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Newsletter of the AICPA
Business Valuation and
Forensic & Litigation Services Section

What's Inside

Valuing Employee Stock Options

By Carolyn Worth, CPA/ABV

A revision in the accounting standards, Financial Accounting Standards Board (FASB) Statement No. 123 (revised 2004), *Share-Based Payment,* requires employee stock options and other share-based compensation awards to be expensed for financial reporting purposes. This revision has a profound effect on corporate earnings by moving the expense out of the fine print and onto income statements. Therefore, it is critical that all companies—whether they are public, private, or venture capital—understand how "share-based payments" should be valued.

Stock options enable employees to buy their company shares at a fixed price within a specified period. Many companies have leveraged stock options as a method of compensating employees in a manner that did not result in a cash outlay and, in most cases, without a charge to a company's earnings.

Before the revised FASB ruling, companies had the option of recording the estimated value of employee stock options (ESO) and employee stock purchase plans (ESPP) as simply a footnote. Now that the fair value of options must be deducted from earnings, this revision can dramatically change a company's picture of profitability. FASB Statement No. 123 (revised 2004) went into effect for public companies for annual periods beginning after June 15, 2005 and for nonpublic companies for annual periods beginning after December 15, 2005.

Since most employee share options lack an actual market price, companies must use a valuation model to assign a value to the award. Corporate America has been actively debating the best valuation models for years, but the FASB decided against imposing any particular method. While there is no single "best method," the Black-Scholes-Merton (BSM) model is the model of choice for most companies implementing the new standard. In certain situations, some companies may be able to obtain sufficiently reliable data to populate a more robust lattice or binomial model, but the historical data should be specific enough to provide a reasonable basis to support key assumptions that predict future employee behavior.

Although the debate will continue over the difficulty of valuing employee stock options, authoritative guidance from the Securities Exchange Commission (SEC) provides important guidelines to help minimize diversity in implementing the new ruling. Companies should be prepared for increased scrutiny around this accounting estimate and should take special care in developing the assumptions to estimate the fair value of share-based payments.

With FASB compelling companies to reflect options in the bottom line, many companies may reconsider their overall compensation practices. One strategy being used to reduce the compensation cost of employee options is to shorten the term of the options. For most companies, stock options will be a smaller portion of compensation in the future. We may see a shift away from issuing stock options, and a trend towards replacing those stock options with restricted stock grants and the use of performance-based equity incentives.

Implementing the Valuation of Employee Stock Options

Companies must recognize the fair value of employee options and other forms of share-based payments in the income statement. The guidance covers:

- Selection of valuation model
- Treatment of market conditions
- Factors to consider in developing key assumptions

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Companies must use a valuation model that reflects the substantive characteristics of the award and assumptions that marketplace participants would use to value the award. Although the statement expresses no preference for the valuation model, most companies continue to use the Black-Scholes-Merton model (BSM) rather than other models such as the binomial lattice model. In valuing employee stock option grants, the FASB requires an option pricing model to take into account:

- Stock price at grant date
- Exercise price
- Expected dividend rate for the expected term of the option
- Risk-free rate for the expected term of the option
- Expected volatility for the expected term of the option
- Expected term

The SEC issued Staff Accounting Bulletin (SAB) 107, *Interaction Between FASB Statement No. 123 (revised 2004), Share-Based Payment, and Certain SEC Rules and Regulations Regarding the Valuation of Share-Based Payment Arrangements for Public Companies*, to provide additional guidance on valuation techniques and assumptions. Two inputs to the BSM, expected volatility and term, received particular attention in the bulletin because of their impact on value and the judgments involved in their estimation. In determining expected volatility, companies generally should consider both historical and implied volatility, if they are available. The bulletin notes that if specific criteria are met, the SEC staff will not object to companies placing exclusive reliance on implied or historical volatility.

In developing the expected term input, SAB 107 confirms that it should be based on historical experience. Where historical experience is not sufficient or not representative, an alternative simplified measure for "plain vanilla" awards (which are very common) is offered. In addition, expected term should be evaluated for groups of employees which exhibit similar exercise behavior—as few as one or two groupings may be appropriate.

Although an option's value is most sensitive to the expected volatility and expected term inputs, problems can arise with respect to any of the inputs. The table below summarizes typical challenges related to the key assumptions to the BSM.

Neither forfeiture nor discounts for lack of marketability should be incorporated in the calculation of fair value using the BSM model. The forfeiture rate is used to adjust the number of options in the amortization of book compensation expense *after* the fair value estimate of a single option is calculated. According to the FASB, any discount for lack of marketability or hedgeability during the vesting period is already reflected through the use of the expected term rather than the contractual term as an input to the valuation model; no additional adjustment should be applied.

Carolyn Worth, CPA/ABV is a partner with KPMG LLP, San Francisco, California.

Key Assumptions	*What to Look Out For*
Expected Volatility	• Implied volatility not considered • Look-back period for historical volatility shorter than expected term • Periods of high volatility selectively excluded • Exclusive reliance on implied volatility when traded options do not meet SAB criteria
Expected Term	• Unexercised options not included in calculation • Historical data not representative of current grant pool—especially when a company changes its grants to include different conditions (such as performance conditions) from those issued previously • Historical data excluded without adequate support • Sample of historical data insufficient for a reliable estimate • Separate employee groups not considered • Use of data from academic studies • Use of factors in lattice models or simulations to forecast early exercise not supported by historical experience or not statistically significant
Expected Dividends	• Historical patterns not considered
Risk-Free Rate	• Rate not based on zero coupon U.S. Treasury instruments • Remaining term of instrument not equal to expected term

Executive Stock Options and Fraud

The likelihood of financial misrepresentation increases substantially when two factors are present: extremely low performance relative to average performance in the firm's industry and high percentages of CEO compensation in stock options. This is the conclusion reported by Jared Harris of the Darden Graduate School of Business Administration at the University of Virginia and Philip Bromiley of the Merage School of Business at the University of California, Irvine. Harris and Bromiley presented their finding in a recent issue of *Organization Management*, a publication of the Institute for Operations Research and the Management Sciences (http://www.informs.org).

The authors examined financial restatements announced between January, 1997 and June, 2002. The 919 restatements were prompted by accounting irregularities, which the U.S. Governmental Accountability Office (GAO) said resulted from "aggressive accounting practices, misuse of facts, oversight, or misinterpretation of accounting rules and fraud."

Professor Bromiley explains, "Millions and sometimes tens of millions of dollars worth of CEO compensation ride on these stock options. That's enough to motivate some executives to deliberately fudge the books so that stock prices go up." Bonuses, however, had little influence on misrepresentation.

The authors also identify firms with massive losses relative to their assets as likely to misrepresent their financials.

Good Governance Policies for Charitable Organizations

Nonprofits, especially charitable organizations, face the challenge of preventing misuse of assets. The Internal Revenue Service (IRS) offers guidance for addressing this challenge in its recently issued discussion draft "Good Governance Practices for 501 (c) (3) Organizations."

As nonprofit organizations continue to grow, so does their need for professional and managerial skills. According to a recent Conference Board report, the talent shortage many for-profit companies are dealing with is also having an impact on nonprofit organizations. As with for-profits, nonprofits will need to deal with the exit of baby boomers from the work force into retirement. However, the same baby boomers may also offer opportunities to nonprofits to meet their talent needs.

The nonprofit sector is being hard hit, according to Jill Casner-Lotto, author of the report, "Boomers are Ready for Nonprofits, But Are Nonprofits Ready for Them?" (The Conference Board Report number is E-0012-07-WG.) Casner-Lotto says, "While growth in the nonprofit sector is outpacing growth in the rest of the economy, talent shortages are already affecting critical service sectors, including health care and social services, in which nonprofits are heavily represented. Also, widespread executive-level and leadership skill shortages currently affecting many nonprofits are predicted to worsen as the sector expands and experienced executives retire."

Nonprofits are growing rapidly in number, size, budgets, and position creation. Their growth outpaces growth in the rest of the economy. According to *Nonprofit Almanac 2007*, U.S. gross domestic product increased by less than 37 percent from 1994 to 2004 after adjusting for inflation. However, all three of the major financial measures of nonprofits (revenues, expenses, and assets) increased by at least 56 percent. Adding to the challenge of labor shortages is the increasing corporate governance prompted by some nonprofits' financial scandals; board members and contributors are holding nonprofits more accountable. Also, growth and consolidation in the sector have resulted in larger organizations requiring more complex management skills.

Typically, nonprofits invest their limited resources in their mission, rather than in developing human resources. Also, contributors often limit their support to specific programs or services rather than the broader organization. Consequently, nurturing staff and leaders and managing succession may be low priorities.

Nevertheless, Opportunity Knocks

The advent of retirement for baby boomers also brings opportunity for nonprofit organizations. Says Diane Piktialis, Mature Workforce Program Leader at The Conference Board, "Many older employees plan to work past traditional retirement age, but not always with their current employers. This burgeoning trend provides a time-tested source of labor for nonprofits."

Experts in the field of civic engagement and aging note that retiring boomers may very likely be looking for a mix of activities—combining paid work for an employer with volunteering for a different nonprofit organization. If this is the case, nonprofits stand to gain in a major way, reaping the benefits of boomers' professional or management skills and experiences in both paid and service positions. Currently, almost a quarter of baby boom volunteers (23 percent) report they provide professional and managerial skills in their volunteering positions, according to the Corporation for National & Community Service.

Good Governance Practices

Inadequate numbers of employees and volunteers increase the vulnerability of charitable organizations to fraud losses. Consider, for example, the consequences of being shorthanded. An organization then cannot easily separate duties related to handling funds. Another possible consequence, especially if seasoned managers are scarce, is lack of awareness of the conditions and situations that foster fraudulent activity and of the red flags that signal the need to investigate possible fraud.

Financial scandals in nonprofits may not seem to be as common as those in public companies since the start of the Enron era. Nevertheless, they occur. Financial losses due to fraudulent activities are particularly troublesome to charitable organizations because they directly reduce resources available to address tax-exempt purposes. The ensuing bad publicity may also reduce contributions and grants. In an effort to deter the vulnerability of charitable organizations to such abuse, the IRS recently

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issued a discussion draft on "Good Governance Practices for 501(c) (3) Organizations."

In the draft, the IRS states that it "believes that governing boards should be composed of persons who are informed and active in overseeing a charity's operations and finances. If a governing board tolerates a climate of secrecy or neglect, charitable assets are more likely to be used to advance an impermissible private interest." To minimize the chance of such abuse, the IRS advises, "Successful governing boards include individuals not only knowledgeable and passionate about the organization's programs, but also those with expertise in critical areas involving accounting, finance, compensation, and ethics."

The IRS also cautions against having very small or very large governing boards: "Small boards generally do not represent a public interest, and large boards may be less attentive to oversight duties." When an organization's governing board is very large, the Service advises establishing an executive committee with delegated responsibilities or advisory committees.

To promote good governance and to ensure that directors understand their roles and responsibilities, the IRS recommends nine practices. Adoption of particular practices is not required for exemption. However, the draft says, "any decision by the Service to conduct a review of operations subsequent to exemption . . . will be influenced by whether an organization has voluntarily adopted good governance practices." (The Review of Operations unit within the IRS Exempt Organizations Examinations follows up on certain organizations within the first three years of their obtaining exempt status.)

The good governance practices include developing a mission statement, a code of ethics, whistleblower policies, a document retention policy, a fundraising policy, and compensation practices. More information about the document retention policy is available on the IRS Web site in IRS publication 4221, *Compliance Guide for 501 (c) (3) Tax-Exempt Organizations.* Other good practices are requiring directors to "exercise due diligence consistent with a duty of care" and also to accept "a duty of loyalty."

To fulfill the duty of loyalty, a director acts in the interest of the charity rather than his or her own, another person's, or an organization's interest. This duty also requires the director to avoid conflicts of interest that are detrimental to the charity. The board should adopt and evaluate a conflict of interest policy that "includes written procedures for determining whether a relationship, financial interest, or business affiliation results in a conflict of interest, and prescribes a certain course of action" when a conflict is identified. In addition, "directors and staff should . . . disclose annually in writing any . . . financial interest that the individual, or a member of the individual's family, has in any business entity that transacts business with the charity."

Financial audits

Financial audits are among the good governance practices. For charities with substantial assets or annual revenue, "its board of directors should ensure that an independent auditor conducts an annual audit. The board can establish an independent audit committee to select and oversee the independent auditor. The auditing firm should be changed periodically (for example, every five years) . . ." Charities with fewer assets or annual revenues should have a CPA conduct an annual audit. Similarly, very small organizations could trade volunteers to perform these tasks.

A final good practice relates to transparency: "By making full and accurate information about its mission, activities, and finances publicly available, a charity demonstrates transparency. The board of directors should adopt and monitor procedures to ensure that the charity's Form 990, annual reports, and financial statements are complete and accurate, are posted on the organization's public Web site, and are made available to the public upon request." (See the article concerning the proposed revisions to Form 990 on page 5.)

The discussion draft of "Good Governance Practices for 501 (c) (3) Organizations" is available at http://www.irs.gov/charities/charitable/article/0,,id=167626,00.html.

Red Flags to Uncover Accounting Fraud

Which companies are most likely to "cook the books?" Growth companies whose operating performance is deteriorating, according to an analysis by Patricia Dechow, an accounting professor at the University of California, Berkeley's Haas School of Business. The Haas School describes the analysis as the "most comprehensive ever of the Securities and Exchange Commission (SEC) Accounting and Auditing Enforcement Releases, which the SEC issues to document enforcement actions against companies, auditors, and officers for alleged accounting misconduct.

Dechow and her coauthors examined more than 2,000 SEC releases from 1982 to 2005. Of these, the final sample of firms that are alleged to have manipulated financial statements numbered 680. The results are outlined in a working paper titled "Predicting Material Accounting Manipulations" (http://www.soxfirst.com/50226711/manipulation.pdf).

The analysts found that firms that manipulate financial results typically also share the following characteristics:

- High growth in cash sales but declines in cash profit margins and earnings growth
- Declines in order backlog and employee headcount
- Abnormally high increases in financing and related off-balance sheet activities such as operating leases.

According to the researchers, "A consistent theme among manipulating firms is that they have shown strong performance prior to the manipulations. Manipulations appear to be motivated by management's desire to disguise a moderating financial performance." Dechow thinks that the reason for disguising the moderating performance is to secure the value of stock-based compensation or to raise capital at better prices.

Industries

More than 20 percent of the manipulating firms were in the computer industry, even though the computer industry accounted for only 11.9 percent of public companies. Retail firms, which

AICPA conference

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Save $100
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Save $50!
off regular member rate

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Bonus Workshop Complimentary for BVFLS & ABV Members:
Saturday, December 1

Pre-Conference Optional Workshops:
Sunday, December 2

Recommended CPE credit:
22 (main conference) and up to 3 (optional workshops) and 4 (BVFLS workshop)

Explore, analyze and understand the trends in Business Valuation services

Snapshot

The current economy is causing a shift in business valuations and has a direct impact on your strategy for growing your services. Knowing the latest trends is the first step to implementing a strategy that works.

The Event

Join business valuation professionals from across the country at this year's National Business Valuation Conference — the largest gathering for valuators — to take the pulse of the industry, hone your skills and network with peers and experts alike. Here, our powerful lineup of expert speakers will explore, analyze and help you fully understand the impact that the current economy has had on business valuation services, as well as the trends that have emerged. Through in-depth sessions, you'll explore current updates, and find out what's on the horizon. And with a learning environment that encourages peer interaction and allows for plenty of Q&A time, you're sure to walk away with a clear-cut action plan for success. Be sure to register today — and learn the trends that shape the market.

Who Should Attend

CPAs, Senior Financial Professionals and Business Valuation Specialists.

Keynote Presentations:

The Economic Impact of Katrina and Rita, by Dr. Loren S. Scott, Professor Emeritus of Economics at LSU

Judge David Laro — A View From the Bench

DON'T MISS:

Pre-Conference Workshops:

- Valuation for Financial Reporting Case Study Workshop
- The Care, Feeding and Destruction of the Valuation Expert
- Business Succession Planning and Exit Strategies

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Conference agenda

TRACKS: **Emerging/Hot Topics** **Fair Value** **Fundamentals** **Litigation** **Niche**

Topics, Speakers, and Agenda are subject to change

SAT., DECEMBER 1, 2007 Pre-Conference Optional BVFLS Workshop

1:00pm-5:00pm	401. Using Media Interviews to Attract Business and Build Awareness for Your Practice — A Practical Training Workshop (Complimentary workshop for BVFLS section members and ABVs. If you are not a BVFLS Section Member or ABV the fee for this session is $150.)

SUN., DECEMBER 2, 2007 Pre-Conference Workshops

(additional fee)

7:00am-6:00pm	Registration and Message Center Open
8:00am-11:00am	Pre-Conference Optional Workshops (select one) (additional charge)
	101. Valuation for Financial Reporting: Case Study Workshop
	102 The Care, Feeding and Destruction of the Valuation Expert
	103 Business Succession Planning and Exit Strategies - Understanding & Planning for Business Ownership Change

SUN., DECEMBER 2, 2007 Main Conference Day 1

12:00pm	Main Conference Begins
12:00pm-12:15pm	Welcome and Introduction
12:15pm-1:30pm	Keynote Presentation 1 The Economics of Disaster: The Economic Impact of Katrina and Rita
1:30pm-2:00pm	Afternoon Refreshment Break in Exhibit Hall
2:00pm-3:15pm	Concurrent Sessions (select one)
Litigation	2 Here Comes the Judge! Valuation and Case Law Update
Niche	3 Healthcare Valuation Developments, Challenges and Solutions in 2007 - Panel Discussion
Fundamentals	4 Transactional Databases: Sanity Checks and Beyond - Panel Discussion
Emerging/Hot	5 Dream the Impossible Dream: Can Specific Company Risk Really be Qualified?
3:15pm-3:30pm	Change Break
3:30pm-4:45pm	Concurrent Sessions (select one)
Fair Value	6 Fair Value GAAP GAAS Overview
Niche	7 Assessing the Value Pricing Spectrum of Closely Held Businesses
Litigation	8 Expert Witness Advocacy — Guilty Until Proven Innocent
Fundamentals	9 Calculating the Cost of Capital for Companies Less than $100 Million in Value
4:45pm-5:00pm	Change Break
5:00pm-6:45pm	General Session and Awards 10 Discounts for Lack of Marketability — Panel: Who's on First, What's on Second, I Don't Knows on Third
6:45pm-8:00pm	Networking Reception/Exhibits

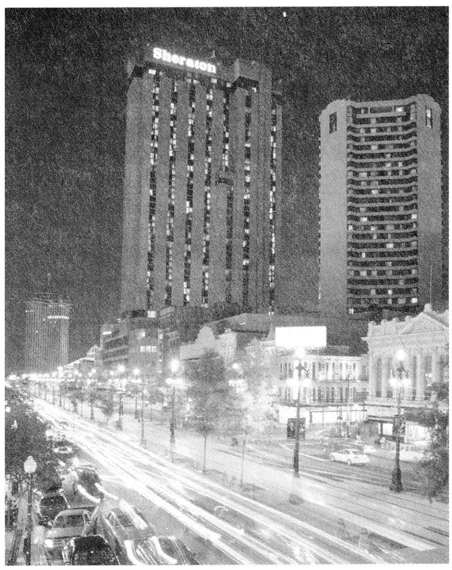
MON., DECEMBER 3, 2007 Main Conference Day 2

7:00am-6:15pm	Registration and Message Center Open
7:00am-8:00am	Continental Breakfast
7:00am-7:50am	201 Town Hall Meeting — ABV Credential Holders
8:00am-9:00am	General Session 11 Appraiser Professional Responsibility
9:00am-9:15am	Change Break
9:15am-10:15am	Concurrent Sessions (select one)
Fair Value	12 Fair Value Panel Discussion
Emerging/Hot	13 NEW: A Family Limited Partnership (FLP) Valuation Example
Litigation	14 The Good, The Bad and the Ugly: Expert Witness Visual Evidence
Fundamentals	15 Quantitative Application in Valuation — Basic Statistical Measures
10:15am-10:45am	Networking Break with Exhibitors

10:45am-12:00pm	Concurrent Sessions (select one)
Emerging/Hot	16 Business Valuation: An Integrated Theory
Niche	17 IRC 409A and SFAS 123R Valuations
Litigation	18 10 Commandments for the First Time Expert Witness
Emerging/Hot	19 Using Duff & Phelps Data to Develop the Cost of Equity
12:00pm-1:15pm	Lunch
1:15pm-1:30pm	Change Break
1:30pm-2:45pm	Concurrent Sessions (select one)
Litigation	20 Collaborative Law — Using a Neutral
Fair Value	21 The Relief from Royalty Method of Intellectual Property Valuation
Fundamentals	22 Standards of Value: The Value Lies in the Eyes of the Beholder (One Company Several "Beholders")
Niche	23 Risks Along the Technology Life Cycle
2:45pm-3:15pm	Networking Break with Vendors
3:15pm-4:45pm	Concurrent Sessions (select one)
Fair Value	24 Hot Topics in Fair Value - SFAS 157
Litigation	25 Tax Valuation Trials — Do's & Don'ts
Fair Value	26 The Relief from Royalty Method of Intellectual Property Valuation (repeat of session 21)
Emerging/Hot	27 S Corporation Valuations — To Tax Affect or Not is No Longer the Issue
4:45pm-5:00pm	Change Break
5:00pm-6:30pm	General Session
	28 Hardball with Hitchner — Ask the Experts

TUES., DECEMBER 4, 2007 Main Conference Day 3

7:00am-1:00pm	Registration and Message Center Open
7:00am-8:15am	Continental Breakfast and Vendor Display
7:00am-8:15am	Early Morning Sessions (select one)
Fundamentals	202 Reports, Reports and More Reports
Fundamentals	203 Subsequent Events and Is There Life After Death Gift
Niche	204 Valuating Musical Works and Literary Rights
Litigation	205 Emerging Issues in Spolation and Electronic Evidence
8:15am-8:30am	Change Break
8:30am-9:45am	General Session — Panel
	29 BV Standards Update with Q&A Panel
9:45am-10:15am	Refreshment Break with Exhibitors
10:15am-11:30am	Concurrent Sessions (select one)
Emerging/Hot	30 Developing Meaningful Discount Rates for Damage Analysis Cases
Niche	31 Niche Vignettes: - Valuation of Automobile Dealerships - Valuation of Businesses in Extractive Industries - Valuation and Other Issues in Restaurants and Bars
Emerging/Hot	32 Business Valuation Issues in Bankruptcy Context
Fundamentals	33 Everything You Ever Wanted to Know About Discounted Cash Flow
11:30am-11:45am	Change Break
11:45am-1:00pm	General Session
	34 A View from the Bench: The Biggest Mistakes Experts Make and a Judges View on How to Avoid Them
1:00pm	Conference Adjourns



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Registration information

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This conference was prepared in accordance with the Joint AICPA/NASBA Statement on Standards for Continuing Professional Education (CPE) Programs effective on January 1, 2002. The recommended CPE Credits are in accordance with these standards; however, your individual state board is the final authority on the acceptance of programs for CPE credit.

CONFERENCE FEE

Registration fees are determined by current membership status in the ABV and BVFLS Section of the AICPA. Please indicate member number on the registration form to obtain the correct discount. Fee for conference includes all sessions, conference materials, continental breakfasts, refreshment breaks, luncheons and reception. Fee for optional workshops include all session materials and refreshment breaks. Note: all registrations rates are shown in US $ Dollars. Registration for groups of 2 or more individuals per organization may qualify for group discounts. Please visit **www.cpa2biz.com/conferences** for more information.
Groups of 10 or more individuals per organization may qualify for additional discounts, please email **service@aicpa.org** for more information and indicate "Group Conference Sales" in the subject line of your email.

Please note: there is no smoking during the conference sessions.

Suggested attire: business casual.

Prices, Topics, Speakers, Fields of Study and Agenda are subject to change without notice.

Program Code: BVAL07

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Full refunds will be issued if written cancellation requests are received by 11/11/07. Refunds, less a $100 administrative fee, will be issued on written requests received before 11/25/07. Due to financial obligations incurred by AICPA, no refunds will be issued on cancellation requests after 11/25/07. For further information, call **AICPA Service Center** at **1-888-777-7077**.

HOTEL AND GROUND TRANSPORTATION INFORMATION

Contact the hotel directly to obtain their policy on reservations, deposits and cancellations. Rooms will be assigned on a space-available basis only. Note, this conference is expected to sell out, so please make hotel arrangements as soon as possible. To receive our special group rates mention and that you will be attending the **National Business Valuation Conference.**

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Please note: AICPA members are entitled to free membership in the Corporate Preferred Level of the **Starwood Preferred Guest Program (SPG)**; where you can accrue points and qualify for special benefits. If you haven't already done so, we encourage you to sign up today at: **http://www.cpa2biz.com/Affinity/Starwood.htm**.

The Sheraton New Orleans is a Starwood Property. Present your SPG membership number upon check-in or when making your reservation to receive valuable Starpoints for your stay.

Ground Transportation — to and from the hotel and airport (please note: rates and times are approximate)

Taxi: $28 each way, approximately 25 minutes each way
Shuttle: $13 each way, approximately 45 minutes each way

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The AICPA has a special arrangement with **Maupin Travel, Inc. of North Carolina** to assist you with your travel arrangements. This travel agency may be reached at **1-800-345-5540**. If you prefer to make your own travel plans, be sure to mention the participating airline's reference number (listed below) to take advantage of deeply discounted "Zone Fares" that do not require a Saturday night stay over. Discounts are valid for round trip registered AICPA meetings or conferences only. **Some restrictions may apply.**

American Airlines	**1-800-221-2255**	**Index #19330**
Delta Air Lines	**1-800-221-1212**	**Refer to US723852916**
United Airlines	**1-800-521-4041**	**Refer to Meeting ID #531SI**

For up-to-date airline information regarding special travel discounts, please visit **www.cpa2biz.com/conferences.**
Due to recent airline industry fare restructuring, we cannot guarantee that the above group travel agreements will be in effect at the time when you are making your travel arrangements. Please contact the airline and/or your travel agency for latest applicable discounts and arrangements.

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Airline and car rental discounts are available only when you or your travel agent book through the 1-800 number. We strongly advise you to confirm your conference registration and hotel reservation prior to making your travel plans. The AICPA is not liable for any penalties incurred if you cancel/change your airline reservations.
Rates are subject to availability.

Registration form

ABV Designees use code **SECTION100** BVFLS members use promotional code **SECTION50** to receive member prices.

MEMBERSHIP INFORMATION

Very important — please be sure to complete.

AICPA Member? ☐ **Yes** ☐ **No**
BVFLS Member? ☐ **Yes** ☐ **No**
ABV Member? ☐ **Yes** ☐ **No**

Membership No. (Required for discount prices)

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Please photocopy this form for additional registrants. If the information on your label is incorrect, please complete the following:

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CONFERENCE FEES Please circle appropriate rate.

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BONUS WORKSHOP — SATURDAY, DECEMBER 1 (complimentary for ABV and BVFLS members) 1:00am-5:00pm				
401 ☐		**complimentary**	**$150**	**$150**
PRE-CONFERENCE WORKSHOPS — SUNDAY, DECEMBER 2 (additional fee) 8:00am-11:00am (select one)				
☐**101** ☐ **102** ☐ **103**	**$150**	**$100**	**$150**	**$150**
Total	**$**______	**$**______	**$**______	

CONFERENCE PLANNER

Select one from each time period. To ensure that adequate seating is reserved for the conference sessions, you must complete this section in advance of the conference.

SUNDAY, DEC. 2	**Concurrent Sessions**			
2:00 pm – 3:15 pm	☐2	☐3	☐4	☐5
3:30 pm – 4:45 pm	☐6	☐7	☐8	☐9
MONDAY, DEC. 3	**Concurrent Session**			
7:00 am – 7:50 am	☐201			
9:15 am – 10:15 pm	☐12	☐13	☐14	☐15
10:45 am – 12:00 pm	☐16	☐17	☐18	☐19
1:30 pm – 2:45 pm	☐20	☐21	☐22	☐23
3:15 pm – 4:45 pm	☐24	☐25	☐26	☐27
TUESDAY, DEC. 4	**Concurrent Sessions**			
7:00 am – 8:15 am	☐202	☐203	☐204	☐205
10:15 am – 11:30 am	☐30	☐31	☐32	☐33

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represent 9.7 percent of public companies, were 13 percent of the manipulating firms. Service firms, such as telecommunications and health care firms, accounted for 12.4 percent of manipulating firms while representing 10.4 percent of public companies.

Additional Findings

Other research findings include:

- Investors had abnormally high expectations about manipulating firms' future growth opportunities. This was evident from the unusually high price-earnings and market-to-book ratios prior to manipulations.
- Manipulating firms tended to have abnormally low free cash flows. Many firms were actively seeking new financing to cover negative operating and investing cash flows.
- Surprisingly, cash sales increased during manipulations. The reason was that many firms allegedly front-loaded their sales and engaged in unusual transactions at the end of the quarter.
- More firms issued either debt or equity in years in which they manipulated financials compared with other years. In addition, cash from financing more than doubled during manipulating years compared with other years.
- Companies engaged in abnormally high leasing activities during manipulation periods, consistent with managements' increased use of the flexibility granted by lease accounting rules, to manipulate their firms' financial statements.
- Accruals increased in manipulating years. Accruals are the difference between reported earnings and actual cash flows, so high accruals indicate more accounting adjustments are being made to boost earnings.
- Revenue was by far the most commonly manipulated line item on the income statements, with 55 percent of the sample firms allegedly manipulating revenue. Types of revenue manipulations included front-loading sales from future quarters, creating fictitious sales, incorrect recognition of barter arrangements, and shipping goods without customer authorization.
- Manipulations of inventory and cost of goods sold occurred in 25 percent of sample firms. Manipulations of allowances, including the allowance for doubtful debts (an estimate of how many customers who purchased good on credit will not pay), occurred in 10 percent of sample firms.

F-score

Dechow and her coauthors devised a Fraud Score, or F-Score, based on their research. Investors, auditors, and regulators could use the F-Score to assess "earnings quality" before determining whether further investigation into possible fraud is warranted. Dechow cites the example of Enron, which received an F-score almost twice as high as the average firm.

Coauthors and Sponsors

Dechow's coauthors include Weili Ge of the University of Washington Business School, Chad Larson of the University of Michigan's Stephen Ross School of Business, and Richard Sloan of Barclay's Global Investors. Their research was sponsored by the Research Advisory Board established by the big four accounting firms to develop a model to help identify firms that manipulate earnings or commit fraud.

IRS Proposes Redesign of Form 990

The Internal Revenue Service released for public comment a discussion draft of a redesigned Form 990, *Return of Organizations Exempt from Income Tax,* which is filed by many public charities and other exempt organizations. The IRS says that the discussion draft constitutes a significant redesign of the form, which has been revised only on a piecemeal basis since 1979. The IRS anticipates using the form for the 2008 tax year (returns filed in 2009).

The redesign of Form 990 is based on three guiding principles: enhancing transparency, promoting tax compliance, and minimizing the burden on the filing organization, which are defined below.

- *Enhancing transparency.* Providing the IRS and its stakeholders with a realistic picture of the organization and its operations, along with the basis for comparing the organization to similar organizations.
- *Promoting compliance.* The form must accurately reflect the organization's operations and use of assets, so the IRS may efficiently assess the risk of noncompliance.
- *Minimizing the burden on filing organizations.* Asking questions in a manner that makes it relatively easy to fill out the form and does not impose unwarranted additional recordkeeping or information gathering burdens to obtain and substantiate the reported information.

The form, instructions, and background material explaining the principles underlying the redesign of the form are available on the exempt organizations portion of the IRS Web site.

Among the highlights of the new form are the following:

- A summary page providing the organization's identifying information and a snapshot of the organization's key financial, compensation, governance, and operational information.
- A portion of the form requiring governance information, including the composition of the board and certain other governance and financial statement practices.
- Schedules that will focus reporting on certain areas of interest to the public and the IRS: fundraising, compensation, hospitals, tax exempt bonds, and noncash charitable contributions.

The comment period for the discussion draft ends September 14, 2007.

The BV Conference

On December 2, 3, and 4, the AICPA National Business Valuation Conference will be held in New Orleans. Testimony to this conference's quality and relevance to BV practitioners is the fact that it has sold out for the past two years.

The topic of one of the general sessions will be the new AICPA valuation standard and how practitioners can implement it into practice. In addition to general sessions, concurrent sessions with several themes will be offered: litigation, fundamentals, fair value measurements for financial reporting, and emerging/hot topics.

As mentioned above, this conference has sold out in the last two years, so register now. For more information or to register for the conference call 1-888-777-7077 or visit www.aicpa.org.

Sessions by the Sea

The AICPA Fraud and Litigation Services Conference will be in San Diego on September 27 and 28.

There may be some irony in the AICPA's scheduling its National Conference on Fraud and Litigation Services in San Diego. That city suffered a much-publicized instance of government fraud and corruption, which was the focus of one the sessions of last year's Fraud and Litigation Services Conference. The session entitled "Government Fraud & Corruption—Investigation of the City of San Diego and Its Pension System" was presented by Troy Dahlberg, JD, CPA/ABV, a managing director and the national practice leader for Kroll's Forensic Accounting and Litigation Consulting Practice. Dahlberg, along with Arthur Levitt, Jr., and Lynn E. Turner, served on the Audit Committee formed to investigate the San Diego City Employees' Retirement System and the city's sewer rate structure.

The San Diego scandal illustrates the consequences of the failure to challenge management and instead to acquiesce to a culture of corruption. Such consequences have been the focus of much of the career of this year's keynote speaker, Joseph L. Ford, Deputy Director of the FBI. In his career with the FBI, Ford has investigated white collar crimes in San Antonio and public corruption and government program frauds in Philadelphia. In the 1990s, he managed several high-profile health fraud investigations, first as head of the health care fraud program at FBI Headquarters, and later in the Tampa, Florida, field office. These investigations included the national "GOLDPILL" investigation and investigations into National Medical Enterprises and Columbia/HCA Healthcare.

In 2000, Ford returned to Headquarters to head the Economic Crimes Unit where he oversaw the FBI's major investigative efforts related to securities and commodities fraud and insurance, telemarketing, and bankruptcy frauds. Following the attacks of September 11, 2001, he was instrumental in uncovering financial evidence related to international terrorism. In early 2002, Ford was named Inspector in Charge of the Enron investigation.

There's More Than Fraud

Although many sessions, of course, will cover fraud topics, the conference also covers the key and related area of litigation services. Each concurrent session period offers two presentations on fraud and two on litigation services. The sessions focusing on fraud will cover emerging fraud topics, not only those relevant to the larger organization, but also those relevant to the small firm practitioner. Sessions will also cover money laundering and data and technology issues. In addition, practitioners will have an opportunity to gain a better understanding of hedge fund fraud and computer crime. Subprime lending issues will also be covered.

Litigation services sessions will cover technical information and also best practices such as those that will help you succeed in giving depositions and growing your niche. For the first time, a live mock trial will give you the opportunity to observe skilled expert witnesses giving testimony, watch the jury deliberate and gain an understanding of how juries process and respond to expert testimony.

The main conference is scheduled for Thursday, September 27 and Friday, September 28 at the Sheraton San Diego Hotel & Marina. It is recommended for 17 CPE credits. An additional 9 credits are available in the optional sessions scheduled for Wednesday, September 26. The optional sessions cover interviewing, measuring business damages, current issues and hot topics in personal injury and wrongful death damages, family law, and hidden ownership elements and detection.

To register for the conference or for more information, call 1-888-777-7077 or visit www.aicpa.org.

Letters to the Editor

Focus encourages its readers to write letters on consulting services issues and on published articles. Please remember to include your name and telephone and fax numbers. Send your letters by e-mail to wmoran@aicpa.org.

T-REX launches new auction marketplace for Chapter 11 creditors

T-REX (Trade Receivable Exchange) launched its auction marketplace for business creditors on May 15th, 2007, calling its launch "a major milestone in the history of trade credit." Typically, creditors whose debtors file for Chapter 11 bankruptcy are at a disadvantage. Stuck with bad debt and knowing it may take years to recover it, the creditors become the prey of "vulture investors," a common label for buyers of distressed debt.

T-Rex is targeting the commercial credit market, unlike the distressed asset exchanges, which focus primarily on consumer assets like houses, cars, and credit card debt.

T-Rex allows creditors to post their auctions at no charge in one of three categories: Bankruptcy Claims, Receivable Put Options, or Trade Credit Insurance. Prequalified investment banks, hedge funds, and insurers then bid against each other in real-time for the auction transaction, helping to ensure the best possible price for the creditor. Winning bidders pay T-REX a commission fee when the auction transaction closes.

The cornerstone of T-REX's new marketplace is pricing transparency. Members can actually see how much other creditors are being quoted for their auction transactions. Additional pricing research tools are available to creditors who upgrade to T-REX's Pro Creditor membership plan ($499 per year).

Auctions are anonymous and nonbinding, which means that the creditor can award its auction to any bidder or none at all. Creditors can analyze detailed bidder profiles and member feedback ratings to help them select the winner of their auction. They can also use T-REX's "creditor-friendly" claim assignment agreement to negotiate better contract terms with the winning bidder.

White-Collar crime: Are constitutional rights being violated?

If you're sitting underneath a tree, and a branch falls on your head, do you burn the tree? In other words – should the tree be punished for the branch's ill-fated descent? For those involved in the criminal prosecution of white-collar crime, it's the critical argument, and it is the focus of research being conducted by Regina Robson JD, an assistant professor of management at Saint Joseph's University. She is using a University-funded grant to research whether corporations should be criminally liable for the actions of their employees.

"As in the cases involving Kenneth Lay from Enron and Bernie Ebbers from WorldCom, individuals and businesses are typically both prosecuted during white-collar criminal cases," explained Robson. "And although both are criminally prosecuted, they each have very different constitutional protections." Her research aims to explore the ethical and legal implications of this gray area.

"Since 2003, we have seen a significant increase in the prosecution of white-collar crime," remarked Robson. "Because of these new policies, companies are required to lean more heavily on their employees during investigations to protect the corporate entity. Prosecutors are driving a wedge between employer and employee while fifth and sixth amendment constitutional rights are called into question."

A recent series of cases involving the criminal investigation of the accounting firm, KPMG, has strengthened constitutional protections for individuals, but has not affected corporate prosecutions.

Robson will draw her analysis and submit an article for publication early this fall.

Electronic data discovery revenues approach $2 billion annually

Electronic data discovery providers continue to increase in numbers, according to the fifth annual Socha-Gelbmann Electronic Discovery Survey report in *Law Technology News* (http://www.law.com/jsp/legaltechnology/PubArticleFriendlyLT.jsp?id=1185959203368). The survey is conducted by George J. Socha Jr., Esq., principal of Socha Consulting LLC and Thomas Gelbmann, principal of Gelbmann & Associates.

The survey covered the 2006 calendar year. Socha and Gelbmann expect, based on consumer and provider expectations, that the market will grow about 33 percent from 2006 to 2007; 28 percent from 2007 to 2008; and 23 percent from 2008 to 2009. If the growth estimates they predict are realized, the electronic data discovery (EDD) market will reach more than $4 billion by 2009.

In their survey, Socha and Gelbmann rank service providers and software providers based on several common factors including experience and reputation, capacity, law firm rankings, corporate rankings, and revenue. Other factors were used depending on whether the provider offered service or software. The report ranks both types of providers overall as well as in various categories such as identification, preservation, collection, processing, review, analysis, production, and presentation.

Socha and Gelbmann also cite several "influencing issues" in the EDD market. Included among these issues is the notion that "Purchasers [of services] are seeking high value services but try to pay only commodity prices." They think three factors may be the main contributors to the "commoditization myth." First are tight client budgets and second are providers who market EDD as "easy." The third factor is users comparing providers based on price because it's easier than comparing on the basis of capabilities.

Quick: How many CFOs have been convicted?

That's the question asked by Kate Plourd in CFO.com (July 18, 2007). The answer provided by the Presidential Corporate Task Force: At least 53 CFOs have been convicted in the past five years, along with 214 CEOs. The Task Force calculates that at least 53 finance chiefs have been brought down by legal action against accounting abuses since 2002.

The Task Force celebrated its success in compiling "a strong record of combating corporate fraud and punishing those who violate the trust

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of employees and investors." In its review of its first five years, the Task Force cited 1,236 convictions in such corporate cases, including 214 chief executives, 23 corporate counsels or attorneys, and 128 vice presidents. In addition, the Task Force noted that during its five years of operations, more than $1 billion in fraud-related forfeitures was distributed to victims of corporate fraud. The charges brought included securities fraud, insider trading, market manipulation, obstruction of justice, false statements, stock option backdating, conspiracy, money laundering, wire fraud, and violations of the Foreign Corrupt Practices Act.

CFO.com later calculated that 63 CFOS were convicted in the last five years. The reason for the discrepancy is that the Task Force list excludes some well-known former finance chiefs who were imprisoned. They include, for example, Enron's Andrew Fastow, and WorldCom's Scott Sullivan, whose cases were handled by the U.S. Attorney's Office. Reporting the discrepancies in CFO.com (8/6/2007), Ms. Plourd explains that a list compiled by the U.S. Department of Justice lists more than 70 names. Several on the list were not CFOs, but presidents, CEOs, or COOs. The list also included one CFO, James Doyle, former CFO of Mercury Finance, who died before he was charged with a crime, and Enron's Kenneth Lay whose death resulted in his record being cleared.

Ms. Plourd also points out that although the Justice Department cited the Sarbanes-Oxley Act of 2002 as one of the tools Congress gave to prosecutors to deal with corporate fraud, only three CFOs on its list were convicted of direct violations of the Act. Most cases ended in a plea agreement. More that 75 percent of defendants pled guilty to charges brought against them.

Call for Nominations - ABV Leadership Award

The ABV Credential Committee has created the ABV Leadership Award as a grassroots campaign to profile emerging or established leaders in the ABV profession and build the ABV community through awareness.

Individuals can be nominated for reasons including, but not limited to, serving in a mentoring role, developing a practice and raising awareness of ABV through speaking engagements, published articles, PR events, meetings with local community or industry organizations or being an ABV ambassador through community service. To make a nomination, please send the name of the person you would like to nominate, their firm name and reason for the nomination to fparker@aicpa.org. The deadline for nominations is October 15, 2007. Awards will be presented at the annual BV Conference in New Orleans, LA.

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