider what they are being engaged to do.

The new meaning of ‘association.’ Historically, the term “association” has been used in reference to an accountant’s involvement with a client’s financial statements (or other assertions of management) with particular regard to communicating that involvement (and the nature and extent thereof) to users; for example, in a report or another reference. An accountant was said to be so associated with a client’s financial statements only if the accountant issued a report to the client (or its governance body) describing the nature and extent of the accountant’s involvement (i.e., the level of service and responsibility taken) with respect thereto. (Prior to SSARS 8, the relationship between reporting and association was said to exist, and a report was required, even when the financial statements were intended only for use by client management, and third-party use was not expected.) But under SSARS 21, a distinction is now made between the association of the accountant...
and the association of the accountant’s name (i.e., in the eyes of third-party users). The preparing accountant is said to be associated without regard to whether the accountant’s name (and level of involvement) is made known to third-party users with the financial statements (e.g., in a report). The nonreporting option without limiting distribution to management is a new concept. Thus, compilation is no longer the minimum service level with which a CPA may be associated with a client’s financial statements unless the accountant is: 1) engaged to perform an attest engagement or 2) unable to comply with the SSARS 21 requirement to either apply a “no assurance” legend to each page or attach an alternative, separate disclaimer thereby requiring the engagement to be upgraded to a compilation.

**Principal preparation performance requirements.** The principal performance requirements applicable to a preparation engagement are summarized below and set forth in greater detail in AR-C sections 70.08–22 and .A5–18.

The standard requires a written understanding in the form of an engagement letter or contract that is signed by both management and the accountant, which documents the terms of the preparation service engagement, including, at a minimum—

- management’s acknowledgment of its responsibilities as set forth in AR-C section 60.25c,
- management’s agreement to the use of a no-assurance legend or a separate disclaimer of assurance, and
- every other item listed in AR-C section 70.A10.

In a preparation engagement, as in a compilation or a review, CPAs must have an understanding of the relevant portions of SSARS 21 (AR-C section 60.12) and must have or obtain an understanding of the financial reporting framework and the significant accounting policies to be used in the preparation of the financial statements. Absent relevant industry experience, the required understanding of the framework and accounting policies may be obtained from AICPA guides, industry publications, financial statements of other entities in the industry, textbooks and periodicals, continuing professional education, or consultation with individuals who are knowledgeable about the industry (AR-C sections 70.12 and .A10). Although not expressly required by the standard, it would be wise to document these alternative sources whenever applicable.

**Omitted disclosures and other departures in preparation engagements.** Just as with compilations, CPAs preparing financial statements may omit substantially all required (or customary) disclosures, so long as they are not aware that any such omission was likely requested by management with the intent of misleading third-party users. (Documentation of the lack of such awareness is recommended by this author, but not required.) The omission itself, along with any other known departures from the applicable financial reporting framework in use, must be disclosed in the financial statements (AU-C sections 70.18–20).

**Applicability of peer review to preparation engagements.** Unless the firm prohibits their acceptance as matter of policy, preparation engagements will be technically subject to peer review, even if their selection is highly improbable. For full-scope “system reviews,” preparation engagements are subject to selection only on a risk assessment basis, as are other engagements (thus making such selection highly unlikely for any firm with an accounting and auditing practice composed primarily of audits). For firms that perform no audits and that qualify accordingly for off-site “engagement reviews,” preparation engagements are subject to selection only in the following limited circumstances:

- A firm performs no accounting or attest service engagements other than preparations.
- An individual is responsible to perform only preparation engagements.
- It is necessary to select a preparation engagement to achieve the required minimum of two selected engagements.

Peer reviewers will seek some assurance that the firm has adequate quality control policies and procedures in place to reasonably assure its management of the firm’s compliance with the applicable standard.

**Compilation and Review Services**

Clearly, the main thrust of SSARS 21 is to provide preparation engagements as an alternative to compilations. This will likely reduce the number of compilations currently being performed, particularly when there is little or no third-party reliance on the financial statements. Third-party users who are accustomed to receiving compilation reports will likely want to continue to do so, even though the look of such reports will change.

Although some have reported that SSARS 21 presents significant changes to these services, in this author’s view, the changes in the appearance of compilation and review reports are the only significant departures from previously operative professional standards. The performance requirements applicable to compilations and reviews remain substantially the same as they were under the predecessor standards. The focus of the remainder of this article is on those changes, including the less significant and more subtle ones; however, some, but not all, of the continuing older requirements are also mentioned briefly.

**Compilation reports.** The unmodified compilation report on GAAP-basis financial statements that is illustrated in the standard appears as a single paragraph; addi-
tional paragraphs are to be added in any of the following circumstances (most of which are discussed briefly below):

- When financial statements prepared on a special-purpose framework (i.e., anything other than U.S. GAAP, including income tax and cash basis)
- When substantially all required or customary disclosures are omitted, or there is another known departure from GAAP or other applicable reporting framework
- When supplementary information (whether required or not) accompanies the financial statements
- When the reporting accountant decides to include an emphasis of matter paragraph (used to draw attention to matters appropriately presented or disclosed), and
- When the reporting accountant is not independent, requiring a lack of independence paragraph (which, if applicable, should be presented last; see next section).

Only supplementary information or discretionary emphasis-of-matter paragraphs require a caption in a compilation report.

Variations in format from the illustrative report examples presented in the standard are permitted so long as all applicable requirements are met. Following is a summary of the minimum requirements for inclusion in a basic compilation report (not necessarily in the order listed) under AR-C section 80.17:

- A statement that management is responsible for the financial statements
- Identification of the financial statements (and supplemental information, if any) that were subjected to the compilation engagement
- Identification of the reporting entity
- Date of the balance sheet and the period covered by the financial statements
- A statement that the engagement was performed in accordance with SSARS as promulgated by the ARSC
- A statement that the reporting accountant did not audit or review the financial statements; was not required to perform any procedures to verify the accuracy or completeness of the information provided by management; and, accordingly, does not express an opinion, a conclusion, or provide any other assurance on the financial statements
- The signature of the reporting accountant or firm
- The city and state where the accountant or firm practices (unless evident in the letterhead)
- The report date (i.e., the date the required procedures were completed).

**Reporting when not independent.** As in the previous standard, a CPA who is not independent may not issue a review report, but may issue a compilation report, provided the independence impairment is noted in a separate paragraph that appears at the end of the report. As previously provided under SSARS 19, the reason independence is impaired may be disclosed, provided that all such reasons are included (AR-C sections 80.22–23 and .A28–30).

Only supplementary information or discretionary emphasis-of-matter paragraphs require a caption in a compilation report.

Additional paragraphs are to be added in any of the following circumstances (most of which are discussed briefly below):

- When financial statements prepared on a special-purpose framework (i.e., anything other than U.S. GAAP, including income tax and cash basis)
- When substantially all required or customary disclosures are omitted, or there is another known departure from GAAP or other applicable reporting framework
- When supplementary information (whether required or not) accompanies the financial statements
- When the reporting accountant decides to include an emphasis of matter paragraph (used to draw attention to matters appropriately presented or disclosed), and
- When the reporting accountant is not independent, requiring a lack of independence paragraph (which, if applicable, should be presented last; see next section).

Only supplementary information or discretionary emphasis-of-matter paragraphs require a caption in a compilation report.

Variations in format from the illustrative report examples presented in the standard are permitted so long as all applicable requirements are met. Following is a summary of the minimum requirements for inclusion in a basic compilation report (not necessarily in the order listed) under AR-C section 80.17:

- A statement that management is responsible for the financial statements
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**Review reports.** The form of a review report under SSARS 21 will now look similar to audit reports issued for private entities. It will have several captioned paragraphs separately describing management’s responsibility and the reporting CPA’s responsibility and conclusion, as well as other applicable items. But the required content will be substantially the same as it was before.

As in audit reports, emphasis-of-matter paragraphs draw users’ attention to matters that are appropriately presented or disclosed in the financial statements. Also as in audit reports, certain emphasis-of-matter paragraphs are mandatory, for example, when financial statements are prepared in accordance with a special purpose framework or with respect to a known departure from GAAP or other framework (AR-C section .A91). Other emphasis-of-matter paragraphs are to be considered for inclusion whenever deemed fundamental by the reporting CPA to expected users’ understanding of the financial statements (e.g., a going concern uncertainty, per AR-C sections .A91). SSARS 21 is silent as to the use of emphasis-of-matter paragraphs in a compilation report (such as for a going concern uncertainty), but they are not precluded. CPAs are well advised to consider including them anyway when circumstances warrant them.

If the reporting CPA considers it necessary to communicate a matter deemed relevant to the users’ understanding of the review (i.e., a matter that is neither presented or disclosed nor required to be presented and disclosed in the financial statements), an other-matter paragraph, not an emphasis-of-matter paragraph, should be placed immediately after both the conclusion and any emphasis-of-matter paragraph. Appropriate captions that are more precisely descriptive than illustrated may be used for other-matter paragraphs (AR sections .A96–98).

Although the language in AR-C section 90.54 clearly implies that any optional reference to the use of another CPA’s work in a review report would properly be placed in an other-matter paragraph (AR-C section .A125–127)—at the reporting CPA’s discretion—it is nevertheless illustrated in Exhibit C (AR-C section .A147) as part of the accountant’s responsibility paragraph. Accordingly, it appears that either alternative placement would be acceptable.

It should be noted that, as under previous standards, there is no such thing as reporting a scope limitation in a review engagement. If a CPA is unable to per-
form sufficient inquiry and analytical procedures to achieve the objectives of a review, or to obtain the requisite representation letter from management, then the review is incomplete, and a review report may not be issued (AR-C section .A64). Although not stated in SSARS 21, it is generally held that a review engagement may be downgraded to a compilation, but only if no intent by the client to mislead users is apparent. The standard does set forth specific criteria for downgrading an audit engagement to a review (AR-C sections 90.86–90 and .A135–137).

Communications to management (or those charged with governance). For the first time, SSARS 21 will require that certain (albeit unspecified) communications be made timely to management (or those charged with governance) in review engagements. Such communications should be those that the reporting CPA deems significant and would likely be similar to such communications required in audit engagements. Examples are indications of possible fraud or noncompliance with laws and regulations (AR-C sections 90.13, 90.51, .A20–24 and .A87–89). The standard does not require that these communications be in writing, but CPAs might wish to protect themselves (especially in circumstances of significant nonmanagement ownership of the client business) against the risk of misunderstanding or denial, and any resultant litigation risk, by requiring, as a matter of internal policy, 1) that such communications be written when judged to be so significant that they warrant management action, and 2) that judgments about possible communication matters that are not made in writing be documented.

Restricted-use report language. SSARS 21 sets forth some relatively uncommon conditions that, if encountered, would require the reporting CPA to include designated use restriction language in a review report (AU-C sections 90.61–62 and .A107–110). However, nothing in this (or any other) standard prohibits including such restrictive language in other circumstances in a CPA’s report or disclaimer of assurance in connection with a review, a compilation, or a preparation engagement. Although it would be ordinarily illogical to place a use restriction paragraph anywhere but last, presumably, an exception would be appropriate in the rare circumstance when reporting an independence impairment is required to be last in a compilation report that is also intended only for specified users.

Report references. The previously required practice of referring to the accountant’s report on each page of the accompanying financial statements (usually in a header or footer) has now been made optional for both compilations and reviews (AR-C sections 80.A19 and 90.A63). In addition, the wording of such references is no longer prescribed and may or may not identify the service level (i.e., compilation or review) applied to the financial statements. Nonetheless, many CPAs will likely continue their previous practice in this regard to reduce the risk that if the report were to be separated from the financial statements, users might place greater reliance upon them than was intended.

Implementation Guidance Is Here

The ASRC has recently issued extensive implementation guidance consisting of recommendations on the application of SSARS 21 in specific circumstances, including engagements for entities in specialized industries, in the 2015 edition of the AICPA Audit and Accounting Guide, “Preparation, Compilation, and Review Engagements,” available from http://www.cpa2biz.com. CPAs are ordinarily required to consider this implementation guidance and any other applicable authoritative interpretive publications (and to document such consideration) when conducting engagements under SSARS 21 [AR-C sections 60.06 (definition of “interpretive publications”), .17, and .A33].

Howard B. Levy, CPA, is a principal and director of technical services at Piercy Bowler Taylor & Kern, Las Vegas, Nev. He is a former member of the AICPA’s Auditing Standards Board and its Accounting Standards Executive Committee, and a current member of the Center for Audit Quality’s Smaller Firms Task Force, and The CPA Journal Editorial Board.
A Closer Look at SSARS 21

What CPAs Need to Know

By Kimberly Fransen

Last year, the AICPA’s Accounting and Review Services Committee (ARSC) issued a new standard to clarify and revise the Statements on Standards for Accounting and Review Services (SSARS). The new requirements, SSARS 21, represent quite possibly the biggest change to the standards since their introduction more than 30 years ago. In addition to making the standards easier to read, understand, and apply, SSARS 21 introduces the financial statement preparation service, as well as significant changes to compilation engagements. The new requirements are effective for engagements on financial statements for periods ending on or after December 15, 2015; thus, it’s important for CPAs to understand the changes and how to best put them into practice.

Financial Statement Preparation Service

AR-C section 70, “Preparation of Financial Statements,” introduces a new type of service—financial statement preparation—that specifies a difference between being engaged to prepare financial statements and merely assisting in preparing financial statements. The appendix in AR-C 70 includes a table with the indicators shown in the Exhibit in order to help CPAs make that determination. Once CPAs determine that they have been engaged to prepare financial statements, they will follow the performance requirements in AR-C 70 to address the following:

■ Preparing the financial statements (specific requirements relate to financial statements that omit substantially all disclosures or that are prepared using a special-purpose framework)
■ Preparing sufficient documentation for the engagement to provide a clear understanding of the CPA’s work
■ Including a legend on each page of the financial statements that no assurance is being provided. If the financial statements do not include such a legend, the CPA should either perform a compilation engagement or issue a disclaimer report specifying that no assurance is provided.

The new requirements, SSARS 21, represent quite possibly the biggest change to the standards since their introduction more than 30 years ago.

The new financial statement preparation service is not the same as the existing management-use-only compilation engagement. After implementing SSARS 21, CPAs will be able to prepare financial statements for use by a third party—not just management—without having to issue a compilation report; consequently, there will no longer be a need for the current guidance allowing management-use-only financial statements. CPAs will be required to describe the financial reporting framework used if the financial statements are prepared in accordance with a special-purpose framework (e.g., cash or tax basis) and will have to disclose any material misstatements, such as those caused by a known departure from the applicable financial reporting framework or inadequate disclosures. In a management-use-only compilation engagement, on the other hand, CPAs would simply state in the engagement letter that material departures from the applicable financial reporting framework might exist and that the effects of those departures, if any, may not be disclosed.

Changes to Compilation Engagements

SSARS 21 also introduced several significant changes to the compilation engagement literature included in AR-C section 80, “Compilation Engagements”:

■ Compilations are now engagement driven, rather than submission driven. Previously, CPAs determined whether they were required to compile financial statements by determining whether they had submitted financial statements based on the criteria in the SSARS literature. Under SSARS 21, CPAs only perform compilations when engaged to do so.
■ There is no longer an option to perform a management-use-only compilation without issuing a compilation report.
■ CPAs are required to obtain an engagement letter signed both by themselves and management or those charged with governance, as appropriate; this requirement to sign the engagement letter is new under SSARS 21.
■ The standard compilation report is much shorter—only one paragraph instead of the previous three—and it includes the city and state where the CPA practices.
■ If financial statements are prepared in conformity with a special-purpose framework, the compilation report should include a separate paragraph regarding that framework.

Impact on Peer Review

In January 2015, the AICPA Peer Review Board approved changes to the AICPA Standards for Performing and Reporting on Peer Reviews, which include financial statement preparation engagements in the scope of a firm’s peer review when a firm either elects to enroll in the program or is already enrolled due to other engagements it performs. A firm is not required to enroll in
the AICPA peer review program if it only performs financial statement preparation engagements under AR-C 70.

The exclusion of financial statement preparation services from peer review is controversial, and there are strong opinions on both sides of this issue. Even though the Peer Review Board excludes from the scope of peer review firms that only perform financial statement preparation engagements, it should be noted that several states require any service performed under the SSARS to be subject to peer review. Accordingly, the AICPA Peer Review Program will need to determine how its program will work within those state requirements.

Implementation

When it comes to putting SSARS 21 requirements into practice, CPAs need to understand the differences between assisting with preparing financial statements, actually preparing financial statements, and performing a compilation engagement. After analyzing the differences, they must decide whether to provide preparation services. For most firms, client needs will drive them to continue to provide compilation services; after explaining the various levels of service available, CPAs can help clients determine which will best suit their needs.

For CPAs preparing financial statements or performing a compilation or review engagement, the first step is obtaining an understanding with the client through an engagement letter. The new standard does not specifically state that the engagement letter must be obtained each year, so it would be possible to update the understanding with the client each year by sending an annual reminder letter or orally discussing the engagement with the client and documenting that discussion. In the author’s view, however, it is likely that most CPAs will obtain engagement letters annually.

CPAs also need to ensure that their financial statement preparation and accountant’s report generation systems are set up to address the SSARS 21 requirements. AR-C 70 includes specific instructions about what should be included on each page of financial statements prepared by a CPA. AR-C 80 and AR-C 90 include specific reporting requirements applicable in all compilation and review engagements.

It’s also important to note that peer review findings have consistently reported problems with compilation and review engagements. Those findings include deficiencies related to compilation and review reports not being prepared in accordance with professional standards and engagement letters either not being obtained or not including the required communications. SSARS 21 requires CPAs to revise their compilation and review reports, as well as their engagement letters.

Given that CPAs sometimes still struggle with the existing reports and engagement letters—which have been around since SSARS 19 was issued in 2009—changing reports and engagement letters will require more attention to detail. Because SSARS 21 introduces such substantive changes, the importance of guidance and training for CPAs cannot be overlooked—and with the effective date looming, the time to implement the new requirements is now.


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<th>EXHIBIT</th>
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<td>Preparing financial statements when the accountant will also compile, review, or audit those financial statements</td>
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<td>Being engaged to prepare financial statements for presentation with the entity’s tax return, other than for submission with the tax return to tax authorities</td>
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Technology in Accounting History

Data computing is a far older practice than most people realize, and it has always been linked to accounting. The Mesopotamians claimed the earliest use of an adding machine—the wire-and-bead abacus—2000 years ago. More recently, in 1890, Herman Hollerith and James Powers invented the punch card, a computing technology that may be familiar to older readers. Punch cards read information that is mechanically stamped into paper, easing the need for handwritten accounts and timesheets and increasing access to data. Articles evaluating accountants use of technology appear from the very beginning of the CPA Journal archives. Although decades-old mechanical technologies may pale in comparison to today’s global digital networks, the CPAs of the past likewise grappled with the still-relevant themes of innovation, evolution, and obsolescence. Every advance in technology has been met by professionals reassessing their skills and adapting to a new environment. Here, we take a look at some of the most compelling technology-driven Journal articles from our archives.

Mechanization of Tax Assessments and Collections

“There is probably no other field of governmental effort that lends itself to mechanization any more than that of taxes and assessments and the ultimate collection of taxes,” wrote Chas. J. Maxcy in the October 1935 Journal (p. 3). In the article, Maxcy presents himself as an advocate of early tax assessment technology—which, at that time, included field cards, assessment rolls, tax rolls, and lot ledgers, all prepared using electrical typing machinery. Maxcy wrote that “The multiplicity of transactions, the necessity of speed, the demand for accuracy and the limitation of time are all factors contributing to the necessity of modernizing this branch of government.” Not only does government benefit from the adoption of technology, but it is obligated to embrace the improved precision it can provide. The article predicted that poor technology could lead to societal breakdown: “When metropolitan communities do not adopt a systematic and orderly method of ascertaining what is the actual valuation of the various properties assessed, opportunities for many irregularities are opened. Property may be under- or overassessed and favoritism may creep in. This results in unrest and dissatisfaction on the part of the taxpayers and in many instances has led to tax strikes with the attendant curtailment of those vital government functions such as education and protection.”

Electrical Operation of Card Files

A prime essential in a filing system is that anything filed may be located with a minimum of time and effort. All manually operated systems are subject to human error, and to lessen the possibility of error and thereby increase the efficiency of the system, methods such as cross indexing, duplicate recording, numerical filing, etc. have been resorted to, elaborating the basic simplicity of a filing system. Recently there has been introduced to the Eastern market a mechanical method of selecting cards, from card files, the equipment used for this purpose is sold under the trade name “Electrofile.” It has been available on the West Coast for several years under the trade name “Selectograph.”

The Electrofile may be adapted to almost any card filing system, where speed of selection and reliability are important factors. Any card in the card files may be selected from merely by placing the card on a selector, depressing keys on a keyboard, then moving the operating bar, and the desired card immediately moves out of alignment in the tray, usually identifying itself so that it may be withdrawn. It is unnecessary to refile the card in the position from which it was withdrawn. It may be placed anywhere in the tray without affecting the speed of selection. The equipment is adaptable to mechanical or manual methods of card indexing, and the design of the machine is such that it will be useful in any department that requires handling records containing names and addresses. The equipment is adaptable to mechanical or manual methods of card indexing, and the design of the machine is such that it will be useful in any department that requires handling records containing names and addresses.

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Electrical Operation of Card Files

Manually filing, sorting, and retrieving data were integral skills for CPAs in the 1940s. A desktop machine called a “selector,” sold under the Electrofile brand name, assisted CPAs in carrying out such tasks, and author Raymond L. Collett described how they worked in the October 1940 issue (p. 24). A card was placed on the selector, and, by depressing keys on a keyboard and moving the operating bar, the typist would choose the selected card. The machine could hold up to 1,000 cards, identified with a series of alphameric symbols. Collett’s long description of the operating steps to mastering card filing systems makes one grateful for computer keyboards—even if they pose a risk for carpal tunnel syndrome.
The Application and Use of Machines and Electronics in Accounting.

In October 1955, author Kermit M. Pennington lamented that machine accounting still required the “limitation” of step-by-step human direction (p. 582). Pennington thought it was high time that CPAs directed the “computers… developed for scientific and mathematical calculations” for their own use. He takes readers on a timeline of computing technology, from the ancient Romans’ use of the abacus, to its adoption in China and Korea, and the development of abacus-like tools in Egypt, Greece, Russia, Armenia, and Turkey. (In an interesting historical note, the author notes that, in January 1955, a Japanese student performed calculations 20 seconds faster than a student with an adding machine!) Pennington brings us through the lesser-known technological advancements of 17th-century France, 1880s America, and 1930s America—leading to 1944, when Harvard University and International Business Machines (IBM) developed the first widely known “thinking machine.” Pennington urged accountants not to take technology for granted, but instead to use it with great care to protect valuable client data: after all, he noted, “the effect of electronic equipment on our economic life is of the same magnitude as the effect of the H-bomb on our military strategy” and “its potentialities must be made to work for the good of all mankind.”

Automation—1894

This brief article, penned in February 1956 (p. 103) by the NYSSCPA’s Committee on History, shows how quickly the pace of technology turns what was once considered an innovation into a historical curiosity. The article remembers Colonel Charles Ezra Sprague, a CPA, banker, teacher, author of the first CPA law, and member of the New York State’s first Board of Examiners. The polyglot invented a revolutionary “savings-bank-teller’s machine” to aid him in bookkeeping duties. “In one operation it made the necessary entry in the depositor’s passbook, recorded it for the bank’s records, and accumulated the day’s total,” writes the committee. Sprague refined and patented the machine and sold it to banks. The machine’s name—automalogothotype—was quite a mouthful. The last one was built in 1917, never to be ordered again. Perhaps rebranding would have helped its longevity?

How CPAs Can Adapt to the Computer

More than two decades before IBM unveiled its personal computer, CPAs were already feeling the “squeeze” of “full computer systems, medium-sized computers, and small-scale ‘desk-size’ computers” being “employed as bookkeeping and data recording devices for banks, manufacturers, retailers, service organizations, and professional firms,” according to John E. Lennox’s December 1965 article (p. 893). Commencing a long contemplation about whether in-office technology is a blessing or a threat, Lennox reminds readers that the computer is a tool created “to speed up man’s thinking abilities,” including business facts and data that an “electronic brain can devour, digest, store, and spout when called upon to do so.” CPAs must master the latest technology, the article concludes, or become devoured by the competition—which among the author counted banks and data processing services that could handle bookkeeping functions, financial statement preparation, and trend forecasting. Lennox described as a case study his own company, which purchased an “add-punch” adding machine (for $9,600!). Using the machine gave the firm employees confidence to upgrade to an NCR Model 3100, a “full accounting machine” with an electric typewriter and paper tape recorder, which helped the firm generate income, purchase an early computer, run feasibility studies, and open two new divisions for accounting and management services. The author’s attitude toward new technology is simple: planning, technical training, and practical experience lead to success.

Editors’ Note: Reproductions of the articles discussed above will be included in the online version of this article.
Tax & Accounting Update

Tax & Accounting Update is provided by Thomson Reuters and based on material published on Checkpoint, its online news and research platform. The Update is a quick-reference guide to the most pressing issues coming down the regulatory and administrative pipeline. Visit https://tax.thomsonreuters.com/daily-newsstand/ for further information and daily updates.

Tax News

OECD releases final report on base erosion and profit shifting. On October 5, the Organization for Economic Cooperation and Development (OECD) released its final package of reports from its Base Erosion and Profit Shifting (BEPS) project. The project is a comprehensive set of recommendations for reforming the international tax regime to prevent multinational companies from shifting their profits into low-tax jurisdictions. The first deadline under BEPS is set for December 2017, a date that—according to a Thomson Reuters survey—one-quarter of corporate tax executives are pessimistic they will be able to meet.

SEC News

Financial reporting and audit task force gains permanent status. The SEC has made the Financial Reporting and Audit Task Force a permanent group within the Enforcement Division, and renamed it the Fraud Group. The changes underscore the heightened importance the agency has given to fighting accounting fraud, which contributed to a 40% jump in enforcement actions against financial reporting abuses in the last reported fiscal year. The number of new financial reporting investigations opened increased by about 30%. The group has identified about 250 public companies that are “of interest,” although the Fraud Group’s chief, Margaret McGuire, did not offer details about individual investigations that have not been made public.

FASB News

Clearer guidance expected on revenue recognition for licenses, promises to customers. On October 5, FASB decided to clarify how businesses account for licenses of intellectual property, which has been a persistent source of questions about the board’s revenue recognition standard. In addition to several clarifications about identifying separate promises, or performance obligations, in a contract with a customer, FASB wants to draw a sharper distinction between the accounting for revenue from licenses of intellectual property that represent a promise to deliver a good or service over time versus a promise to be satisfied at a point in time.

Income tax disclosure proposal poised for early 2016 release. FASB is planning a proposal for the first quarter of 2016 that would require businesses to provide expanded information in their financial statement notes about the tax implications of their foreign earnings, as well as more details about domestic taxes. The proposal is expected to include requirements that multinational companies provide a breakdown of income taxes associated with foreign earnings versus domestic income and a further breakdown of significant foreign earnings by jurisdiction. In addition to a breakdown of taxes by country, FASB wants more details about tax expense. A company’s current tax expense line is made up of several items, including taxes recognized, deferred tax liabilities, and taxes on foreign earnings that were earned and remitted in the reporting period.

PCAOB News

Inspection staff sees added risks in mergers. On October 1, the PCAOB said it is concerned that the increase in corporate mergers is adding to the risks that auditors have to contend with. The board believes the heightened pace of mergers increases the likelihood that an audit client could misapply, or the audit firm could misinterpret, the accounting or audit guidance for making fair value measurements of the acquired assets or liabilities assumed, identifying flow reporting mistakes and profit shifting by U.S. companies to lower tax jurisdictions.

The OECD released its final package of reports from its BEPS project.

IASB News

Insurers may get three extra years to adopt financial instruments standard. The IASB agreed to grant relief to insurers applying the board’s separate-but-related financial instruments standard. Insurance companies will have the option of waiting until 2021 to adopt the amendments in the financial instruments standard. If they adopt the guidance at the 2018 effective date, they can cut from the income statement the effects of the mismatch caused by the standards’ different requirements.

GASB News

Survey seeks information on costs of preparing financial statements. A GASB survey of state and local governments is seeking information on the work they do to prepare financial statements. GASB said the survey results will help it review the costs and benefits of its basic financial reporting model. The accounting board said it wants the survey responses by December 15. “This survey is primarily focused on the activities directly associated with preparing, auditing, and making government financial reports available to users,” GASB stated in the survey’s introduction. The accounting board said information “related to reviewing the accuracy of accounts and closing the funds are an integral part of the year-end process for government preparers as well, but are not the primary focus of this survey.”
GASB Responds to Criticisms of Financial Reporting for Governments

The standards issued by GASB during the past 30 years have given users of governmental financial statements unprecedented insight into how U.S. state and local governments use the money entrusted to them.

A recent CPA Journal article—“Deficiencies in Accounting and Financial Reporting of State and Municipal Governments” (James Naughton and Holger Spamann, June 2015, p. 16)—suggests that the time has come to replace those standards with public company accounting rules, an accounting regime not intended for governments or developed with their unique circumstances in mind. In the same issue, Editor-in-Chief Richard H. Kravitz calls for CPAs to insert themselves into this matter in order to ensure trust in our government institutions (“Accounting for State and Municipal Government,” p. 8).

We wholeheartedly agree that CPAs—and, in fact, all state and local government stakeholders—should become more involved in the standards-setting process. We also agree that high-quality financial reporting is essential to fostering trust in our government institutions. We disagree, however, that adopting public company accounting standards will achieve these results.

Governments are fundamentally different from public companies in a number of important ways—not the least of which is that they are designed to provide services to taxpayers rather than to deliver returns to investors. This fact was recognized more than three decades ago by the Financial Accounting Foundation (FAF)—the independent, not-for-profit organization that oversees both FASB and GASB—when, in 1984, it created GASB to set GAAP specifically for U.S. state and local governments.

Like FASB—which the SEC has designated to set public company accounting standards—GASB sets standards through an independent process designed to hear and consider a broad range of views from its state and local government stakeholders throughout the country. While often lengthy, GASB’s process ensures that we have carefully evaluated potential outcomes of a standard prior to its issuance. This is done to ensure that a standard will provide financial statement users with the information they need, while avoiding any unintended consequences that might render it more costly or complex than the value of that information to citizens, investors, and other users.

I’d also like to clear up misconceptions about the role of GASB standards in the examples presented in the articles. In support of a call for a change in the standards-setting structure, Naughton and Spamann cite alleged reporting deficiencies in current governmental standards. We agree that the need to highlight severe fiscal stress should be explored—a topic that GASB is currently researching and which looks beyond the going-concern literature—because governments rarely go out of business. However, based on current state and local government standards, a knowledgeable financial statement user can identify situations where severe fiscal stress exists. For example, the 2006 comprehensive annual financial report for Jefferson County, Alabama, reflects a significant deficit in “sanitary operations.” Moreover, the financial statements in the years leading up to the 2011 bankruptcy clearly reflected significant, growing annual and cumulative deficits.

Kravitz cites the Chicago parking meter sale to argue in favor of adopting public company accounting rules. It is important to point out that the valuation of those assets (noted as a reporting deficiency) would have been the same under private sector accounting standards. Similar clarifications could be presented for each case noted in the Naughton and Spamann article and Kravitz’s editorial.

We wholeheartedly agree that CPAs—and, in fact, all state and local government stakeholders—should become more involved in the standards-setting process. While there’s always room for improvement, we believe that GASB standards yield information that helps citizens, investors, and other financial statement users reach informed decisions and enhance governments’ accountability to their stakeholders. Replacing standards that have been developed with more than 30 years of input from state and local government financial statement users, preparers, and auditors is not an advisable course—it would not bring about the results imagined by the authors.

David A. Vaudt, CPA
GASB Chairman
Norwalk, Conn.

The Authors Respond: Reconciling Budgetary Performance with GASB Statements

We are very grateful for David A. Vaudt’s comments on our article...
and appreciate this opportunity to respond. We agree that GASB provides an enormous amount of information and that GASB standards are a work in progress. We also agree that simply adopting FASB standards without recognizing some of the differences in business practices (e.g., revenue from sale of goods versus tax collections) would be unwise. These points were clear in our article.

The core argument in our article, which was not addressed directly by Vaudt’s letter, is that there are elements of an effective accrual accounting system that are currently absent from public sector reporting. In particular, one of the key differences between FASB and GASB reporting that we talk about at length in our article is FASB’s requirement to produce a cash flow statement using the indirect method. This statement reconciles accrual-based performance (i.e., net income) to cash-based performance (i.e., change in cash), something that is absolutely critical to understanding economic performance.

We believe that a statement which reconciles the differences between cash-based performance on the budget and accrual-based performance on the GASB financial statements is a critical first step in improving public sector financial reporting. We acknowledge that there are many aspects of the budgetary process that will make this very difficult to implement, but we believe it is a worthwhile endeavor because this type of reconciliation would be invaluable.

It would illuminate more clearly many of the accounting gimmicks that we and others have identified in public sector finances. It would also encourage the adoption of standards that are closely aligned with the accrual principles inherent in FASB standards because any differences between the accrual measures and actual cash outlays would be captured in the reconciliation. As we noted in our article, recent GASB publications, such as its Preliminary Views, “Recognition of Elements of Financial Statements and Measurement Approaches,” suggest that GASB is presently moving away from accruals and toward more cash-based measures. This is a dangerous path, and one we hope that GASB does not pursue.

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Northwestern University
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Holger Spamann, PhD
Harvard Law School
Cambridge, Mass.

New York Comptroller’s Office Responds to Criticisms of Transparency

Thank you for your recent article on financial transparency which references the State of New York’s annual financial statements (“The DATA Act: A Look at the Future for Local Government Financial Reporting?” by Rebecca Bloch, Hussein Issa, and Amanda Peterson, June 2015, p. 36). We acknowledge that the complexity of the accounting standards we are required to adhere to influences the way we report state finances. Despite that complexity, New York State consistently ranks at or near the top among all states for timeliness (within 120 days of fiscal year-end) and quality. (The state has been the recipient of the Government Finance Officers Association’s Certificate of Achievement for Excellence in Financial Reporting award for 26 consecutive years.)

To aid our citizens in interpreting and understanding our financial statements, we also prepare supplementary reports to the Comprehensive Annual Financial Report (CAFR), such as the “Financial Condition Report” and the comptroller’s “Citizens’ Guide.” These supplementary reports aim to provide taxpayers with selected financial, economic, and demographic information in an easy-to-understand format. Additionally, we are working toward improving our reporting delivery using electronic formats. The monthly and annual comptroller’s “Cash Basis” reports are now available in Excel format on our website, offering users the ability to download and analyze this data. In the longer term, we intend to implement software solutions that publish the CAFR and other financial reports in a more “data-friendly” format. All of these changes complement the comptroller’s efforts to expand financial transparency through our “Open Book” website, which provides detailed information on state and local government finances (http://www.openbooknewyork.com/).

New York State is proud of the timeliness and quality of its financial reporting, and we will continue to implement data transparency solutions that advance the Comptroller’s goal of better educating our citizenry about how tax dollars are spent.

John C. Traylor
Executive Deputy Comptroller for Operations
Office of the State Comptroller
Albany, N.Y.

The Author Responds

We commend New York State and the Office of the State Comptroller in its great efforts to act as a leader in promoting transparency in financial reporting among states. We hope the DATA Act provides a path to move government financial reporting and data accessibility into a new era.

Rebecca Bloch, PhD, CPA
Fairfield University
Fairfield, Conn.

Another Perspective on Transparency

Editor’s Note: A contrarian view of the fiscal health of New York State is provided here by Bill Bergman, the director of research at Truth in Accounting, a nonprofit group committed to educating citizens about their government’s financial information. Truth in Accounting’s board of directors and advisors include a former U.S. comptroller general, a former member of the Public Oversight Board, a former director of the Chicago Mercantile Exchange, and former Big Four partners.
We applaud the Office of the State Comptroller for making a strong commitment to transparency and would encourage more states to the same. We also appreciate that GASB has finally adopted standards that will raise the bar for transparency and increase the visibility of key metrics for a state's finances.

GASB Statements 67 and 68, once implemented, will markedly transform balance sheets for many state and local governments, including those of New York. But these standards—both dealing with accounting and financial reporting for pension plans—still haven’t been fully implemented, even in jurisdictions like New York, which could have chosen early adoption. After including obligations that we believe should be on the balance sheet—obligations that have accumulated over decades—New York State is one of the most heavily indebted states in the Union.

We have related concerns about budget accounting, which has historically allowed real expenses to run outside “balanced budget” calculations. By our calculation, New York is now facing large unfunded retirement obligations. A negative $131 billion shortfall has been driven by compensation and other costs incurred in prior years but not paid in those years (this figure is derived from New York’s March 31, 2014, audited Comprehensive Annual Financial Report and retirement plans’ actuarial reports). Instead, these costs have been shifted to future taxpayers.

Retiree healthcare benefits account for a surprisingly high share of that total. About three-fourths of New York’s retirement debt is not reported on the balance sheet. Greater transparency is needed from governments and standards setters.

For a fuller discussion, see our information sheet “The Financial State of New York” http://www.truthinaccounting.org/library/doclib/NY-2-Pager.pdf. We are glad that the topic is garnering attention in publications like The CPA Journal and encourage all CPAs to get informed and involved.

Bill Bergman, MBA
Director of Research,
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Adjunct Instructor, Loyola University,
Chicago, Ill.
In 2015, New York State CPAs continued to report satisfaction with tax preparation and commercial tax research packages: the overall weighted-average ratings increased across both categories. Cost remained an important issue, especially for tax research resources. This year’s survey on tax preparation software examined “value for cost” and the ratings reflected an improvement in “average cost” for the third consecutive year. The average cost rating for commercial tax research software packages increased substantially relative to the last few years and reached its highest level since 2012. More survey participants reported taking advantage of free resources for tax research, particularly in their everyday practice activities.

But the challenges of the 2015 tax season appear to have created greater difficulties for tax professionals. The majority of respondents experienced complications from tax law changes under the Patient Protection and Affordable Care Act of 2010, including determining the exemption qualifications and receiving incorrect Forms 1095-A, “Health Insurance Marketplace Statement.” More than one-quarter of survey respondents reported significant problems related to late or incorrect Forms 1099 or Schedules K-1. In addition, many participants faced identity theft issues; more than half had to resolve rejected e-filed returns due to suspected identity theft.
The tax season compression problem of recent years continued in early 2015, with tax preparers facing a brave new world of health insurance reporting, accounting method changes, and e-filing authorization that left many questions unanswered, even into March. Individual taxpayers who purchased health insurance from healthcare exchanges had to wait for original or corrected Forms 1095-A before their returns could be filed. The simplified “repair regulations” (Revenue Procedure 2015-20), permitting small business taxpayers to change their accounting method to expense former capital improvements as repairs without filing for an accounting method change, were not issued until March. Also released in March was updated electronic signature guidance that enabled a completely paperless e-filing process by providing options for taxpayers’ signatures.

According to IRS filing season statistics, the number of tax returns e-filed by tax preparers decreased more than 4% by the end of the first week of February, whereas self-prepared returns increased by 7%. Tax professionals did not catch up with 2014 e-filing statistics until April 17, 2015 (http://www.irs.gov/uac/2015-and-Prior-Year-Filing-Season-Statistics). One 2015 survey respondent extended more tax returns than usual to allow time to analyze the consequences of the repair regulations and make the most beneficial tax decision. Another stated, “I have been doing this for over 30 years, and it is getting harder and harder to get things done by April 15.”

According to the National Taxpayer Advocate’s July 2015 report on the most recent filing season, the IRS had to implement reporting requirements for the Patient Protection and Affordable Care Act of 2010 (ACA) and the Foreign Account Tax Compliance Act of 2010 (FATCA) while coping with a diminished operating budget (down 17% since 2010; http://www.taxpayeradvocate.irs.gov/2016ObjectivesReport). Something had to give, and that was customer service. The IRS answered only 37% of taxpayer calls, with an average hold time of 23 minutes; tax professionals fared slightly better, answering 45% of calls, but with an average hold time of 45 minutes.

**A Brief Comparison**

As in previous years, the most prominent tax software vendors—CCH, Intuit, and Thomson Reuters—appealed to a range of user demographics with multiple tax preparation and tax research products. The 2015 ratings for these vendors’ tax preparation products represent 236 (91%) of the 260 ratings received. Consistent with prior years, 35% of respondents used Intuit tax return preparation packages, 34% used CCH, and 22% used Thomson Reuters. Drake Software, the top-rated product for the past five years, continued to hold its own with a clientele of smaller firms.

CCH and Thomson Reuters products represented 108 (73%) of the 179 commercial tax research software package ratings submitted for the 2015 survey. CCH materials were used by 36% of respondents and Thomson Reuters’ resources were used by 37%, a decrease from 41% and 45%, respectively, in 2014. Parker Tax Publishing, the new kid on the tax research block, gained ground in this year’s survey with almost 11% of the commercial tax research ratings. In addition to commercial products, many respondents rated websites for tax research. The IRS website, state tax websites, and other Internet sources received 68% of the total tax research ratings, up from 47% in 2014.

Cost has always been the lowest-rated feature of both tax preparation and tax research software. To try to gain a more accurate reading on what the cost issues might be, the survey asked respondents to also rate the value of a product compared to its cost (i.e., the “value for cost”). The 2015 ratings for tax preparation software reflected an improvement in the average cost rating for the third consecutive year; the average cost rating for commercial tax research software increased substantially, relative to the past two years, and is at its highest level since 2012. Similar to previous years, several respondents expressed dissatisfaction with the value of the software. Interestingly, one respon-
dent observed that some vendors market products to both tax professionals and individual taxpayers, effectively using the profits from high-priced commercial tax preparation software to develop low-cost software that takes business away from practitioners. With respect to tax research products, more survey participants took advantage of free resources, which might represent a source of some of the dissatisfaction.

Survey Overview

To find out how tax preparers used technology to address tax season challenges, the 2015 tax software survey utilized an online questionnaire format that allowed a broad spectrum of professionals to participate. It included the tax software ratings queries from prior years, with changes in some of the features reviewed and an option to write in a package not listed. New questions included the use of mobile devices by employees, the number of years respondents had used the reviewed software, and reasons for switching tax products. The list of possible tax season issues was expanded, as was the approach to identifying the importance of particular software features.

To solicit survey participants, the NYSSCPA e-mailed the 2015 tax software questionnaire to approximately 9,000 Society members who indicated an interest in tax in their membership information. Consistent with results in prior years, 220 surveys were completed. A profile of respondents in Exhibit 1 indicates that this year’s survey participants remained similar to those in previous years, reflecting national demographics. The mean and maximum number of tax returns prepared increased over 2014, reflecting participation by some larger firms; The median number of individual returns (300) and entity returns (100) remained consistent. The number of full-time tax professionals was slightly higher in 2015; the per-

### EXHIBIT 2
Ratings of Tax Preparation Software

<table>
<thead>
<tr>
<th>Company</th>
<th>Number of Responses</th>
<th>Value for Cost</th>
<th>Ease of Use</th>
<th>Customer Support</th>
<th>Availability of Forms</th>
<th>Accuracy (Low Error Rate)</th>
<th>Overall Rating</th>
<th>Overall 2014</th>
<th>Avg. Years Used</th>
</tr>
</thead>
<tbody>
<tr>
<td>Abacus Tax Software</td>
<td>1</td>
<td>4.00</td>
<td>2.00</td>
<td>4.00</td>
<td>1.00</td>
<td>3.00</td>
<td>3.00</td>
<td>—</td>
<td>2</td>
</tr>
<tr>
<td>Agile Tax Software</td>
<td>1</td>
<td>5.00</td>
<td>5.00</td>
<td>3.00</td>
<td>5.00</td>
<td>5.00</td>
<td>4.00</td>
<td>1.00</td>
<td>&gt; 10</td>
</tr>
<tr>
<td>ATX</td>
<td>20</td>
<td>4.35</td>
<td>3.95</td>
<td>3.50</td>
<td>4.30</td>
<td>4.05</td>
<td>3.85</td>
<td>3.93</td>
<td>8</td>
</tr>
<tr>
<td>CCH Axcess Tax</td>
<td>8</td>
<td>2.71</td>
<td>2.88</td>
<td>3.25</td>
<td>3.88</td>
<td>3.75</td>
<td>3.50</td>
<td>3.20</td>
<td>2</td>
</tr>
<tr>
<td>CCH ProSystem fx</td>
<td>60</td>
<td>3.43</td>
<td>3.75</td>
<td>3.83</td>
<td>4.35</td>
<td>4.53</td>
<td>3.92</td>
<td>3.98</td>
<td>9</td>
</tr>
<tr>
<td>Drake Software</td>
<td>20</td>
<td>4.70</td>
<td>4.20</td>
<td>4.70</td>
<td>4.30</td>
<td>4.40</td>
<td>4.45</td>
<td>4.70</td>
<td>4</td>
</tr>
<tr>
<td>GoSystem Tax RS</td>
<td>13</td>
<td>3.38</td>
<td>3.31</td>
<td>3.77</td>
<td>4.38</td>
<td>4.08</td>
<td>3.85</td>
<td>3.50</td>
<td>8</td>
</tr>
<tr>
<td>Intuit ProSeries</td>
<td>34</td>
<td>3.62</td>
<td>4.06</td>
<td>3.29</td>
<td>3.62</td>
<td>3.94</td>
<td>3.76</td>
<td>4.03</td>
<td>9</td>
</tr>
<tr>
<td>Intuit Tax Online</td>
<td>6</td>
<td>4.00</td>
<td>4.17</td>
<td>3.33</td>
<td>4.33</td>
<td>4.67</td>
<td>4.17</td>
<td>3.29</td>
<td>7</td>
</tr>
<tr>
<td>Lacerte Tax</td>
<td>51</td>
<td>3.02</td>
<td>4.38</td>
<td>3.84</td>
<td>4.00</td>
<td>4.27</td>
<td>3.84</td>
<td>3.82</td>
<td>9</td>
</tr>
<tr>
<td>TaxACT</td>
<td>3</td>
<td>5.00</td>
<td>3.67</td>
<td>3.33</td>
<td>3.67</td>
<td>3.67</td>
<td>4.00</td>
<td>4.50</td>
<td>8</td>
</tr>
<tr>
<td>TaxWise</td>
<td>1</td>
<td>3.00</td>
<td>5.00</td>
<td>3.00</td>
<td>5.00</td>
<td>5.00</td>
<td>3.00</td>
<td>3.14</td>
<td>9</td>
</tr>
<tr>
<td>Overall 2015</td>
<td>260</td>
<td>3.57</td>
<td>3.94</td>
<td>3.83</td>
<td>4.16</td>
<td>4.31</td>
<td>3.95</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall 2014</td>
<td>293</td>
<td>3.21</td>
<td>3.95</td>
<td>3.92</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3.93</td>
<td></td>
</tr>
<tr>
<td>Overall 2013</td>
<td>241</td>
<td>3.18</td>
<td>3.97</td>
<td>3.84</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3.79</td>
<td></td>
</tr>
<tr>
<td>Overall 2013 w/o ATX</td>
<td>212</td>
<td>3.07</td>
<td>4.05</td>
<td>4.03</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3.91</td>
<td></td>
</tr>
</tbody>
</table>

Scale: 1 = Very Dissatisfied to 5 = Very Satisfied; Familiarity: 1 = Low to 5 = High
percentage of professional practice in tax was slightly lower, but continued to reflect the presence of small to midsize firms, as well as both very small and very large firms. Respondents were generally very experienced tax preparers, with almost 80% reporting more than 20 years of experience.

**Tax Preparation Software**

The survey listed 17 of the most commonly used commercial tax return software vendors, based on a review of print and electronic media. Of the 220 respondents, approximately 94% indicated that they used at least one tax preparation software package, and almost 20% evaluated more than one product. Respondents reported using 13 of the 17 listed tax return software packages (summarized in Exhibit 2), and 260 ratings were analyzed in total. No write-in ratings were submitted.

Participants rated each tax preparation software package on six factors—value for cost, ease of use, customer support, availability of forms, and accuracy (low error rate)—based on a scale of 1 (very dissatisfied) to 5 (very satisfied). In addition, respondents provided an overall rating for the package using the same scale. Compared to recent years, the overall ratings improved somewhat, though the average overall rating of 3.95 in 2015 was almost identical to the average overall rating of 3.93 in 2014.

Approximately 43% of the ratings received were for CCH ProSystem fx (60 ratings) and Lacerte Tax (51 ratings), two of the higher-priced providers. Of the seven packages with more than 10 ratings, the overall ratings were between 3.76 and 4.45, with Drake Software (20 ratings; 4.45 average) rated highest overall for the fifth consecutive year. As in the previous two years, UltraTax CS (42 ratings; 4.19 average) came in second place. CCH ProSystem fx (60 ratings; 3.92 average) retained its hold on third place. GoSystem Tax RS (13 ratings; 3.85 average), ATX (20 ratings; 3.85 average), and Lacerte Tax (51 ratings; 3.84 average) tied for fourth place. Intuit ProSeries (34 ratings; 3.76 average) experienced a substantial drop from its 2014 tie for third place, falling to last place in the 2015 survey.

### EXHIBIT 3

**Tax Preparation Software Usage**

<table>
<thead>
<tr>
<th></th>
<th>Percentage of Responses</th>
<th>ATX</th>
<th>CCH ProSystem fx</th>
<th>Drake Software</th>
<th>GoSystem Tax RS</th>
<th>Intuit ProSeries</th>
<th>Lacerte Tax</th>
<th>UltraTax CS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Individual tax returns prepared:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 500</td>
<td>59%</td>
<td>80%</td>
<td>43%</td>
<td>75%</td>
<td>39%</td>
<td>76%</td>
<td>57%</td>
<td>52%</td>
</tr>
<tr>
<td>500–999</td>
<td>18%</td>
<td>0%</td>
<td>12%</td>
<td>20%</td>
<td>15%</td>
<td>12%</td>
<td>23%</td>
<td>21%</td>
</tr>
<tr>
<td>1,000–1499</td>
<td>4%</td>
<td>10%</td>
<td>4%</td>
<td>0%</td>
<td>0%</td>
<td>3%</td>
<td>2%</td>
<td>10%</td>
</tr>
<tr>
<td>1,500 or more</td>
<td>19%</td>
<td>10%</td>
<td>41%</td>
<td>5%</td>
<td>46%</td>
<td>9%</td>
<td>18%</td>
<td>17%</td>
</tr>
<tr>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td><strong>Full-time tax preparers:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 5</td>
<td>60%</td>
<td>75%</td>
<td>34%</td>
<td>95%</td>
<td>23%</td>
<td>70%</td>
<td>63%</td>
<td>62%</td>
</tr>
<tr>
<td>5–9</td>
<td>12%</td>
<td>5%</td>
<td>19%</td>
<td>0%</td>
<td>0%</td>
<td>15%</td>
<td>8%</td>
<td>17%</td>
</tr>
<tr>
<td>10–19</td>
<td>6%</td>
<td>0%</td>
<td>9%</td>
<td>0%</td>
<td>0%</td>
<td>6%</td>
<td>6%</td>
<td>5%</td>
</tr>
<tr>
<td>20 or more</td>
<td>22%</td>
<td>20%</td>
<td>38%</td>
<td>5%</td>
<td>77%</td>
<td>9%</td>
<td>23%</td>
<td>16%</td>
</tr>
<tr>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td><strong>Firm’s practice is in tax:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 25%</td>
<td>17%</td>
<td>10%</td>
<td>16%</td>
<td>15%</td>
<td>0%</td>
<td>26%</td>
<td>16%</td>
<td>9%</td>
</tr>
<tr>
<td>25–49%</td>
<td>15%</td>
<td>15%</td>
<td>24%</td>
<td>15%</td>
<td>15%</td>
<td>6%</td>
<td>20%</td>
<td>10%</td>
</tr>
<tr>
<td>50–74%</td>
<td>23%</td>
<td>15%</td>
<td>22%</td>
<td>20%</td>
<td>15%</td>
<td>24%</td>
<td>29%</td>
<td>31%</td>
</tr>
<tr>
<td>75% or more</td>
<td>45%</td>
<td>60%</td>
<td>38%</td>
<td>50%</td>
<td>70%</td>
<td>44%</td>
<td>35%</td>
<td>50%</td>
</tr>
<tr>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td></td>
</tr>
</tbody>
</table>
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The weighted-average rating for each feature in 2015 was compared to the rating for that same feature in 2014. Unlike previous surveys, the 2015 questionnaire solicited a rating for value for cost, rather than just cost. While this aimed to gather perceptions about the same feature, the change in terminology might have influenced ratings, which increased somewhat compared to previous years. Although (value for) cost continues to be the least satisfactory feature overall for many of the tax preparation packages, the overall average value for cost rating in 2015 improved for the third consecutive year (relative to the previous ratings for cost); it did not fall substantially below ratings for several other features. Interestingly, for four of the seven packages with more than 10 ratings, value for cost was not the lowest-rated feature; furthermore, it was the highest-rated feature for both ATX and Drake Software. Ratings for ease of use have been consistent over the past several years and were essentially flat relative to 2014. The average rating for customer support, which has fluctuated in recent years, declined somewhat. Two new features rated in 2015, accuracy (low error rate) and availability of forms, immediately became the highest- and second-highest rated features, respectively.

The following discussion focuses on the seven tax preparation software packages that received more than 10 ratings. The ratings for the other six packages are presented for completeness, but should be interpreted with caution because they represent the opinions of relatively few respondents.

The average overall rating for tax preparation software packages—at its highest since 2011—reflected continuing overall satisfaction on the part of respondents. The overall rating for four of the seven packages receiving more than 10 ratings...

### EXHIBIT 4
Ratings of Tax Research Software

<table>
<thead>
<tr>
<th>Company</th>
<th>Number of Responses</th>
<th>Value for Cost</th>
<th>Ease of Use</th>
<th>Customer Support</th>
<th>Timely Update</th>
<th>Company Reliability</th>
<th>Overall Rating</th>
<th>Avg. Years Used</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bloomberg BNA</td>
<td>14</td>
<td>3.43</td>
<td>3.14</td>
<td>3.25</td>
<td>3.57</td>
<td>4.43</td>
<td>3.50</td>
<td>3.63</td>
</tr>
<tr>
<td>CCH</td>
<td>53</td>
<td>3.15</td>
<td>3.25</td>
<td>3.34</td>
<td>4.19</td>
<td>4.08</td>
<td>3.46</td>
<td>3.57</td>
</tr>
<tr>
<td>Checkpoint</td>
<td>54</td>
<td>3.61</td>
<td>3.67</td>
<td>3.35</td>
<td>4.13</td>
<td>4.15</td>
<td>3.79</td>
<td>3.80</td>
</tr>
<tr>
<td>Intuit ProLine</td>
<td>5</td>
<td>4.00</td>
<td>3.60</td>
<td>4.40</td>
<td>4.20</td>
<td>4.60</td>
<td>3.83</td>
<td>3.00</td>
</tr>
<tr>
<td>Kleinrock</td>
<td>5</td>
<td>3.40</td>
<td>3.20</td>
<td>2.80</td>
<td>3.00</td>
<td>3.00</td>
<td>3.20</td>
<td>3.67</td>
</tr>
<tr>
<td>Parker Tax Pro</td>
<td>16</td>
<td>4.63</td>
<td>3.81</td>
<td>3.54</td>
<td>4.33</td>
<td>3.87</td>
<td>3.94</td>
<td>3.75</td>
</tr>
<tr>
<td>Tax Analysts</td>
<td>1</td>
<td>4.00</td>
<td>3.00</td>
<td>3.00</td>
<td>5.00</td>
<td>4.00</td>
<td>3.00</td>
<td>1.00</td>
</tr>
<tr>
<td>Westlaw</td>
<td>1</td>
<td>4.00</td>
<td>4.00</td>
<td>3.00</td>
<td>5.00</td>
<td>4.00</td>
<td>5.00</td>
<td>1.50</td>
</tr>
<tr>
<td>Overall 2015</td>
<td>149</td>
<td>3.55</td>
<td>3.47</td>
<td>3.37</td>
<td>4.10</td>
<td>4.10</td>
<td>3.65</td>
<td></td>
</tr>
<tr>
<td>Overall 2014</td>
<td>179</td>
<td>3.02</td>
<td>3.24</td>
<td>3.24</td>
<td>3.87</td>
<td>4.07</td>
<td>3.59</td>
<td></td>
</tr>
<tr>
<td>Overall 2013</td>
<td>186</td>
<td>3.11</td>
<td>3.37</td>
<td>3.48</td>
<td>3.87</td>
<td>4.08</td>
<td>3.58</td>
<td></td>
</tr>
<tr>
<td>IRS Website</td>
<td>143</td>
<td>4.13</td>
<td>3.35</td>
<td>1.69</td>
<td>3.17</td>
<td>3.20</td>
<td>3.06</td>
<td>3.47</td>
</tr>
<tr>
<td>State Tax Dept. Website</td>
<td>123</td>
<td>4.14</td>
<td>3.13</td>
<td>2.03</td>
<td>3.22</td>
<td>3.13</td>
<td>3.11</td>
<td>3.39</td>
</tr>
<tr>
<td>Other Internet Search</td>
<td>47</td>
<td>4.49</td>
<td>3.77</td>
<td>2.15</td>
<td>3.21</td>
<td>3.14</td>
<td>3.54</td>
<td>3.79</td>
</tr>
<tr>
<td>Overall 2015 Plus Free</td>
<td>462</td>
<td>3.98</td>
<td>3.37</td>
<td>2.37</td>
<td>3.49</td>
<td>3.46</td>
<td>3.31</td>
<td></td>
</tr>
<tr>
<td>Overall 2014 Plus Free</td>
<td>337</td>
<td>3.83</td>
<td>3.35</td>
<td>2.65</td>
<td>3.58</td>
<td>3.83</td>
<td>3.55</td>
<td></td>
</tr>
<tr>
<td>Overall 2013 Plus Free</td>
<td>331</td>
<td>3.75</td>
<td>3.42</td>
<td>2.84</td>
<td>3.67</td>
<td>3.91</td>
<td>3.53</td>
<td></td>
</tr>
</tbody>
</table>

Scale: 1 = Very Dissatisfied to 5 = Very Satisfied; Familiarity: 1 = Low to 5 = High
ratings increased; ATX, GoSystem Tax RS, and Lacerte Tax also showed increases in the ratings of all individual features common to both 2014 and 2015. The overall rating of the other three packages decreased; Drake Software’s ratings for individual features all declined slightly, whereas CCH ProSystem fx and Intuit ProSeries had a mix of increases and decreases.

The average ratings of all of the features for the tax preparation software packages were higher than 3 (out of 5). Top-rated Drake Software was the highest rated product on value for cost and customer support; the second highest-rated product overall, UltraTax CS, ranked first on both availability of forms and accuracy (low error rate). Lacerte Tax was the highest rated package on ease of use.

Similar to 2013 and 2014, Drake Software, ATX, and Intuit ProSeries were ranked first, second, and third on cost. ATX, GoSystem RS, and Lacerte Tax all improved on ease of use, while the other packages declined. In addition, ATX and GoSystem RS were the only packages that reflected improved ratings for customer support.

The ratings for availability of forms were generally quite high, with an average of 4.16 across all packages. Among the seven packages rated by more than 10 respondents, UltraTax CS had the highest score for availability of forms (4.40), followed by GoSystem Tax RS, CCH ProSystem fx, and ATX tied with Drake Software, all of which earned ratings of 4.30 or higher. Lacerte Tax was in a distant fifth place at 4.00; its sister product, Intuit ProSeries, was notable for a relatively low rating of 3.62 for availability of forms.

The other new feature rated in 2015 was accuracy (low error rate). This was the highest-rated individual feature, with an average of 4.31. UltraTax CS received the highest rating on this feature (4.57), with CCH ProSystem fx (4.53) close behind. Drake Software also earned an above-average rating on this feature, followed by Lacerte Tax, GoSystem Tax RS and ATX, all of which received ratings over 4.00. With a rating of 3.94, Intuit ProSeries was the lowest rated package on accuracy.

**EXHIBIT 5**
**Tax Research Software Usage**

<table>
<thead>
<tr>
<th></th>
<th>Percentage of All Responses</th>
<th>Bloomberg BNA</th>
<th>CCH</th>
<th>Checkpoint</th>
<th>Parker Tax Pro</th>
<th>IRS Website</th>
<th>State Tax Dept. Website</th>
<th>Other Internet Search</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual tax returns</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>prepared:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 500</td>
<td>59%</td>
<td>50%</td>
<td>49%</td>
<td>41%</td>
<td>88%</td>
<td>61%</td>
<td>63%</td>
<td>66%</td>
</tr>
<tr>
<td>500–999</td>
<td>18%</td>
<td>0%</td>
<td>21%</td>
<td>15%</td>
<td>6%</td>
<td>15%</td>
<td>15%</td>
<td>17%</td>
</tr>
<tr>
<td>1,000–1,499</td>
<td>4%</td>
<td>7%</td>
<td>6%</td>
<td>4%</td>
<td>0%</td>
<td>4%</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>1,500 or more</td>
<td>19%</td>
<td>43%</td>
<td>24%</td>
<td>40%</td>
<td>6%</td>
<td>20%</td>
<td>19%</td>
<td>15%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>Full-time tax preparers:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 5</td>
<td>60%</td>
<td>14%</td>
<td>49%</td>
<td>28%</td>
<td>94%</td>
<td>59%</td>
<td>61%</td>
<td>68%</td>
</tr>
<tr>
<td>5–9</td>
<td>12%</td>
<td>22%</td>
<td>17%</td>
<td>24%</td>
<td>0%</td>
<td>12%</td>
<td>10%</td>
<td>7%</td>
</tr>
<tr>
<td>10–19</td>
<td>6%</td>
<td>21%</td>
<td>2%</td>
<td>9%</td>
<td>6%</td>
<td>7%</td>
<td>8%</td>
<td>6%</td>
</tr>
<tr>
<td>20 or more</td>
<td>22%</td>
<td>43%</td>
<td>32%</td>
<td>39%</td>
<td>0%</td>
<td>22%</td>
<td>21%</td>
<td>19%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>Firm’s practice is in tax:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 25%</td>
<td>17%</td>
<td>14%</td>
<td>15%</td>
<td>4%</td>
<td>0%</td>
<td>15%</td>
<td>15%</td>
<td>17%</td>
</tr>
<tr>
<td>25–49%</td>
<td>15%</td>
<td>36%</td>
<td>13%</td>
<td>17%</td>
<td>19%</td>
<td>16%</td>
<td>15%</td>
<td>13%</td>
</tr>
<tr>
<td>50–74%</td>
<td>23%</td>
<td>29%</td>
<td>28%</td>
<td>29%</td>
<td>25%</td>
<td>24%</td>
<td>25%</td>
<td>10%</td>
</tr>
<tr>
<td>75% or more</td>
<td>45%</td>
<td>21%</td>
<td>44%</td>
<td>50%</td>
<td>56%</td>
<td>45%</td>
<td>45%</td>
<td>60%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
</tbody>
</table>
In summary, ATX and GoSystem Tax RS showed substantial increases in their overall ratings, while Lacerte Tax and UltraTax CS showed modest increases. Although it continued to be the top-rated tax preparation package, Drake Software’s overall rating declined notably. Similarly, Intuit ProSeries showed a sizable decrease in its overall rating, and CCH ProSystem fx, showed a more modest decrease. For all but Drake Software, most respondents had used the software package rated for several years.

Exhibit 3 provides descriptive information about the tax preparation software users for the packages rated by 10 or more participants. Although there did not appear to be major shifts in the size of the firms utilizing these packages, both ATX and Lacerte Tax were used by more midsize firms and fewer small firms than in the past. Overall, respondents rating CCH ProSystem fx, Lacerte Tax (and, to some extent, UltraTax CS) represented a cross-section of firm size categories, including larger practices and more midsize firms. UltraTax CS participants also included slightly more small firms than in prior years. ATX, Drake Software, and Intuit ProSeries were used primarily by firms preparing fewer returns, with fewer full-time tax preparers, and with 50% or more of their practice in tax.

**Tax Research Software**

Respondents also rated the nine most commonly used tax research software packages (based on a review of print and electronic media), as well as free resources, such as the IRS website, if they had used the products currently or recently. Survey participants were more likely to use multiple tax research products than to use multiple tax preparation packages or websites, and many respondents rated several options. Almost 57% of the respondents indicated that they used at least one commercial tax research software package or resource, and 12% used more than one. Approximately 68% of participants used the IRS website, state tax websites, or other free online tax resources. Exhibit 4 summarizes the ratings for these products.

The survey issued 149 ratings for eight tax research software packages, and an additional 313 ratings were received on the IRS website, state tax department websites, and other Internet searches. No write-in ratings were submitted. Of the four products with at least 10 ratings, Checkpoint had the most users (54), followed closely by CCH (53), with Parker Tax Pro (16) and Bloomberg BNA (14) farther behind. Fewer than 10 respondents rated Intuit ProLine, Kleinrock, Tax Analysts, and Westlaw; thus, although their ratings are presented for completeness, they should be interpreted with caution. Lexis-Nexis did not receive any complete ratings, so it is omitted from the survey results. Of the free tax research resources, the IRS website had the most users (143), followed by state tax department websites (123) and other Internet searches (47). While individual provider ratings reflected a mix of increases and decreases from 2014, the overall tax research software ratings reflect increases from the prior year. The overall ratings for the most used tax research products are generally closer than those for the tax preparation packages, ranging from 3.46 to 3.94 (out of 5) for 2015.

Participants ranked the software packages on a scale of 1 (very dissatisfied) to 5 (very satisfied). The weighted-average overall rating for the commercial products was 3.65 (out of 5), a slight increase from the overall ratings of 3.59 in 2014 and 3.58 in 2013. The overall rating of all products (commercial plus free internet resources) was 3.31 in 2015, as compared to 3.55 in 2014. While the commercial tax research ratings have been remarkably consistent over the past few years, survey participants were less satisfied with the IRS and state tax websites in particular, with their ratings declining in almost every area.

For the four commercial packages with more than 10 responses, the overall ratings for Bloomberg BNA and CCH declined from 2014. Checkpoint remained close to its 2014 rating, and Parker Tax Pro (16 ratings; 3.94 average) gained enough responses to be included in this discussion and increased its overall rating performance to take over first place. Checkpoint (54 ratings; 3.79 average) dropped to second place behind Parker Tax Pro, even though its overall rating was consistent with 2014. Bloomberg BNA (14 ratings; 3.50 average) and CCH (53 ratings; 3.46 average) came in at third and fourth place, respectively, with substantial ratings

---

**EXHIBIT 6**

Providers with Highest Ratings

<table>
<thead>
<tr>
<th></th>
<th>Tax Preparation Software</th>
<th>Tax Research Software</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cost</strong></td>
<td>Drake Software</td>
<td>Parker Tax Pro</td>
</tr>
<tr>
<td><strong>Ease of Use</strong></td>
<td>Lacerte Tax</td>
<td>Parker Tax Pro</td>
</tr>
<tr>
<td><strong>Customer Support</strong></td>
<td>Drake Software</td>
<td>Parker Tax Pro</td>
</tr>
<tr>
<td><strong>Availability of Forms</strong></td>
<td>UltraTax CS</td>
<td>—</td>
</tr>
<tr>
<td><strong>Accuracy (Low Error Rate)</strong></td>
<td>UltraTax CS</td>
<td>—</td>
</tr>
<tr>
<td><strong>Timely Updates</strong></td>
<td>—</td>
<td>Parker Tax Pro</td>
</tr>
<tr>
<td><strong>Company Reliability</strong></td>
<td>—</td>
<td>Bloomberg BNA</td>
</tr>
<tr>
<td><strong>Overall Rating</strong></td>
<td>Drake Software</td>
<td>Parker Tax Pro</td>
</tr>
</tbody>
</table>
declines from 2014. The average overall ratings for the commercial products have been consistent from one year to the next, although individual tax research packages have fluctuated quite a bit. There appears to be a narrowing of the concentrated use of the commercial packages at the same time that free resources are seeing increased access. The competitive field is much broader than in prior years, and respondents are expanding their research activities beyond the traditional providers.

The average ratings of individual features generally increased in 2015, compared to 2014, for the commercial providers. The value for cost ratings for the commercial packages increased overall, compared to the cost rating in 2014 (3.55 in 2015, 3.02 in 2014). The value for cost rating for all four tax research packages was higher than the cost rating in 2014, with Parker Tax Pro in first, followed by Checkpoint, Bloomberg BNA, and CCH. The ease of use rating (3.47) also increased relative to 2014 (3.24) and was the highest seen in recent years; although this decreased for Parker Tax Pro, this package received the highest rating for ease of use, followed by Checkpoint, CCH and Bloomberg BNA. Both Checkpoint and CCH had increases in the ease of use rating, while Bloomberg BNA experienced a decline.

Customer support ratings also increased overall for the commercial packages (3.37 in 2015, compared to 3.24 in 2014) and for Parker Tax Pro, which earned the top spot for this feature. The customer support ratings for Checkpoint decreased, but it tied with CCH for the second highest on this feature. Although Bloomberg BNA also maintained its customer support rating compared to 2014, it was ranked fourth of the packages with 10 or more ratings.

The average rating for timely updates for the commercial packages was 3.55, an increase from 3.87 in 2014 and the highest reported in recent years. Parker Tax Pro experienced an increase in this rating, and it was the top ranked commercial package for timely updates, followed by CCH, which increased in 2015. Checkpoint’s rating for timely updates was comparable to the previous year, and it ranked third of the packages with more than 10 ratings. Finally, Bloomberg BNA’s rating for timely updates decreased, ranking the lowest of these packages.

The ratings for company reliability have been fairly consistent, 4.10 on average in 2015, compared to 4.07 in 2014 and 4.08 in 2013. This rating increased for Bloomberg BNA, ranked first; stayed about the same for Checkpoint, ranked second; and decreased for CCH, ranked third. Despite an increase in its company reliability ranking, Parker Tax Pro ranked fourth on this feature. With the exception of Parker Tax Pro, all of the commercial tax research products rated by more than 10 respondents had been used for several years; Parker Tax Pro is clearly the newcomer, with most respondents who rated it having used the software for just one or two years.

The number of ratings received for free tax websites substantially increased, suggesting that they are becoming a more popular resource for tax professionals. Interestingly, the overall ratings for free tax research resources decreased from 2014; unsurprisingly, they were lower than the overall ratings of the top-rated commercial products. Although this is pure speculation, it is possible the ratings loss partially resulted from customer service issues and not just failure to manage the web presence.

The IRS website once again received the most ratings of all commercial and free research tools. Overall, ratings of individual features for these free products generally decreased compared to those reported in 2014, with cost (value for cost) as the most highly rated feature—likely reflecting the free access. The overall rating for the IRS website rating decreased from 3.47 in 2014 to 3.06 in 2015, while the rating for state tax department websites decreased from 3.39 in 2014 to 3.11 in 2015. The overall rating for other Internet resources showed a decrease from 3.79 in 2014 to 3.54 in 2015.

### EXHIBIT 7
**Important Software Features**

<table>
<thead>
<tr>
<th></th>
<th>Tax Preparation Software</th>
<th>Tax Research Software</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Average Rating</strong></td>
<td><strong>Rank</strong></td>
<td><strong>Average Rating</strong></td>
</tr>
<tr>
<td>Ease of Use</td>
<td>3.70</td>
<td>1</td>
</tr>
<tr>
<td>Cost</td>
<td>4.33</td>
<td>2</td>
</tr>
<tr>
<td>Accuracy</td>
<td>4.52</td>
<td>3</td>
</tr>
<tr>
<td>Timely Updates</td>
<td></td>
<td>3.55</td>
</tr>
<tr>
<td>Customer Support</td>
<td>4.62</td>
<td>4</td>
</tr>
<tr>
<td>Your Familiarity</td>
<td>4.68</td>
<td>5</td>
</tr>
<tr>
<td>Availability of Forms</td>
<td>4.80</td>
<td>6</td>
</tr>
<tr>
<td>Availability of States</td>
<td>5.25</td>
<td>7</td>
</tr>
<tr>
<td>Company Reliability</td>
<td>5.72</td>
<td>8</td>
</tr>
<tr>
<td>Data Security</td>
<td>5.85</td>
<td>9</td>
</tr>
</tbody>
</table>

**Note:**

- Tax Preparation: Rating scale is 1 (most important) to 9 (least important)
- Tax Research: Rating scale is 1 (most important) to 7 (least important)
While the value for cost rating for all three of the free tax websites declined compared to 2014, they were still all rated at 4.0 or higher, with the IRS and state tax department websites receiving nearly identical ratings of 4.13 and 4.14, respectively, as compared to 4.84 and 4.69 in 2014. Other websites received an average value for cost rating of 4.49, as compared to 4.59 in 2014—but because this rating combines figures for multiple free tax research websites, it is not possible to identify a single “best value.” Similarly, customer support ratings decreased for both the IRS and state tax department websites, while remaining about the same for other websites. The ratings for timely updates decreased for the IRS website, remained the same for state tax department websites, and increased for other Internet websites. Finally, company reliability ratings for the IRS and state tax department websites decreased, while they increased for other Internet websites.

Free research websites appear to be used by firms of all sizes, reflecting the survey respondents’ broad demographics. Exhibit 5 provides descriptive detail on tax research software users. Bloomberg BNA, CCH, and Checkpoint have representation across all firm sizes, but Parker Tax Pro was used almost exclusively by small firms. Only Bloomberg BNA had fewer ratings from small firms than from medium and larger firms, though CCH and Checkpoint both were used by a substantial number of large firms. The IRS website, state tax department websites, and other Internet resources were used across all firm sizes, but used disproportionately more by smaller firms. This is similar to what has been reported in previous years.

**The Cost of Tax Software**

In light of open-ended comments from survey respondents and the very consistent low ratings of cost (value for cost), the current pricing for tax software products listed in the survey was examined. Not all of the products publicize their prices, and the pricing structure for tax preparation software varies across products, with some offering a flat fee for unlimited returns and others using per return pricing. Similarly, some software package prices include both individual and entity returns, whereas others are priced separately. Of the tax preparation packages rated by 10 or more respondents, ATX, CCH ProSystem fx, Drake Software, and Intuit ProSeries offer one price for unlimited returns, with Drake offering the lowest price and CCH ProSystem fx at the high end. Looking at the value for cost ratings for these four packages, Drake is rated the highest and CCH ProSystem fx the lowest. Thus, although the packages may offer different features, satisfaction with “value for cost” parallels the pricing of the product.

Only two of the tax research software products make price information readily available. Parker Tax Pro offers a price that is significantly lower than CCH; their respective ratings for value for cost are consistent with this pricing.

An unofficial listing of prices, as of June 2015, for products covered in this survey will be available from http://www.cpaj.com.

**Other Technology Issues**

In 2015, there were major changes in the top-rated packages by feature. Exhibit 6 shows the providers with the highest ratings for each feature. For the tax preparation software, Drake Software retained the highest ratings for cost and customer support, as well as the highest overall rating, but lost ease of use to Lacerte Tax. UltraTax CS, frequently second best, gained the top spot on the two new feature ratings, availability of forms and accuracy (low error rate).

Among tax research software, Parker Tax Pro took over the highest ratings for cost, ease of use, customer support, and timely updates, as well as the highest overall rating; Bloomberg BNA achieved top ranking for company reliability. Checkpoint generally came in at second or third place on most of the individual feature ratings, resulting in its second place overall ranking.

On the 2015 survey, respondents were asked to rank the importance of individual features in order, rather than identify their most important items. This resulted in some interesting changes from

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**EXHIBIT 8**

Use of Other Technologies

<table>
<thead>
<tr>
<th>Feature</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Implemented a paperless environment</td>
<td>50%</td>
<td>51%</td>
</tr>
<tr>
<td>Utilized scanning software for tax data</td>
<td>21%</td>
<td>22%</td>
</tr>
<tr>
<td>Used online version of software</td>
<td>26%</td>
<td>29%</td>
</tr>
<tr>
<td>Used portals for clients to upload tax data documents</td>
<td>30%</td>
<td>35%</td>
</tr>
<tr>
<td>Used pay-per-return pricing</td>
<td>34%</td>
<td>32%</td>
</tr>
<tr>
<td>Sent tax returns to some/any clients electronically</td>
<td>88%</td>
<td>85%</td>
</tr>
<tr>
<td>Purchased tax research software in connection with tax preparation software</td>
<td>24%</td>
<td>26%</td>
</tr>
<tr>
<td>Provided telecommuting option for staff</td>
<td>22%</td>
<td>28%</td>
</tr>
<tr>
<td>Used mobile tax applications</td>
<td>—</td>
<td>10%</td>
</tr>
<tr>
<td>Allowed employees to use mobile devices for work</td>
<td>—</td>
<td>70%</td>
</tr>
</tbody>
</table>
the 2014 selections. For tax preparation software, consistent with 2014, ease of use was considered, by far, the most important feature (see Exhibit 7). In an interesting turn of events, the tax preparation package rated highest for ease of use, Lacerte Tax, was at the bottom of the overall rankings. There was a substantial gap between ease of use and the next most important feature, cost, which was ranked as the least important in 2014. Accuracy, included for the first time in 2015, came in as the third most important feature for tax preparation software. Another new feature, data security, was rated as least important.

For tax research products, cost was rated as the most important, with ease of use in second place. Timely updates ranked third most important. In 2015, there was a stronger relationship between individual feature ratings and overall ranking for tax research tools than in the past. The highest-rated tax research package, Parker Tax Pro, had the top ratings for cost, ease of use, and timely updates. Customer support continued to be the least important feature, possibly indicating a user preference for “plug and play,” as well as a flexibility to adapt to free websites that generally do not offer user support.

Cost has historically been the lowest-rated feature for both tax preparation and research software. In 2015, both the tax preparation and tax research packages with the best value for cost ratings also achieved the highest overall ratings. In addition, for 2015, cost was rated as the second most important and most important feature for tax preparation and tax research software, respectively. Does this mean that survey participants are becoming more cost-conscious? Although users could presumably reduce cost by switching packages, the majority of survey respondents (76%) have not switched packages within the past five years, and 87% of respondents do not plan to switch software products within the next year; however, 13% reported that they had switched tax preparation software, 5% had switched tax research software, and more than 6% had switched both within the past five years. Almost 38% made the change because of cost issues, 28% reported concerns about software performance as the driving factor, and 9% experienced a discontinued product. Almost 9% expect to switch tax preparation software within the next year, more than 2% planned to change tax research products, and 1% wanted to change both resources.

Customer support was rated as the fourth most important feature for tax preparation software, but it was the least important feature for tax research resources. While its relative importance may not have increased, more tax professionals reported actually using customer support in 2015. Telephone assistance continued to be the most popular form of technical support for tax preparation software, with 56% using it often or frequently and 41% using it occasionally. Other forms of customer support were less prevalent; e-mail was used often or frequently by 17% of survey respondents and occasionally by 51%, while online support was used often or frequently by 22% of respondents and occasionally by 50%. Usage of live chat decreased among survey respondents compared to 2014, with only 4% using it often or frequently and 8% using it occasionally. 

Exhibit 8 shows that 51% of respondents have implemented a paperless environment, consistent with 50% in 2014; however, only 12% of nonusers were interested in adopting the tools, down from 20% in 2014. The reported use of scanning software also remained similar to prior years, with 22% currently using it and 23% considering it. The percentage of respondents sending at least some tax returns electronically to clients decreased to 85%, but the percentage of returns transmitted in this fashion increased to 41%. Approximately 24% send at least 90% of clients’ returns to them electronically, compared to 20% in 2014. More survey participants used the online version of software (29% in 2015; 26% in 2014) and portals for clients to upload tax data documents (35% in 2015; 30% in 2014). The number of respondents considering these two options remained similar to previous years, with 9% indicating an interest in online software and 16% in client portals for the future. Some of the newest tax preparation products—such as Agile Tax, CCH Axcess Tax, and Intuit Tax Online—are exclusively online, but they did not garner many ratings in this year’s survey. The use of pay-per-return pricing decreased to 32% in 2015, with only 3% considering it. The percentage of respondents purchasing tax research software in connection with their tax preparation product increased slightly to 26% in 2015, although there appears to be a trend toward using Google for tax research, which may make packaged products less attractive.

The 2015 survey found an increasing number of respondents (28%) offered a...
telecommuting option for their staff, while another 5% were considering it. Changing work environments may naturally lead firms to find that different tools are better suited for different situations. The use of mobile devices has taken hold, and 70% of respondents allowed employees to use them for work. While data security issues might not yet have come to the forefront (see Exhibit 7), approximately half of those firms limited use to company-owned devices.

The 2015 tax season challenges appear to have created more problems for tax practitioners to deal with. The majority experienced problems from tax law changes under the ACA, with 62% having minor problems and 9% indicating significant problems. With regard to determining exemption qualifications under the ACA, 45% reported minor problems and 9% noted significant problems; furthermore, 36% reported minor problems and 10% noted significant problems with incorrect Forms 1095-A (see Exhibit 9). The number of respondents indicating difficulties related to late or incorrect Forms 1099 or Schedules K-1 grew significantly to 27% and 26%, respectively, with smaller increases in those experiencing minor problems.

Respondents to the 2015 survey were not exempt from the widespread problem of identity theft. More than half had minor problems with rejection of e-filed returns due to identity theft, and another 11% had significant problems. One participant stated that “the problems with identity theft should be resolved by the IRS sooner rather than later, as it is a substantial problem.” The delayed availability of digital signatures for e-filing affected fewer practitioners, with 30% having minor or significant problems; this might reflect tax practitioners’ pragmatic approaches to working around constraints. More than half, however, reported problems with compliance with the repair regulations. One participant stated that the repair regulation work was worth the effort because “we have yet to see a repair reg study that didn’t yield a tax benefit to our client.”

The website information for the tax software vendors utilized by 2015 survey participants is listed in Exhibit 10.

### Analysis and Summary

As in prior years, New York State CPAs continue to report relying on some of the most popular tax software resources, with some interesting changes for 2015. In certain respects, New York State CPAs’ preferred tax software resources conform to some national trends, but diverge from others. For example, respondents to The CPA Journal’s annual survey have often provided less generous ratings than those found in other surveys, as well as some on-point comments. New York State CPAs might approach the new “new thing” with a pragmatic perspective of what serves their clients and their firm best before making substantial changes to their practices.

Survey participants expressed general satisfaction with commercial tax preparation and research software resources. With the exception of customer support, overall tax preparation software ratings were up, although there was substantial fluctuation among individual products. Similarly, overall ratings for commercial tax research software increased, but specific providers’ rat-

### EXHIBIT 9

<table>
<thead>
<tr>
<th>Tax Season Problems</th>
<th>No Problems</th>
<th>Minor Problems</th>
<th>Significant Problems</th>
<th>N/A</th>
</tr>
</thead>
<tbody>
<tr>
<td>General issues with the ACA</td>
<td>27%</td>
<td>62%</td>
<td>9%</td>
<td>2%</td>
</tr>
<tr>
<td>Determining exemption qualifications under the ACA</td>
<td>40%</td>
<td>45%</td>
<td>9%</td>
<td>5%</td>
</tr>
<tr>
<td>Incorrect Forms 1095-A for reporting under the ACA</td>
<td>42%</td>
<td>36%</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td>Late delivery of or corrections to Forms 1099</td>
<td>17%</td>
<td>51%</td>
<td>27%</td>
<td>5%</td>
</tr>
<tr>
<td>Late delivery of or corrections to Schedules K-1</td>
<td>16%</td>
<td>54%</td>
<td>26%</td>
<td>4%</td>
</tr>
<tr>
<td>Rejection of e-filed returns due to identity theft</td>
<td>29%</td>
<td>54%</td>
<td>11%</td>
<td>6%</td>
</tr>
<tr>
<td>Delayed availability of digital signatures for e-filing</td>
<td>44%</td>
<td>26%</td>
<td>4%</td>
<td>26%</td>
</tr>
<tr>
<td>Compliance with repair regs (tangible property regulations)</td>
<td>30%</td>
<td>35%</td>
<td>22%</td>
<td>12%</td>
</tr>
</tbody>
</table>
ings reflected a mix of increases and decreases. Ease of use was rated as the most important feature for tax preparation software, and the second most important for tax research software. In the reverse, cost ranked first for tax research products and second for tax preparation tools.

The 2015 survey results show that substantially more respondents are relying on free resources for tax research, such as the IRS and state tax websites. Many reported defaulting to Google searches rather than commercial research tools. The ACA’s complex reporting requirements were rumored to generate more business for tax preparers, but that does not appear to have materialized. The IRS reported that, as of August 28, 2015, the percentage of total e-filed individual income tax returns submitted by tax professionals had declined from 64% in 2012 to 60% in 2015. Self-prepared tax returns were up to 40% of total e-filed individual returns (http://www.irs.gov/uac/2015-and-Prior-Year-Filing-Season-Statistics). Although only 1% of the 2015 survey respondents reported losing a large enough share of business to do-it-yourself software or free-filing alternatives to be concerned, the majority of respondents (55%) acknowledged they have lost some clients to these options. This is a slight increase from the 52% who reported losing some clients in 2014.

Identity theft has become such a problem that it was the number one tax scam on the IRS’s annual list. Tax preparers especially must be on the alert for identity theft, due to the potential reputation damage for those affected by these scams (see Mark Lee Levine, “Tax Scams Déjà vu—The IRS’s Annual ‘Dirty Dozen,’” The CPA Journal, December 2014, pp. 28–34) states that tax preparers must particularly be on alert for identity theft due to the reputation damage for those affected by these scams.

Still, taxpayers should not expect much help from the IRS on this issue. According to the National Taxpayer Advocate’s July 2015 report on the most recent tax-filing season, the IRS answered only 17% of calls from taxpayers whose returns were rejected under suspicion of identity theft, with an average hold time of 28 minutes. More than 600,000 taxpayers had their returns frozen due to the operation of identity theft filters, leaving it to taxpayers to resolve the issue (http://www.taxpayeradvocate.irs.gov/2016 ObjectivesReport).

Despite the frustrations of adjusting to last-minute tax law changes and waiting for belated guidance, New York State tax professionals are generally satisfied with their tax preparation and tax research software. They continue to search for the best solutions and take advantage of both commercial and free technology to improve their practices. One survey participant, however, reported it doesn’t always work out for the best: “We switched to a new data source preparation during the last tax season that did not work very well at all. It was very ‘buggy,’ and cost way too much money. We are still a time away before robots take all of our accounting jobs.”

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EXHIBIT 10
Tax Software Vendors

<table>
<thead>
<tr>
<th>Company</th>
<th>Website</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agile Tax</td>
<td>agiletax.com</td>
</tr>
<tr>
<td>ATX</td>
<td><a href="http://www.cchfs.com">www.cchfs.com</a></td>
</tr>
<tr>
<td>Bloomberg BNA</td>
<td><a href="http://www.bna.com/tax">www.bna.com/tax</a></td>
</tr>
<tr>
<td>CCH</td>
<td><a href="http://www.cchgroup.com">www.cchgroup.com</a></td>
</tr>
<tr>
<td>Checkpoint</td>
<td>tax.thomsonreuters.com</td>
</tr>
<tr>
<td>Drake Software</td>
<td><a href="http://www.drakesoftware.com">www.drakesoftware.com</a></td>
</tr>
<tr>
<td>GoSystem RS</td>
<td>tax.thomsonreuters.com</td>
</tr>
<tr>
<td>Intuit ProLine</td>
<td>accountants.intuit.com</td>
</tr>
<tr>
<td>Intuit ProSeries</td>
<td>accountants.intuit.com</td>
</tr>
<tr>
<td>Intuit Tax Online</td>
<td>accountants.intuit.com</td>
</tr>
<tr>
<td>Kleinrock</td>
<td>support.cch.com/Kleinrock</td>
</tr>
<tr>
<td>Lacerte Software</td>
<td>accountants.intuit.com</td>
</tr>
<tr>
<td>LexisNexis</td>
<td><a href="http://www.lexisnexis.com">www.lexisnexis.com</a></td>
</tr>
<tr>
<td>Parker Publishing</td>
<td><a href="http://www.parkertaxpublishing.com">www.parkertaxpublishing.com</a></td>
</tr>
<tr>
<td>TaxACT</td>
<td><a href="http://www.taxact.com">www.taxact.com</a></td>
</tr>
<tr>
<td>Tax Analysts</td>
<td><a href="http://www.taxanalysts.com">www.taxanalysts.com</a></td>
</tr>
<tr>
<td>TaxSlayer</td>
<td><a href="http://www.taxslayerpro.com">www.taxslayerpro.com</a></td>
</tr>
<tr>
<td>TaxWise</td>
<td><a href="http://www.taxwise.com">www.taxwise.com</a></td>
</tr>
<tr>
<td>UltraTax CS</td>
<td>tax.thomsonreuters.com</td>
</tr>
<tr>
<td>Westlaw</td>
<td>legalsolutions.thomsonreuters.com</td>
</tr>
</tbody>
</table>
The United States’ entry into World War II marked the start of the largest business undertaking in the nation’s history, and accountants were needed to keep track of records and act as auditors. New taxes and regulations on manufacturing required their expertise—but public accounting firm staffs were decimated due to military enlistments and the draft. Although all CPA firms were affected to some extent and all made contributions to the war effort in one form or another, it was the predecessors of the firm now known as Deloitte that arguably supplied the most high-level talent. The firms that today comprise Deloitte—including Haskins & Sells; Touche, Niven & Co; and McLaren, Goode, West and Company—provided numerous partners to the Washington war machine. Their efforts helped ensure victory and led to innovations in accounting and auditing.
ributions to World War II
leagues at Deloitte’s Predecessor Firms

By Dale L. Flesher, Gary John Previis, Mark E. Jobe, and Andrew D. Sharp

J
Japan’s bombing of Pearl Harbor on December 7, 1941, marked the official involvement of the United States in World War II, but the nation had already been indirectly involved since the German invasion of Poland in 1939. The need for additional government revenues to support the war effort was tremendous: Defense expenditures for 1942 ($22.905 billion) were nearly double federal revenues ($12.547 billion). By 1943, revenues had jumped to $21.947 billion, but defense expenditures were nearly triple that, at $63.414 billion. New taxes eventually softened the deficit. By 1944, the full effect of the war-related tax changes had taken effect; tax collections doubled from the preceding year, and although defense expenditures again increased, the rate of increase was less than the rate of change in federal revenues. Because nondefense outlays also increased in 1942 and 1943, the federal deficit for both years was nearly equal to total defense expenditures.

In the midst of all of these new taxes was a need for more accountants to account for the new money that the government spent on the war effort and to conduct audits of defense contracts. New regulatory bodies, such as the Office of Price Administration (OPA), also contributed to the need for more accountants.

Fortunately, many CPAs patriotically served their country in this time of need. Perhaps most memorable: those who worked for the predecessor firms of today’s Deloitte, including Haskins & Sells (the largest), Touche, Niven & Co, and McLaren, Goode, West & Company.

Serving the Country

With the onset of World War II, times were tough on the home front. Able-bodied young men—and some not so young—were drafted or enlisted. The following sections highlight some of the profession’s major contributions to the nation during this time.

Haskins & Sells. This firm saw 408 employees leave the firm to join the war effort; most notable of these was the firm’s managing partner, Arthur H. Carter. A Kansas native and a 1905 graduate of
West Point, he had become the managing partner of his father-in-law’s firm, Haskins & Sells, in 1930 and was widely lauded for his 1933 congressional testimony that kept the auditing franchise within the accounting profession. Carter had been invited to testify before Congress because, from 1930 to 1933, he ably served as president of the NYSSCPA. Carter, a colonel during World War I, was called back in 1941 to be the executive accountant for the U.S. Department of War. In 1940, Henry L. Stimson was again appointed to serve as Secretary of War, and he wanted to be surrounded by the best possible staff that he could possibly have. With this in mind, he remembered Carter from their experience together during Stimson’s prior stint as Secretary of War (1911–1913) and invited him to serve as the head of the army’s accounting division (John W. Queenan, “Arthur H. Carter: A Memorial,” Haskins & Sells Reports, vol. 2, Spring 1965, pp. 14–15). Carter’s responsibilities included the accounts and all fiscal services of the War Department. He held this position until his retirement from the Army in February 1946. Carter was initially given the rank of brigadier general and promoted to major general in 1943. He had been awarded the Distinguished Service Medal during World War I and had an Oak Leaf Cluster added in World War II.

Andrew Stewart, another of the firm’s senior partners, who attained the rank of colonel, joined Carter in Washington in March 1941. Stewart served as the 1941/42 NYSSCPA president. He was the deputy director (i.e., assistant to Carter) in the Office of the Fiscal Director until October 1945 (Arthur B. Foye, Haskins & Sells: Our First 25 Years, New York: Haskins & Sells, 1970). Carter and Stewart oversaw a staff of more than 10,000 employees who issued approximately 8 million checks each month in amounts reaching as much as $500 million per month. They also oversaw the auditing of cost-plus, fixed-fee construction, and supply contracts (Foye, 1970, p. 92). In a speech at the American Institute of Accountants (AIA) annual meeting in 1942, Stewart summarized Carter’s duties as follows:

The importance of professional accounting experience in these matters has been recognized in the recent reorganization of the War Department by the concentration of responsibility for supervision of all the foregoing in the Fiscal Division, Headquarters, Services of Supply, of which one of our members is Director. The head of this Division is also Budget Officer and acts as Comptroller of the War Department. The Budget Officer of the War Department is charged with the duty of securing the necessary funds to carry out the plans, programs, and operations of the War Department and to assure the adequacy of the financial administration of such funds. He is required to arrange for the defense and justification of such funds before the Bureau of the Budget and Congress, to allocate funds to the various Services of Supply in accordance with the program, and to prescribe the methods of record-keeping and reporting to show the use of the funds so allocated.

Indeed, Carter and his assistant held important positions in the U.S. government, even as they were still affiliated with Haskins & Sells. In addition to handling the day-to-day accounting activities of the War Department, the two accountants introduced some innovations and efficiencies into government operations. One of their major innovations concerned audits of defense contracts: Auditing manuals were prepared setting forth procedures for auditing cost-plus-fixed-fee construction and supply con-
tracts, in which the principle of selective auditing was first enunciated for application to Government contracts. Close cooperation was established with the Comptroller General, who, under the law, was required to pass upon the legality of all expenditures, and it was arranged that he would make his examinations at the projects where the necessary information was available instead of in Washington, where all vouchers had previously been sent. These changes resulted in substantial savings in the cost of administration. (Foye 1970, p. 94).

On the surface, this may not sound that innovative, but two major points should be noted. First, the “principle of selective auditing” was used for the first time. In other words, Carter and Stewart decided to use sampling to audit defense contracts. Given the shortage of manpower, it was not possible to audit every contract, as had been done in the prewar years. According to Stewart, the decision to audit was based on the internal control system maintained by the contractor (Stewart 1942, p. 18).

Second, the Haskins & Sells partners convinced Comptroller General Lindsey C. Warren that it would be more efficient to send the auditors to where the cost documents were located, rather than having all documents sent to Washington. One of the main advantages of this fieldwork procedure was a reduction in the numbers of copies of supporting documents to be prepared. Since the founding of the General Accounting Office (GAO) in 1921, all government audits had been conducted in Washington; thus, Carter’s recommendations to conduct field audits and on selected contracts amounted to a major change in federal auditing, as did the recognition that internal controls should impact the level of auditing activity. Effective in August 1942, Warren created the War Contract Project Audit Section to carry out Carter’s recommendations (Roger R. Trask, *GAO History, 1921-1991*, 1991).

Following the war, Stewart headed a Haskins & Sells staff of 14 in an engagement at General Douglas MacArthur’s headquarters in Japan.

On paper, Carter remained managing partner of Haskins & Sells through 1947; in actuality, Arthur B. Foye ran the firm through March 1946 and officially took over as managing partner following Carter’s retirement in 1947. Carter lived until 1965, when he died just three days short of turning 81.

Another longtime Haskins & Sells partner, George P. Auld, had served in World War I as a commander in the Supply Corps. From 1915 to 1918, he had been chief accounting officer in the Navy. He had received the Navy Cross in 1919 and in 1924 was made an Officer of the French Legion of Honor. In February 1941, Auld was asked by Secretary of the Navy James Forrestal to reenter government service and establish a division to audit contract costs under the defense procurement programs.

In this role, he organized panels of supervising auditors throughout the country. The panels relied on members of 70 different CPA firms throughout the nation to conduct periodic inspections of auditing procedures and reviews of contractors’ methods of internal control and cost determination. Auld was also a member of the Navy Price Adjustment Board. He resigned from his Navy work in September 1942 because of ill health (Foye 1970, p. 96). Auld was replaced by another noted public accountant: Paul Grady, originally with Arthur Andersen and later with Price Waterhouse & Co. The use of auditing panels for reviews of defense contracts did cause some consternation in professional circles—should CPAs audit contracts entered into by their own audit clients, or did this represent an independence issue? Some firms refused to accept such business, although the question remained undecided through the duration of the war.

After the war ended, Francis A. Cox became a Haskins & Sells partner. He had joined the firm in 1935, following his graduation from New York University. He entered the Naval Reserve as an ensign in 1942 and became chief accountant of the Navy Price Adjustment Board in New York and Washington. He was discharged in 1946 with the rank of lieutenant commander. He stayed with Haskins & Sells until 1951 when he joined the *New York Times*, first as controller and later as chief financial officer. He died in May 1982 at the age of 68 (“Francis A. Cox, 68, A Times Executive,” *New York Times*, May 6, 1982, p. D27).

Another person loosely connected with Haskins & Sells, Thomas H. Sanders of Harvard University, was also active with respect to the accounting aspects of the war. Sanders, who had been a coauthor of a 1938 research project (“The Statement of Accounting Principles,” by Sanders, Hatfield, and Moore) funded by the Haskins & Sells Foundation, served during the war as chief of the cost analysis section of the War Production Board (WPB) and as a member of price adjustment boards. Sanders spoke at the AIA’s annual meeting in Chicago in 1942 (Thomas H. Sanders, “Renegotiation of Contract Prices,” *Wartime Accounting*, 1942, pp. 33–44). As discussed later, Haskins & Sells was criticized for Sanders’ participation.

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**FOR FURTHER READING**


on price adjustment boards, even though he was not an employee of the firm. Yet another important contributor to the war effort was the AIA’s 1941/42 president, N. Loyall McLaren. Born in 1892 and a graduate of the University of California at Berkeley (interestingly, he wrote the lyrics to the school’s fight song), he was the son of Norman McLaren, who had started a CPA firm in San Francisco in 1895 that evolved into McLaren, Goode, West & Company, which was merged into Haskins & Sells in 1952. Before the merger, McLaren, Goode, West & Company was the oldest and largest firm on the West Coast. N. Loyall McLaren, like his father before him, served as president of the California Society of CPAs (1928). John Lansing Carey, the longtime executive secretary of the AIA, recounted McLaren’s war service began on Dec. 7, 1941:

Over the radio came the news of the Japanese attack on Pearl Harbor. After a period of shocked silence, Mr. McLaren said, “This means war. I am going into uniform.” Shortly after, he was sworn in as an officer of the United States Navy with the rank of commander, and later was promoted to captain, serving as chief of the cost and audit division of the Office of Procurement and Material. He offered to resign as president of the Institute, but the executive committee rejected this offer. Mr. Wellington, the immediate past president, was named as acting chairman of the executive committee, to preside at meetings which the president might be unable to attend. (John L. Carey, *The Rise of the Accounting Profession to Responsibility and Authority, 1937-1969*, 1970)

In January 1942, while still president of the AIA, McLaren went on active duty as a commander in the Naval Reserve; he was quickly ordered to Washington to serve with the Cost Inspection Service. In early May 1942, the Price Administration Act was passed, and McLaren was named as chairman of the New York Division of the Navy price adjustment board. It was McLaren who recommended that the price adjustment board be moved out of Washington, D.C., because it was too difficult to get contractors to attend meetings in what was then an overcrowded city. McLaren later organized a San Francisco branch of the board and personally selected its members (N. Loyall McLaren, *Business and Club Life in San Francisco: Recollections of a California Pioneer Scion*, 1978, p. 187).

As head of the price adjustment board, McLaren took part in the renegotiation of contracts between military suppliers and the government. McLaren was the elected leader of the accounting profession during the early months of the war, and he led by example. His presidential address at the AIA’s annual meeting in 1942 included the following:

The part which must be taken by our profession is crystal clear—individually and collectively we must demonstrate that in war, as in peace, we are eager and fully prepared to do all that our country has the right to expect of us (Carey 1970, p. 46).

On the other hand, McLaren stated that he “was unquestionably the worst president of the American Institute they ever had. Because I did practically nothing” (McLaren 1978, p. 200). McLaren continued to remain a visible leader even after he was no longer the Institute’s president. The National Association of Cost Accountants (NACA) invited him to speak at its annual meeting in 1943 on the topic of renegotiation of war contract prices. He was also a keynote speaker at the AIA’s annual meeting in St. Louis in 1944, where he discussed the Surplus Property Act of 1944.

Near the end of the war, McLaren continued his public service as treasurer of the United Nations Conference Committee in San Francisco and later, during the summer of 1945, was accounting advisor to the United States Delegation with the Allied Commission on Reparations (the Yalta Agreement) in Moscow. Dividing the spoils of war among the various nations required an unimpeachable accounting system, and it was McLaren’s job to create both the accounting and auditing systems. As part of that assignment,

At the end of the war, he retired from the Navy with the rank of commodore and was eventually promoted to rear admiral in the Naval Reserve in 1956. In 1947, McLaren was asked to conduct a survey of the Internal Revenue Bureau. In 1961, the University of California awarded him an honorary doctorate; additional honorary doctorates followed from the University of San Francisco (1963) and Whittier College (1972). Because of his accounting skills and his willingness employ them for the good of mankind, McLaren had many friends throughout the country, including former Presidents Herbert Hoover and Dwight Eisenhower (Foye, 1970, pp. 108–109). Even Prince Philip of Great Britain was an acquaintance.

**Touche, Niven & Co.** The Touche side of the firm also had its contributors to the war effort, including a future managing partner, Lieutenant Colonel John W. McEachren. In 1929, after one year’s experience as a cost accountant at a large Detroit pharmaceutical company, McEachren had approached the firm’s auditor, George Bailey, to discuss an error in the federal tax accrual. Bailey was impressed with McEachren and quickly hired him for Ernst & Ernst. Years later, a merger would form Touche, Niven, Bailey & Smart.

With the commencement of the war, McEachren was commissioned in April 1942 in the Office of the Fiscal Director of the Army. Despite the ongoing war, McEachren maintained his professional activities; he was one of the main speakers at the AIA’s 1942 annual meeting in Chicago (“Determination of Contract Costs by the War Department,” Wartime Accounting, 1942, pp. 20–22). He was also the keynote speaker at the June 1943 annual meeting of the National Association of Cost Accountants (“Cost Determination Under Audited War Contracts,” National Association of Cost Accountants Yearbook, 1943, pp. 6–18). McEachren’s NACA speech was summarized the next day in the New York Times, indicating its significance to corporate America. Many of these individuals worked together on war-related projects. For example, McEachren collaborated with McLaren in devising the forms used for contract renegotiations. Although Bailey did not go into the military, he was seen as a resource on wartime accounting. He was one of the two keynote speakers at the NACA 1944 annual meeting (“Cost Phases of War Contract Termination,” National Association of Cost Accountants Yearbook, 1944, pp. 29–47).

Another Touche contributor was Jacob P. Friedman of the New York office; he was appointed in October 1941 to a special committee of the AIA that recommended revisions to the accounting system of post exchange service at Army installations. Charles R. Whitworth, a Touche, Niven & Co. partner in Chicago, accepted a commission as assistant supervisor of cost estimates for the U.S. Signal Corps. Another partner, Edward H. Wagner Jr. of the St. Louis office accepted a commission as lieutenant commander in the Naval Reserve in May 1942. Within one month, he was working with the supply corps in the Office of the Secretary of the Navy. Wagner published an article, “Renegotiation Reminders,” in the May 1945 issue of the Journal of Accountancy (pp. 352–355) that dealt with the regulations of the War Contracts Price Adjustment Board.

Victor H. Stempf, was president of the AIA. Stempf had also served as NACA president early in the war and previously as NYSSCPA president. In April 1944, Stempf was appointed to the Committee on Post-War Tax Policy, under a grant of $100,000 from the Falk Foundation, with the goal of drafting of a postwar federal tax program.

**Criticism of the Profession’s War Efforts**

Though many would laud these contributions to the nation’s war effort, they did not go without criticism. An article by Drew Pearson, a United Feature Syndicate columnist, was critical of the role of Haskins & Sells:

There is a lot of backstage indignation over the manner in which members of one Wall Street accounting firm, Haskins & Sells, dominate the cost accounting work of the Army and Navy. Cost accounting, under cost plus contracts, is extremely important. Furthermore, the Army and Navy are both engaged in scaling down some of these contracts through Price Adjustment Boards. The men who rule on these price adjustments can save the government billions of dollars—or on the other hand, they can permit billions in profits to industry. …

It so happens that executives from Haskins & Sells occupy key accounting posts. It also happens that Haskins & Sells is the accounting firm which handles the work of General Motors and du Pont, two companies which have received very large government orders. …

On the Navy’s Price Adjustment Board is George P. Auld, a member of the Haskins & Sells firm. High in the Army’s cost and supply service is Brig. Gen. Arthur H. Carter, a partner of Haskins & Sells, and son-in-law of Sells. Then in the cost accounting branch of the War Production Board is Dr. Thomas H. Sanders, professor of accounting at the Harvard Business School, who has been close to Haskins & Sells and has done some work for the Haskins & Sells Foundation.
member of Haskins & Sells is Lieut. Col. Andrew Stewart, now in the accounting branch of the War Department. (“The Washington Merry-Go-Round,” United Feature Syndicate, Aug. 18, 1942)

The article did go on to say that Carter and Auld had patriotically served in the Army and Navy during World War I and in their present positions were careful to have the accounts of former clients supervised by other Army and Navy accountants. For example, it was noted that one such client, General Motors, had more than $2 billion in war contracts and that even a reduction of 1% would mean a $20 million savings to the federal government. To inflame the situation, Pearson, a famous columnist, reported that the firm was already being bitterly condemned by the SEC for the “obviously manipulated” financial statements in the Associated Gas and Electric Co. case, wherein “the accounting firm lacked independence.” The article concluded that “members of this same firm now sit in high Army-Navy positions where they will need to exercise great independence” (Pearson 1942). The article may not have been a smoking gun, but it surely caused some readers to doubt the independence of the members of the price adjustment boards.

It should be noted that the appointment of businessmen to the price adjustment boards was a conscious decision on the part of the government. The War Department made the decision to organize a new group consisting of businessmen or retired businessmen instead of assigning pricing duties to established government agencies or bureaus (McLaren 1943, p. 29).

World War II was a difficult period for all CPAs, with clients experiencing new laws and regulations, new taxes, shortages of materials and manpower, and greater demands for increased productivity. The need for accounting services increased dramatically, but despite the demands on CPAs, the Deloitte predecessor firms of Haskins & Sells, Touche, Niven & Co, and McLaren, Goode, & West & Co. contributed firm manpower to the war effort.

World War II consumed the American psyche during the early 1940s. Public accountants were no different than other citizens in this respect. Still, CPAs maintained their professionalism and the leadership of the profession. Deloitte’s predecessor firms, especially, played an important role in the war. Two managing partners, Carter and Stewart, served during the war at the level of colonel or higher, and they accounted for the largest business project in history. Lasting innovations during this time included the concept of audit sampling, conducting government audits in the field, and using the client’s internal control system to determine the extent of auditing procedures.

Though Deloitte, more than any other firm, sent its leaders to serve the government and the profession, all large CPA firms were affected. For example, Arthur Andersen reported that 220 men—67% of its 1941 staff—were in the armed forces by the middle of 1943. Andersen responded by calling back retirees, reverting to a six-day workweek, and encouraging overtime (A Vision of Grandeur, Arthur Andersen, 1988, p. 67). Besides losing staff, Peat Marwick (predecessor of KPMG) sent one top partner, William M. Black, to serve on the War Production Board (T. A. Wise, Peat, Marwick, Mitchell & Co.: 85 Years, 1982, p. 41). Price Waterhouse similarly contributed men at the staff level (at least 40% of the 1941 staff) and one partner, Paul Grady (David Grayson Allen and Kathleen McDermott, Accounting for Success: A History of Price Waterhouse in America, 1993, p. 84).

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**Intuit-sponsored blind study conducted by a third-party market research company in the summer of 2014. Represents the average returns achieved per employee among tax preparers who use Lacerte versus the average returns per employee achieved using an alternate tax preparation software.

1 Testimonials represent the individual experiences of these customers. Intuit does not represent that results are typical or that the experiences will apply to all customers since each tax preparer is unique.

2 AICPA Journal of Accountancy Survey. ProSeries received a ranking of 4.1 out of 5 points for “How easy was it to use?” This was among the highest ranking among comparable tax software packages. From the AICPA August 2014 Tax Software Survey, which reviewed ProSeries 2013.
How to More Effectively Comply with the Requirements of SAS 128

By Terry J. Engle and Nicholas J. Mastracchio, Jr.

In Brief

This article describes the salient requirements of SAS 128, Using the Work of Internal Auditors, and demonstrates how the International Professional Practices Framework (IPPF), promulgated by the Institute of Internal Auditors (IIA), can be utilized as a normative standard to achieve highly effective evaluations of an audit client’s internal audit function in compliance with its requirements. While this article primarily focuses on the evaluation of internal audit functions during independent financial statement audits, much of the information should be of value to all CPAs that are called upon to evaluate an organization’s internal audit function.
The AICPA’s Auditing Standards Board (ASB) recently promulgated the clarified Statement on Auditing Standards (SAS) 128, *Using the Work of Internal Auditors*, effective for audits of financial statements for periods ending on or after December 15, 2014. The pronouncement supersedes SAS 65, “The Auditors’ Consideration of the Internal Audit Function in an Audit of Financial Statements.” The ASB also had redrafted AU section 322, “The Auditor’s Consideration of the Internal Audit Function in an Audit of Financial Statement,” for clarity, and added guidance to AU-C 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement”. The ASB task force commenced in February 2013 with the objective of reflecting on the developments in the internal auditing environment and changes in practice regarding the interactions between external and internal auditors. The ASB wanted to converge with the International Auditing and Assurance Standards Board (IAASB) pronouncement of International Standards on Auditing (ISA) 610. Because ISA 610 was also under revision, the ASB waited until the ISA redrafting was complete.

At first, ISA 610 was redrafted to conform to the clarity format with no changes; however, the IAASB decided that it needed to be more responsive to the issue of direct assistance by the internal audit staff. The IAASB had some difficulty dealing with direct assistance, and the final pronouncement was not issued until March 2013.

SAS 128 focuses on the external auditor’s responsibilities when using the work of internal auditors during independent financial statement audits. SAS 128 does not apply if an audit client does not have an internal audit function. In addition, this SAS does not apply if the client has an internal audit function, but the external auditor finds that the activities of the function are not relevant to the financial statement audit, if—based on the auditor’s preliminary understanding of the internal audit function—the external auditor does not expect to use the function. It is important to realize that external auditors are not required to use a client’s internal audit function during a financial statement audit. That said, external auditors cannot completely ignore a client’s internal audit function when one exists. AU 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,” requires that while obtaining the required understanding of an audit client, the external auditor should obtain an adequate understanding of the client’s internal audit function in order to properly plan the external audit and to decide whether the internal audit function can be used. It should be recognized that an ineffective internal audit function might be a weakness in the monitoring component of internal control rising to the level of a significant deficiency. Material weaknesses should be communicated in writing to management, and to those charged with governance following the requirements of AU 265, “Communicating Internal Control Related Matters Identified in an Audit.”

### EXHIBIT
Mapping SAS 128 Requirements to International Professional Practices Framework Requirements

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Internal audit function’s assurance and consulting agendas are commonly relevant to the external audit.

External auditors should gather sufficient and appropriate evidence in order to make an evaluation of these three critical internal auditing attributes. SAS 128 clearly states that the degree to which the client’s internal audit function possesses these attributes—not only determines whether the external auditor can use the internal audit function in obtaining audit evidence, but these attributes significantly influence the extent to which the internal audit function can be used. The standard provides some basic guidance that external auditors can follow in evaluating these three critical internal auditing attributes.

Objectivity
SAS 128 states, “Objectivity refers to the ability to perform tasks without allowing bias, conflicts of interest, or undue influence of others to override professional judgments” (SAS 128, para. 7). The standard provides guidance as to factors that the external auditor should consider in the evaluation of the objectivity of internal auditors. Two salient factors that should be focused upon are the organizational positioning of the internal audit function, and the reporting relationships of the Chief Audit Executive (CAE). Other suggested factors to consider are whether the internal audit function is free of conflicting managerial or operating responsibilities, and whether those “charged with governance” are instrumental in the significant resource and employment decisions affecting the CAE, and more broadly, the entire internal audit function. Finally, external auditors should consider the following:

- Whether the internal auditors are members of relevant professional bodies and their certifications that obligate them to obtaining continuing professional education.

Application of a Disciplined Approach
One of the most important new requirements introduced by SAS 128 is that in order for external auditors to be able to use a client’s internal audit function, the external auditors must be satisfied that the internal audit function uses a “systematic and disciplined approach, including quality control.” Relative to the prior auditing standard governing the use of internal auditors (i.e., SAS 65), this requirement represents an additional evaluation that must be performed while determining whether the client’s internal audit function can be used. The external auditor’s evaluation of this attribute is intended to address the risk that: “the external auditor inappropriately uses internal audit-like work performed in an informal unstructured, or ad hoc manner” (SAS 128, para. A14). SAS 128 suggests that in evaluating this critical internal auditing attribute, the external auditor may assess factors such as the internal audit functions use of audit documentation (i.e., work papers), the use of documented audit programs, and whether the internal audit function has appropriate quality control policies and procedures in place.

Obtaining Audit Evidence
Under SAS 128 requirements, external auditors are allowed to utilize a client’s internal audit function in obtaining audit evidence after the external auditors have evaluated the internal audit function and found it to be sufficiently objective, competent, and effectively utilizing a “systematic and disciplined approach, including quality control.” The nature, timing, and extent of this internal audit utilization should be based on the degree to which these three essential attributes are found to be present and effectively operating. In addition, SAS 128 recognizes that the specific facts and circumstances of each client situation can properly affect the external auditor’s internal audit utilization decisions. SAS 128 mandates that the external auditor is solely responsible for the audit opinion, and should be sufficiently involved in the audit. To prevent inappropriate use of the internal audit function, external auditors should plan to
de-emphasize internal audit usage as the use of judgment in the audit increases, as the assessed risk of material misstatements increases, and because the assessed level of internal audit competence and objectivity decreases.

When external auditors elect to utilize a client’s internal audit function, the function can be used in two primary ways: 1) The external auditors may use the existing work product of the internal auditors, and 2) the internal auditors can provide “direct assistance.” SAS 128 provides detailed guidance on the proper use of internal auditors in each of these ways.

**Using the Existing Work of the Internal Audit Function**

Internal audit functions’ assurance and consulting agendas are commonly relevant to the external audit. For example, internal audit assurance engagements commonly involve the evaluation of the reliability and integrity of financial information, the assessment of the effectiveness of internal controls over financial reporting, and the evaluation of the operational effectiveness of the organization’s overall enterprise risk management system. External auditors should assess whether the internal auditors’ existing work product—or planned work—addresses these areas, and is thereby relevant to the external audit strategy. External auditors can obtain relevant information by performing procedures such as reading relevant internal audit reports and reviewing internal audit work papers.

If the external auditors find the work of internal auditors relevant and plan on using the existing work of the internal auditors in obtaining audit evidence, the external auditor should communicate with the internal auditors and attempt to coordinate activities. In addition, the external auditor should supervise and review their work.

The previous discussion makes it clear that, under the clarified auditing standards, external auditors are currently required to evaluate a client’s internal audit function on all audits where an internal audit function is present. While the use of
the internal audit function when gathering audit evidence is not required, the evaluation of the internal audit function is required. In situations where external auditors find the internal audit function relevant to the strategy and objectives for the external audit, and elect to utilize the internal auditors, a more in-depth evaluation is client internal audit functions. Furthermore, if external auditors are satisfied that a client’s internal audit function is in compliance with the requirements of the IPPF, the external auditors can have a high level of assurance that the client’s internal audit function possesses the critical attributes that are necessary for reliance on mandatory guidance by implementing alternative practices. The mandatory guidance applies to all entities and individuals that perform internal auditing services, but the IIA can only sanction IIA members and recipients of or candidates for IIA professional certifications for violations. Unlike the public accounting profession where statutory sanctions are typically available, the internal auditing profession primarily relies on the voluntary compliance.

Beyond the mission, the IIA categorizes the other six components of the IPPF (the following components are adapted from http://www.theiia.org):

- Core principles for the professional practice of internal auditing
- Definition of internal auditing
- Code of ethics
- International standards for the professional practice of internal auditing (standards)
- Practice advisories (implementation guides)
- Supplemental guidance.

Additional Guidance

The recently promulgated Mission of Internal Audit “articulates what internal audit aspires to accomplish within an organization,” but the core principles, “taken as a whole, articulate internal audit effectiveness” (http://www.theiia.org). The definition of internal auditing describes modern internal auditing, and the code of ethics conveys the minimum ethical requirements for individuals and organizations to follow while in the practice of internal auditing. The International Standards for the Professional Practice of Internal Auditing (Standards) are the primary source of detailed mandatory, and presumptively mandatory, requirements that all individuals and organizations in the practice of internal auditing should follow.

Turning to the recommended guidance, the practice advisories (implementation guides) provide detailed guidance to assist internal auditors in complying with the mandatory guidance. Individual practice advisories are directly related to individual standards, and they are most commonly promulgated when the IIA believes that additional guidance is needed for the effective and efficient adherence to a standard. Practice advisories address overall approaches and methodologies, but they do not con-
tain detailed processes or procedures. The more detailed guidance is found with the supplemental guidance (e.g., Practice Guides; http://www.theiia.org)

How External Auditors Use IPPF

External auditors can utilize the mandatory guidance of the IPPF (primarily the requirements contained in the Code of Ethics and Standards) as a widely accepted normative standard when evaluating a client’s internal audit function, and when deciding whether to rely upon the work of an internal audit function during an external audit. While it is beyond the scope of this article to comprehensively cover all the guidance of the IPPF that may be relevant to the overall evaluation of an internal audit function, the following discussion will demonstrate how the requirements of the IPPF exceed the minimum requirements of SAS 128 for external auditors to be allowed to rely upon the work of internal auditors.

The Exhibit depicts the critical internal audit attributes that must satisfy external auditors before they are allowed to rely on a client’s internal audit function under SAS 128. The Exhibit maps specific examples of mandatory IPPF guidance that address each attribute.

Quality Control

SAS 128 makes it clear that before an external auditor can utilize a client’s internal audit function, the external auditor should be satisfied that the client’s internal audit function has an effective system of quality control. IPPF Standard 1300, Quality Assurance and Improvement Program, has an explicit provision stating: “The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.”

Collectively, the suite of standards addressing the required quality control system (in Exhibit) requires that the quality control system consists of both internal quality control assessments performed by the internal audit personnel, other qualified individuals from within the organization, and external quality assessments. A qualified outside assessor or assessment team must conduct the required external assessments. This required quality control system rigorously assesses many attributes of the internal audit function, especially adherence to the required attributes for quality control systems as they evaluate the quality control systems of their clients. When a client is found to have a quality control system in compliance with the IIA standards, this provides a very high level of assurance that the client’s internal audit function has a very effective quality control system in place that fulfills the SAS 128 requirements.
Independence and Objectivity

The “objectivity” requirements of SAS 128 are met with several independence and objectivity requirements contained in the Code of Ethics and Standards. The IPPF’s concept of independence attaches to the internal audit function collectively, while the concept of objectivity refers to the mental attitude of individual internal auditors. Standard 1100 contains the unconditional requirement that: “The internal audit activity must be independent, and the internal auditors must be objective in performing their work.” Many find the concept of “the independence of an internal administrative reporting relationships (e.g., the CAE reporting to the CFO), external auditors should realize that the functional reporting relationship to the board (audit committee) is critical to the internal audit functions independence and may compensate for the less than optimal administrative reporting. Standard 1111 states: “The chief audit executive must communicate and interact directly with the board.”

The Code of Ethics and Standards explicitly addresses the objectivity of each and every internal auditor; for example, Standard 1120 states: “Internal auditors must have an impartial, unbiased attitude and avoid any conflicts of interest.” The code devotes one of its four ethical principles to objectivity. In part, the principle says: “Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments.” The code also has several rules of conduct that promote the objectivity principle. For example, Rule 2.1 prohibits internal auditors from participating “in any activity or relationship that may impair or presume to impair their unbiased assessment.” According to rule 2.2, internal auditors “shall not accept anything that may impair or be presumed to impair their professional judgment.”

In summary, the IPPF specifies that internal audit functions, and individual internal auditors, must be both independent and objective. The code of ethics and the standards contain explicit requirements that external auditors can look to as they evaluate the “objectivity” of their client’s internal audit function in compliance with SAS 128.

The code of ethics and the standards contain explicit requirements that auditors can look to as they evaluate the “objectivity” of their client’s internal audit function in compliance with SAS 128.

Competency

The Code of Ethics and Standards explicitly addresses competency. The competency principle of the code states, “Internal auditors apply the knowledge, skills, and experience needed in the performance of internal audit services.” Three ethical rules support this principle by clarifying that internal auditors are to only provide services for which they are qualified, they should follow the IIA Standards, and they should continually improve their proficiency. The standards themselves support Code of Ethics and Standards competency requirements. Standard 1200, Proficiency and Due Care, requires that “engagements must be performed with proficiency and due care.” Several related standards in the 1200 series contain some specific requirements to achieve the mandate of Standard 1200. Standard 1230, Continuing Professional Development, contains an unconditional requirement: “Internal auditors must enhance their knowledge, skills, and other competencies through continuing professional development.” It should be noted that certified internal auditors, in the practice of internal auditing, have a continuing professional education reporting requirement of 40 hours annually.

A Systematic and Disciplined Approach

While it is beyond the scope of this article to comprehensively describe all of the requirements that conclusively demonstrate that the use of a “systematic and disciplined approach” is required under the IIA standards, the Exhibit lists a representative sample of applicable standards to make the point. Notice that internal auditors have to meet specific requirements in four distinct stages of a formal internal audit assurance or consulting engagement (i.e., engagement planning, fieldwork, reporting, and monitoring). Standard 2200 addresses proper engagement planning, stating: “Internal auditors must develop and document a plan for each engagement, including engagement objectives, scope, timing, and resource allocations.” It should be noted that other standards related to planning require that engagement objectives be developed, and that work programs be created and documented. It should be recognized that the planning requirements for internal audit
functions are very similar to the planning requirements for external auditors.

Standard 2300, *Performing the Engagement,* and several other standards in the 2300 series provide the primary requirements for engagement fieldwork. Collectively, the guidance requires that internal auditors gather the necessary evidence to achieve engagement objectives, properly document their work, and the internal auditors conducting the fieldwork must be properly supervised. Standard 2400, *Communicating Results,* and several other standards in the 2400 series collectively require that internal auditors communicate the results of engagements, and the standards provide overall guidance on the form and content of engagement communications.

Unlike the public accounting profession, the internal auditing profession does not have a required internal audit report form. The final stage of an internal audit engagement is “monitoring.” Standard 2500 states: “The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.”

As the previous discussion illustrates, the standards contain detailed requirements that must be fulfilled in the planning, fieldwork, reporting, and monitoring stages of formal internal audit assurance and consulting engagements. If a client’s internal audit function is complying with the IPPF, the external auditor can have a high level of assurance that the function is using a “systematic and disciplined approach” in compliance with SAS 128 requirements.

**Utilizing the Internal Audit**

SAS 128 promotes the effective utilization of a client’s internal audit function, as long as the external auditors are satisfied that the client’s internal audit function is sufficiently competent and objective and that it follows a systematic and disciplined approach, including quality control. This article has described the salient requirements of SAS 128 and demonstrated how external auditors can use the recently revised IPPF to effectively comply with the provisions of this clarified auditing standard. The Institute of Internal Auditors has made the mandatory guidance of the IPPF available (free of charge) on https://www.theiia.org, under “Standards & Guidance.”

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As 2015 comes to a close and companies begin to think about preparing Form 10-K annual reports and first-quarter 2016 Form 10-Q reports, disclosures concerning cyber risk that should be included in SEC filings are among the key issues requiring the attention of managers and boards of directors alike. Cyber risk disclosure is not a new issue; it has formally been on the SEC’s high-interest list since October 2011, when the staff of the SEC’s Division of Corporation Finance issued guidance on the disclosure obligations relating to cyber risk, cybersecurity, and cyber incidents (see, for example, “SEC Cybersecurity Disclosure Guidance Is Quickly Becoming a Requirement,” Gerry H. Grant and C. Terry Grant, The CPA Journal, May 2014).

A Review of the Staff’s Guidance
The SEC staff’s views, which are contained in CF Disclosure Guidance: Topic 2, Cybersecurity, are consistent with relevant existing disclosure considerations and requirements that could arise in connection with just about any business risk. The staff acknowledges the concerns of constituents that furnishing detailed information could compromise an entity’s cybersecurity efforts. The staff accordingly emphasizes that disclosures of such a nature are not required under the federal securities laws. In general, the staff reminds registrants that, depending upon specific facts and circumstances, a discussion about cyber risk and cybersecurity matters could be required in Forms 10-K and 10-Q as part of the disclosures included in the following:

■ Risk factors, when such matters are deemed to be among the most significant factors that make an investment in the company’s securities speculative or risky
■ Management discussion and analysis (MD&A), if the costs or other consequences associated with one or more known incidents or the risk of potential incidents represent an event, trend, or uncertainty that is reasonably likely to have a material effect on results of operations, liquidity, or financial condition, or would cause reported financial information not necessarily to be indicative of future results
■ Legal proceedings, if they concern any material pending legal proceeding involving a cyber incident
Disclosure controls and procedures, when cyber incidents pose a risk to the entity’s ability to record, process, summarize, and report information required to be included in filings with the SEC.

In addition, the staff guidance cautions that cyber risks and cyber incidents could have an impact on a company’s financial statements, including: 1) claims resulting from breach of data privacy, 2) loss or diminished value of intellectual property, and 3) the direct and indirect costs of remediating the effects of a successful cyber attack and of preventing future attacks.

**Recent Developments**

During the four years since the issuance of the staff guidance, the SEC has dramatically increased its focus on cyber matters. In response, many companies have taken heed and have incorporated discussions concerning cybersecurity risk into their standard risk factor and MD&A disclosures. Indeed, Audit Analytics, a research company providing audit regulatory and disclosure intelligence, reports that cybersecurity disclosure in the risk factors section of SEC filings has become quite common (http://www.auditanalytics.com/blog/exploring-the-disclosure-of-cybersecurity/). Commissioners and staff have, in public statements, recently signaled that the SEC will continue to heighten its efforts concerning cyber matters. While its initial interest centered on regulated financial institutions and key market players (i.e., securities exchanges, broker/dealers, alternative trading systems), the SEC has begun to expand its attention to cover the general population of public companies, perhaps in response to the spate of highly publicized incidents of cyber attacks on companies operating in a wide range of nonfinancial industries and sectors.

In March 2014, the SEC hosted a round table to discuss cybersecurity and the issues and challenges it raises for market participants and public companies, and how these issues are being addressed in practice. Among the matters discussed at the round table was the effectiveness of current cybersecurity related disclosure guidance. While some panelists noted that many of the current disclosures in SEC filings are “boilerplate” in nature and repeat almost verbatim the words from the SEC staff’s guidance document, other panelists expressed caution that providing specifically tailored information could increase a company’s vulnerability because such information might include details that would help attackers infiltrate the company. Overall, panelists indicated a preference for principles-based guidance rather than prescriptive rules. Regarding the role of the board of directors in cybersecurity matters, panelists noted that while increasing numbers of boards are engaging outside experts for assistance in evaluating cybersecurity risks, they did not believe that companies should be required to have a separate cybersecurity committee or a dedicated expert on the board or one of its committees.

So far, neither the SEC nor its staff has taken any action to follow up on the March 2014 round table, and it’s uncertain whether additional staff guidance or formal rules will be issued or proposed any time soon—if at all. Moreover, the PCAOB has shelved plans to issue a practice alert devoted to cyber-
security. Instead, auditors of public companies are left with the general requirements in PCAOB AS 12, *Identifying and Assessing Risks of Material Misstatement*, to obtain an understanding of the company’s information system, how the company uses information technology, and how IT affects the entity’s financial statements.

Increased SEC Enforcement Action

Based on information reported in the *Cybersecurity Law Report* (https://www.wilmerhale.com/uploadedFiles/Shared_Content/Editorial/Publications/Documents/the-secs-two-primary-theories-in-cybersecurity-enforcement-actions.pdf), the SEC has, during the past few years, become more active in the enforcement aspect of cybersecurity:

- In the first 18 months after the staff guidance was issued in October 2011, the SEC sent comment letters to approximately 50 public companies requesting information about cyber incidents and information security, effectively requiring companies to commit to disclosing the existence of past cyber incidents.
- The SEC has quickly moved from comment letters to enforcement and currently has multiple active enforcement investigations involving data breach events under way.
- As it relates to disclosures, the SEC’s specific interest falls into the categories of 1) disclosure following a cyber incident, and 2) whether ongoing disclosure in filings accurately reflect the nature and severity of the cyber risks facing the issuer.
- Regarding disclosure after a cyber incident, the SEC seeks to understand how the issuer evaluated whether the incident was (or should have been) deemed material and whether any disclosures made about the incident were timely, complete, and accurate. It also may be that the SEC’s interest concerning disclosure of a cyber incident rests on Regulation FD, which generally prohibits selective disclosure of material non-public information to third parties and requires simultaneous disclosure to the market at large.
- As for continuing disclosure, the commission’s focus is based directly on the cautionary language contained in the staff guidance document itself that material information regarding cybersecurity risks and cyber incidents is required to be disclosed in order to make other required disclosures not misleading. Thus, as with other operational and financial risks, the adequacy of cybersecurity disclosure should be reviewed on an ongoing basis.

Although not directly relating to disclosures, it appears that the SEC has recently begun to express an enforcement interest on controls containing financial reporting data based on section 404 of the Sarbanes-Oxley Act of 2002, which requires public companies to maintain a system of internal control over financial reporting (ICFR). In the context of a cyber breach, according to the *Cybersecurity Law Report*, the SEC’s theory appears to be that cybersecurity is relevant to ICFR because security breaches could allow an intruder to tamper with the financial statements or underlying financial data or records.

Reporting and Disclosure Considerations

In preparing Form 10-K for 2015 and Forms 10-Q in 2016, assuming that the SEC does not issue any further guidance and given the commission’s recent elevated enforcement activity, it is critical to ensure that consideration be given to addressing the specific points emphasized in the SEC staff’s guidance when evaluating the disclosures to be included in risk factors. This includes, as applicable, to the following: 1) the aggregate materiality of individually insignificant cyber incidents that have occurred, 2) direct and indirect costs of remediation and prevention, 3) risks associated with cyber incidents that could remain undetected for an extended period of time, 4) risks associated with outsourced functions, and 5) whether the registrant carries mitigating insurance coverage. Moreover, if a cyber incident has occurred during the year, consideration should be given to the impact of the breach on disclosure controls and procedures and ICFR.

Finally, regarding MD&A, consideration should be given to the potential impact of a cyber incident that occurred during the period on future revenues and costs, including costs relating to litigation and future cash flows.

Allan B. Afterman, PhD, CPA, is the author of numerous treatises on financial reporting and SEC practice and has consulted with governments on the establishment of national securities laws and financial reporting standards. He is a former adjunct professor in the Booth School of Business at the University of Chicago, and was assistant to the national director of SEC practice at a major public accounting firm.
Auditing Conference
Tuesday, 11.24.15
14 Wall Street, New York City
A Deep-Dive Look at the Most Important Issues Currently Facing Auditors
Visit nysscpa.org/audit15 or call 800-537-3635 to register!

Exempt Organizations Conference
Wednesday, 12.2.15
Citi Executive Conference Center
153 East 53rd Street, New York City
A Fresh Look at the Latest Challenges and Opportunities Facing Nonprofits
Visit nysscpa.org/exempt15 or call 800-537-3635 to register!

Annual Tax/Plenary Conference
Tuesday, 12.8.15
Baruch College
55 Lexington Avenue, Vertical Campus
14th Floor, Room 14-220
New York City
The Must-Attend Practitioner-Focused Tax Event of the Year
Visit nysscpa.org/tp15 or call 800-537-3635 to register!

Trust and Estate Tax Conference
Tuesday, 12.15.15
Bernstein Global Wealth Management
1345 Avenue of the Americas
New York City
Dealing with Current and Future Tax Law Changes Impacting Your Estate and Trust Administration Clients
Visit nysscpa.org/trusttax15 or call 800-537-3635 to register!
Defending a Cash Business Taxpayer in an Indirect Method Case

By Eric Smith

Taxpayers involved in cash businesses are frequently under the incorrect impression that they are audit-proof and free from risk of criminal liability when the income and deductions reflected on their tax returns match their business’s books and records. While cash businesses by their nature make demonstrating understatements of income or overstatements of expenses generally more difficult, the government has developed numerous indirect methods to overcome these issues in either an audit or prosecution of cash business taxpayers. Because these indirect methods focus on recreating the taxpayer’s income over one or multiple tax years, a professional defending such a taxpayer will usually need to painstakingly examine all of the taxpayer’s assets, liabilities, and expenditures during that period. This article will describe the most common types of indirect methods used by the government and the most frequent defenses used in defending such taxpayers.

What Is an Indirect Method?

The IRS or a criminal prosecutor may use either a direct method or an indirect method to show unreported income or improper deductions. In a direct method case, the government will use direct evidence (e.g., the testimony of witnesses with firsthand knowledge or documentary evidence) to demonstrate that the taxpayer’s return is inaccurate. The direct method is commonly called the “specific items” method, because the government seeks to demonstrate that a specific item either appearing or failing to appear on the return is erroneous. Therefore, in a criminal direct method case involving omitted income, the government will frequently call the taxpayer’s accountant as a witness to testify that the prepared returns did not include the omitted income and will provide documentary evidence demonstrating that the omitted income was attributable to the taxpayer. For example, if the alleged unreported income was interest earned in a foreign bank account, the government would have a strong case of tax evasion if it can elicit testimony that the taxpayer never disclosed the existence of the account when the accountant was preparing the returns and can produce bank account statements showing that the taxpayer was the beneficial owner of the foreign account. The direct method is the government’s preferred approach, because it is simplest, most accurate, and, according to the Internal Revenue Manual (IRM), hardest to rebut.

By contrast, in an indirect method case, the government does not have direct evidence to establish an inaccuracy on the taxpayer’s return and thus must use other means to demonstrate the error. These methods are usually used by the government against taxpayers involved in cash businesses where either no records of their receipts have been kept, or the receipts do not match the income and expenses the government alleges were attributable to the taxpayer. The evidence in an indirect method case will most often consist of bank account statements and asset statements that can be used to demonstrate that the taxpayer’s economic situation changed during the period in a manner attributable to unreported income or overstatement of deductions.

Types of Indirect Methods

The three most common types of indirect methods of proof used to prove a deficiency are—

- the net worth method,
- the bank deposits method, and
- the expenditures method.

The net worth method was the first indirect method to receive judicial approval, most prominently in the 1954 Supreme Court decision Holland v. United States (348 U.S. 121). As the name suggests, this method attempts to reconstruct income by measuring the increase in the taxpayer’s net worth during the taxable year or years by creating opening and closing net worth statements. Assets are listed on these opening and closing statements at their tax basis (as opposed to fair market value) so as to avoid including unrealized appreciation. Any increase in the taxpayer’s net worth is then reduced by all nontaxable income, such as loans and gifts received by the taxpayer during such period. This amount, after certain adjustments are made taking into account available exemp-
tions, deductions, and credits, should generally approximate the taxpayer’s taxable income. In either a criminal case or a civil audit in which the net worth method is used, the government must establish the taxpayer’s starting net worth with reasonable certainty. Otherwise, any increase could be argued to have been attributable to the liquidation of assets in the taxpayer’s possession at the beginning of the year.

Because the bank deposits method is much simpler than the net worth method, it has become the IRS’s preferred method in civil audits. In the typical bank deposits case, the government will examine deposits made into all of the taxpayer’s accounts in order to establish three essential elements: 1) unidentified bank deposits substantially in excess of reported income, 2) a starting point or opening cash balance, and 3) an ongoing business or some other taxable source capable of generating income in excess of what was reported. In civil audits, where all deposits into a taxpayer’s account are assumed to be taxable income, this third element is generally excluded.

The expenditures method involves looking at the total cash expenditures made by the taxpayer during the year and subtracting the income reported on the taxpayer’s return and nontaxable sources of income received by the taxpayer. As with the other two indirect methods, the government is also required to demonstrate a starting point and business or other taxable source of the income. Similar to the net worth method, an expenditures method case generally must begin with a determination of the taxpayer’s opening and closing net worth in order to ensure that the expenditures were not the result of sales of property held at the beginning of the period.

Defenses for Taxpayers

One of the most common defenses taxpayers can raise against an indirect method case is to question the government’s starting position (i.e., the opening net worth or opening cash balance). This “cash hoard defense” entails the taxpayer claiming that any increase in net worth or unidentified bank deposits or cash expenditures were attributable to a large amount of cash on hand that had been accumulated in prior years. The cash hoard defense is strengthened when it can be demonstrated that the taxpayer made large cash purchases during the applicable period.

Because of the frequency with which the defense is raised, a prosecutor or the IRS will generally view the claim of a large cash hoard with a great deal of skepticism, and will try to refute this claim with circumstantial evidence. Prior to raising this defense, CPAs should ensure that the claim is creditable. Specifically, the practitioner preparer needs to be able to demonstrate that the taxpayer’s income from prior years was sufficient to accumulate the claimed cash hoard and, at least with respect to a net worth or expenditures case, wouldn’t have been depleted by making cash purchases of property reflected on the government’s opening net worth statement. This defense will also likely be rejected where the taxpayer’s actions are inconsistent with having a large cash hoard. For example, making ATM withdrawals in small increments, taking out loans with high interest rates, and making periodic payments for appliances and furniture have all been cited by the Department of Justice as evidence that the taxpayer did not have a large cash hoard.

The other favored defense in an indirect method case is to claim that the source of the funds attributable to the increase in the taxpayer’s net worth, bank deposits, or expenditures was a nontaxable source. In a criminal context, the government has an obligation to investigate leads furnished by the taxpayer regarding nontaxable sources that are reasonably feasible of being checked out. In a civil audit, any nontaxable sources of income not reflected in the agent’s calculation will reduce the calculated tax liability.

The most common nontaxable sources claimed by taxpayers are gifts, inheritances, borrowed funds, or loan repayment. CPAs must also be on the lookout for other increases in assets arising from gains that are either nonrecognized or partially recognized under the Internal Revenue Code. These include the sale and acquisition of a residence or an installment sale, as well as an increase in receivables that is not deemed income during the period due to the taxpayer’s method of accounting (e.g., cash basis).

Even where the sources are taxable, CPAs may be able to argue, in either a criminal case or in a civil audit, that the increases are attributable to sources that, although taxable, would not have been readily apparent to the taxpayers. This could demonstrate noncriminal intent or indicate that fraud was not present. For example, a nontaxable condemnation award may include taxable interest that was not separately stated and therefore easily overlooked.

Protecting Taxpayers

The IRS and state tax authorities have developed several indirect methods of proof that can be used against taxpayers with cash businesses. By their nature, these indirect methods rely on circumstantial evidence to demonstrate that the taxpayer has underreported income or overstated deductions; this makes them potentially overbroad while, at the same time, susceptible to the defenses described above. CPAs advising such professionals should keep such strategies at hand if an audit or legal action arises.

Eric Smith, JD, is an attorney at Kostelanetz & Fink, LLP, New York, N.Y.
Many tax professionals overlook the New York City tax on rent paid by tenants to their landlords for occupancy of commercial premises. On numerous occasions, the authors have explained the city’s commercial rent tax (CRT) filing and remittance obligations to a client—and they responded, “We are the tenant paying rent; we are not the landlord. Are you serious?”

Unfortunately, many commercial tenants are unaware of the city’s CRT, presenting a significant tax risk. It is especially important to understand the CRT, because the Department of Finance is currently scrutinizing this area closely, using enhanced matching programs to identify non-filers. This article will provide an essential overview of the city’s CRT.

Overview

The CRT is imposed on tenants for the occupancy or use of property for commercial activity in certain parts of Manhattan. A CRT return is due, and a tax remittance may be required, when a taxpayer 1) rents space for any trade, business, profession, or commercial activity below 96th Street in Manhattan; 2) pays annual or annualized gross rent of at least $200,000; and 3) does not qualify for any of the available exemptions. When tax is due, the taxpayer is responsible for filing three quarterly returns and an annual return to report the full year’s activities. The CRT operates on a fiscal tax year of June 1 through May 31. See the Exhibit for the filing deadlines.

For CRT purposes, a taxpayer is renting space, or is deemed a “tenant,” if the requirements outlined above are met and the taxpayer is paying rent as a lessee, sublessee, licensee, or concessionaire. CRT may also be due if the space is occupied in a building owned by a party related to the taxpayer, such as the following:

- Family member (i.e., a spouse or parent)
- Joint owner of the property
- Corporation of which the taxpayer is an officer or shareholder
- Property owned by a subsidiary or parent corporation
- Officer or stockholder.

Occupancy or use of property also includes the rental of billboards that are placed in the taxable CRT area and meet the above-noted criteria for being subject to CRT.

Computation of CRT

Gross rent is the starting point of the CRT computation. Gross rent includes the fixed rent per the lease, the tenant’s required payments on behalf of the landlord for real estate taxes, water rents or charges, sewer rents, or any other expenses normally payable by the landlord of the property. Expenses for improvement, repair, or maintenance of the rented space are not included. In the event that rent is either wholly or partially measured by a percentage of gross receipts from sales generated from the premises or rented space, the gross rent will be, at a maximum, 15% of the total gross receipts for the period.

Once gross rent has been determined, taxpayers may be allowed deductions for arriving at base rent. Deductions from gross rent include rent paid by a subtenant, as well as any exemptions allowed under the City Commercial Revitalization Program. The resulting base rent is used to determine whether a tax remittance or filing obligation exists. If the base rent is between $200,000 and $250,000, the taxpayer will have a filing obligation, but the tax rate will be 0%. If the base rent (as determined above) is $250,000 or more, the taxpayer will have a filing and payment obligation. Once the base rent has been computed, taxpayers are then entitled to deduct 35% of their rental payments from such base rent in arriving at rent subject to tax. The resulting amount is subject to tax at a 6% rate.

When computing CRT, it is important to understand that if more than one property is rented by the same tenant in Manhattan below 96th Street, the applicability of the tax and total tax liability is determined for each location. For example, if a tenant leased multiple floors within one location, the total base rent must be aggregated to determine the base rent subject to CRT and whether a CRT return is due.

New York City Commercial Rent Tax

Avoiding Traps for the Unwary

By Corey Rosenthal, Arvinder Kaur, and Patrick Duffany

many tax professionals overlook the New York City tax on rent paid by tenants to their landlords for occupancy of commercial premises. On numerous occasions, the authors have explained the city’s commercial rent tax (CRT) filing and remittance obligations to a client—and they responded, “We are the tenant paying rent; we are not the landlord. Are you serious?”

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- Family member (i.e., a spouse or parent)
- Joint owner of the property
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When computing CRT, it is important to understand that if more than one property is rented by the same tenant in Manhattan below 96th Street, the applicability of the tax and total tax liability is determined for each location. For example, if a tenant leased multiple floors within one location, the total base rent must be aggregated to determine the base rent subject to CRT and whether a CRT return is due.
In addition, taxpayers whose base rent falls within $250,000 and $300,000 will receive a tax credit against the CRT due, reducing the tax rate below 6%.

**Exemptions**

Taxpayers who meet any of the following exemptions do not have a CRT filing or payment obligation:

- The taxpayer’s annualized base rent is less than $250,000 before applying the 35% rent reduction, and the taxpayer qualifies for the City Commercial Revitalization Program special reduction. As noted above, taxpayers are still required to file a CRT return if their annual gross rent is more than $200,000.
- The taxpayer is renting the premises for 14 days or less during the tax year.
- The taxpayer (other than hotel operators) uses at least 75% of the floor space to rent to others for residential purposes.
- The taxpayer is a governmental body or nonprofit religious, charitable, or educational organization. Other nonprofit organizations will be exempt if they receive a written tax exemption from the Department of Finance and the property is not used for commercial purposes.
- The rented property is located in the World Trade Center area.
- The rented property is located in the City Commercial Revitalization Program abatement zone and is being used for retail sales purposes.
- The taxpayer is a theatrical production that qualifies for an exemption for the first 52 weeks after production begins.

**Other Considerations**

**Tax rate.** As noted above, the CRT rate is 6% of the base rent; however, a 35% rent reduction is allowed for all taxpayers. Considering this rent reduction, the actual effective tax rate on base rent is 3.9%. In addition, a tax credit is allowed if the annualized base rent before the 35% base rent reduction is between $250,000 and $300,000.

**Commercial Revitalization Program (CRP).** The law provides incentives to certain businesses that relocate to the designated commercial revitalization zone in downtown Manhattan. The benefits are based on the length of the lease, type of lease, and capital expenditures made with respect to the qualifying leased space. An application must be completed in order to receive the incentives. Under this program, two types of benefits are received: The first is an abatement of real estate taxes that are passed through to the tenant by the landlord, and the second is a reduction to the gross rent that would otherwise be subject to CRT.

**Matching programs and audit risk.** Since 2011, the general corporation and unincorporated business tax returns specifically ask whether CRT returns are due; if so, they determine whether such returns have been filed.

Tax preparers should determine whether taxpayers are required to file CRT returns in order to properly respond to these two questions. Furthermore, all taxpayers should evaluate their rental activities below 96th Street in Manhattan to determine whether a liability exists. If the two additional questions regarding the CRT are answered “no,” or left blank, the Department of Finance will generally initiate an inquiry.

In addition to the above method of selecting audits, it is the authors’ understanding that the department also utilizes real property income and expense statements that are filed by landlords to report income and expenses for the property they own. This reporting generally includes a list of tenants and how much income is received from these tenants as rental income.

**Voluntary Disclosure and Compliance Program.** The city’s Voluntary Disclosure and Compliance Program (VDCP) provides CRT nonfilers with the opportunity to come forward voluntarily to rectify any past noncompliance issues while providing penalty abatement and, in many cases, a limited look-back period. Voluntarily coming forward and entering into an agreement with the department can result in significant savings, but timing is always essential with such programs. If the department contacts a taxpayer prior to its representative reaching out voluntarily, the taxpayer will not be eligible for the VDCP. As a result, the taxpayer will be subject to penalties, which could be as much as 50% of the tax due, plus applicable interest.

**Take Notice**

All CPAs with clients (or their own businesses) operating below 96th Street in Manhattan should remember to evaluate whether a CRT liability exists. If so, they should remember the aggressive stance taken by the Department of Finance’s audit division towards finding non-CRT filers.

Corey Rosenthal, JD, is a principal, Arvinder Kaur, CPA, is a manager, and Patrick Duffany, CPA, is a partner, all at CohnReznick LLP.

**EXHIBIT**

**Required Filings**

<table>
<thead>
<tr>
<th>Form</th>
<th>Period</th>
<th>Due Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>CR-Q1</td>
<td>Jun. 1–Aug. 31</td>
<td>Sep. 20</td>
</tr>
<tr>
<td>CR-Q2</td>
<td>Sep. 1–Nov. 31</td>
<td>Dec. 20</td>
</tr>
<tr>
<td>CR-Q3</td>
<td>Dec. 1–Feb. 28</td>
<td>Mar. 20</td>
</tr>
<tr>
<td>CR-A</td>
<td>Jun. 1–May 31</td>
<td>Jun. 20</td>
</tr>
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Note: No quarterly returns are required when no tax is due.
Virtually all of a CPA’s clients have some sort of financial investment. This could be a money market fund or savings account, or a 401(k) or 403(b) account with their employer. These may not traditionally be thought of as investments, but they are—and individuals need assistance on what to do and how to build a portfolio to accomplish their goals.

**Goals**

Before crafting an investment plan, it is necessary for individuals to define their goals and objectives. CPA financial planners should explain to clients that this is the first step in developing a sound investment strategy. The process includes the following:

- Determining a time frame, be it 1 year, 8 years, or 20 years
- Setting cash flow targets, including sources of cash (i.e., income) and expenditures
- Establishing an adequate rainy day fund
- Devising a method to preserve assets while ensuring reasonable growth consistent with projected needs
- Not taking unnecessary risks.

Goals in personal investing and wealth management should be driven by projected cash flow requirements and not by the acquisition of wealth. Planning should be focused on attaining a fund that will provide cash flow adequate to secure the individual’s needs. Too many people lose sight of the purpose of their assets and take excessive risks to accumulate additional assets when the increased amounts would not change their financial situation one iota—but a modest loss would cause a curtailing of planned activities. CPA financial planners should transmit to clients that “losses usually hurt more than gains benefit” and that realistic goals should lead their decisions. Once that is done, assistance with asset allocation and location can start.

**Asset Allocation**

Asset allocation is a method of apportioning investments to help accomplish investing goals. The object is to balance investments so that the overall portfolio growth and cash flow objectives will be attained, consistent with a level of risk that needs to be assumed and is acceptable to the client. Asset allocation should be done for long-term (a minimum of seven years) portfolios. This allows for some degree of the market’s inevitable ups and downs to balance out. It also allows compounding to work its wonders. If the time horizon is shorter, different criteria should be used, as the asset allocation methods suggested in this article will not apply.

Asset allocation needs to be individually tailored. An allocation plan for someone age 40 would be completely different from a plan for someone age 70 with the same amount of funds to invest. Irrespective of what is suggested, CPAs should assist their clients in assessing their risk tolerance; if they are not comfortable or are insecure with a category, then it should be forgone. Nevertheless, in such situations, CPAs should then endeavor to learn more about the client’s insecurities so they can give the category a fair chance to become part of the portfolio.

Asset allocation is about arranging investments. It is not about organizing all of one’s assets—although that is never a bad idea. For that reason, it is suggested to not include rainy day funds, homes, rental property, businesses, collectibles and other assets that do not generate cash flow, are illiquid, or are set aside for a specific purpose. To the extent some of these investments are sensitive to inflationary growth, they should be considered in the asset allocation mix, perhaps with a greater allocation toward fixed income. Debt is not part of asset allocation and should be paid down as sensibly as possible before committing funds to a long-term path.

**Two Major Categories**

For most individuals, two broad categories in 25% increments are all that is needed. It is easy to grasp, much less confusing, and it works. As portfolios change, percentages can be refined, adjusted, or reproportioned. Too many choices thwart a clear understanding of what the client is doing and hide the true risks. The two broad categories are stocks and fixed income (i.e., bonds and CDs). The five broad allocation choices are as follows:
With rare exceptions, it is not prudent for most people to completely exclude either stocks or fixed income, which would leave them exposed to excesses that can occur. For instance, if all the funds were in bonds and rates dropped significantly on reinvested funds, cash flow would drop and the investor would not have any ability for sustainable growth in asset values. If all the funds were in stocks, it would indicate a very aggressive posture that is not prudent for long-term financial security.

The next option—50% of each—is a good middle ground for many people. It provides for half the assets providing a guaranteed cash flow and the other half the ability to grow along with growing dividend payments.

The other choices tend toward either end of the spectrum with a 75/25 split—75% in stocks represents an aggressive posture, while 25% in stocks indicates a more conservative attitude with a desire for greater guaranteed cash flow with less risk of loss.

**Diversification**

A goal of asset allocation is to minimize risk by dividing investments to a portion that will grow over time as well as dividends that will also grow, and fixed income investments that will provide a steady and somewhat guaranteed cash flow, but which will not grow. Within each category there should be diversification, so that not too much weight or dependence is placed on any one issue or sector. How this is achieved differs for stocks and fixed income.

**Stocks.** Stocks can be diversified through the ownership of a combination of large mutual, index, or exchange traded funds. When considering the funds there should be a mix between large- and small-cap companies and those with possible international exposure—although about 40% of the revenues of the 500 largest U.S. companies are derived from outside the United States, providing a global element to such an investment.

**Fixed income.** Fixed income is more difficult to invest in. For shorter terms, insured bank certificates of deposit serve needs up to five years, but for higher yields, investors need to venture into bonds with longer terms, up to 20 or more years. Bond funds carry great risks of loss as interest rates increase, and there is no fixed maturity date. Typically, fixed-income investors look for safety and bond funds do not provide this. Contrarily, longer-term bonds that have the same risks of declining on rate rises are less risky if the intention is to hold the bonds until maturity and the investor has the ability to do this. If there is a threat that the bonds might need to be sold beforehand, then they should not be considered. One suggestion for bonds is to create a ladder stretching to perhaps 20 years; the longer the term, the greater the interest payments will be. To illustrate, divide an investor’s fixed-income funds by 20 and have that amount come due each year for the 20 years. Each year, a choice can then be made with that 5% of your fixed income funds: spend it, invest it elsewhere, or continue the ladder with a new 20-year bond. Reinvesting for 20 years will result in higher rates than the one that came due, increasing the portfolio’s cash flow. The authors suggest a caution: individual bonds should not be more than 10% in any one company, and no more than two companies should be in any one sector. This is not an easy plan to implement, but most traditional brokers can help clients implement such an arrangement. After a client buys the bonds, she should sit tight and hold them to maturity.

**A Path to Security**

Asset allocation presents a method of investing that provides balance consistent with long-term financial goals and risk tolerance. It is a tool that needs to be considered. Many decisions need to be made to implement a sound plan, and CPA financial planners should be the primary advisor to lead their clients on a path to financial security.

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The defendants in retirement plan fiduciary lawsuits—including directors and officers—often argue that they have no liability because they are not expressly named or appointed as plan fiduciaries. Courts, however, have routinely rejected these arguments based upon the extension of fiduciary liability under the Employee Retirement Income Security Act of 1974, as amended (ERISA) to functional fiduciaries who exercise authority or control over plan management.

A director or an officer may be a plan fiduciary with respect to certain matters but not to others, because fiduciary status is established only “to the extent” the person exercises authority or responsibility over plan assets or plan management. Courts do not distinguish between named fiduciaries and functional fiduciaries. Moreover, a plan fiduciary would be liable for the breach of fiduciary responsibility of another fiduciary, with respect to the same plan, if that plan fiduciary enabled the other fiduciary to commit a breach (if he has knowledge of the breach and makes no reasonable effort under the circumstances to remedy it).

Taking Action

Directors and officers acting, or deemed to have acted, as an ERISA fiduciary are strongly encouraged to take action to remedy perceived improprieties in actual plan operation in order to avoid personal liability. Cofiduciary liability is considered joint and several liability; therefore, plan fiduciaries are personally liable for breaches of duty. Courts have systematically found that a fiduciary has an ongoing duty to monitor the activities of a cofiduciary they have appointed or to whom they have delegated duties.

Courts have rejected the argument that individual directors who are named fiduciaries were no longer liable for fiduciary breaches because they had delegated their authority to a plan committee. Rather, plan fiduciaries delegating substantial authority appear to retain a substantive level of fiduciary responsibility, and possibly residual responsibility, which could subject them to liability for a breach of fiduciary duty. Courts are reluctant to discharge named fiduciaries from liability when damages to a plan are alleged; see, for example, Defazio v. Hollister, Inc., 2008 WL 958185 (E.D. Cal. Apr. 8, 2008), or Briscoe v. Fine, 444 F. 3d 478, 486–87 (6th Cir. 2006).

Although cases do not generally discuss the scope and frequency of required performance reviews, courts have determined that an annual review of the performance of plan committee fiduciaries is sufficient to adequately discharge the duty to monitor. Nevertheless, the facts and circumstances may dictate more frequent and extensive reviews.

A Board's Responsibility

Courts recognize that corporate boards achieve greater efficiency by allocating specific responsibilities and delegating specific duties to specialized committees. Courts do not require boards to monitor a committee's individual decisions, which would undermine the rationale of creating specialized committees to govern effectively.

Because the primary exposure for companies and their boards and officers arises under ERISA, lawyers continue to create new theories to assign ERISA liability to directors and officers based upon the functional definition of fiduciary. Accordingly, boards and management need to understand how they can avoid fiduciary liability under ERISA.

Directors and officers who appoint plan committees have a duty to monitor their activities. Similarly, officers who hire employees to serve as plan fiduciaries also create a duty to monitor the activities of these employee fiduciaries.

A corporate director or an officer who exercises discretionary authority or control over fiduciary conduct is held to a fiduciary standard, but being an individual who is a director or an officer does not de facto make one a fiduciary. Nevertheless, courts have found that employers have sufficient control over plan assets and over fiduciary decision making to be considered a co-fiduciary.

ERISA—not common law agency principles—defines whether a company, and therefore its board of directors, is liable for its employees’ actions. The duty to monitor requires the appointing fiduciary to follow a process to peri-
Periodically review the performance of the appointed fiduciary. Note that ERISA emphasizes the decision making process, not whether (in hindsight) the proper or best decision was made on behalf of the plan.

Lone Agents

In many instances, courts that have recognized a breach of the duty to monitor have also identified the fiduciary as participating in the fraud, self-dealing, or exercising influence over the fiduciary’s decisions. Appointment power includes the duty to monitor and creates liability for cofiduciary breaches.

A director, officer, or employee who acts as an ERISA fiduciary does not act as an agent of the employer, and thus will be liable for any breach of fiduciary duty. Plan obligations are different than corporate obligations: For example, a corporation can be sued for failing to meet an obligation (i.e., pay a debt), whereas directors and officers can be sued personally for failing to meet an obligation to plan participants.

Fiduciary Duties

Plan fiduciaries must, as a matter of law, act in the best interest of the plan and for the exclusive benefit of plan participants. A corporation may receive an ancillary benefit, provided plan fiduciaries follow this exclusive benefit rule and comply with the duties of loyalty and prudence. These duties require 401(k) plan fiduciaries to avoid using plan assets to pay excessive fees; diversify plan asset investment by offering a diversified investment menu; and continue to monitor investment menu alternatives, including mutual funds, separate accounts, stable value funds, and employer securities.

The standard directors and officers (D&O) liability insurance policy does not customarily cover claims against directors and officers acting in their capacity as ERISA fiduciaries. Fiduciary liability policies are designed to cover a company, its directors and officers, all of its employees, and its retirement plans against loss for breach of fiduciary duty and wrongful administration.

Nevertheless, the cost of defending a lawsuit is significant, and therefore insurance is strongly recommended for any director or officer making fiduciary decisions. Claimants may allege errors in judgment, breaches of duty, or wrongful acts related to the D&O organizational activities. Wrongful administration includes any wrongful act, negligent errors and omissions in the administration of a retirement plan, selection of inappropriate advisors or service providers, and a failure to monitor plan asset investment alternatives.

Serving Two Masters

Directors and officers acting as plan fiduciaries serve two masters: the corporation and the plan. Accordingly, directors and officers need to avoid engaging in a prohibited transaction providing the corporation or themselves with a benefit, such as a release of claims using plan assets or leveraging plan assets.

In some cases, boards and officers have been found liable for a breach of fiduciary responsibility as a result of a sudden and significant downturn in a company's stock price when employer securities are held by a plan. Boards and officers have been found liable for a breach of fiduciary responsibility as a result of the payment of excessive fees with plan assets. Many lawsuits have been filed against companies and plan fiduciaries because of their alleged mismanagement of fees charged by plan service providers.

To avoid or minimize fiduciary liability, employers should consider appointing independent fiduciaries to manage and monitor the plan’s investment menu, the plan’s fee arrangements, and the plan’s investment in employer securities. These independent fiduciaries should have no actual or perceived relationship with the company, or its directors and officers, and these fiduciaries should assume responsibility for plan investment and plan administration.

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Tax-related identity theft is the use of the personal identifying information of another person to file a false tax return for the purpose of obtaining a fraudulent refund. Quite often, taxpayers first become aware that their identity has been stolen when they attempt to electronically file their tax return. Tax preparers are on the front lines, as indicated by the 2015 tax software survey. More than half of survey participants experienced minor problems with e-file rejections due to identity theft, and another 11% reported significant problems.

In its 2016 “Objectives Report to Congress,” the Taxpayer Advocate Service reported that the IRS stopped processing more than 3.8 million suspicious tax returns as of May 31, 2015, and almost 700,000 identity theft cases were still open as of that date. It can take six months to one year for the IRS to resolve identity theft cases; unfortunately, more than 20% have been closed prematurely.

The high levels of identity theft occurrence followed by slow resolutions make it imperative that tax practitioners and taxpayers know what resources are available to them.

Identity Theft Resources

IdentityTheft.gov (http://www.identitytheft.gov) is a good place for CPAs to start. It provides checklists that allow users to select steps or issues and drill down to further resources and external links. The stages for resolving tax-related identity theft include calling the IRS right away if an IRS notice was received, and completing IRS Form 14039, “Identity Theft Affidavit.”

The information on reporting a misused Social Security number contains links to the online application for a new card. Sample letters are available for communicating with credit card companies, obtaining records about the identity theft, and dealing with debt collectors.

The Federal Trade Commission Consumer Information webpage on identity theft (http://www.consumer.ftc.gov/features/feature-0014-identity-theft) offers community resources, such as brochures on “Identity Theft: What to Know, What to Do” and “Identity Theft: What to Do Right Away.” The FTC also offers a 68-page book, Taking Charge: What to Do If Your Identity Is Stolen, that provides detailed information on how identity theft occurs, how to reduce risk, and how to address the problems that arise, including sample letters, an identity theft victim’s complaint and affidavit form, and an annual credit request form (https://bulkorder.ftc.gov/system/files/publications/pdf-0009-taking-charge.pdf).

The FTC also provides a tax-related identity theft web page, although the tax-related information can also be accessed under the general identity theft materials (http://www.consumer.ftc.gov/articles/0008-tax-related-identity-theft).


Larger publications provide more detailed information for tax preparers. For example, Publication 1345, “Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns,” is a 60-page guide for electronic return originators that addresses implementing security and privacy standards, safeguarding the e-file system from fraud and abuse, and verifying taxpayer identification numbers, as well as including all of the practical policies and procedures of the e-file program (https://www.irs.gov/pub/irs-pdf/p1345.pdf). Publication 4557, “Safeguarding Taxpayer Data,” a 12-page booklet that explains how to protect taxpayer data and report breaches, includes a thorough checklist plus links to standards and best practices.

on the public-private partnership known as the Security Summit, which was formed to develop methodologies to detect and prevent identity theft.

The Treasury Inspector General for Tax Administration (TIGTA; http://www.treasury.gov/tigta) offers a useful two-page brochure, “Victim Assistance Related to Identity Theft” with a listing of 10 contacts, from the IRS Identity Protection Specialized Unit to the National Organization for Victim Assistance (https://www.treasury.gov/tigta/docs/Victim%20Assistance%20Related%20to%20Identity%20Theft.pdf). The easiest way to find TIGTA’s information on identity theft is to pull up the press releases under the Publications link. The website includes a dedicated contact page to report the impersonation of an IRS representative—scams which have cost taxpayers over $14 million in the past two years (https://www.treasury.gov/tigta/contact_report_scam.shtml).

TIGTA’s “Results of the 2015 Filing Season” is a downloadable 34-page report that covers several key areas of focus, such as the effect of tax law changes on the 2015 filing season, comparative statistics for 2015 and 2014, and an analysis of key tax provisions for 2015. The document discusses the decline in the number of confirmed identity theft returns from 380,000 in 2013 to 140,000 as of April 30, 2015. The reason for the decline is the stronger rejection filter that prevents suspicious returns from being processed. This is good news for the general public, but bad news for any taxpayers whose truthful tax returns were rejected (https://www.treasury.gov/tigta/auditreports/2015reports/201540080fr.pdf).

The Social Security Administration (http://www.ssa.gov) offers an eight-page downloadable brochure (SSA Publication 05-10064), “Identity Theft and Your Social Security Number,” that describes common tactics for stealing Social Security numbers, how to review work history with the SSA to check for false wage reports, and contact information for several organizations. Most importantly, the brochure explains when and how to apply for a new Social Security number (http://www.socialsecurity.gov/pubs/EN-05-10064.pdf).

The Identity Theft Resource Center (http://www.idtheftcenter.org) is a nonprofit that provides no-cost assistance for victims of identity theft. The ITRC website offers victim help, identity theft protection tips, and consumer information. The organization also strives to educate individuals and businesses, and promote best practices for fraud and identity theft detection, reduction, and mitigation through the use of articles, surveys, and white papers. The website materials include an extensive collection of fact sheets and tip sheets, with links to further information. The ITRC also offers a free ID Theft Help mobile application for both iOS and Android that provide much of the website’s information, as well as connects users to ITRC advisors (http://www.idtheftcenter.org/itrc-app.html).

Due Diligence

While the AICPA’s Statements on Standards for Tax Services and the IRS’s Circular 230 allow tax preparers to rely on information furnished by clients, there is still a presumption of due diligence, as well as common sense. Tax professionals don’t want to find themselves unwitting parties to the commission of tax fraud, especially given the incredible growth in the identity theft “industry.” Tax preparers may even face professional liability in connection with identity theft (Sandra S. Benson, “Aiding and Abetting Fraud by Filing False Tax Returns,” The CPA Journal, April 2014, pp. 50–55).

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Private sector payroll, as reported by ADP, improved in September, with a gain of 200,000 jobs; however, the August total was revised downward, from 190,000 jobs to 186,000. So far this year, net job growth has averaged 195,000 per month, which is about twice what is needed to keep pace with the growth in the working age population. Goods-producing employment rose by 12,000 jobs, while service providers added 188,000 jobs. Low oil prices are still causing energy producers to cut back and detract from the job gains other economic sectors have seen. Moody’s Analytics expects payroll employment gains averaging near 200,000 per month through the end of this year and accelerating to well over 200,000 in 2016.

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It’s Amazing What CPAs Can Do

Pension Consulting Is an Old Practice, but a New Specialty

By Matthew Gaglio

I thank my father for giving me a clear understanding of the value of qualified pension plans. His career path led him to a general agency with New England Life that also specialized in pension administration, and he became a “pensioner.” His knowledge served as the bridge to my focus on wealth preservation through qualified plans, particularly their use as a catch-up tool and tax shelter.

A Chance Meeting

Although this knowledge was always with me, my defining moment took place 23 years ago when I met an individual who had just reviewed his current year’s joint tax return with the couple’s CPA. He told me that his CPA advised him to just pay the tax due, because his business was profitable. I didn’t agree with this strategy, so I suggested a bifurcated defined benefit/defined contribution 401(k) plan for him and his spouse. As a result, I was able to generate $150,000 in annual contributions for them. I will never forget that day, since it changed the course of my career. If it were not for some minimal level of understanding surrounding qualified retirement plans, my chance meeting with that individual would have amounted to nothing more than a dinner acquaintance. Instead, it was a lost opportunity for his CPA, who was ultimately relieved of his services and lost out on years of tax returns for my new client’s multiple businesses, and the likely referrals that would have followed.

Losing a Valuable Skill

In 1992, CPAs did not view a qualified retirement plan as a resource for tax planning because they were not taught to. At one time, CPAs were instrumental in helping small business owners create retirement plans for themselves and their employees. They worked closely with pension specialists and actuaries to develop a plan strategy to meet the unique goals and objectives of each client, remaining involved year after year to review annual limits and laws to ensure the plan was delivering the maximum tax benefits. This began to change with the Tax Reform Act of 1986, which eliminated many of the incentives for small businesses to provide pension plans. As a result, CPAs and other financial advisors began removing themselves from the process.

By the time of the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001, which worked alongside other legislation to bring the focus back to customized tax design, the damage had been done. The “producer” group (i.e., attorneys, CPAs, insurance representatives, actuaries and investment advisors) was fragmented, with only a handful of people remaining who remembered and understood the importance of tailored plan design.

Without a bridge like the one I had from my father, the connection to EGTRRA’s enhancements is gibberish to many of today’s CPAs. To them, retirement planning is nothing more than products sold and administered by others.

Finding the Way Back

Industry experts agree that the greatest wealth transfer in American history will take place over the next 10 years. As advisors—whether CPAs, pension experts, or insurance representatives, or others—our ethical responsibility is to help our clients protect that wealth. While this certainly includes safeguarding assets from the Bernie Madoffs of the world, it also involves preserving as much of that wealth as possible for the next generation. The only way to do that is to work together on behalf of our clients.

The last three decades have left many business owners and their employees largely on their own when it comes to retirement planning. They have suffered from a serious lack of advocacy, left to rely on 401(k) plans, IRAs, and other assets under management (AUM) plans to safeguard their future safety net. These “one-size-fits-all” designs simply do not adequately preserve wealth.

But the qualified retirement plan is making a comeback, and I would argue that CPAs should make a comeback as well. Our clients want and deserve expert guidance. They want to know someone they trust—someone who knows what’s important to them—is looking out for their financial well-being.

At my firm, we take a personal, hands-on approach to retirement planning. For us, retirement planning should never be product driven. Instead, plans should be designed first around individual goals; products should be discussed only after these factors are defined.

All aspects of financial planning have tax implications, and no one knows an individual’s needs, risk exposures, and hopes for the future better than their CPA. By taking a more strategic role in the retirement planning process and working hand-in-hand with a team of other professional advisors, CPAs can help their clients effectively maximize tax benefits for the short term, while ensuring they are able to pass on a greater portion of their accumulated wealth. This, in turn, will result in a happier, more loyal client base, helping CPAs strengthen and grow existing accounts and win new business.

Matthew Gaglio is a registered representative and financial advisor of Park Avenue Securities LLC (PAS).
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