Vendor Incentives: Out of the Shadows and into the Sunlight

By Brandt R. Allen, Paul W. Farris, David E. Mills, and Robert J. Sack

Each year in the United States, manufacturers, distributors, and retailers exchange billions of dollars to win sales from resellers or promote the products of the sellers. These payments are an integral part of the marketing plans of many sellers and resellers, and in some industries they have become so ingrained in the business that the players cannot operate without them, regardless of how effective they might actually be. These payments go by many names: rebates, trade discounts, supplier funds, slotting fees, advertising allowances, dealer incentives, markdown money, bill backs, buy downs, off-invoice allowances, return privileges, lease incentives, charge backs, and others. More emotionally loaded names include push money, kickbacks, price protection, penalties, and pay-to-stay. Throughout this article, the term "vendor incentives" will be used.

The financial details of these programs—who pays whom, how much, and what is given in exchange—are usually known only to the direct participants. That degree of confidentiality is understandable given the sensitive nature of the arrangements, but the failure to disclose how significant these programs have become for the sellers and resellers is problematic. At best, the failure to disclose carries the danger of misleading investors; at worst, it may shield graft and deceptive dealing. Because the payments involved often are contingent on future performance, estimates are required and the resulting accruals can be subject to the pressures of earnings management. It is time for investors to be given the information needed to assess the flow of these payments through the accounts of sellers and resellers.

Lurking in the Shadows

It is striking, in view of the prominence of vendor incentive programs, how little reporting there is of this activity. The little information available suggests that the sums are large. For example, PepsiCo reported net revenues of $43.2 billion in 2009. In the management's discussion and analysis (MD&A) segment of its Form 10-K, the company reported "sales incentives and discounts" of $12.9 billion, suggesting that these expenses were 30% of net revenues. Ten years prior, PepsiCo reported vendor incentives equal to only 19% of net revenues. These burgeoning discounts and allowances go to various distributors and retailers, but there is no way to know how much was paid in cash and how much was subject to a period-end accrual. Investors learn little more from the financial reports of PepsiCo's customers. Wal-Mart, one of PepsiCo's principal retail customers, acknowledges receiving "volume incentives" and other payments, but does not disclose their magnitude:

> Wal-Mart receives money from suppliers for various programs, primarily volume incentives, warehouse allowances and reimbursements for specific programs such as markdowns, margin protection and advertising. Substantially all allowances are accounted for as a reduction of purchases and recognized in our Consolidated Statements of Income when the related inventory is sold. (Wal-Mart annual report, 2009)

Like Wal-Mart, many large U.S. manufacturers, distributors, and retailers acknowledge in their financial fil-

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Meet the Press

Building a Relationship with the Public

During the past fiscal year, NYSSCPA members appeared in the news nearly 400 times across a broad spectrum of media—in radio, television, online, and in print newspapers and magazines. Not all professional associations offer these opportunities. That's because not all professional associations understand the value of fostering relationships with the press.

Twenty-five years ago, I aggressively sought to enhance the Society's media relations program. We had thousands of CPA members available as knowledgeable resources on business, economic, and government issues, yet financial journalists and ultimately the public weren't benefitting from this knowledge because our media relations program wasn't as strong as it could be. Who else to better educate reporters on how to read financial statements than the professionals who audit the financials? As an independent, objective source, the Society is in the best position to connect the profession with the press because we don't represent any firm or business—we represent the profession and what it stands for.

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CPAs don't generally seek the spotlight. But because New York is the financial and media capital of the country, we realized they didn't need to be. Business reporters understand something that our elected officials and policymakers sometimes forget—a CPA perspective offers an objective and transparent statement of the facts. CPAs are straight shooters; if they weren't, they would not be very good at their jobs. The same is true for reporters. Maybe that's why the Society's media relations program has been so successful: We earned our reputation with the media the same way reporters earn their reputations—by developing trust.

Most financial reporters are not CPAs, but when they write about accountancy they need to sound like they are. Add to this challenge the fact that reporters are routinely assigned to beats in which they may have no familiarity. I've seen more than one sports reporter be reassigned to the business desk with a background in finance limited to some good sports metaphors. Business journalists don't always call the Society looking for story sources. Sometimes they are just looking for background or an understanding of basic accounting processes, such as the importance of counting inventory in an audit. After talking with us, reporters are armed with better information and can use it to ask more informed questions. So although our members appeared in the news nearly 400 times this past year, the profession's message was delivered many times over that figure, even when a member wasn't directly quoted.

Most CPAs are passionate about their profession and even more of them care about getting it right. If a 20-minute conversation helps a reporter get it right, both the profession and the public are served. That's why for years we've provided an annual free seminar for journalists on how to read financial statements. This event is always led by one or two CPA members, usually one who works in higher education, and editors all across the state send their reporters to these classes because they know that an educated press leads to an educated public. The value of these seminars is also realized in the long-term. Entry-level reporters who attended our seminars in the 1990s are now

high-profile reporters with major publications. And they still call us every day. Whether we're working behind the scenes or in the headlines, we tell the CPA story day after day.

In an effort to show how much the NYSSCPA appreciates the good work of journalists who get it right, I launched an annual financial journalism awards program to honor these reporters: the NYSSCPA Excellence in Financial Journalism Award. We just held our annual awards ceremony in May. The NYSSCPA isn't a national organization, but reporters from across the country flew into New York to attend the ceremony because winning this award really means something to them. We hear it every year: "If the New York State Society of CPAs is giving me an award for this story, I know I got it right." And that means a lot, because if that's what some of the biggest names in financial journalism are saying at our awards ceremony, then we know we got it right too. ❑

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ings that they pay or receive incentive payments. But few details are provided for investors to assess. Target's 2008 balance sheet shows vendor receivables of $236 million, but there is no indication of how much the company received in total during the year. It is likely that the total was considerably more than $236 million.

In a 2007 study, "Shopper-Centric Trade," Cannondale Associates reported that vendor incentives accounted for more than half of the marketing budgets of many consumer goods manufacturers. In some cases, they were the largest expense after cost of goods sold. And in almost all sectors, vendor incentives were growing rapidly. PepsiCo's disclosure indicates that, during the past 10 years, vendor incentives tripled while net revenues did not quite double.

The level of vendor incentive activity appears to vary significantly across companies—even across companies in the same industry. While PepsiCo states that it paid incentives equal to 30% of the company's net revenues, Coca-Cola's were only 14%, according to its 2009 Form 10-K. The numbers can be quite large: Kellogg Company paid incentives equal to 40% of its net revenues, as stated on its 2009 Form 10-K. In none of these instances do we know how much was actually paid out during the year or how much was accrued at the beginning or end of the year.

To get a more complete picture, the authors looked at a subset of the Standard & Poor's (S&P) 500 Index disclosures for 2007. (Using the S&P Global Industry Classification Standard [GICS] codes, the three largest companies, by revenue were chosen in each of 46 industry segments, excluding energy, finance, and utilities.) Of the 124 companies that met these criteria, 70 reported paying incentives, 20 reported receiving incentives, and seven reported both. Only 12 of these companies disclosed the amounts they paid or received, and only 10 actually reported the receivable or payable related to those incentives. None of the companies provided full disclosure in terms of the income statement impact and balance sheet accruals arising from their vendor incentives.

The authors do not propose to argue for disclosure of competitively sensitive details of these programs. Instead we argue for a more complete disclosure of the programs' accrual and cash effects. The SEC has for many years required companies to provide exhibits in their annual reports with a four-column analysis of the allowance for uncollectible receivables: beginning balance, provision for the year, accounts written off during the year, and ending balance. In 2009, PepsiCo charged its operating results with a $40 million provision for possible future uncollectible accounts. It also charged off $21 million as being worthless, leaving a balance of $90 million to cover $4,714 million in year-end receivables. Investors can use this kind of information to evaluate a company's accounts receivable activity. It follows that investors could use similar information to evaluate the portion of a company's vendor incentive activity subject to estimates and accruals, which are referred to below as "contingent incentives."

The Business Purpose for Vendor Incentives

The tactical purposes of vendor incentives are many. Some are designed to increase resellers' sales efforts, by increasing the manufacturer's share of dealer push, or to obtain initial distribution of new products. Others are offered to reimburse retailers for bearing risks such as inventory spoilage or stocking items with uncertain demand. Some vendor incentives are designed to enlist reseller cooperation in meeting competitive threats.

Vendor incentive programs can be complex and may take many forms. Incentives may take the form of fixed payments or payments that depend upon the quantities sold by the reseller. For example, retailers might ask for a fixed payment to include a manufacturer's logo in a feature advertisement; or the manufacturer might agree to reimburse the retailer for a certain percentage of dollar volume during a year, as long as the retailer submits qualifying proof of performance. In some cases, agreed-upon fixed payments are accrued by the vendor and the credits are allocated pro rata to several invoices over a longer period.

When paid to elicit a reseller's cooperation, incentive payments may precede or follow the reseller's performance. For example, slotting allowances are often paid in cash or free goods before a single item is sold. These payments encourage the retailer to accept the product into its assortment (or to assign the product a "slot" in the chain's distribution center). Other payments are "off invoice," meaning that the customer's invoice is reduced by the amount of the discount. Finally, "bill backs" are retrospective promotional payments to retailers; these demonstrate that a service has been rendered or a marketing objective achieved (e.g., increased shelf space, a special display, or a temporary price promotion) to warrant the payment. The timing of incentive payments varies from one manufacturer's program to another, depending upon the company's distribution strategy. In addition, because retailers generally prefer off-invoice to contingent promotions, the timing of incentive payments may signal the balance of power between the manufacturer and its retail customers.

From a strategic perspective, the purpose of many vendor incentives is to overcome a channel coordination problem in the supply chain, such as the double-marginalization effect on selling prices. Double marginalization occurs when a manufacturer and a reseller, such as a retailer, each make unilateral pricing decisions to extract as much value as possible for themselves without taking full account of how much value the other extracts. The retailer may find that increasing prices to consumers will generate incremental profit (e.g., holding a manufacturer's prices constant) even though this causes a reduction in unit sales. While higher prices may increase the retailer's profit, the loss in unit sales reduces the manufacturer's profit. As a response, the manufacturer might increase its own prices to make up for lost volume. The unintended consequence of independent pricing decisions in the channel is that prices to consumers are too high, and the companies' combined margin is too low. In other words, the total profit pie shrinks.

Vendor incentive payments can help overcome this double-marginalization problem. For example, a volume discount reduces the double-marginalization distortion by encouraging incremental sales; the retailer's pricing decisions are driven by the manufacturer's lower incremental prices rather than its higher first-item prices.

Vendors have generally moved toward programs that reward customers for long-term increases in sales to avoid pitfalls in volume purchase programs. Nevertheless, these long-term programs are more likely to rely on management estimates of what is achievable.

Another channel coordination problem that vendor incentive programs help overcome is the under-provision of downstream selling effort. If the sales volume of a manufacturer's products depends on the retailer's selling effort (e.g., displays, advertising, customer service), there is a tendency for the retailer to exert less effort than the manufacturer would prefer. This happens because the retailer bears the full cost of the selling effort it exerts, but captures only part of the incremental retail margin that effort produces. The retailer generally disregards (and probably doesn't even know) the impact of its decision on the manufacturer's profit stream. Just as with double marginalization, the under-provision of downstream selling effort reduces sales volume and the companies' combined margin. The selling effort problem can be addressed by employing vendor incentives that shift part of the retailer's cost onto the manufacturer. Various discount strategies effectively reward resellers for devoting more resources and effort to increasing sales volume.

Vendor incentive programs can be effective ways to realign incentives and combat channel coordination problems. By increasing the size of the profit pie in the supply chain, these pricing practices can be advantageous for every participant. The widespread use and sheer size of these promotional programs suggest that businesses perceive their benefit.

Marketers often worry that the benefits derived from ever-expanding promotional programs may be short-lived. The long-term implications of manufacturers competing with promotional programs include greater complexity and less predictability in competitive interactions, especially as large resellers become more sophisticated in their dealings with suppliers. Marketers also recognize, however, that incentives may escalate unnecessarily if competitors face a "prisoner's dilemma." But rather than trying to get rid of trade deals altogether, most businesses simply try to get the most out of them.

From a financial reporting perspective, the distinction between off-invoice discounts and discounts that are contingent upon the future performance of a service or achievement of a marketing objective is important. While shareholders have an interest in both types of discounts, only off-invoice discounts are reflected fully in reported net sales and margins. Reporting practices for contingent discounts are not uniform across companies, and often shareholders cannot assess them. The focus in this article is solely on these contingent incentives. The authors are interested in seeing them reported separately and fully because otherwise they can become a tool for earnings management. In the PepsiCo example, investors must know how much of the $12.9 billion in incentives and discounts was contingent in order to assess the degree to which the incentives were subject to management's judgment.

Using Incentives Programs to Manage Earnings

Most incentive plans require the recipient to meet certain goals during a specific time frame. The time frame that applies to one recipient is not the same as others. So when the seller company offering incentives prepares its financial statements, management must estimate the extent to which its customers will meet their program goals, making them eligible to receive incentive payments. Based on those estimates, management then accrues a pro rata share of the expected payment or receipt. The reseller company, anticipating those payments, goes through the same estimation process. Logically, some companies will report conservative estimates and others will lean in the opposite direction. (And, of course, there might be differences of opinion even within a company as to whether a program recipient will meet the program goals and qualify for the incentive payment.) Given the magnitude of the payments involved in some of these programs, even a small change in such estimates could have a significant impact on the companies' reported earnings.

The market punishes companies that fail to meet earnings projections, even by a penny. Given the pressure to meet earnings targets, and given the subjectivity of the estimates required to establish the accrual for incentive payments (whether to be paid or received), it would seem likely that those accruals are occasionally subject to some bending for earnings management purposes. Occasionally, a management team goes beyond simple bending and uses an incentive program accrual as a basis for fraudulent reporting.

Consider the case of U.S. Foodservice (USF), the second-largest food distributor in the United States. USF was acquired by Ahold, a large international grocery company, in April 2000. A massive fraud within USF was discovered in 2003. After an investigation, the SEC filed suit, saying in its complaint that during 2001 and 2002, USF "made no significant profit on most of its end-sales to its customers. Instead, most of USF's operating income was derived from promotional allowances." The SEC charged that key members of USF management "engaged in or substantially participated in a scheme whereby USF reported earnings equal to or greater than its earnings targets, regardless of the company's true performance. The primary method used to carry out this fraudulent scheme … was to improperly inflate USF's promotional allowances." The SEC claimed that executives distorted actual earnings by inducing vendors to sign false confirmations, manipulating vendors' accounts receivable, and making false statements to the company's auditors and colleagues within the company (complaint, *SEC v. Michael Resnick, Mark P. Kaiser, Timothy J. Lee, and William Carter* [04 cv 5824 {Holwell} SDNY, 7/27/2004]).

Or consider the case of Kmart, the nation's second-largest discount retailer at the time it filed for bankruptcy on January 22, 2002. The SEC alleged that in the period just prior to bankruptcy, Kmart executives misstated the company's financial reports by "pulling forward" the recognition of contingent incentive payments. Several Kmart divisions had negotiated vendor discounts that were dependent upon Kmart's purchase of additional goods from the vendor. But Kmart division heads prepared documents, with the assistance of some vendors' marketing per-

sonnel, that misrepresented the discounts as applying to past purchases. In its complaint, the SEC stated that "Kmart's profitability became increasingly dependent on [vendor] allowances in the years preceding bankruptcy," and "Kmart's accrual methodology [used to account for the vendor allowances] together with management's unrealistic earnings expectations, put tremendous pressure on Kmart officers and employees at the end of the fiscal year to collect allowances" (complaint, *SEC v. Levine, Spake, Berlin, and Ely* [2.05 cv 73328, 8/29/2005]).

The SEC has brought similar cases based on fraudulent reporting of vendor allowances against other companies, such as Ingles Markets and Fleming. (See *SEC v. Ingles Markets* [LR 19673, 4/27/2006] and *SEC v. Fleming Companies* [LR 18884 9/14/2004]. See also SEC Press Release 2004-129.) There is also more recent evidence about how consumer packaged-goods companies may increase end-of-period promotions in order to improve reported quarterly sales and profits. (See Craig J. Chapman and Thomas J. Steenburgh, "An Investigation of Earnings Management through Marketing Actions," working paper, Harvard Business School, December 2009.)

The SEC's 2001 Proposal

As noted previously, for many years, the SEC's rules have required a four-column activity analysis (beginning balance, additions, usage, and ending balance) for "allowance for doubtful accounts." This analysis must be attached as an exhibit to the company's annual report filed on Form 10-K. This requirement addresses the concern that establishing an allowance for potentially uncollectible receivables is an exercise that relies on management's subjective judgment about the future. The SEC believes that investors benefit from disclosure of the factual basis (e.g., what was added to the allowance and what was charged off) for management's judgment about uncollectible receivables. Comparing the ins and outs in the allowance account from year to year, and making comparisons with other companies in the same industry, would help an investor assess the quality of the company's accounts receivable, the company's policies for extending credit to its customers, and the degree of conservatism that is built into the company's financial statements generally. The SEC also recognized that this kind of disclosure provides ancillary benefits if it causes management to pay closer attention to the process that establishes the allowance for doubtful accounts.

In early 2001, the SEC proposed a new set of disclosures that would provide details of transaction flows through a wide range of accounts from a company's balance sheet. At that time, the SEC was concerned about the pressure Wall Street was placing on management to meet earnings projections in what SEC Chairman Arthur Levitt once called "The Numbers Game" (speech by Levitt before the New York University Center for Law and Business, September 28, 1998). Because the cost of failing to meet Wall Street's earnings expectations was so high, there was concern that some managers might "manage" their earnings to meet those expectations by irregular means. There are, of course, many ways to manage earnings, and one of them is to manage the amounts the company records in its various valuation accounts and its accruals for liabilities. The 2001 proposal would have required companies to extend the four-column analysis previously required for the allowance for doubtful accounts to many other similar accounts, including expected liabilities for—

- environmental remediation;
- income and franchise taxes;
- ongoing litigation;
- warranty repairs;
- sales discounts and allowances; and
- expected losses on inventory.

Had it been approved, this proposal would have applied the same antiseptic of sunlight to these accounts as was previously applied to the allowance for doubtful accounts. But the proposal never won approval.

Reaction to the proposal at the time was mixed. There was general support for the SEC's objectives, but there was some opposition to specific requirements, such as the inclusion of liability accounts related to environmental, tax, and other litigation-prone issues. The concern was that disclosure might provide a road map for opposing litigants, causing more harm than good for investors. There was also concern that, because of its scope, complying with the proposal would have been daunting. Several commentators argued that the cost of compliance would exceed any benefit enjoyed by investors. Others observed that investors had generally expressed no interest in a significant expansion of disclosure rules. For these and perhaps other reasons, the proposed rule was never adopted and the matter was dropped.

A Proposal

The authors would like to revive interest in one component of the SEC's dropped proposal. We believe that public companies should be required to provide, in an exhibit to their annual reports, a four-column analysis of any vendor incentives program that is material to the company's operations, consisting of—

- beginning balance in the accrual (or receivable);
- provision made during the year (or the expected revenue recorded);
- payments made (or the cash received); and
- ending balance in the payable (or receivable).

This disclosure proposal bears an obvious resemblance to the long-standing requirement that calls for reporting details about a company's allowance for doubtful accounts. It would give investors insight into a critical area of the company's operations, regardless of whether the company is on the paying or receiving end of a vendor incentive program. In addition, it would provide a perspective on management's judgment regarding the estimation of accruals. Analyzing the relationship between the accruals at the beginning of one year and the end of the previous year, and the provisions and payments made in each year, would provide a basis for evaluating the reasonableness of the year-end accrual. It also would provide a basis for assessing the degree of conservatism as exercised in developing that accrual. At a minimum, it surely would help market analysts ask some probing questions during an analysts' meeting or an earnings release phone call.

This proposal is much less sweeping than the SEC's 2001 proposed rule because it is limited to contingent vendor incen-

tives. The cost of compliance should be more manageable because of the proposal's limited scope. In addition, the necessary data should already be available within the company simply for control purposes. Respondents to the SEC's 2001 proposal suggested that investors had not asked for the data that lie behind judgmental accruals. But the authors believe the investor community has made clear its real interest in this type of disclosure. In 2007, the CFA Institute called for a new form of income statement that would distinguish between cash and accrual transactions, that is, between changes based on arm's-length transactions and estimates made by management. As examples of the kinds of estimates that the CFA Institute would like to see reported separately, the institute offered additions to bad debts, sales returns, and allowances ("Comprehensive Business Reporting Model," July 2007). Beyond the benefits for the investor community, this disclosure requirement would benefit the companies themselves: It would focus management's attention on the process by which period-end accruals are established, the controls required to ensure compliance with the company's policies and procedures, and the ongoing challenge to the effectiveness of the company's various vendor incentives programs.

It is conventional wisdom in the marketing community that sudden and significant increases in the use of discounts and price-off incentives may signal a company's underlying weakness. At the very least, it signals a major change in strategy. These are not matters that should be hidden in the shadows where investors cannot see them. When the sizes, amounts, and terms of a company's discounts and allowances are contingent on the performance of channel partners, investors have a right to be informed about the ins and outs in the related accounts. In addition to the amounts involved, the timing of vendor incentives and the degree to which they are "voluntary" are important aspects of these programs. In any situation where amounts vary significantly from year to year, or where the composition of the company's vendor incentives program changes (e.g., more or less reliance on contingent programs), a straightforward reporting of the ins and outs of the accrual should be supplemented with explanatory text.

The authors do not imagine that compliance with our proposed requirement would be straightforward. Compliance no doubt would require conversations among CFOs, marketing executives, and sales managers about exactly which contingencies are associated with a company's promotion programs. These conversations would likely lead to greater clarity about what the promotion terms are, why the promotions are being offered, whether the intended objectives are being achieved, and whether these programs are the most efficient way to achieve specific marketing and sales objectives.

Into the Sunlight

Vendor incentives are pervasive in the U.S. economy and often play an important and beneficial role in commerce. At the same time, they are nearly invisible to investors studying companies' financial statements. The authors' thesis is that more and better disclosure would benefit investors and financial markets generally. We also think that corporate officers and board members would derive ancillary benefits from this kind of disclosure. We have argued that the magnitude of the discounts, and the necessity of reporting estimates of their final effects, call for a more comprehensive approach to disclosures in financial reports. Retailers like Wal-Mart and Target should disclose the total discounts recorded each period, as well as the amounts received during the year and the total vendor receivables on the balance sheet at year end. The same is true for manufacturers like Dell, Harley-Davidson, and Pfizer. Analysts and investors need to be able to monitor the cost and effectiveness of promotion programs. Senior business leaders also need a comprehensive understanding of their companies' incentive programs regardless of whether they are giving, receiving, or both. Many factors warrant disclosure in the current business environment: the growth and diversity of incentive programs, the sensitivity of accruals to reported results, the potential for fraudulent reporting related to vendor incentive programs, and the interest of the analyst community in accrual management. It's time to bring vendor incentives into the sunlight. ❑

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IRS Eases Rules on Liens for Taxpayers

By Tracy Becker

In February 2011, the IRS announced important changes to its lien filing practices that lessen the negative impact on taxpayers. The new policy will significantly reduce the number of liens the IRS places on property owned by delinquent taxpayers and will make it easier for taxpayers owing $25,000 or less to get existing liens withdrawn.

For those taking advantage of the new policy, it will significantly impact their credit scores and enable them to qualify for mortgages and other loans previously unattainable because of low credit scores caused by the IRS tax liens. It is up to diligent CPAs to be proactive and guide individuals through the lien filing practices to help prevent their credit from deteriorating.

The IRS uses liens to establish a legal claim to a taxpayer's property when the taxpayer has an unpaid tax debt. A new tax lien can drop a credit score between 40 and 120 points. Tax liens can remain on credit reports for years, even once tax bills are paid and liens removed, hurting the ability of taxpayers to get loans. They can even affect taxpayers' ability to land jobs in a world where more prospective employers are checking credit scores.

Previously, even if a tax debt were paid in full, a record of the delinquency would remain on the borrower's record for seven years—severely hampering the individual's borrowing ability until the delinquency aged at least four years and was paid.

To ease the burden on taxpayers, the IRS has raised the minimum amount of tax debt that prompts the filing of a tax lien from $5,000 to $10,000. For those owing $25,000 or less, the IRS will make it easier to obtain tax lien withdrawals once a taxpayer pays off the tax debt or sets up a payment plan that will end in full payment. To speed the withdrawal process, the IRS has streamlined its procedure to allow internal IRS collection personnel to withdraw the lien. No court filings are involved. But CPAs need to know that the cleaning of the credit reports does not happen automatically.

The IRS will withdraw a lien only if the taxpayer requests a withdrawal letter in advance after the taxpayer has fully paid the taxes due or enters into a direct debit installment agreement (DDIA) in which monthly payments to the IRS are automatically withdrawn from the taxpayer's bank account. Liens will be withdrawn after a probationary period demonstrating that direct debit payments will be honored.

Under the new policy, once the IRS withdraws the lien, the borrower's credit record will be wiped clean and his credit score will be affected positively. The new policy could increase a client's credit score by more than 100 points, which could be the difference in getting a loan and saving thousands of dollars in monthly mortgage payments.

SIDEBAR

Success Story 1

A successful lawyer wanted to purchase a $1 million condominium in Florida as a second home. Unfortunately, he had three tax liens on his credit report and his credit score was 30 points lower than approval requirement. The author's firm advised the lawyer's accountant to have him pay the liens in full and request a withdrawal letter. The lawyer quickly paid off what he owed the government and all of the liens were removed. Once the withdrawal letter was issued, the author's firm forced the bureaus to update the deletion of the liens, and the lawyer's report reflected the new status with no public records. The result was that the lawyer's credit score increased by 80 points and he was not only approved for the loan, but also received the best rate and a reduced monthly payment.

Success Story 2

Mortgage eligibility will be particularly affected because of the strict requirements banks have enforced, and also because many mortgages today are insured by the Federal Housing Administration (FHA), which does not look kindly on borrowers who are delinquent in paying the government.

A young, recently married couple were aspiring first-time home buyers who wanted to purchase a new home with an FHA loan. Because the wife had a $7,000 tax lien, the couple was denied financing. The author's firm educated the CPA on the new program, and he was able to get the couple into a payment plan, request a withdrawal letter, and ultimately had the tax lien deleted from her credit report.

The couple bought the house they wanted. Without the IRS program, this couple would have had to wait about five years to pay off the lien before purchasing a home.

Success Story 3

A recently divorced woman wanted to go back to school to enhance her ability to earn a greater income. She needed to get approval for student loans and ultimately wanted to purchase a new home for her and her family.

When she applied for government-insured student loan funding, she was rejected due to a $15,000 tax lien outstanding on her credit report. Her CPA, after being educated in regard to these tax changes, informed her of the IRS's new plan and charged her a fee to make sure the withdrawal letter was requested and an "in full" payment plan was set up. Within a short period of time, the lien was removed from her credit profile and she was on her way to a new life.

Advising on Lien Withdrawal

Individuals need to be educated on what serious financial damage a lien can do to their credit score. It may trigger higher interest rates on loans and increasing monthly mortgage payments, or outright rejection for a loan or a job. Student loans, which are backed by the government, may also be rejected because of tax liens on credit reports.

Understanding these rules can save CPAs from angry clients asking, "Why didn't you know about this and tell me I was eligible? This could have saved me a fortune on a refinance or given me the opportunity to buy the house my family needed." Advising clients properly on this matter will benefit an accountant's practice because happy clients refer more business.

Individuals with a tax lien needs to know the new policy, what they must do, and how they must pay in full or enter into a payment agreement via direct debit that ends in full payment. Clients must be told that if they settle for less than the full debt owed, they will not be eligible for the withdrawal of lien.

If CPAs do not want to charge a fee for this service, but decide to advise clients on the process, they should send the taxpayer to the online payment agreement application on the IRS website to request a "withdrawal of lien letter" prior to entering into a DDIA. Liens will be withdrawn after a probationary period demonstrating that direct debit payments will be honored.

Liens will not be withdrawn automatically, however. Once full payment of taxes is made or payment plan probationary periods are completed successfully, the taxpayer or the CPA must advocate and take the proactive step of requesting the bureaus to remove the lien from the taxpayer's credit profile.

CPAs should advise clients to check their credit within 30 days to make sure the bureaus have updated the new IRS information on the credit profile. If the lien continues to show up, however, an accountant should seek out a credit restoration company to get the lien removed.

IRS officials state that they are trying to minimize the burden on taxpayers while collecting the proper amount of tax. But tax preparers should be there to ease a taxpayer's burden, especially when a taxpayer has taken the proactive step of entering into a direct debit agreement.

Installment Agreements for Small Businesses

The IRS is also making streamlined installment agreements available to more small businesses. The payment program will raise the dollar limit to $25,000 to allow additional small businesses to participate. Currently, only businesses with under $10,000 in liabilities can participate. Small businesses will have 24 months to pay, but if they do so, like individual taxpayers, they must also enroll in a direct debit installment agreement.

Paying off a tax lien can save hundreds of thousands of dollars in interest, in addition to enabling taxpayers to qualify for mortgages or other loans.

It is not the act of just paying off the lien that enables the savings, but its removal from the credit report that increases the scores. It is imperative that CPAs help individuals save as much money as possible in these tough economic times and earn the credit they need and deserve. The government is willing to work with taxpayers, and accountants have a duty to do so as well. ❑

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Guidance for Accounting Professors

By Stephen Scarpati

when reflecting upon their choice of career, many CPAs look back to a particular college accounting professor as a source of influence. In return, many accounting professors warmly recall the assistance they were able to give students. While the benefits of a successful CPA career are obvious to many, from the standpoint of a 19-year-old undergraduate trying to pick a major, the decision is daunting. The demands of a challenging accounting curriculum can be intimidating. Add the complex regulations and rigorous examination for CPA licensing and the expectations can be overwhelming to a young student. Accounting professors can play a vital role in guiding students on a path toward a CPA career.

Accounting educators should be up-to-date on the key aspects of their vocation. They must be knowledgeable of the many changes in accounting principles and reporting. They also need to be alert for the latest developments in teaching delivery to enhance the learning experience in the classroom. In addition, college educators must be well-informed about the most recent professional regulatory changes.

One way accounting professors gain insight into current issues is by attending conferences like the NYSSCPA's Higher Education Conference, which was held in March of this year and gathered educators from colleges across the New York region.

Important topics covered at this conference included—

- accounting curriculum,
- recent regulations,
- social media, and
- recruiting.

Accounting Curriculum

International Financial Reporting Standards (IFRS). The biggest development in the accounting curriculum continues to be IFRS. With IFRS now included in the CPA exam and convergence with U.S. GAAP nearing, IFRS must be incorporated into the college accounting program of study. The decision that each college must make is whether international accounting should be taught separately or incorporated into existing accounting courses. The consensus from attendees at the conference was that most colleges are choosing the latter—incorporation of international content into existing courses.

Providing an update on the latest IFRS developments were two directors in the National Professional Services Group of PricewaterhouseCoopers, Nicole Berman and Guilaine Saroul. They reported that more than 100 countries require, permit, or plan to converge or convert to IFRS, including Canada. Starting this year, our neighbor to the north now requires IFRS as published by the International Accounting Standards Board (IASB). Early adoption (prior to 2011) was permitted for consolidated and standalone financial statements upon application to securities regulators; however, U.S. GAAP is also acceptable for U.S.-listed issuers.

Berman and Saroul offered the following suggestions on what organizations should be doing now:

Focus on the challenge. The next several years will bring major changes to U.S. financial reporting. Whether changes arrive through convergence, an SEC-mandated adoption of IFRS, regulation, or continued IFRS use by subsidiaries and counterparties, the effect on U.S. businesses will be considerable.

Use scenario planning. Incorporate likely convergence and IFRS adoption expectations into strategic thinking and business planning. Consider the effects various alternative paths could have. Identify and consider the implications of business, accounting, tax structure, financing, long-term contractual commitment, investor, control systems, and workforce-related issues.

Maintain corporate oversight. IFRS adoption for statutory reporting continues in many jurisdictions. It's important to consider transition timing, strategies, and policy decisions of non-U.S. subsidiaries that are increasingly likely to be on some form of IFRS in the foreseeable future. Closely follow international acceptance of IFRS for statutory purposes.

Identify what you can do now. Be mindful of the aspects of convergence and conversion that will take the longest. If highly probable changes can be made efficiently and without waste, get started addressing those challenges. Consider smaller controlled one-off projects where desirable.

An important contribution to the international accounting dialogue was provided by Jeffrey Mechanick, an assistant director at FASB. Mechanick offered the following key points:

- The focus of FASB is not just on convergence but convergence and improvement.
- The issues that are being addressed are not only for accounting practices but also for regulation and enforcement.
- Four convergence topics were identified as being high priority: financial instruments, leases, revenue recognition, and insurance.

Forensic accounting. Forensic accounting continues to emerge as a popular subject in accounting curriculum on college campuses. Students enjoy the real-world events incorporated into the courses. One such case was presented by former FBI Special Agent Joseph Dooley, who led the investigation in the $3 billion fraud perpetrated by Martin Frankel.

In his presentation, Dooley guided the audience through the complex global investigation. He shared copies of evidence, including charred remains of burned documents, handwritten notes, cancelled checks, and affidavits. He also included newspaper clippings and interviews with Frankel. Eventually, Frankel was arrested, convicted, and imprisoned.

Recent Regulations

Over the years, one of the most popular presenters at the Higher Education Conference has been Daniel Dustin, executive secretary of the New York State Board for Public Accountancy. Dustin continued his contribution this year with much informative guidance as the state continues to implement the Public Accountancy Act of 2008. His commentary addressed the points outlined below.

- Education for professional accountancy content must incorporate—
  - financial accounting and reporting,
  - cost or managerial accounting,
  - taxation,

- auditing and attestation services,
  - ethics and professional responsibility,
  - business and accounting communications, and
  - accounting research.
- Online courses are allowed in New York State.
- The expectation is that a bill requiring an MBA degree for public accountancy will not be introduced in the legislature.
- Nationally, applications to take the CPA exam have been rising.
- Changes to the CPA exam beginning January 1, 2011, include—
  - updated content, including testing of IFRS;
  - new authoritative literature (codified FASB standards);
  - new research task format;
  - task-based simulations in AUD, REG, FARE; and
  - written communications in BEC.
- Passing rates for the CPA exam are in the 47% range for each of the four sections.
- The AICPA has not received any complaints about IFRS questions on the exam.

Social Media

College professors are keenly aware of the social media wave enveloping the current generation of students. Tom Hood of the Business Learning Institute and the Maryland Association of CPAs spoke at the Higher Education Conference about the role of social media in the lives of young people. Technology is changing the world, but it is not just increasing the speed, content, and volume of information, it is also changing the attitudes and expectations of those who use it. Hood explained that traditional social networking through Chambers of Commerce, class reunions, and friends has been augmented with Twitter, LinkedIn, and Facebook. Hood also gave interesting examples of how some CPAs dramatically expanded their contacts and grew their businesses through well-developed social media strategies. He also offered compelling suggestions for incorporating social media to enhance classroom learning. These included the following:

- Use social media to connect to thought leaders.
- Employ tools that engage and share insights.
- Utilize blogging to support continuous informal learning.
- Draw upon blogs that support training.

Recruiting

It's important for accounting professors to stay current with the job market for accounting majors. To that end, the Higher Education Conference brought in a panel of recruiters representing four different organizations. They were: Heather Cohen, human resources director of WeiserMazars LLP; Mary Kebbe, who is responsible for training and development for controllers at Goldman Sachs; Pamela Krepchin, Northeast campus recruiting leader for Deloitte LLP; and Brendan Molloy, who oversees the campus recruiting team for KPMG's Northeast region. The panel members discussed their current hiring plans as well as their expectations for the accountants of tomorrow. Their comments included the following:

- Campus hiring is on the upswing after recent flat years, both for full-time employment and internships.
- With New York's new CPA regulations, accounting majors have alternatives to the traditional career start at an accounting firm.
- The firms characterized their young accountants as proactive, adaptable, flexible, and possessing good technical skills.
- On the other hand, the new generation of accountants generally could use improvement in writing skills, oral communication, and the skills for working in a professional environment.

It's crucial that accounting educators keep up with developments affecting the profession and enhance their knowledge in order to aid their students. Current information in the fields of accounting curriculum, New York licensing regulations, social media, and recruiting will better enable college accounting professors to mentor CPAs of the future. ❑

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