

Statewide Accounting Bureau

Governmental Accounting Conference

April 23, 2019



Objectives

- Enhance each attendees knowledge of Governmental Accounting Standards issued by the Governmental Accounting Standards Board (GASB)
 - Examine currently issued standards and currently issued exposure drafts
- Provide guidance on what constitutes capital expenditures
 - Best practices, case studies, challenging transactions
- Review best practices on financial policies



Topics to Cover

- GAAP Update
- GASB Current Projects
- Accounting for Capital Assets
- Financial Policies
- Fraud/Forensic Accounting – Cyber Crimes

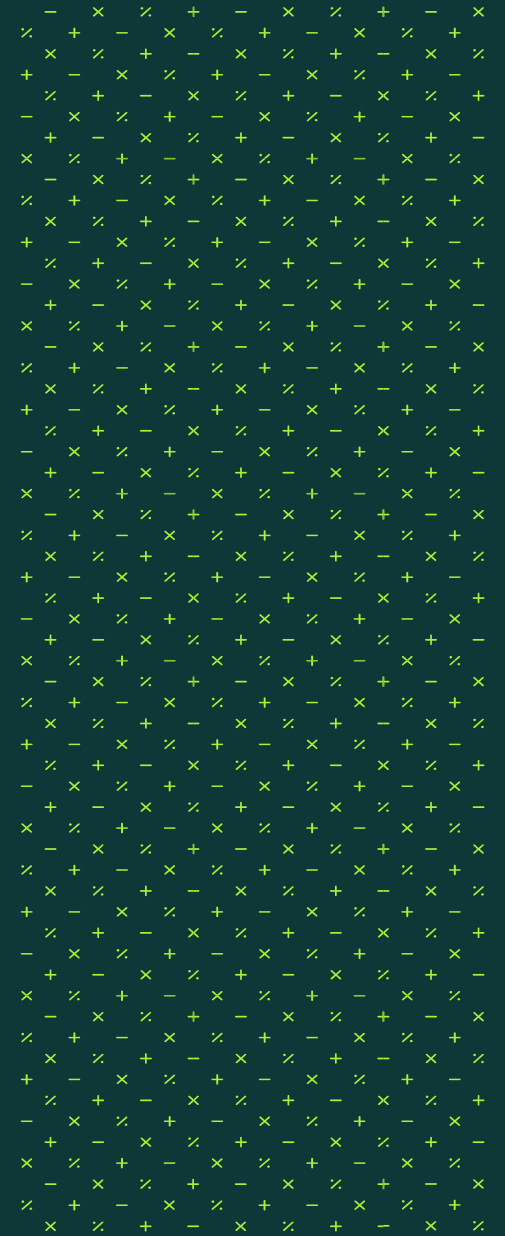




MOSSADAMS

Gearing Up for Change: GAAP Update

State of Montana
Government Conference
April 23, 2019



Jim serves as the Firm's National Practice Leader for Government Services. He just completed two terms as the AICPA representative to GASAC, responsible for assisting the GASB in setting their technical agenda and providing information to/from the AICPA. Jim's career spans over 30 years specializing in service to government organizations.

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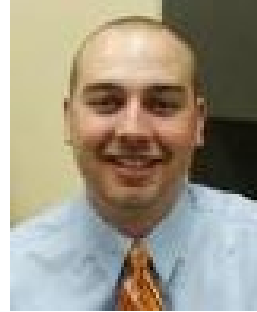


Farmer...or accountant...better not give up my day job.

Montana Connections



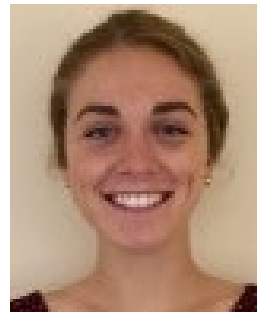
Anna



Kenny



Emily

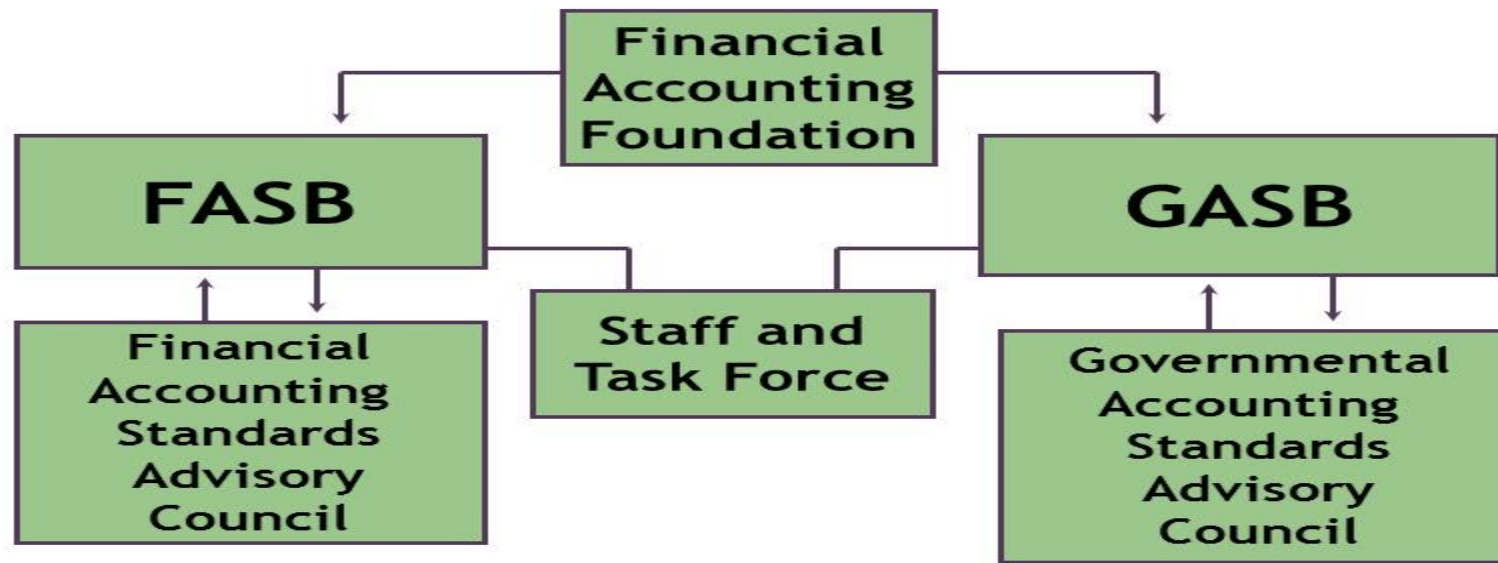


Kathleen



GASAC

Organizational Structure for Setting Standards



GASAC - duties

- Advise the Board on issues
- Alert on possible new agenda items
- Assist in setting project priorities
- Provide GASB communication to/from our respective associations



Learning Objectives



- Apply requirements of GASB 83 and identify challenges related to implementation
- Evaluate requirements of GASB 84 and assess potential fiduciary activities
- Assess GASB 87 and to help identify all leasing activities and impact of implementation
- General awareness of other new standards
- A quick look at GASB's current projects



Upcoming GASB Standards & Dates

Standard	Effective date
GASB 83 – Certain Assets Retirement Obligations	Periods beginning after <u>June 15, 2018</u>
GASB 84 – Fiduciary Activities	Periods beginning after <u>December 15, 2018</u>
GASB 87 – Leases	Periods beginning after <u>December 15, 2019</u>
GASB 88 – Certain Disclosures Related to Debt	Periods beginning after <u>June 15, 2018</u>
GASB 89 – Capitalized Interest	Periods beginning after <u>December 15, 2019</u>
GASB 90 – Majority Equity Interests	Periods beginning after <u>December 15, 2018</u>



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GASB 83

Certain Asset Retirement Obligations



Defining an Asset Retirement Obligation

“Legally enforceable liability associated with the retirement of a tangible capital asset ”

Translation: A government that has legal / contractual obligations to perform future retirement activities related to its capital assets should recognize a liability based on the guidance in GASB 83.

Key terms for discussion:

Tangible capital asset

Permanent retirement

Scope & Exclusions

- What are some examples? There are some obvious ones:
 - Nuclear power plant decommissioning
 - Dismantling and removal of sewage treatment plants
- And some not so obvious ones:
 - Contractually required land restoration, such as removal of wind turbines
 - Obligations to remove data from computers when disposed

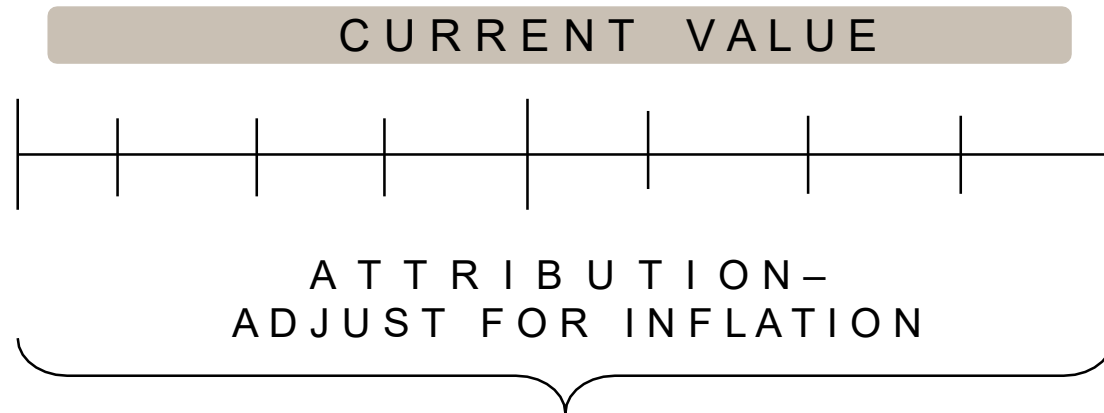


Scope & Exclusions

- What's scoped out of this standard?
 - Obligations arising from plans to sell / dispose of a tangible capital asset
 - Landfill closure – covered in GASB 18
 - Obligations associated with maintenance, not retirement
 - Pollution remediation obligations arising from other than normal use of the asset
 - Others described in GASB 83



GASB 83 – ARO Illustration



What is the impact on financial reporting?

	ARO Liability	Deferred Outflow
Initial measurement	Estimate <u>current value</u> of outlays	Equal to ARO liability
Subsequent measurement	Adjust for inflation annually	Amortize over asset's useful life*

**Expense all at once if asset is abandoned before being placed into service*



Defining Current Value

“The measurement of an ARO should be based on the best estimate of the current value of outlays expected to be incurred”

Translation: This differs significantly from the FASB standard which requires discounting to present value and accretion expense to be recorded each year.

Impact: Current value is a simpler method to estimating the liability as it removes the judgment involved in determining a reasonable discount rate



Implementation Issue
#1 – How do you
ensure you've
identified all AROs?



Implementation Issues

Challenge	Steps to consider
Identifying all AROs (Completeness)	Initiate joint meetings between accounting/finance, operations, and management to discuss GASB 83 to help identify all possible AROs





Implementation Issue
#2 – What if the AROs
were never measured
previously?



Implementation Issues

Challenge	Steps to consider
Initial measurement (Valuation)	Determine if outside expertise is needed to measure the ARO. This may take considerable time – initiate discussions as early as possible





Implementation Issue
#3 – What if there is
joint ownership in the
asset and the other
owner is a FASB
follower?



Implementation Issues

Challenge	Steps to consider
Joint ownership (Rights & Obligations, Valuation)	Consider how the asset is currently being valued and whether that meets the GASB requirements. Note that GASB 83 allows governments with less than 50% ownership to use the measurement methods utilized by the majority owner.



Key dates & notes

- Effective for reporting periods beginning after June 15, 2018
- Retrospective application is required, if practicable, for all periods presented



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GASB 84

Fiduciary Activities



Why did GASB address Fiduciary Activities?

- Wide diversity in practice
- Fiduciary activities of similar circumstances were reported more often in general governments – but not consistently in business type special purpose governments
- Entities applied different criteria in determining the existence of fiduciary relationships



Types of Fiduciary Funds

- Pension (and other employee benefit) trust funds
- Investment trust funds
- Private-purpose trust funds
- Custodial funds

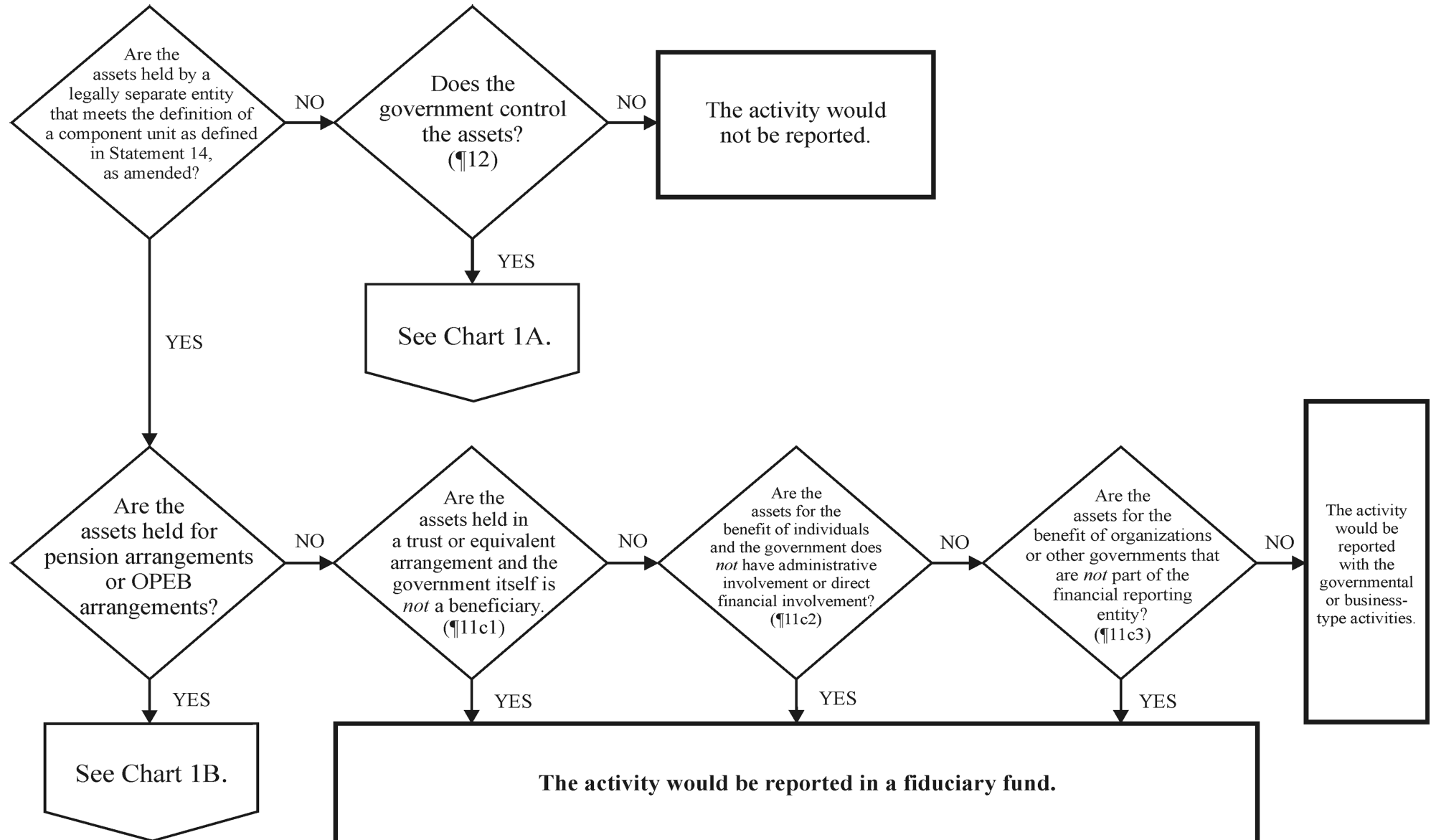


Fiduciary Activities you may see

- Activity funds held for another organization or other individuals
- Circuit court funds of another government
- 401(k) Plans
- Cemetery trust funds
- Minors' trust
- Postemployment benefit plans
- Jail inmate accounts
- Deferred compensation plans



Chart 1



Definitions for Flowcharts

Control of Assets:

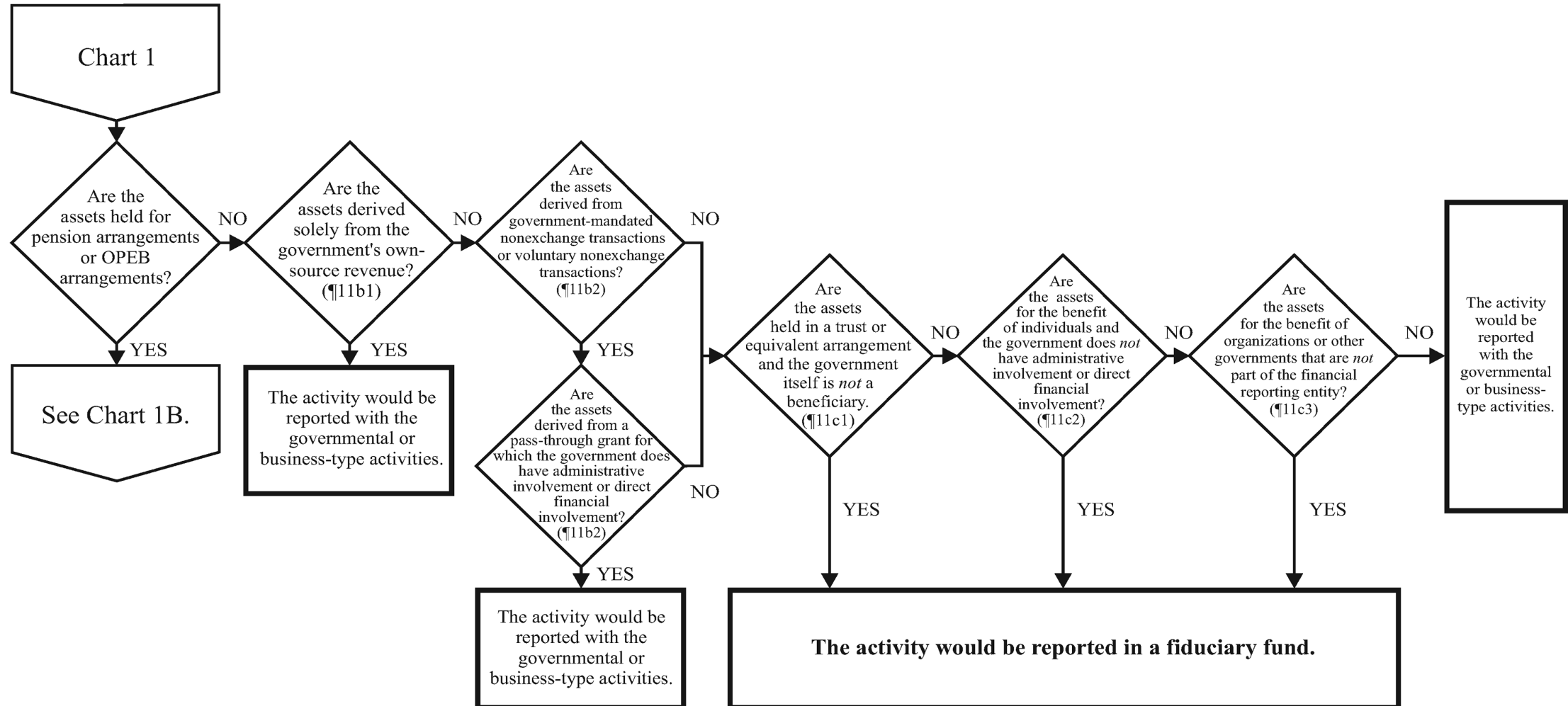
(a) holds the assets, or

(b) has the ability to direct the use, exchange, or employment of the assets in a manner that provides benefits to the specified or intended recipients*

**Restrictions from legal or other external restraints that stipulate the assets can be used only for a specific purpose do not negate a government's control of the assets.*



Chart 1A



Definitions for Flowcharts

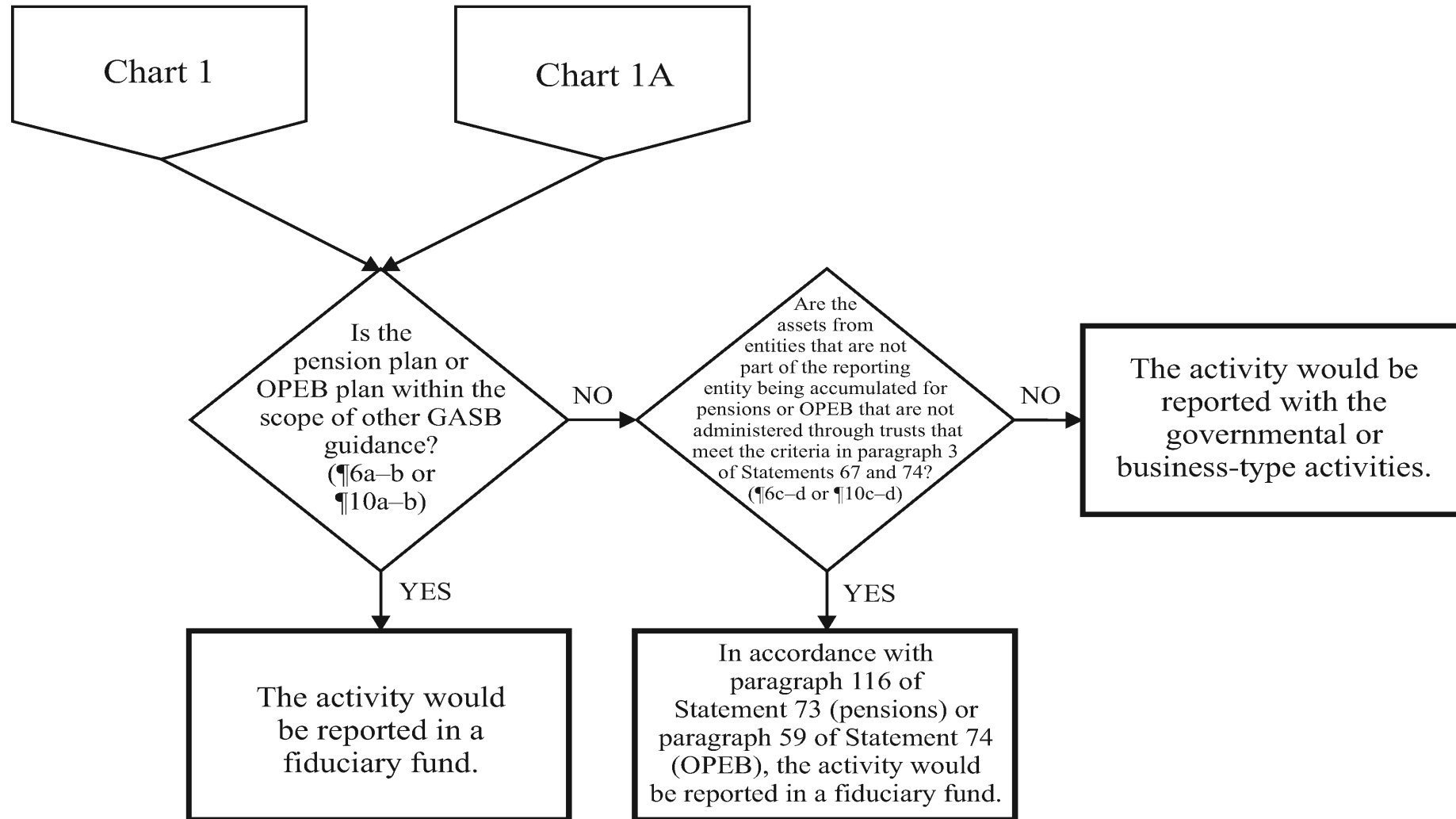
Own-Source Revenues:

Revenues that are generated by a government itself, and includes

- Exchange and exchange-like revenues (for example, water and sewer charges) and investment earnings
- Derived tax revenues (such as sales and income taxes) and imposed nonexchange revenues (such as property taxes)



Chart 1B



Key dates & notes

- Effective for reporting periods beginning after December 15, 2018
- Retrospective application is required, if practicable, for all periods presented



GASB 84 – Things to Think About

- Identify potential fiduciary population
- Gather information on the resources provided and the beneficiaries – who, what, why
- Use the flowcharts
- Consult the implementation guide (expected May 2019)
- Consult with auditors and GASB



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GASB 87

Leases



How will 87 impact financial reporting?



- New lease definition: “Right to use asset”:
 - The right to obtain the present service capacity from use of the underlying asset
 - The right to determine the nature of use of the underlying asset



How will 87 impact financial reporting?

	Assets	Liability	Deferred Inflow
Lessee	Intangible asset (right to use underlying asset) – value of lease liability plus prepayments and initial direct costs that are ancillary to place asset in use	Present value of future lease payments (includes fixed payments, variable payments based on index or rate, reasonably certain residual guarantees)	N/A
Lessor	<ul style="list-style-type: none"> • Lease receivable • Continue to report leased asset 	N/A	Equal to lease receivable plus any cash received up front that relates to a future period.



How will 87 impact financial reporting?

	Assets	Liability	Deferred Inflow
Lessee	Amortize the intangible asset over shorter of useful life or lease term	Reduce by lease payments (less amount for interest expense)	N/A
Lessor	<ul style="list-style-type: none"> • Depreciate leased asset (unless indefinite life) • Reduce receivable by lease payments (less payment needed to cover accrued interest) 	N/A	Recognize revenue over the lease term in a systematic and rational manner.



How will 87 impact financial reporting?

- **Exceptions**
 - Short-term leases
 - Leases that transfer ownership
 - Intangibles
 - Biological assets (timber, plants, animals, etc.)
 - Inventory
 - Assets financed with outstanding conduit debt
 - Supply contracts, such as power purchase agreement (do not convey control of the underlying asset)



What do clients need for implementation?

- Gather all executed lease documents currently in effect, including amendments
- Gather other contracts that convey a “right to use” an underlying asset
- Identify key provisions in lease documents – lease term, extension or termination provisions, payment provisions, implied interest rate
- Bridge the gap – Effective communication between departments is vital to ensure all leases are identified



Implementation Challenges

Identifying the lease term

- Starts with and only includes the noncancelable period, unless the following are reasonably certain of occurring:
 - Option to extend – Add to lease term
 - Early termination – Remove from lease term
- Reassess lease term if the following occur
 - Option to extend – Exercised, but not initially expected
 - Option to extend – Not exercised, but initially expected



Implementation Challenges

Understanding lease incentives

- Incentives provided at or before inception of lease
 - Result: Direct reduction of lessee's lease asset
- Incentives provided after inception of lease
 - Result: Reduction of payments for period provided
 - Result: Reduces present value of lease liability



Implementation Challenges

Identifying contracts with multiple components

- Step 1: Separate into lease and non-lease components, or multiple lease components
- Step 2: Allocate consideration to multiple underlying assets if
 - Differing lease terms exist
 - Assets are in differing major asset classes for disclosure
- Step 3: Allocation
 - Maximize observable info – Allocate based on explicit terms
 - Use best estimate based on professional judgment



Implementation Challenges

Lease modifications - result from amendments to a lease contract, not from exercising options in the original contract

- Report as a new lease if new assets are added, otherwise:
 - Re-measure the lease liability
 - Adjust the lease liability and lease asset by the difference between the re-measured liability and the liability balance before the modification.



Implementation Challenges

Sublease accounting should be separate from the original lease – can't offset the original lease liability

- Disclosures for original lessee (now the lessor)
 - Include subleases in the general description of the lease arrangements
 - Lessor transactions related to subleases should be disclosed separately from the original lessee transactions



Implementation Challenges

What about intra-entity leases?

- If there are leases with blended component units?
 - Eliminations should take place for internal leasing activity before financial statements are aggregated
- If there are leases with discretely-presented component units?
 - Treat like normal leases, but present the receivables and payables as separate line items on the financial statements



Best Practices for Implementation

When should we start on implementation?

- Facts:
 - 1) Effective date is periods beginning after December 15, 2019
 - 2) Initial time investment can be significant for applying the provisions, data entry, journal entries and disclosure
- Answer: NOW!



Best Practices for Implementation

What changes should we consider to internal controls?

- Facts:
 - 1) Implementation of GASB 87 may require new IT systems, spreadsheets, and other tools, creating new control risks.
- Next Steps:
 - 1) Ensure proper setup and monitoring of user access to modules / spreadsheets utilized for tracking leases
 - 2) Establish clear roles for preparation and approval of lease determinations, calculations and journal entries



Best Practices for Implementation

What other impacts do we need to consider?

- Facts:
 - 1) Debt agreements often contain restrictive financial covenants that can be impacted by significant accounting changes
- Next Steps:
 - 1) Identify all financial covenants and calculate the ratios based on implementation of GASB 87 – in compliance still?
 - 2) Any other changes in internal policies necessary?



How can technology be utilized?



- Save lease documents as searchable pdf files and bookmark key lease provisions
- Require that all lease documents be scanned and indexed in one central repository
- Utilize any existing debt management software to automatically generate amortization schedules and create journal entries





GASB 88

Certain Debt
Disclosures



Definition of debt

GASB 89, par 4:

“...debt is defined as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established.”



Required footnote disclosures

In addition to other disclosure requirements:

- Amount of unused lines of credit
- Assets pledged as collateral
- Events of default with finance-related consequences
- Termination events with finance-related consequences
- Subjective acceleration clauses



Required footnote disclosures

Classification

- Notes should separate information regarding direct borrowings – from other debt



Required footnote disclosures

Footnote Illustration





GASB 89

Interest Costs Incurred During Construction



No more interest capitalization!

Supersedes GASB 62, par 5-22

- Interest costs incurred during construction period are considered a period expense





Implementation Issue:
Are any of your charges for services designed to recover capitalized interest?





GASB 90

Majority Equity
Interests



Majority Interest

- Owning a majority of the stock
- Holding a majority interest in a partnership, LLC, LLP



Examples



- Community development organizations
- Research institutions
- Health clinics
- Management service agencies

Accounting

If the equity interest meets the definition of an investment

- Use the equity method of accounting (GASB 62 par 205-209)
- No component unit reported



Accounting

If the equity interest does not meet the definition of an investment

- Use the equity method of accounting (GASB 62 par 205-209)
- Report the component unit
- For CU's meeting criteria for blending – the equity interest asset and net position get eliminated in the blending process.



Accounting

If the equity interest is held by a special purpose government engaged only in fiduciary activities

- Follow guidance in GASB 72, par 64



Accounting

If a government acquires 100% equity interest in a legally separate organization

- The acquired entity is required to follow guidance in GASB 69 (Government Combinations) which may require restating asset and liability balances



GASB Current Projects





An illustration of a woman with blonde hair in a bun, wearing a black business suit and a headset, pointing towards a green screen. The screen displays the text "CONCEPTUAL FRAMEWORK" in large white capital letters. Below this, in a white box, is the text "meaning, definition, explanation...". The entire scene is framed by a dark blue border with white horizontal bars at the top and bottom.

Conceptual Framework - Recognition



Conceptual Framework - Recognition

Project description

- To develop recognition criteria for *whether* information should be reported in state and local governmental financial statements and *when* that information should be reported.



Conceptual Framework - Recognition

Project history

- 2005 – added to the technical agenda
- 2007 – deliberations began
- 2011 – preliminary views issued, public hearings held
- 2012 – project put on hold
- 2018 – 2nd preliminary views issued
- 2019 – Board is deliberating



Conceptual Framework - Recognition

Issues GASB wants to address

- Current resources measurement focus has no *conceptual foundation*
- Want maintain goal of a short-term perspective
- Remove inconsistencies with short-term perspective
 - Reporting long-term receivables, inventories, prepaid expenses
- Provide guidance for more complex transactions – SCAs, derivatives, etc.
- Provide more consistency in application of the ‘available’ criteria



Conceptual Framework - Recognition

Current proposal

- More symmetry between reporting assets and liabilities
- Assets recognized include cash and other financial resources to be converted to cash within the next year
- Liabilities from short-term transactions recognized as incurred
- Assets and liabilities from long-term transactions would be recognized when payments to be received or paid become due



Conceptual Framework - Recognition

Project timeline

- 2019 – Public hearings to be held
- 2020 – Issue exposure draft, public hearings
- 2022 – Issue final standard





Revenue and Expense Recognition



Revenue and Expense Recognition

Project description

- To develop a comprehensive application model for the classification, recognition, and measurement of revenues and expenses.



Revenue and Expense Recognition

Project history

- 2016 – added to technical agenda, deliberations begin
- 2018 – invitation to comment issued, public hearings held
- 2018/2019 – Board is deliberating



Revenue and Expense Recognition

Current models being evaluated

- **Exchange/non-exchange**
 - Recognize exchange transactions based on earnings recognition approach
 - Recognize non-exchange transactions based on GASB 33
- **Performance obligation/non-performance obligation**
 - Transactions with performance obligations – recognize based on performance obligation recognition approach
 - Transactions absent performance obligations – recognize based on GASB 33



Revenue and Expense Recognition

Project timeline

- 2019 – deliberations
- 2020 – invitation to comment to be issued
- 2020 – preliminary views to be issued, public hearings
- 2021 – exposure draft to be issued
- 2023 – final standard to be issued



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Reporting Model Re-examination



Reporting Model Re-Examination

Project history

- 2013 – pre-agenda research
- 2015 – added to technical agenda, deliberations begin
- 2016 – invitation to comment issued
- 2017 – public hearings
- 2018 – preliminary views issued
- 2019 – deliberations on-going



Reporting Model Re-Examination

Project description

- To make improvements to the financial reporting model to enhance the effectiveness of the model in providing information that is essential for decision-making and enhance the ability to assess a government's accounting and address certain application issues.



Reporting Model Re-Examination

Issues GASB wants to address

- MD&A – explore options to make it less ‘boilerplate’ in nature
- Government-wide statements – explore alternatives to the statement of activities, and if a cash flow statement should be required
- Major funds – explore options for providing additional information for debt service funds
- Governmental funds – in conjunction with conceptual framework, develop financial format consistent with the measurement focus and basis of accounting
- Proprietary funds – evaluate operating indicators



Reporting Model Re-Examination

Project timeline

- 2019 – deliberations, public hearings
- 2020 – issue exposure draft
- 2022 – issue final standard



Questions?





**THANK
YOU**





Capital Asset Accounting in Governments

State of Montana Government Conference
April 23, 2019

What We Will Cover

- Challenges and difficulties in accounting for capital assets
- Lessons learned from your peers involving internal controls over capital assets
- Capital Assets Best Practices for Local Governments



What does GAAP say?

Capital assets are assets that 1) are used in operations and 2) have an initial useful life in excess of one year. The term embraces both tangible assets (land, buildings, building improvements, vehicles, machinery, equipment, works of art, historical treasures, infrastructure) and intangible assets (easements, software, water rights)

- Resources with present service capacity the government presently controls
- Present service capacity – capability to enable the government to provide service and fulfill its mission
- Control – ability of the government to utilize the resources present service capacity and to determine the nature and manner and use, contractual rights, legal ownership



What does GAAP say?

What about improvements – when would you capitalize?

- increase their utility (through increased capacity or serviceability)
- extend their total estimated useful life.



Challenges and difficulties

- Integrity of existing capital asset information
- What is or is not a capital asset?
- Annual additions and retirements of capital assets
- Timeline for annual updates
- Property control of minor but sensitive assets
- Title issues (examples – joint operations, transit)

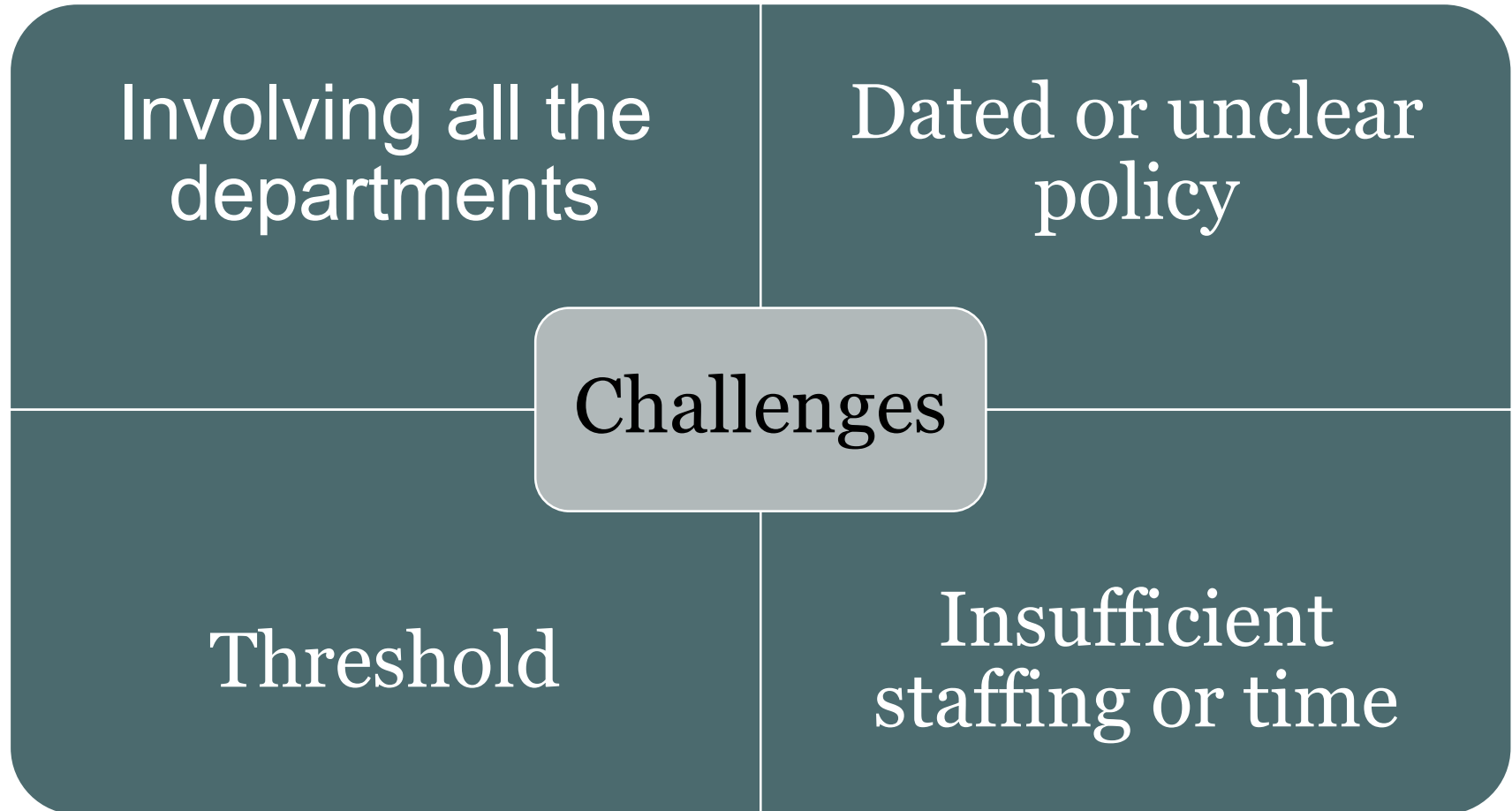


Integrity of existing capital asset information

- Last asset inventory
- Last verification of existing data
- Unrecorded assets
- Unreported retirements
- Enhancements
 - Increase of capitalization threshold
 - Multiple capitalization thresholds
 - Edit, streamline, adjust data



Annual additions



Examples of current expenditures

Buildings – painting, roof re-surfacing, replace HVAC, re-carpet, plumbing repair and replacement, upgrade electrical service, landscaping.

Roads – Re-stripe, replace culvert, replace signage, replace guardrail, re-surface existing road, bridge joint repair, replace streetlight

Use your judgement





Annual retirements - challenges

- Unreported Retirements?
- Incomplete data?
- Communication problems?
- Too busy?
- Seems unimportant?
- Whose responsibility is it?
- Federal surplus case



Other challenges

No schedule or timeline for reporting

Policy in place not being followed

Minor, but sensitive items – what are those?

- Items that cannot be controlled centrally
- Department items
- Probably already being done – but is there a policy?
- GFOA recommended practice on ‘control of minor but sensitive items’



Other challenges



CWIP

- Often no reporting
- Many questions regarding capital versus expenditure
- Questions on elements of historical cost
- Either too much or too little detail



Example challenges from your peers

- Prior period adjustments
- Disposal of asset that does not exist in the records/books
- Software conversion resulted in discovery of multiple capital asset policies by department
- CWIP
- Inventory of assets

- Audience examples??



Best Practices

Establish a clear and concise Capital Asset Policy

Importance of capitalization threshold or multiple thresholds

Short and to the point

Examples

Include a timeline

Responsibilities

Follow the Policy

Establish, communication, and follow updating procedures

Responsibility: Who, what, where, when, how, why

Templates for additions and disposals

Annual reporting Process

Asset additions and retirement

Capital assets only

Additions in year of acquisition

Retirements in year of disposal

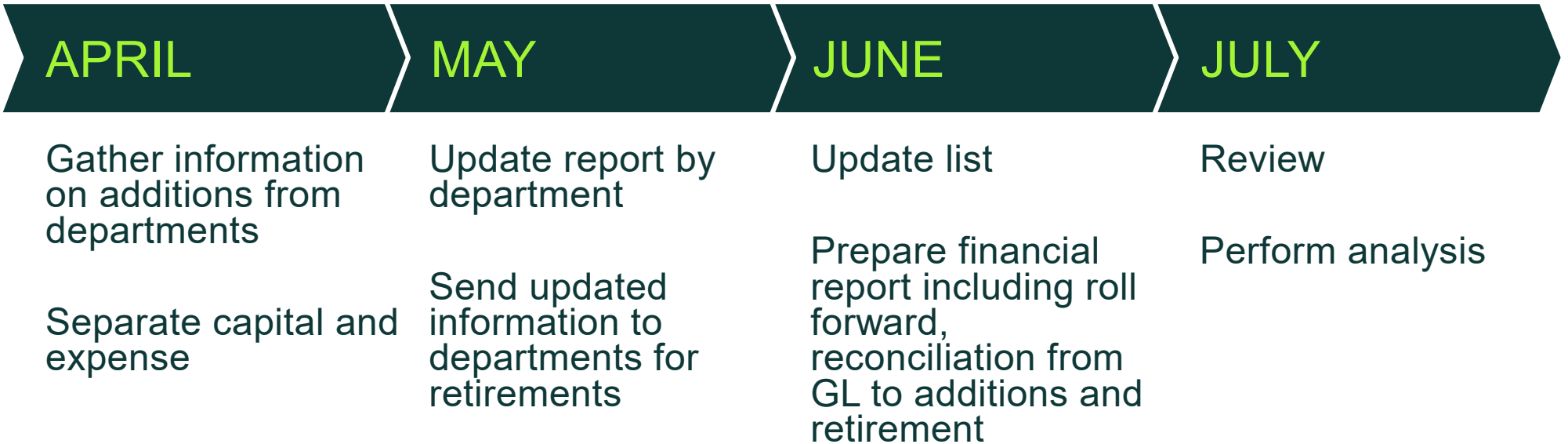
CWIP capitalized in year put into use.

High level analysis

Challenge departments with no disposal



Example timeline



GFOA Best Practices and Advisories

(referenced for your future use)

- Establishing Appropriate Capitalization Thresholds for Capital Assets
- Establishing the Estimated Useful Lives of Capital Assets
- Ensuring Control over Noncapitalized Items
- Capital Asset Assessment, Maintenance and Replacement Policy
- The Need for Periodic Inventories of Tangible Capital Assets



Establishing Capitalization Thresholds for Capital Assets

- Capitalization is primarily a financial reporting issue
 - Principal concern should be the information needs of the users of the financial reports
 - While it is essential to maintain control over all potentially capitalizable items, there are much more efficient ways to accomplish that task
- From GFOA Best Practice – Oct 2005
- Consider different thresholds for different classes of capital assets



Establishing Capitalization Thresholds for Capital Assets – GFOA Best Practice Recommendations

- Capitalize only if estimated useful life of at least two years (review for compliance with State expectations)
- Thresholds are best applied to individual items rather than groups of items
- Threshold should never be below \$5,000
- Governments that are recipients of federal awards should be aware of federal requirement that prevent the use of capitalization thresholds in excess of certain specified maximum amounts for purposes of federal reimbursement
- Exercise control over potentially capitalizable items that fall under operative capitalization threshold



Questions?

THANK YOU!



The material appearing in this presentation is for informational purposes only and should not be construed as advice of any kind, including, without limitation, legal, accounting, or investment advice. This information is not intended to create, and receipt does not constitute, a legal relationship, including, but not limited to, an accountant-client relationship. Although this information may have been prepared by professionals, it should not be used as a substitute for professional services. If legal, accounting, investment, or other professional advice is required, the services of a professional should be sought.

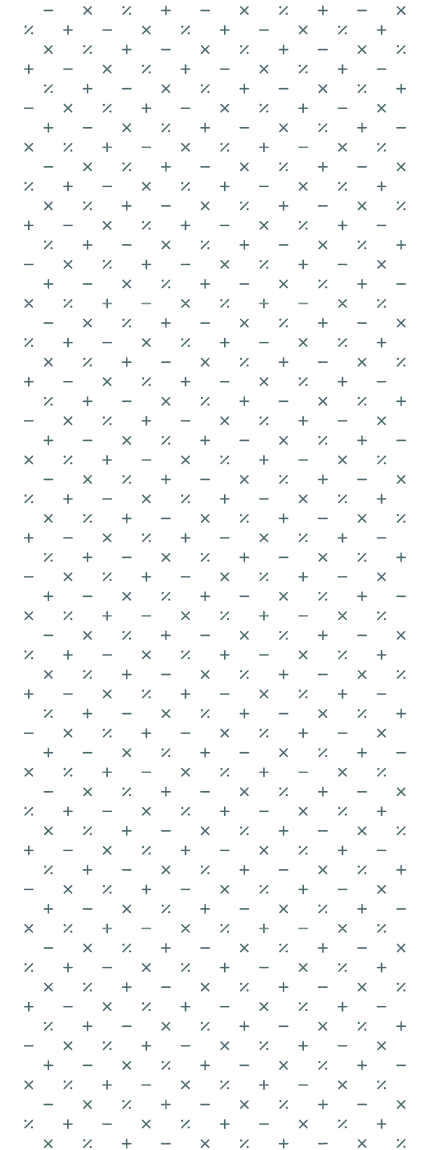




Financial Policies

State of Montana Governmental Conference

April 23, 2019



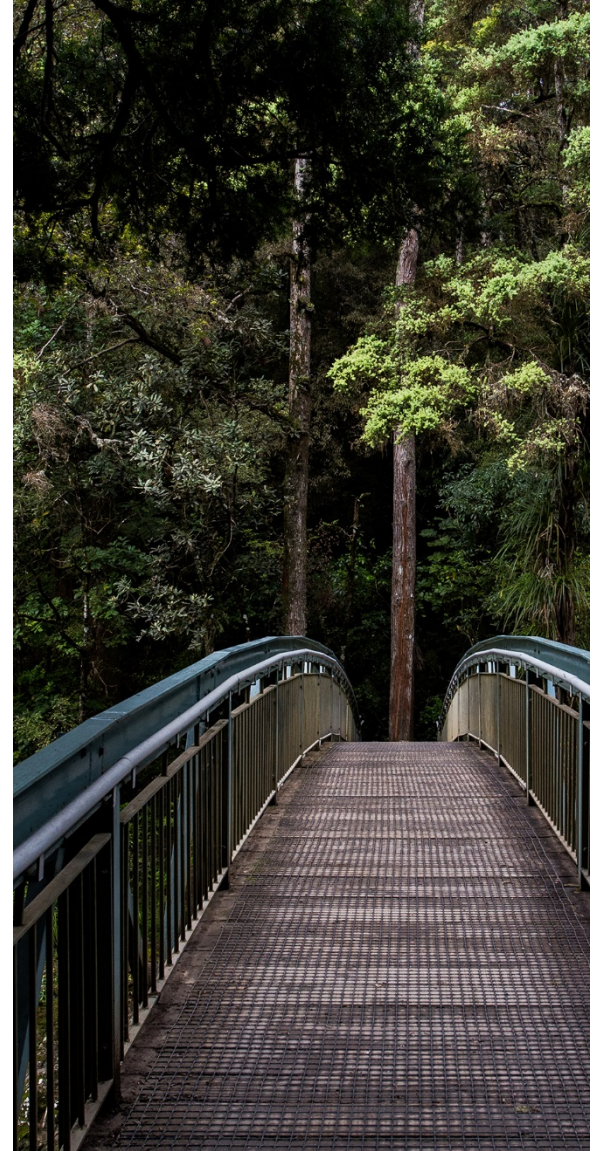
At the end of this session,
participants will be able to:

- ❖ Identify best practices for financial policies following a review of GFOA best practices.
- ❖ Better understand the disclosure requirements in annual external financial statements.





Financial Policies – GFOA Best Practices



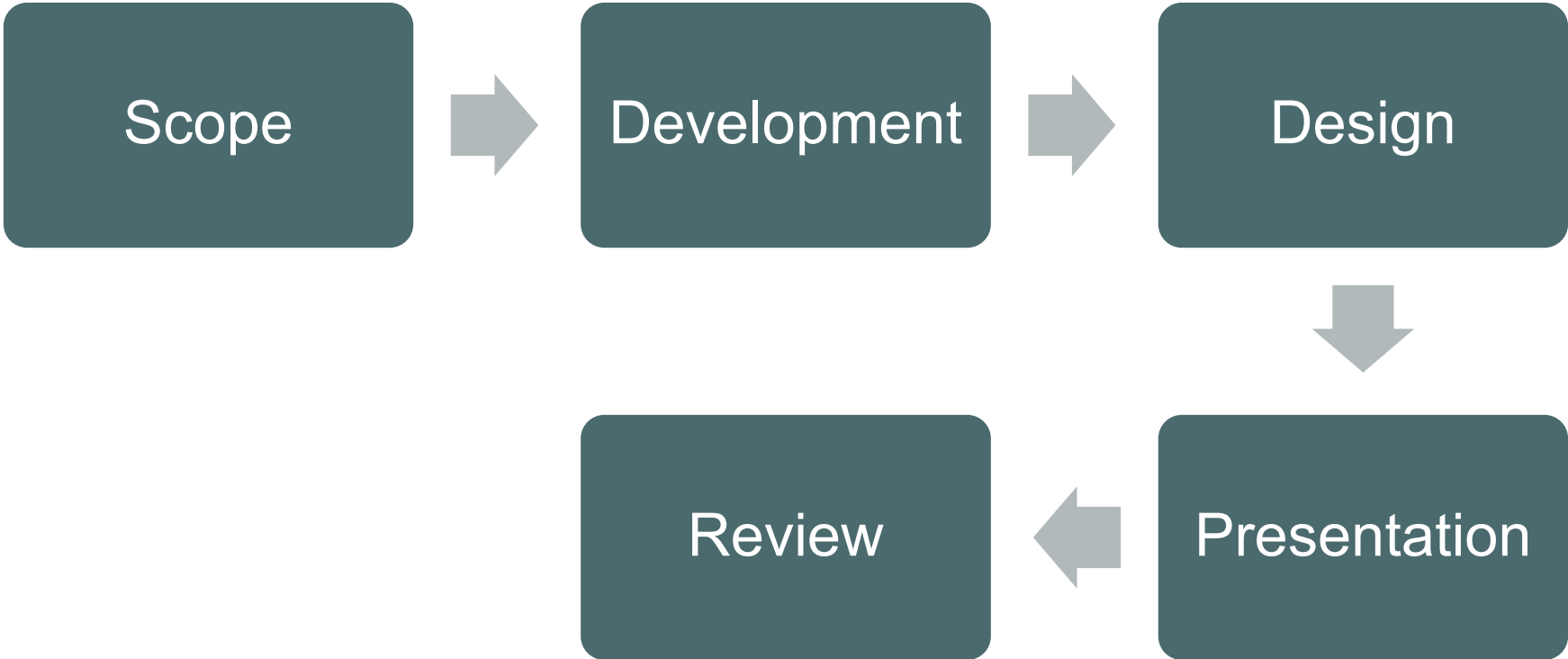
Overall Financial Policies to Consider for Adoption



Overall Financial Policies to Consider for Adoption (continued)



Adopting Financial Policies – GFOA Best Practices



Fund Balance Guidelines for the General Fund – GFOA Best Practices

- Focus on unrestricted fund balance (GAAP)
 - Committed fund balance
 - Assigned fund balance
 - Unassigned fund balance
- Minimum level of *unrestricted fund balance* should approximate 2 months of regular revenues or regular expenditures
- Consider the following in the context of long-term financial planning:
 - Revenue predictability, expenditure volatility
 - Perceived exposure to one-time outlays
 - Availability of other resources
 - Impact on bond rating
 - Commitments and assignments



Fund Balance Guidelines for the General Fund – GFOA Best Practices (continued)

Finance Reports for Reconciling Designated Funds (cont.)

Reconcile to the Budget (if applicable), YTD Expenditures and Encumbrances on the Operating Ledger Summary

Reconcile to the Cash in Treasury and/or the Fund Balance on the General Ledger

- Use and replenishment – generally, should replenish within one to three years of use
- Consider:
 - Budgetary reasons behind the fund balance targets
 - Recovering from an extreme event
 - Political continuity
 - Financial planning time horizons
 - Long-term forecasts and economic conditions
 - External financing expectations

Determining Working Capital Targets for Enterprise Funds – GFOA Best Practices

- Use working capital as the measure of available margin or buffer in enterprise funds
- Defined as current assets minus current liabilities
- Recommendations:
 - Establish appropriate allowance for uncollectibles
 - Ensure inventories and prepaids included in current assets are realistic one-year estimates
 - Target of no less than 45 days worth of annual operating expenses
- Considerations and factors for setting a working capital target:
 - Support from general government
 - Transfers out
 - Cash cycles
 - Customer concentration
 - Demand for services
 - Control over rates and revenues
 - Asset age and condition
 - Control and volatility of expenses
 - Management plans for working capital
 - Debt position



Common Reserve Programs

1 General Fund – Fund Balance

2 Capital Asset Major Repairs & Replacements

3 Employee Benefits

4 “Rainy Day” Funds

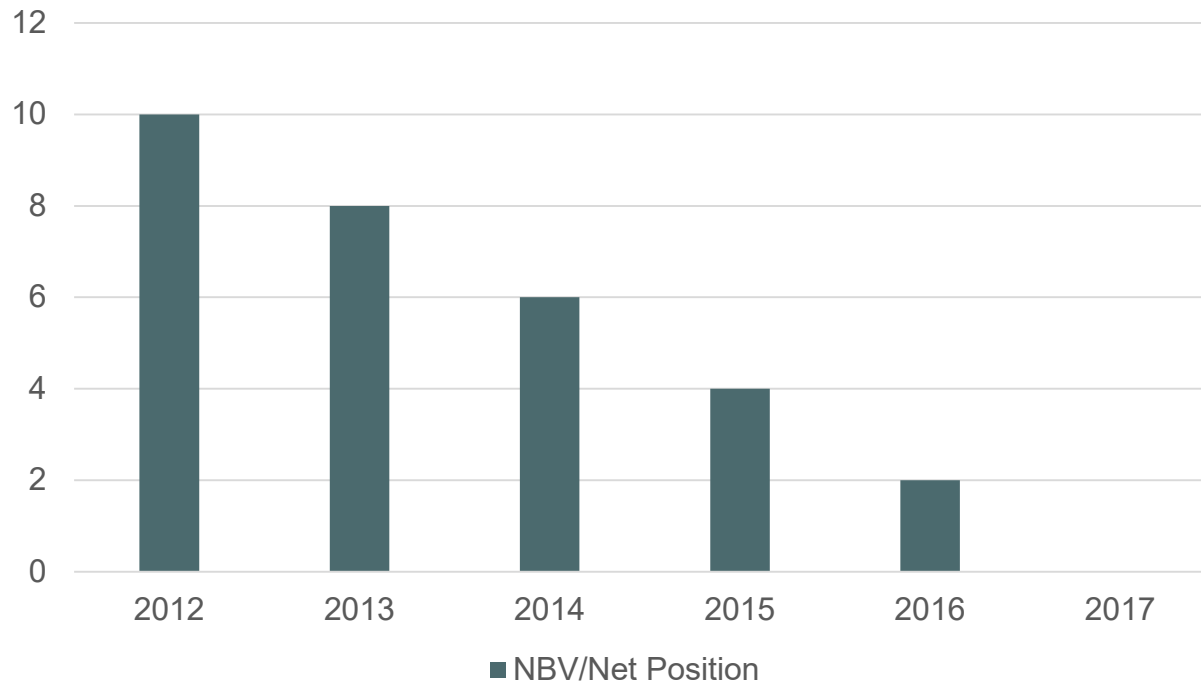


Capital Planning – GFOA Best Practices

1. Description of how an organization will approach capital planning.
2. Definition of what constitutes a capital project.
3. Establish a capital improvement program review committee.
4. A description of the role of the public and stakeholders in the process.
5. Identification of how decisions will be made in the capital planning process.
6. Requirement that the planning process includes an assessment of fiscal capacity.
7. Procedure for accumulating necessary capital reserves for both new and replacement purchases.
8. Policy for linking funding strategies with useful life of the asset.
9. Requirement that a multi-year capital improvement plan be developed and it include long-term financial considerations.
10. Process for funding to ensure capital project funding is consistent with legal requirements.
11. Requirement that the plan include significant capital maintenance projects.
12. Provisions for monitoring and oversight of the CIP program, including reporting requirements.



Capital Asset Reserve Idea (\$10k Auto purchased 2012 – Five Year Life)

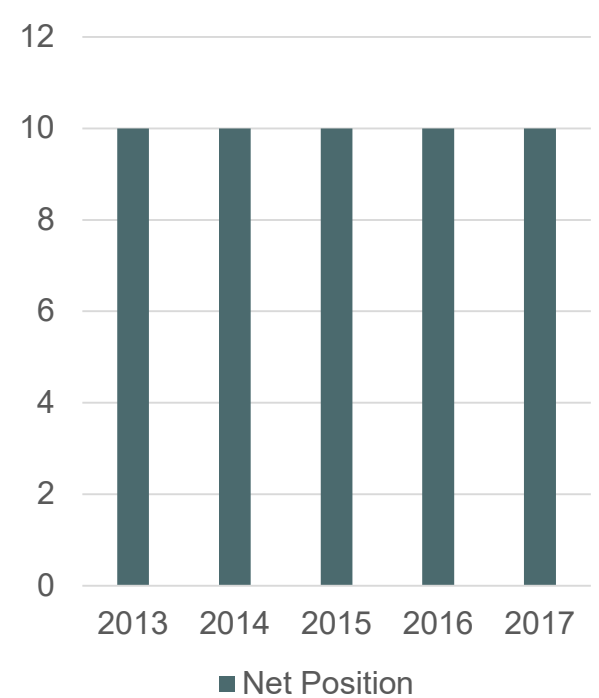
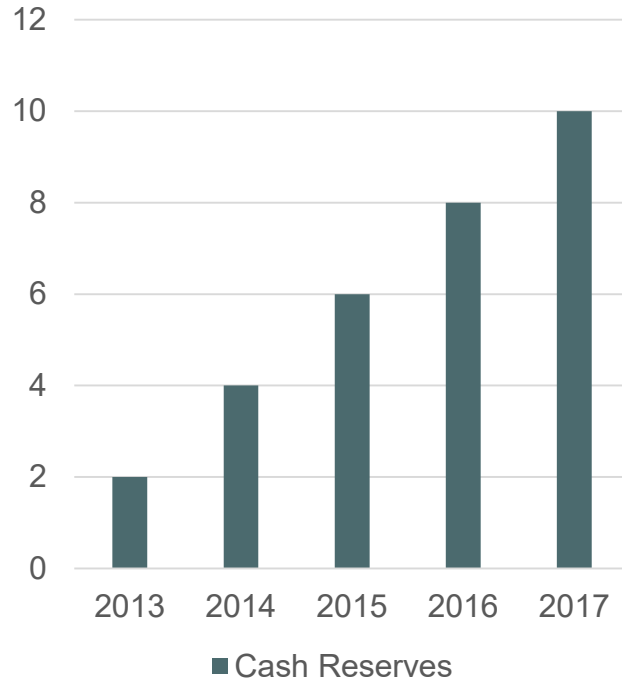
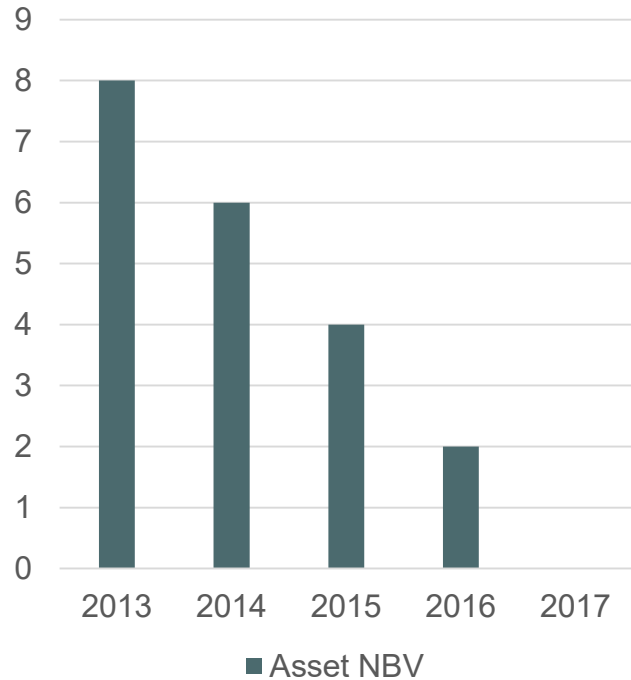


Capital Asset Reserve Idea

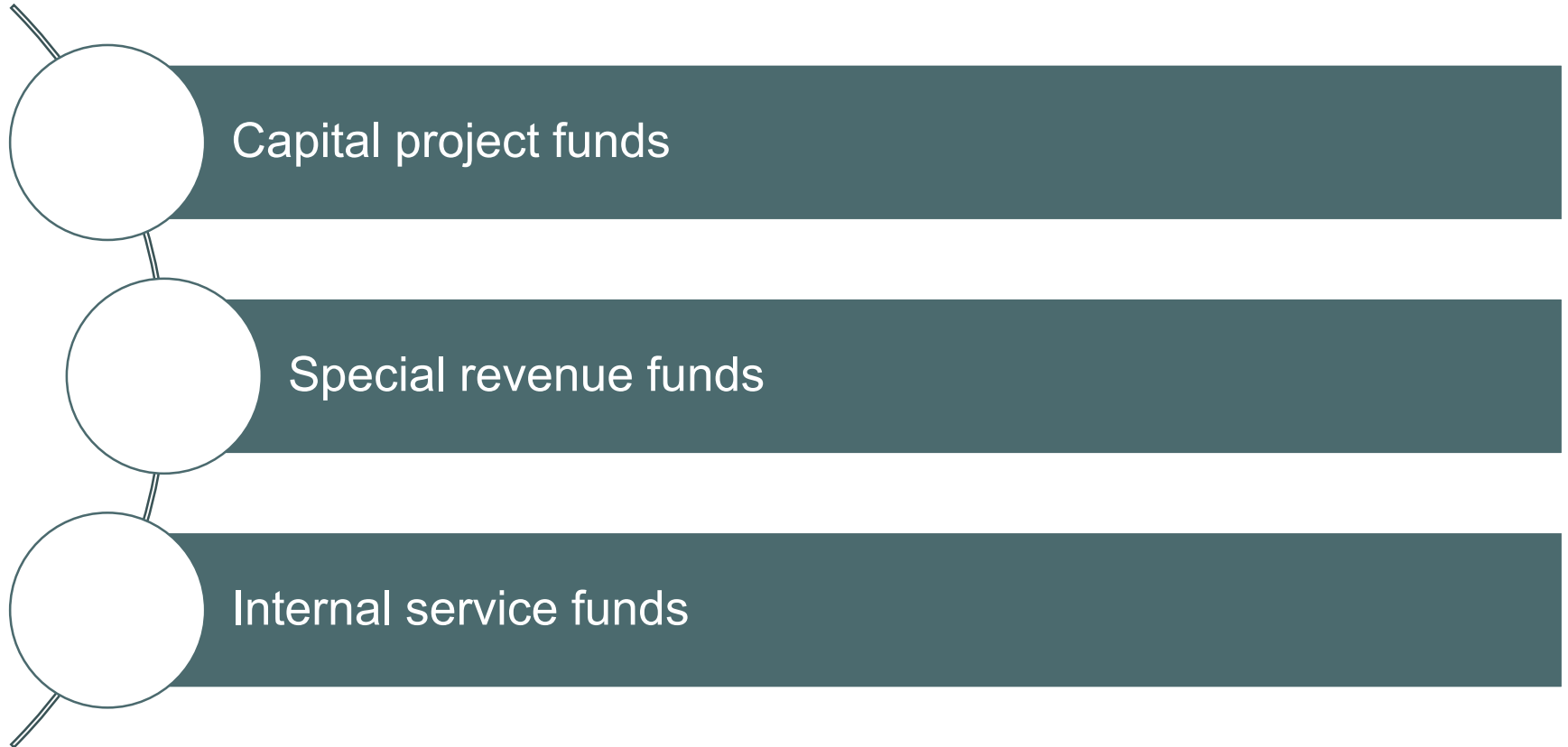
(\$10k Auto purchased 2012 – Five Year Life – Replaced 2017)



13



Fund Types that Can Accommodate Capital Reserve Programs



Pricing Internal Services

Identify goals

- Govern demand for a service
- Develop enterprise rate models
- Calculate indirect costs
- Provide input for full costing
- Discuss value of service
- Promote competition in service delivery
- Customize service levels for different customers

Decide basis for allocation

- Cause and effect relationship
- Benefit received
- Fairness
- Legal constraints

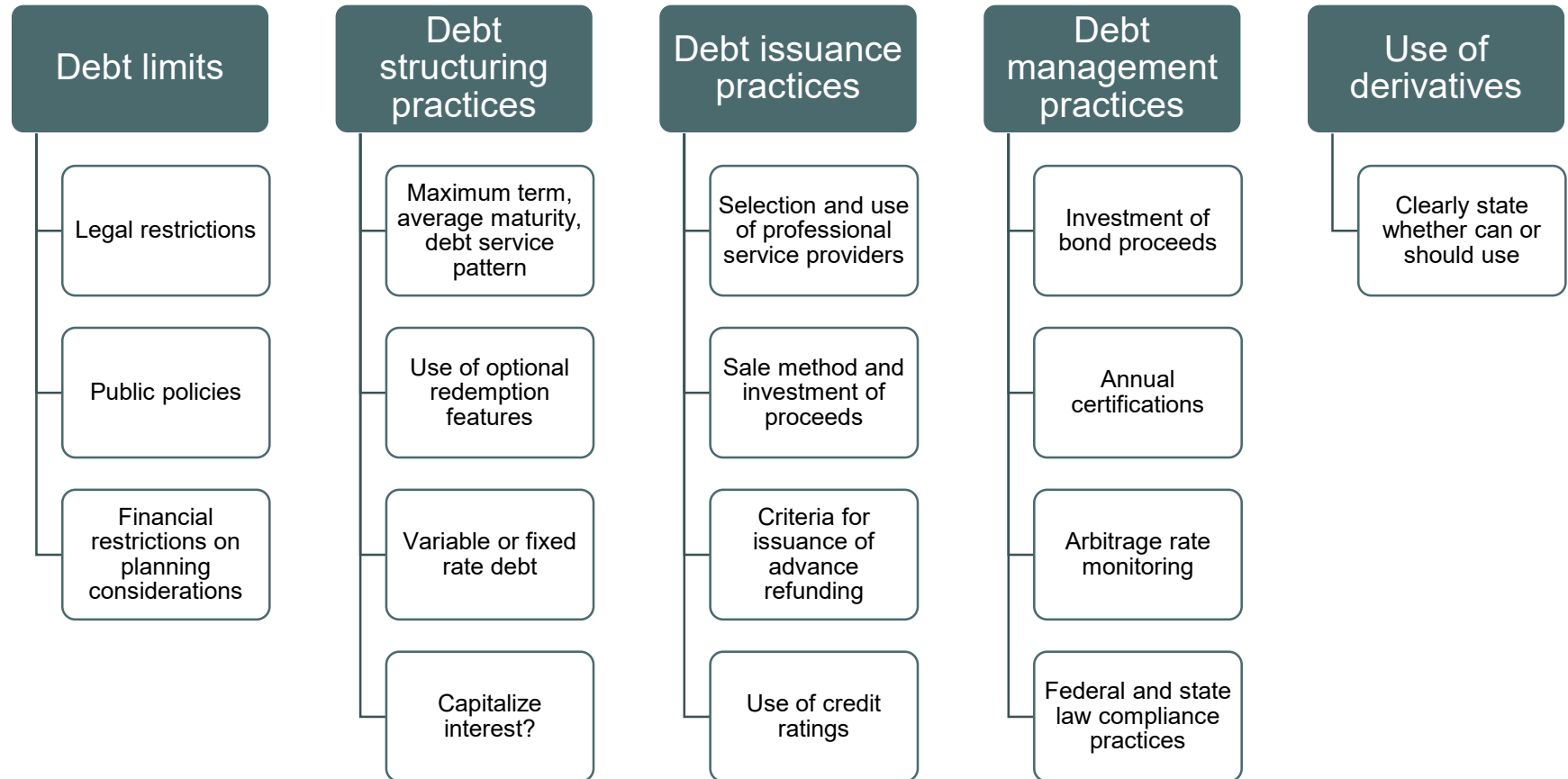


Examples of Cost Allocation Bases

Internal Service	Basis
Payroll processing	No. of employees, no. of checks
Budgeting	Labor hours, size of budget
Insurance	No. of employees, experience
Legal services	Direct labor hours
Office space and/or rent	Square feet of space occupied
Procurement services	No. of Pos, dollar volumes, direct labor
Vehicle costs	Miles driven, hours used
Information technology	No. of devices, server time, no. of desk calls, direct labor hours



Debt Management – GFOA Best Practices



BONUS! Long-Term Financial Planning – GFOA Best Practices

Elements

Time horizon
– 5 to 10
years in the
future

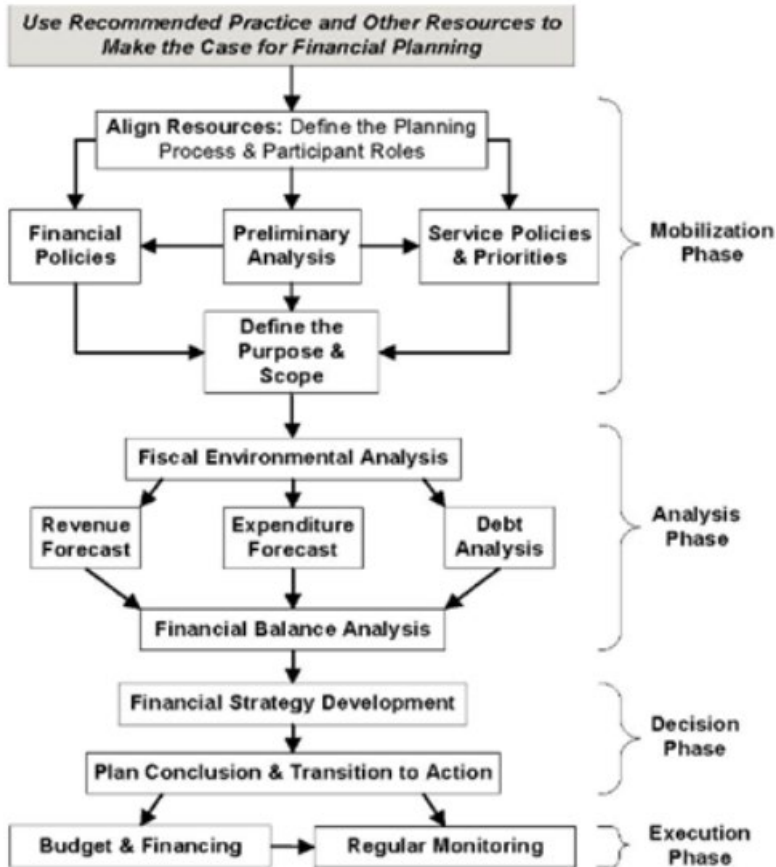
Scope –
consider all
appropriated
funds

Frequency –
update as
needed

Content –
should
include an
analysis of
the financial
environment

Visibility –
should be
easy to learn
about and
obtain!





BONUS! Long-Term Financial Planning – GFOA Best Practices

Mobilization

- Alignment of resources
- Preliminary analysis
- Identify service policies and priorities
- Validate financial policies
- Define purpose and scope of planning

Analysis

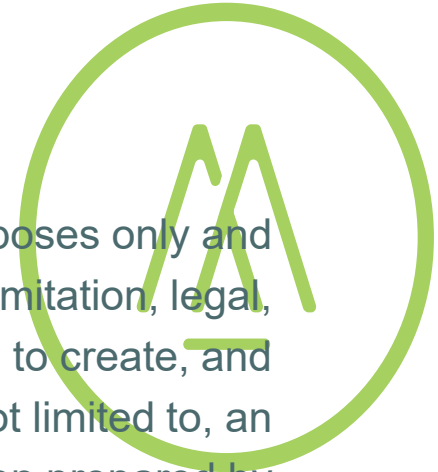
- Information gathering
- Trend projection
- Analysis

Decision

- Buy-in
- How will you execute for results?

Execution

- Put strategies into action – through the budget, financial performance measures, and action plans!



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THANK
YOU

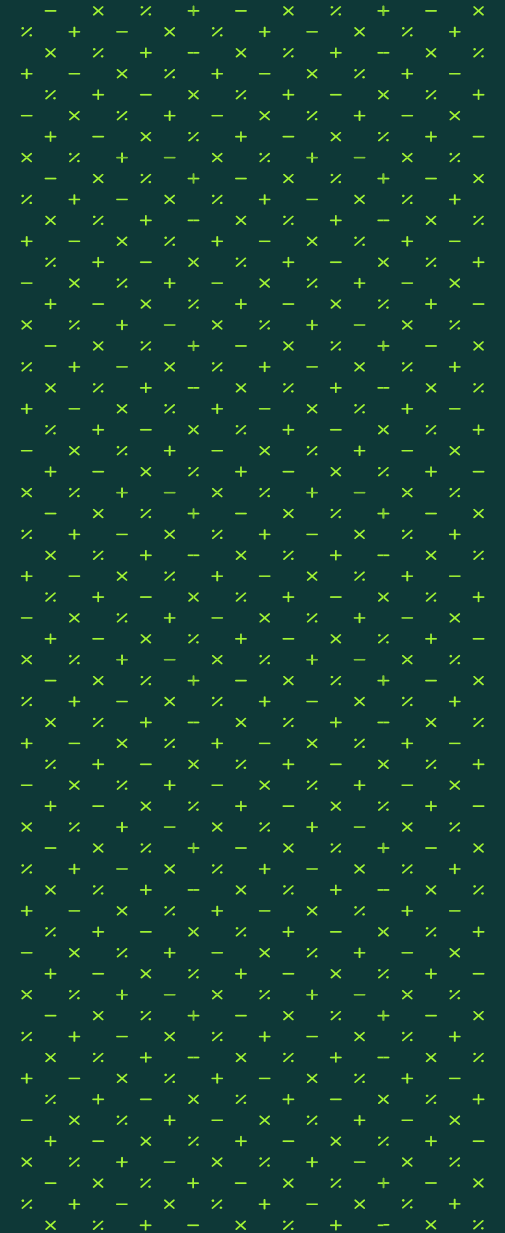


MOSSADAMS

Internal Controls, Recent Frauds, Cybercrimes

State of Montana Governmental Conference

April 23, 2019



Agenda

- Fraud cases in the headlines
- What went wrong with internal controls
- Corrective actions taken



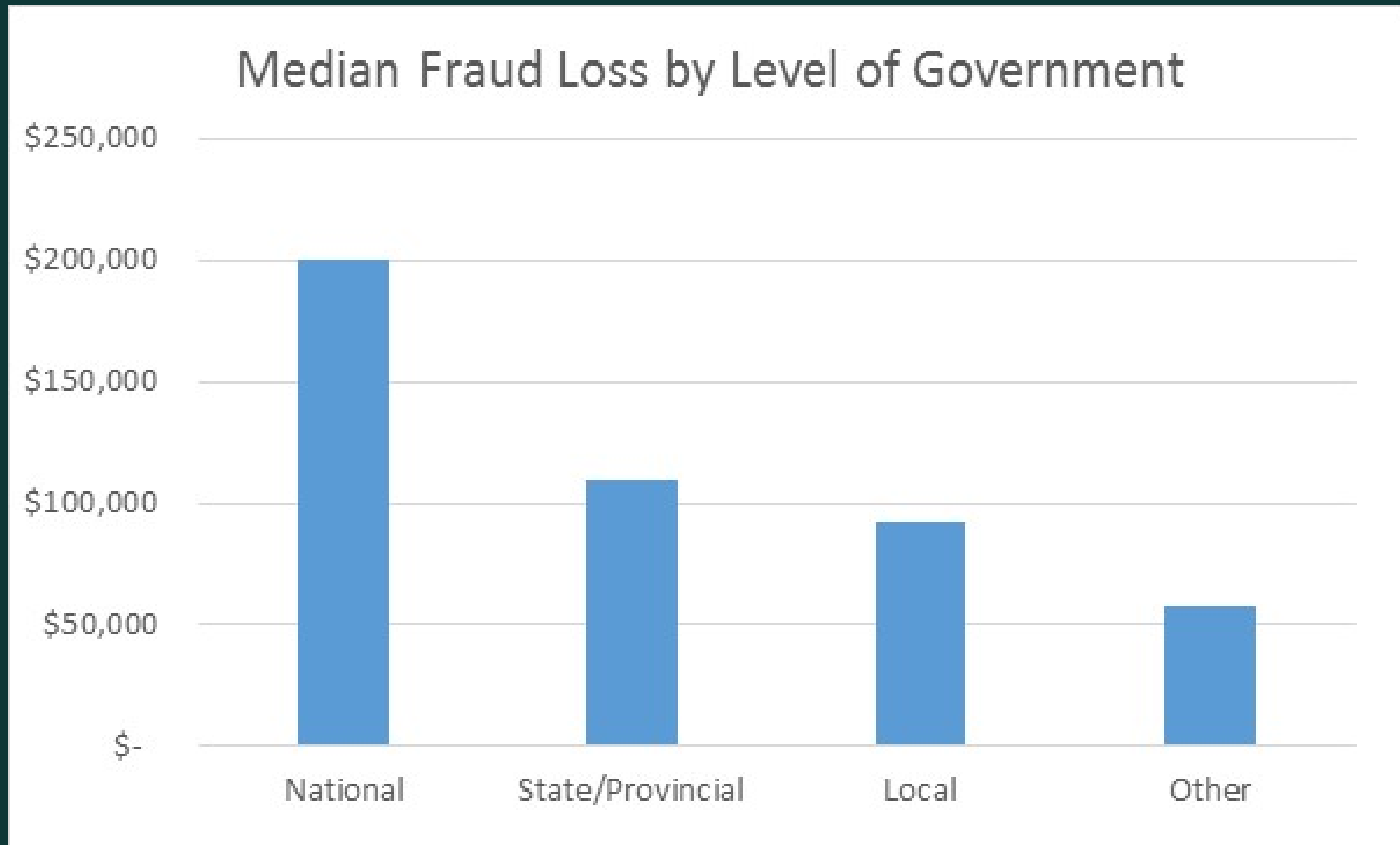
REPORT TO THE NATIONS

2018 Global Study on Occupational Fraud and Abuse

What levels of governments
are victimized by
occupational fraud?

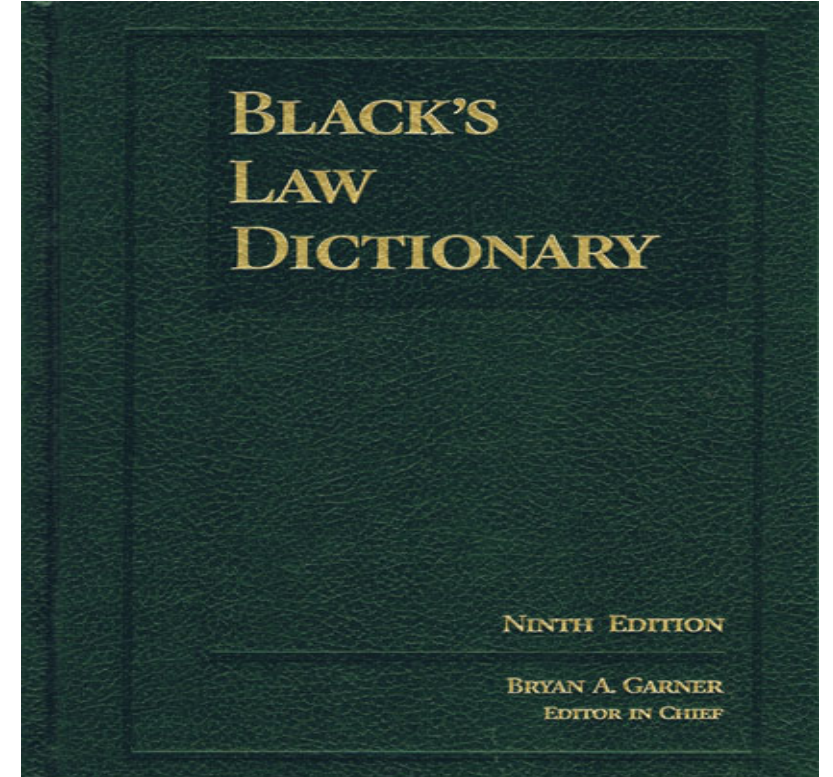
REPORT TO THE NATIONS

2018 Global Study on Occupational Fraud and Abuse



Definition of Fraud

...all multifarious means which human ingenuity can devise, and which are resorted to by one individual to get an advantage over another by false suggestions or suppression of the truth. It includes all surprise, trick, cunning, or dissembling, and any unfair way by which another is cheated.



Definition of Waste

*The needless, careless, or **extravagant** expenditure of an organizations funds, incurring of **unnecessary** expenses, or mismanagement of organization resources or property. Waste does not necessarily involve private use or personal gain, but almost always signifies **poor management** decisions, practices, or controls.*

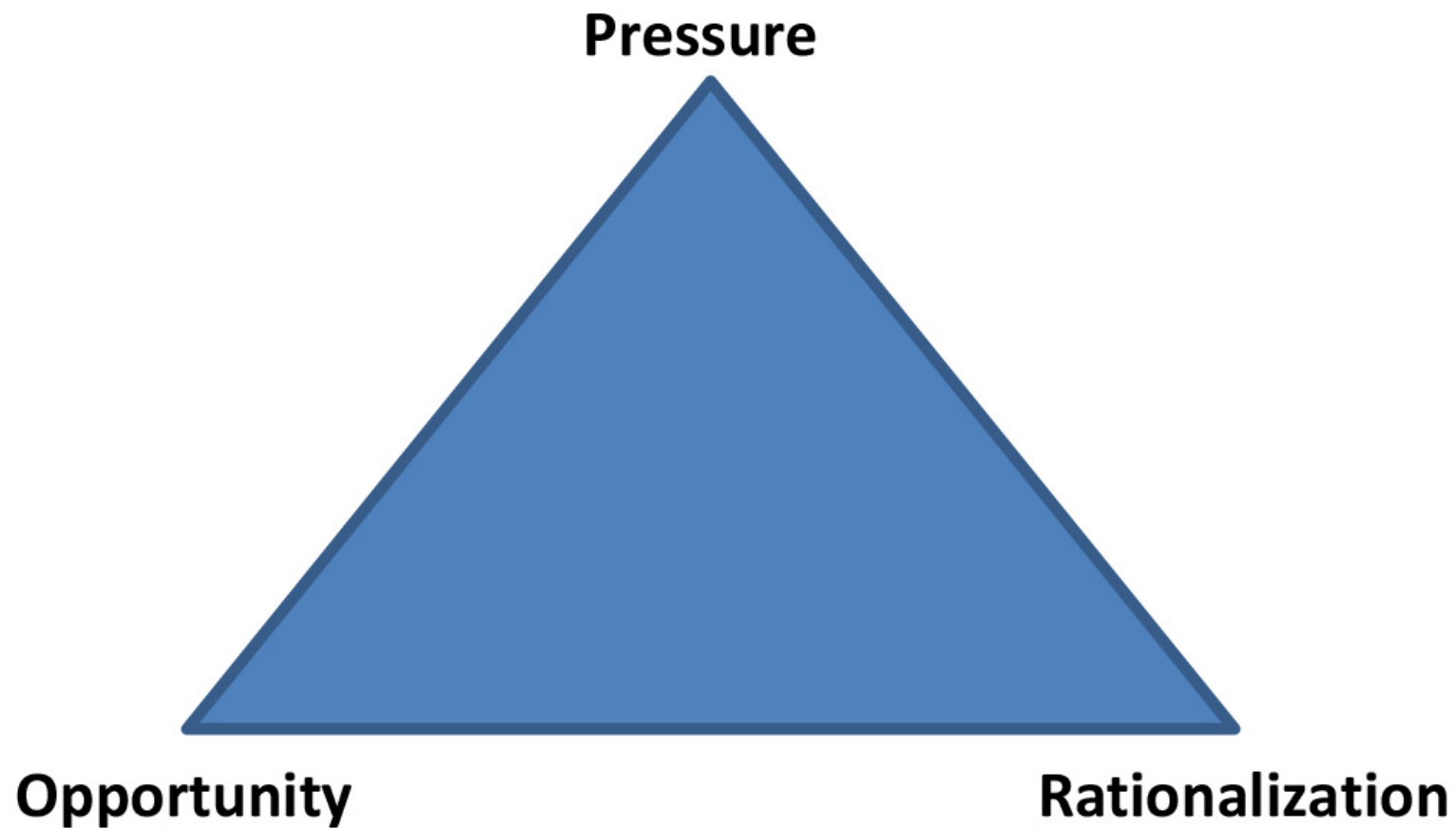


Definition of Abuse

*The **intentional, wrongful, or improper** use or destruction of organization resources, or seriously improper practice that does not involve prosecutable fraud. Abuse can include the excessive or improper **use by an employee or official's position** in a manner other than its rightful or legal use.*



Fraud Triangle



Components of Internal Control

Control environment

Risk assessment

Control activities / control procedures

Information & communication systems

Monitoring



Types of Controls

Preventive

Detective

Corrective

Manual and/or Automated



Former Eugene Catholic school advancement director sentenced to 2½ years in prison



MOST POPULAR

- 1 Two massage parlors raided in Springfield, three arrested
Apr 1 at 8:29 AM
- 2 5 arrested on drug charges related to Springfield teen's death
Mar 30 at 8:06 PM
- 3 Tall chin from 'Pirates of the

By Chelsea Deffenbacher

[Follow](#)

Posted Jan 28, 2019 at 5:08 PM

Updated Jan 28, 2019 at 5:08 PM

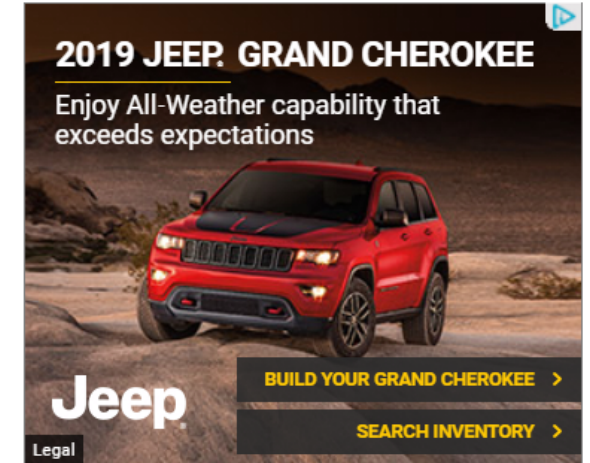


A man accused of embezzling from a Eugene private school and a scholarship foundation last summer was sentenced Monday to 2½ years in prison for the theft of more than \$53,000.

Sean Thomas Jones, 42, of Springfield, who served as the advancement director for O'Hara Catholic School in Eugene and was a board member for the Open Door Foundation, [embezzled \\$3,900 from the school, and \\$50,800 from the Open Door Foundation](#), a privately funded organization that provides scholarships to families that allow their children to attend the private Catholic school.

Eugene police, who arrested Jones in July 2018, said Jones used his position to forge documents and fraudulently obtain access to financial accounts so he could divert funds for his personal use over a three-year period.

On Jan. 11, Jones pleaded guilty to all 12 felonies filed against him, including several counts of forgery, aggravated theft, and computer crimes. On Monday, he was sentenced to 30 months in prison.




Falsified reimbursement check

OPEN DOOR FOUNDATION
715 W 18TH AVE
EUGENE, OR 97402


1010
51-7278/211
01


April 3, 2017 Date

PAY to the *O'Hara Catholic School*
Order of *O'Hara Catholic School* \$ *5,000.00*

Five thousand and 00/100 Dollars  Photo Safe Deposit™ Details on back

FIELDPOINT PRIVATE BANK & TRUST®

FOR *Reimbursement*  NP



Harland Clarke COLONIAL CLASSIC®



Not deposited into School's account

026672784 1060

5000006320

OPEN DOOR FOUNDATION

431300000451619591000040131107

123206024 < B O

ENDORSE HERE

CREDITED TO THE ACCOUNT OF
THE WITHDRAWAL NAMED PAYEE
BANK of the CLASS OF DESI
8002120000 DOWNTOWN, OR



CHECK HERE IF MOBILE DEPOSIT

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE

RESERVED FOR FINANCIAL INSTITUTION USE

Do not cash if

- Any of the features listed above are missing or appear altered
- Fugitive ink on back looks pink or has disappeared
- Brown stains and colored spots appear on both front and back



Memo descriptions on fraudulent checks

Needy family expenses/costs

Reimbursement for stamps \$98, Office Supplies \$145.96 (??) Software \$1,863.93

Reimbursement for foundation housekeeping, printer, scanner

Reimbursement

Reimbursement for Ten (??) Fundraiser supplies - see receipts

Cash for Struggling Family

Payment and Reimbursement (??)

Ladies Tea & Luncheon Raffle Prizes Reimbursement

Reimbursement - Ladies Tea

Administrative Fees

(blank - no memo description)

Prize/Expense Reimbursement

Reimbursement

Reimbursement

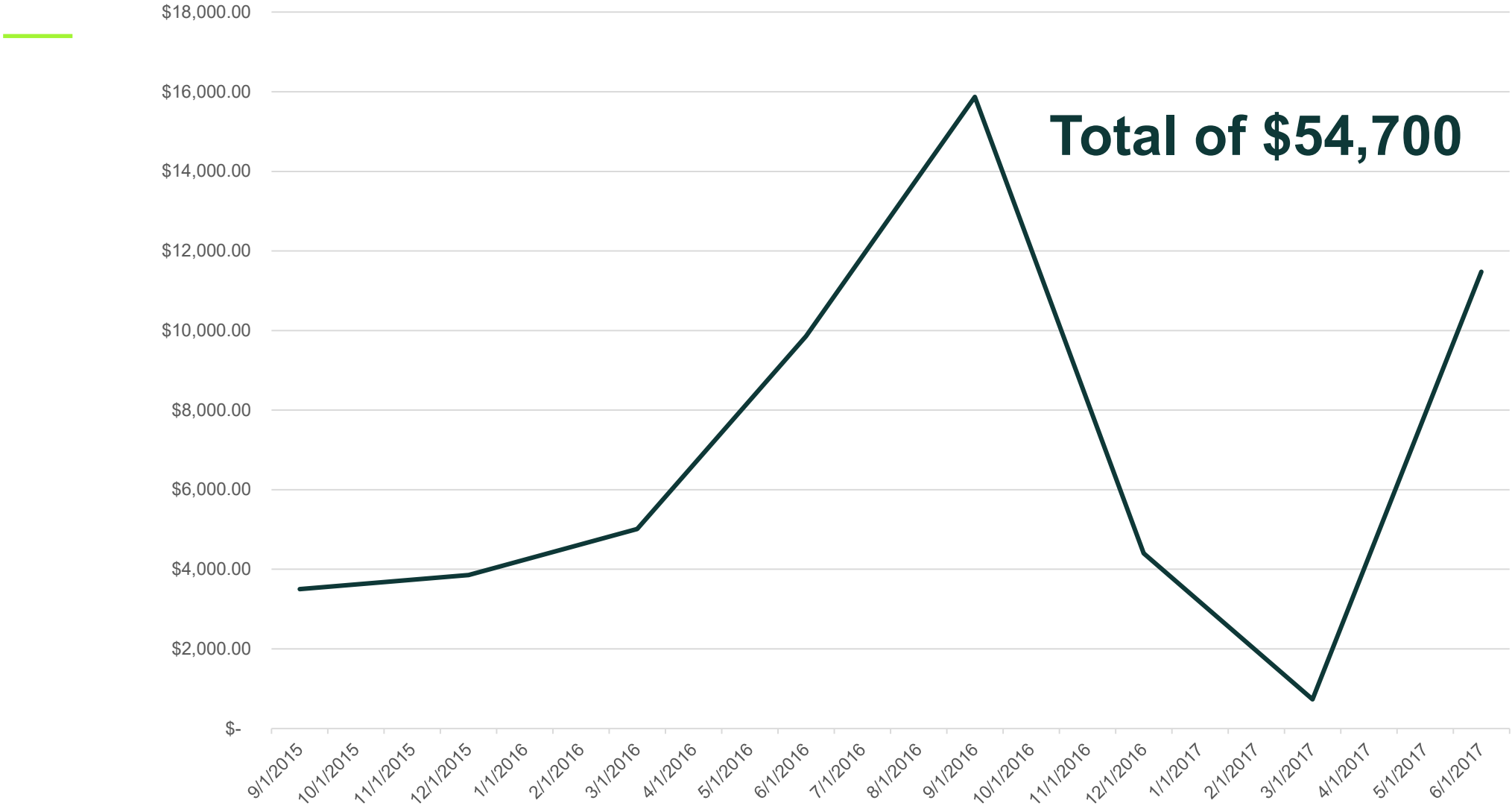
Reimbursement

Reimbursement (??)

Reimbursement & Fees



Dollars Stolen Over Time: August 2015 – May 2017



What went wrong?

- Trust, but verify
- Falsified Board meeting minutes
- Timely review needed
- Job evaluation



Final Thoughts

- Community trust
- IRS reporting requirements
- Bank's obligation
- Internal controls added



\$6.5 Million Embezzled from City of Pasadena



Danny Wooten, City Department of Public Works Management Analyst

- 52 years old, in-charge of relocating utility lines
- City's Underground Utility Program ran by Public Works and Utility departments
- Homeowners filed for up to \$3,750 in reimbursements
- Tyrone Collins was an electrical contractor doing that work
- Two churches invoiced for UUP work
- Accused of 53 counts of embezzlement over 11-year period



How did he do it?

- Forged signatures and faked invoices
- Wooten always filed invoices of \$20,000 and \$23,750
- Wooten also added a “4” on checks in front of the \$3,750
- First 3-4 years, invoices submitted appeared ok
- Next 5 or so years, some invoices filed with no address, or addresses already invoiced
- City paid Collins, and then Collins paid Wooten through money orders or bank transfers
- City also paid a temporary City employee, Melody Jenkins, who then paid Wooten



Results of embezzlement

- Wooten was sentenced to 14 years in prison
- Collins was sentenced to 7 years in prison
- Jenkins had charges dropped
- City recouped \$5 million through insurance and \$200,000 from audit firm
- City fired Finance and Public Works Directors without cause, others on administrative leave



Corrective actions put in place

- Paid audit firm \$400K to investigate fraud and provide recommendations
- Implemented \$6.4M Tyler Munis system with automated controls
- Payments route through several electronic approvals prior to payment
- Once payment approved by program head, payment cannot be altered
- System allows employees to perform analytical review
- Program no longer run by two departments
- Nearly every department head turned over in subsequent two years
- City hired an internal auditor



ACFE's 2018 *Report to the Nations on Occupational Fraud and Abuse*.....

Corruption schemes occurred in 38% of the reported cases with a median loss of \$250,000



Red flags for corrupt employees

- Success rate in market where bribes are common
- Reputation for accepting gifts
- Extravagant lifestyle
- Makes decisions in areas others are responsible for
- Makes excuses for deficiencies
- Extreme personal pressures
- Friendly social relationship with contractors
- Wheeler-dealer attitude



Common Bribes

- Alcohol
- Clothes and jewelry
- Sexual favors
- Lavish entertainment
- Paid holidays
- Free luxury transportation
- Free use of resort facilities
- Gift of briber's inventory or services



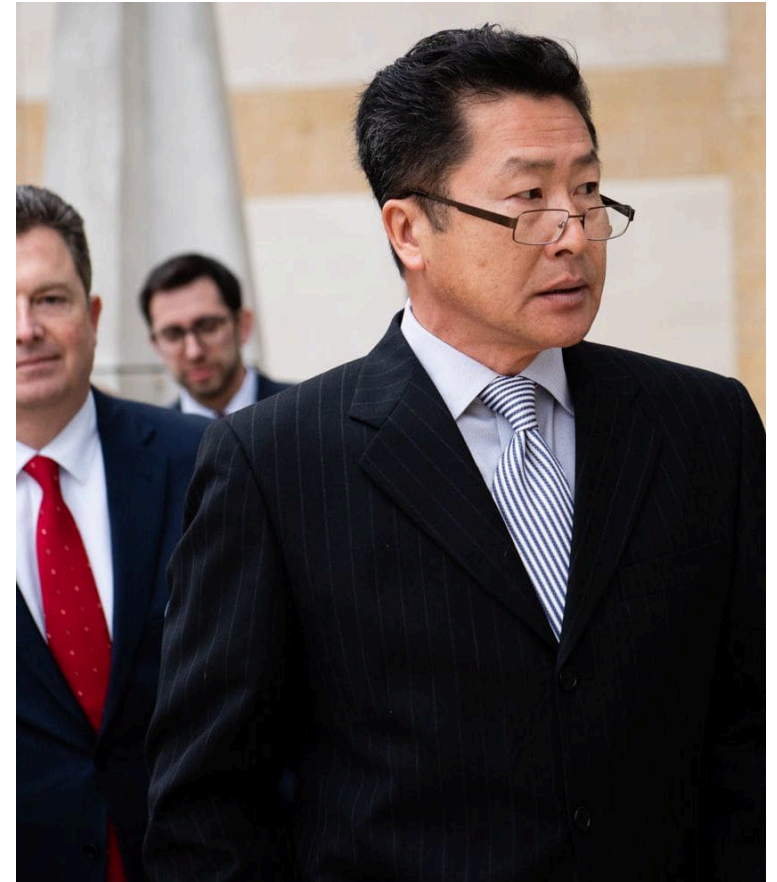
\$6.7 Million Embezzled from Montgomery County, MD



MONTGOMERY COUNTY
ECONOMIC DEVELOPMENT
CORPORATION MARYLAND

Byung II “Peter” Bang, COO of County’s Department of Economic Development

- 58 years old, 20-year employee
- Bang oversaw budgets for incubators
- Bang was authorized to request County pay incubators
- County partnered with Maryland Economic Development Corp and Maryland Conference & Visitors Bureau
- Chungbuk Province provided \$2 million to County incubators, which County would repay in 2015
- County received summons from IRS in April 2017 for all Bang and Chungbuk related records
- Charged with wire fraud and filing false tax returns over 6-year period



How did he do it?

- Department of Finance oversaw incubator program
- County setup incubator fund with Chungcheongbuk province in South Korea
- Bang setup Chungbuk Incubator Fund LLC and 4 bank accounts
- Created fraudulent invoices, which he approved for payment
- Circumvented County procurement freezes during tight budget years
- False development initiatives funded by
 - \$1.2 million from Maryland Economic Development Corp.
 - \$44K from Maryland Conference & Visitors Bureau



Results of embezzlement

- Pressure to commit fraud came from gambling addiction
- Unreported income was \$6.3 million resulting in \$2.3 million underreported federal taxes
- Bang was sentenced to 15 years in prison
- All embezzled money spent
- County to get \$1 million from Bang's retirement at \$137K from home sale



Corrective actions put in place

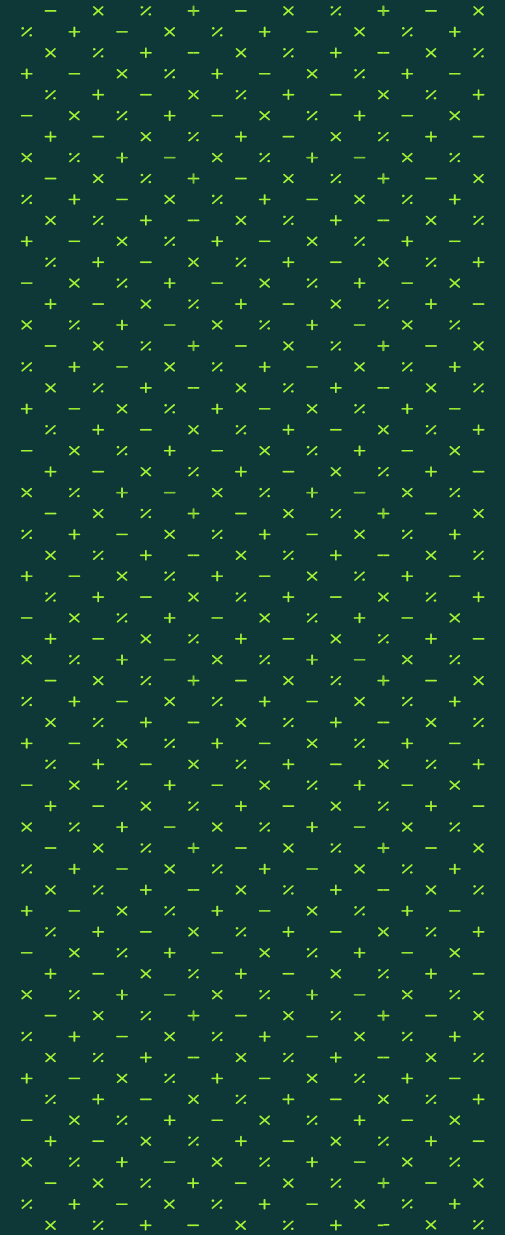
- Hired audit firm to investigate fraud and provide recommendations
- County privatized most of the economic development program
- Additional controls added for irregular procurement agreements
- Compliance unit added to Finance Department
- Monthly GAAP financial statements required from each incubator and annual audits
- Reconcile due to/due from accounts on a quarterly basis
- More hands on department oversees program, rather than Department of Finance
- Execute grant agreements for incubator grants with specific terms, conditions, including restrictions on using County funds





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Cyber Fraud



Agenda

- State of Cybersecurity
- Types of Cyber Fraud



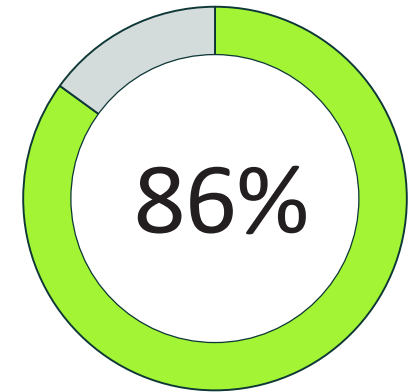


The State of Cybersecurity

State of Cybersecurity Today

It's no longer a question of whether a network will be compromised, but when a network will be compromised.

COMPANIES
that experienced **at least one** cyber incident



Source: 2017/18 Kroll Annual Global Fraud and Risk Report

5 billion

Total number of records breached.

Source: 2018 Year End Data Breach QuickView Report by Risk Based Security

\$3.86 million

Average cost a company pays for a data breach.

Source: 2018 Cost of a Data Breach Study - Ponemon Institute

\$6 trillion

Cost of cyber crime by 2021. More profitable than the trade of illegal drugs.

Source: 2017 Official Annual Cybercrime Report



Types of Sensitive Data

Personally Identifiable Information (PII): Any data that could potentially identify a specific individual.

Cardholder Data: Data associated with payment cards such as primary account numbers, card verification values (CVV), or track 1 & 2 data.

Protected Health Information (PHI): Individually identifiable health information that can be linked to a particular person. Protected by HIPAA.

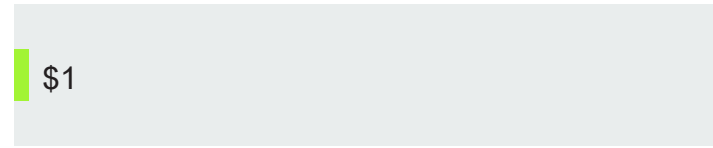
Proprietary Information (PI): Information an organization wishes to keep confidential.



The Going Price of Your Data

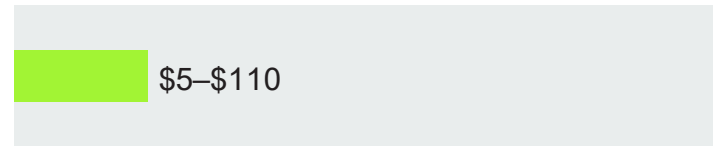
SOCIAL SECURITY NUMBER

Including name

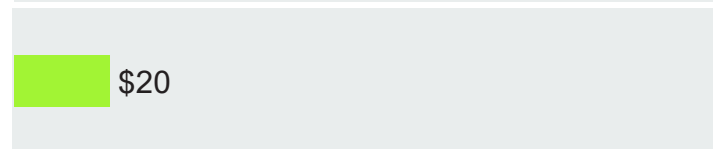


CREDIT CARD

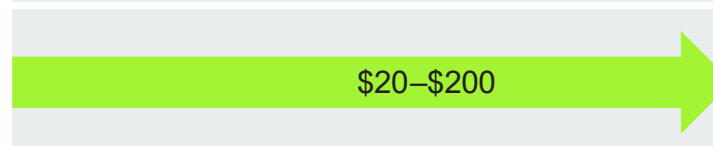
low end includes number, type, expiration date, CCV number, and account holder's name, while the high end includes the SSN, address and DOB



DRIVERS LICENSE

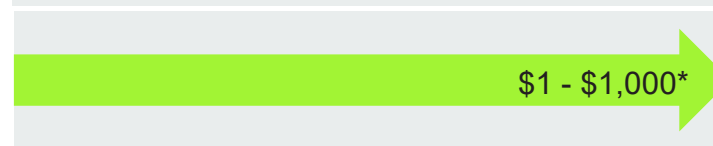


ONLINE PAYMENT SERVICES (PAYPAL)



MEDICAL RECORD

Including SSN, banking details, demographic, job details







*Depends on how complete they are as well as if its a single record or an entire database

Source: 2017 study by Experian



Fraudster/Attacker: Motives, Targets, Impact

Organizations today face four main types of cyber adversaries

	MOTIVES	TARGETS	IMPACT
 NATION STATE	<ul style="list-style-type: none"> Economic, political, and/or military advantage 	<ul style="list-style-type: none"> Trade Secrets Sensitive business information M&A information Critical financial systems 	<ul style="list-style-type: none"> Loss of competitive advantage Regulatory inquiry/penalty Disruption to critical infrastructure
 ORGANIZED CRIME	<ul style="list-style-type: none"> Immediate financial gain Collect information for future financial gains 	<ul style="list-style-type: none"> Financial/payment systems Personally identifiable information Payment card information Protected health information 	<ul style="list-style-type: none"> Regulatory inquiry/penalty Consumer and shareholder lawsuits Brand and reputation Loss of consumer confidence
 HACKTIVISTS	<ul style="list-style-type: none"> Influence political and/or social change Pressure business to change practices 	<ul style="list-style-type: none"> Corporate secrets Sensitive business information Critical financial systems 	<ul style="list-style-type: none"> Disruption of business activities Brand and reputation Loss of consumer confidence
 INSIDERS	<ul style="list-style-type: none"> Personal advantage, monetary gain Professional revenge Patriotism Bribery or coercion 	<ul style="list-style-type: none"> Sales, deals, market strategies Corporate secrets Business operations Personal information Administrative credentials 	<ul style="list-style-type: none"> Trade secret disclosure Operational disruption Brand and reputation Loss of consumer confidence





Cyber Fraud Examples

Common Fraud Schemes

Spearphishing

An email that asks for information—login credentials or bank details—in the hopes of someone innocently responding and providing it.

CEO Fraud/Whaling

This method is the same as spearphishing but targets C-level executives.

Ransomware

Hackers gain access to a system using malicious software, then encrypt sensitive data and hold it hostage—along with your ability to conduct business—until a demand is satisfied.

Malicious Code and Scareware

These are programs such as viruses, trojans, worms, and others that disrupt normal computing to exploit system security flaws.



Social Engineering

“Amateurs hack systems, professionals hack people.” – Unknown

Definition: The art of manipulating people into performing actions or divulging confidential information

- Techniques include email, social networks, phone calls, physical
- Preys on the natural inclination to trust and help others



Phishing/CEO Fraud/Whaling

Definition: Email fraud method in which the perpetrator sends out legitimate-looking email in an attempt to gather personal and financial information from recipients

- Phishing usually involves a problem situation that requires you to take immediate action and “verify” personal information
- Purchase of gift cards
- Focus on accounting personnel and sales



CEO Fraud Characteristics

- The fraudster insists on communicating only via email—insists they “can’t talk right now.”
- No work signature. “Sent from my iPhone.”
- No specifics on the invoice or vendor for the payment. The entire email is vague and depends on the authority of the sender’s position to prevent questions.



AFGlobal CEO Fraud Example

- AFGlobal's Director of Accounting received a series of emails from someone claiming to be the CEO.
- After receiving the initial email, he received a call from someone posing as an attorney from KPMG saying fees in the amount of \$480,000 were needed.
- Follow-up email with wiring instructions followed.
- A week later a request for \$18 million was made—this is when he became suspicious.



Glen, I have assigned you to manage file T521. This is a strictly confidential financial operation, to which takes priority over other tasks. Have you already been contacted by Steven Shapiro (attorney from KPMG)? This is very sensitive, so please only communicate with me through this email, in order for us not to infringe SEC regulations. Please do not speak with anyone by email or phone regarding this.
Regards, Gean Stalcup



CEO Fraud Prevention

Verify that the request is genuine:

- Always verify any wire transfer through multiple means. Never rely solely on email. Talk to the person on the phone, find them in person, etc.
- Establish strict procedures around invoice payment and wire transfers.
- Immediately report any suspicious email to your IT department.
- Do not give out information over the phone or email without authorization.



Ransomware

Definition: A type of malware that attempts to extort money from a computer user by infecting and taking control of the victim's machine, or the files or documents stored on it

- Typically, the ransomware will either “lock” the computer to prevent normal usage or encrypt the documents



How Does Malware/Ransomware Get Installed?

- A pop up window, webpage, or email warning from what looks like an official authority
- Ransomware is usually installed when you do one of the following:
 - Open a malicious email attachment
 - Click a malicious link inside of an email, instant message, or on a social networking site
 - Visit a malicious site
- Save and/or copy your data to the shared network drive AND offline media



City of Atlanta Ransomware Attack

- On March 22, 2018, five of 13 municipal departments were hit with ransomware attack
- Utility billing, public works, court, and HR systems were impacted
- Ransom was set at \$51,000, which the city did not pay
- SamSam variant ransomware was used – first identified in 2015
- The city had only begun to address multiple severe vulnerabilities identified during an IT security audit
- \$2.7 million has been paid thus far to recover systems, which were down for almost a week
- Final cost could be around \$17 million according to Atlanta-Journal Constitution



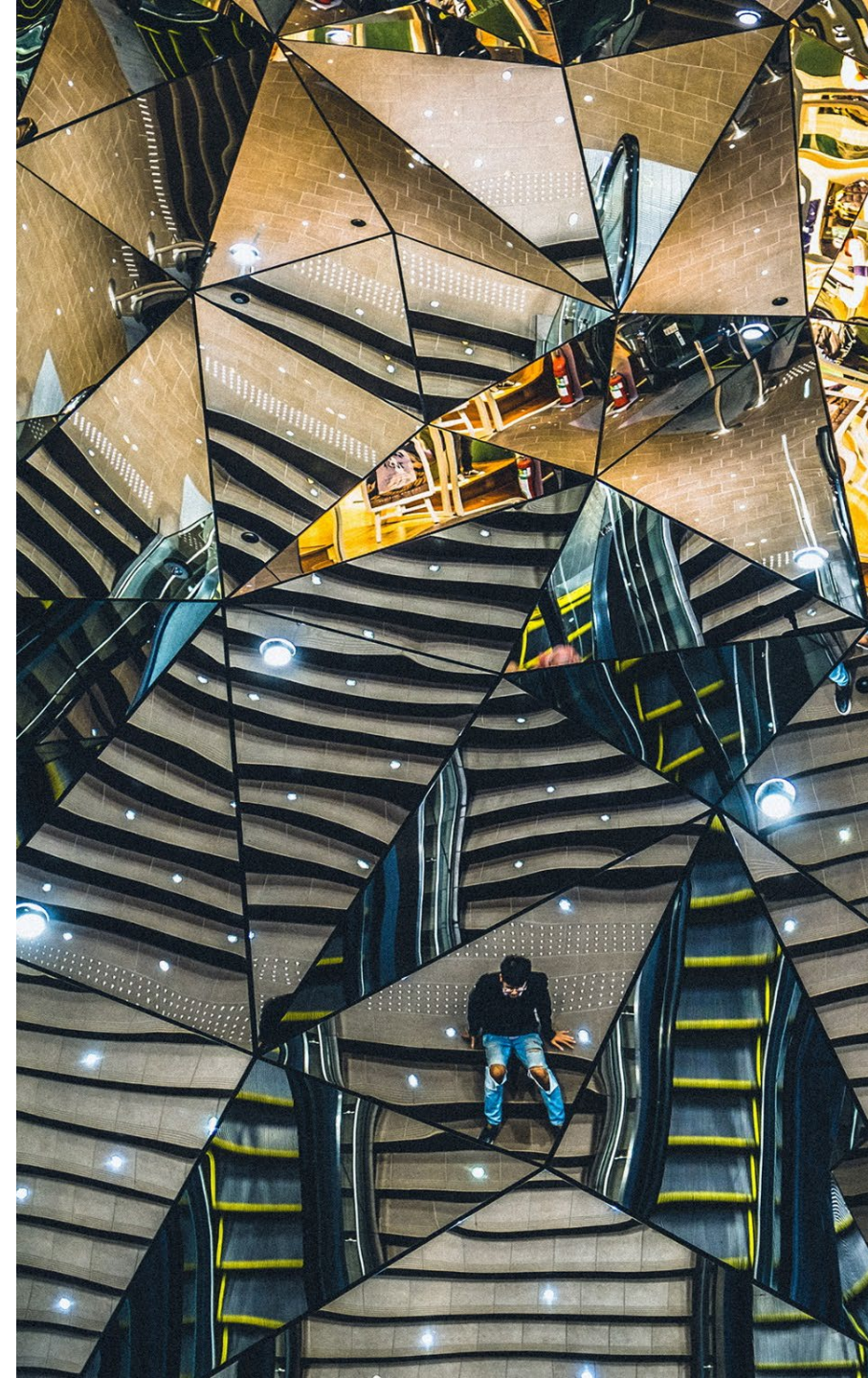
Crypto Mining Fraud

- Crypto mining is a legal activity, crypto jacking is not
- Attackers hijack systems to mine digital currencies, also known as drive-by crypto mining
- Became the biggest threat in 2018, ahead of ransomware, and remains that way in 2019
- Examples of current scams
 - Fraudulent cloud mining companies
 - Fake coin exchanges
 - Mining malware



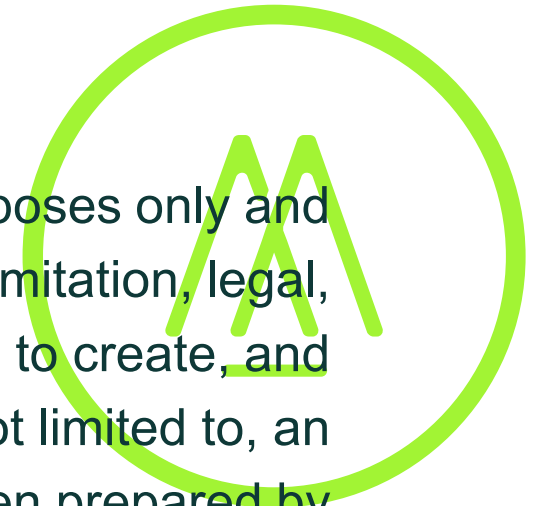
Takeaways

- Cyber attacks and fraud will continue to evolve in sophistication
- Internal controls need to be evaluated and assessed through enterprise and cyber risk assessments
- Ensure that multiple layers of controls are in place: prevent, detect, and correct
- Stay vigilant and informed



Questions?





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