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## Members in Business and Industry, April 2002

American Institute of Certified Public Accountants (AICPA)

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## Business and Industry

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Published for AICPA members in business & industry. Opinions expressed in this CPA Letter supplement do not necessarily reflect policy of the AICPA.

Pamela Green	John Morrow	Ellen J. Goldstein
supplement editor, project manager	Vice President, New Finance	CPA Letter editor
212/596-6034 fax 212/596-6025	212/596-6085	212/596-6112
e-mail: <a href="mailto:pgreen@aicpa.org">pgreen@aicpa.org</a>	e-mail: <a href="mailto:jmorrow@aicpa.org">jmorrow@aicpa.org</a>	e-mail: <a href="mailto:egoldstein@aicpa.org">egoldstein@aicpa.org</a>

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Wanted: Cases on Ethics & Fraud Issues

## Wanted: Cases on Ethics & Fraud Issues

The AICPA and the AICPA Foundation are jointly sponsoring the creation of a Web-based collection of cases covering the topics of ethics and fraud, and we invite your participation in this project. Compensation is available for writing a case, provided the author complies with the guidelines set out below.

The term ethics in part encompasses the Principles of Professional Conduct as stated in the AICPA Professional Standards: Code of Professional Conduct and Bylaws, including, but not limited to the following:

- Article I—In carrying out their responsibilities as professionals, members should exercise sensitive professional and moral judgments in all their activities.
- Article III—Integrity. To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.
- Article V—Due Care. A member should observe the profession’s technical and ethical standards; strive continually to improve competence and the quality of services; and discharge professional responsibility to the best of the member’s ability.

Many states require CPA licensees to have a minimum number of CPE credits in ethics in each reporting period, but do these CPAs know how to apply ethics rules? While we do not have all the facts with Enron, this corporate bankruptcy has shown us that there are many issues in business and our profession that must be addressed to minimize the number and impact of future corporate scandals. Moreover, in tough economic times some members may experience situations where there may be coercion or temptation to back away from unclear and ambiguous business issues.

Our goal is to improve our members’ and others’ awareness, competence, and confidence in dealing with difficult and possibly illegal accounting and business decisions. In addition, we hope to provide education to business professionals, the academic community and others on some of the ethical dilemmas that arise in the executive suite and how they are resolved. The cases will be used in AICPA education programs, and will also be downloadable from the Web to be used in education at the undergraduate, graduate, executive and professional levels.

Cases should be prepared in a manner that will present all relevant facts to the reader, concluding with the question “what would you do?” As an educational tool, we suggest this is best accomplished by creating a dialogue between a number of fictitious characters acting out key roles in the company. Further details follow:

- Cases must present common managerial ethical dilemmas. We encourage cases, to be based on actual events but with fictitious names in a style similar to the cases in the Harvard Business Review. The cases should be written in a format that protects confidence and anonymity. Cases should present the ethical issues in a situation in which a business professional stood up to management on bad or illegal accounting practices. Explain what happened and what the professional did. What was the management faced with? What was the environment? What was the policy involved, if any?
- The AICPA will solicit analysis from corporate executives, experts in business ethics and fraud, and other experts interested in the topics of ethics and fraud.
- To avoid duplication of content, authors should submit an outline of the case to the AICPA in advance. If you are interested in writing a case or if you would like to partner with someone who will write the case for you, contact Roslyn Kessler at [rkessler@aicpa.org](mailto:rkessler@aicpa.org) for more information. Final manuscripts must be

typed with double spacing, one-inch wide margins and font 10 or 12. Electronic submission is encouraged. Please submit your outline as soon as possible but no later than May 31st.

Are You Providing the Right Information to Your Project Manager?

## Are You Providing the Right Information to Your Project Manager?

By Diana I. Angelis, PhD, Assistant Professor, Defense Resources Management Institute, Naval Postgraduate School

How important is cost information to the success of a project? How involved should you be in the project? What is the most important thing you can do to help with each phase of the project? What kind of cost information is most important to each phase of the project? If you are a cost manager for a project, or if you have been asked to provide cost information for a project, you may have asked yourself these questions.

Project managers answered these questions and more in a survey conducted recently by the Project Management Interest Group of CAM-I, an international consortium of companies, consultancies and academics. The survey is part of a study to determine the cost information needed for a successful project.

Industry and government project managers were asked about the kind of cost information needed during the three phases of a project (planning, execution and closure.) A total of 117 respondents provided the following answers:

1. How important is cost information to the success of each phase of the project?

Cost information was described as “important,” “very important,” or “essential” for most activities in every phase of the project.

2. How involved should the cost manager be in each phase of the project?

The cost manager should be an active participant in all phases of the project.

3. What is the most important thing a cost manager can do to help with each phase of the project?

In all phases the cost manager is expected to provide historical, projected and current information about the budget and the cost of the project. In addition,

the cost manager should provide analysis of the data presented and be able to interpret the information for the project team.

4. What kind of cost information is most important to each phase of the project?

Historical and projected total cost and budget are most important during the planning phase, while projected and current total and budget costs are most important during the execution phase and closure phases. Information about direct costs and labor hours is also very important to all phases.

5. Are project managers receiving the important cost information?

Project managers are receiving most of the cost information they feel is important, but there is room for improvement in the availability of historical costs during the planning phase and estimated costs during the execution phase.

6. What is the quality of the cost information received by project managers?

Cost information received in each phase was given an average rating of “medium” for quality, with the quality of historical costs being generally lower than projected or current costs. Surprisingly, there was almost no relation between the importance of cost information and the quality of the information received. This reveals a significant gap between the information project managers receive and the quality of that information.

The results of this survey provide empirical evidence of the importance of cost information to the success of a project from the point of view of project managers. It also provides insight into the relative importance of different kinds of cost (historical, projected and current) and different types of cost information to each phase of the project. Cost managers can use this information to determine if their cost systems are providing the needed information to support project managers.

In addition, the survey shows that cost managers should be actively involved in every phase of the project, and it provides information about what cost managers can do to help ensure the success of the project. Cost managers can use this information to improve the support they provide to project managers.

The one area that should be of particular interest to cost managers is the quality of cost information received by project managers. The survey revealed a significant shortfall in this area. While further research is needed to determine how the quality of cost information can be improved, the results should alert cost managers to the possibility of this problem in their own organizations.

For further information on this survey, contact Dr. Diana I. Angelis at [diangeli@nps.navy.mil](mailto:diangeli@nps.navy.mil).

## What Are My Professional Responsibilities?

By Renee Rampulla, Technical Manager—Professional Ethics Division

As a member in business and industry, what are my professional responsibilities?

The AICPA requires that all members, including those in business and industry, adhere to the AICPA Code of Professional Conduct. It is imperative that you are knowledgeable with regard to the rules of conduct and their interpretations, as they apply. Listed below are some examples of the application of such rules.

### Integrity and Objectivity

Member Linda Chambers\* is a CPA and the Chief Financial Officer for Brookings Incorporated. At the request of the external auditors, Linda signed the client representation letter stating that, “There has been no communications from regulatory agencies concerning noncompliance with or deficiencies in financial reporting practices.” Earlier that month she had received an inquiry from the Securities and Exchange Commission (SEC) concerning the company’s revenue recognition policy.

As a member, Linda has a responsibility to the company’s external accountants. She is required to be candid in disclosing the communication received from the SEC. In addition, Linda may not sign documents containing materially false and misleading information. Linda could potentially be in violation of:

### Rule 102-Integrity and Objectivity

Interpretation 102-1-Knowing misrepresentations in the preparation of financial statements or records, and Interpretation 102-3-Obligations of a member to his or her employer’s external accountants.

### General Standards

The controller, member Dale Weinstein\*, CPA, of Brookings Incorporated recorded a material sale of merchandise on the last day of the first quarter. Dale never received notification of a sales invoice or received any shipping documentation to ascertain that the sales transaction had actually occurred. Although this was a departure from company policy, Dale recorded the transaction.

Dale did not exercise due professional care and had a responsibility to obtain sufficient relevant data that would provide him with a reasonable basis for his

conclusion. Dale could potentially be in violation of Rule 201 - General standards of the AICPA Code of Professional Conduct.

## Accounting Principles

In a response to an SEC inquiry, member John Sterling\*, the CEO of Brookings Incorporated, writes: "The Company's financial statements are presented in conformity with generally accepted accounting principles, and I am not aware of any material misstatements." Earlier that morning, John had been present at a meeting with the company's external accountants discussing a material error in those same financial statements.

John cannot express, in the written communication with the SEC, that the financial statements are in accordance with generally accepted accounting principles and are free of material errors when he knows that his statement is false. As a member, John could be potentially in violation of Rule 203-Accounting Principles of the AICPA Code of Professional Conduct.

## Acts Discreditable

"I have been so busy with the company's initial public offering that I have failed to file my personal income tax returns for the last two years," said member Susan Allen\*.

Susan may not realize it, but she has a responsibility to comply with applicable federal, state or local laws regarding the timely filing of her personal tax returns. She could now also be potentially in violation of:

### Rule 501-Acts Discreditable

Interpretation 501-7 Failure to file tax return or pay tax liability.

The above represents only a few examples of the many business and industry member violations. At times, some situations could result in more than one violation.

The entire AICPA Code of Professional Conduct can be viewed by accessing the AICPA web site (<http://www.aicpa.org/about/code/index.htm>).

\*Fictitious name.

What type of guidance would be useful to you?

We are in the process of constructing a web site especially for members in business and industry where you will be able to access all of the information on the AICPA Professional Code of Conduct rules and interpretations. Also, we will be developing some cases and in order to make them relevant we would appreciate your help by

sending us suggestions on what areas you would like to see covered in the cases. Please send your suggestions to [rrampulla@aicpa.org](mailto:rrampulla@aicpa.org).

## Sixth Annual CAM-I/AICPA Cost and Performance Management Symposium

As a united country strides along the road to economic recovery, we invite you to join your peers in Tempe, Ariz., May 14–16, 2002, for the premier cost and performance management event of the year. You will discover how organizations just like yours are using leading-edge cost and performance management initiatives to gain the strategic advantages and operating efficiencies demanded by today's highly competitive economy.

The CAM-I/AICPA Cost and Performance Management Symposium is ideal for all industries and levels of experience. It covers management solutions developed by top manufacturing firms, service companies and government organizations. It dives into activity-based costing (ABC), activity-based management (ABM) and target costing and outlines how to use each of these systems to drive profit and performance. You'll learn how to link ABC and ABM with the Balanced Scorecard™ and review the latest developments in performance management, key cost drivers, target costing and activity based budgeting.

The featured keynote speaker for this year's event is Gary Heil, founder of the Center for Innovative Leadership, developer of the acclaimed "Leadership Lessons from the Fast Lane," and an examiner for the prestigious Malcolm Baldrige Award. With his signature wit and laid-back charm, Heil will offer lessons from today's best leaders that will challenge your traditional ways of thinking, acting and leading.

You can earn up to 28 CPE credits by also attending one of the four optional full-day workshops:

- CAM-I's Introduction to Strategic Cost Management
- The ABC's of Activity-Based Costing
- Linking Activity Analysis to Improved Budgeting & Processes—New for 2002
- The Era of the Real-Time Enterprise with Active Enterprise Management—New for 2002
- or one of the two optional half-day workshops:
  - Developing and Implementing a Balanced Scorecard
  - Beyond Budgeting—New for 2002

This conference was prepared in accordance with the Joint AICPA/NASBA Statement on Standards for Continuing Professional Education effective on Jan. 1,



2002. The recommended CPE credits are in accordance with these standards; however, your individual state board is the final authority.

For more information, or a conference brochure, visit [cpa2biz.com/conferences](http://cpa2biz.com/conferences).

Beyond Budgeting: A Better Way to Predict Spending

## Beyond Budgeting: A Better Way to Predict Spending

By Neal R. VanZante, Professor of Accounting, Texas A&M University-Kingsville

Traditional budgeting practices start with predetermined maximum spending limits which lead to re-writing the business plan to fit expenses, focus on functional departments—not on processes, and are not linked to the future incoming workload. The traditional budget process focuses on what managers are allowed to spend, and not what resources they need. Thus, the traditional budget process fails to identify waste, does not identify the incoming workload, does not support continuous improvement, does not identify cost drivers, and appears to have a general lack of ownership and buy-in. Other criticisms of the traditional budgeting process are that it is extremely time-consuming for the benefits achieved, it results in arbitrary cost increases or reductions, and it focuses on resource inputs instead of the outputs generated by those inputs. In short, traditional budgeting practices do not appear to be connected to overall organizational strategy.

Is there a better way? How does one best estimate the level of organizational spending required in future periods? Activity based budgeting (ABB), which is based on the principles of activity based costing (ABC) and activity based management (ABM), offers distinct advantages to the traditional budgeting approach. ABB provides opportunities for better communication of objectives throughout the company, allows for an optimum utilization of resources, and focuses on “continuous improvement.” An effective ABB model will identify the level of resources required to perform each activity, the relationships between activities and resulting output, and how changes in output expectations affect the required activities. Using ABB, management is provided the opportunity to focus on questions about why activities are performed, what they cost, and how often they need to be performed. ABB allows the budgeting process to be linked with overall organizational strategy.

ABB is not just ABC backwards. Simply calculating activity based costing “backwards” under most conditions does not provide an adequately useful answer. ABC is capacity-insensitive when applying the predictive view of extrapolated cost rates. Future demand volume, mix, and adjustments for each capacity resource must

be considered. Estimating expenses involves matching future capacity with estimated needs. Two key principles need to be recognized. First, the workload is the number of units of an activity required based on demand. Second, the amount of an activity required can be equated to the amount of a resource that will be needed.

In a two-part article in the Sept. and Oct. 2000 editions of Strategic Finance, Robin Cooper and Regine Slagmulder provide an excellent explanation of why the ABB process involves more than simply reversing an ABC system. They identify and explain that there are differences between spending and consumption patterns, secondary outputs and fungible resources, as well as an unavailability of detailed knowledge.

Yes, there is a better way. ABB works because (1) it is a predictive model, not a historical snapshot; (2) it is capacity-aware and reflects utilization consumption rates; and (3) it reflects fixed, variable, semi-variable, and step-fixed function consumption of resources.