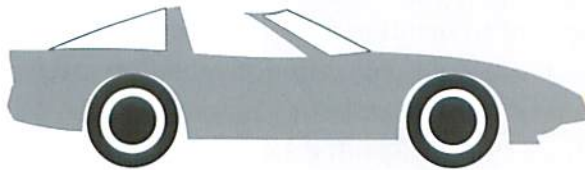




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HEADLIGHTS

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WHEN DID YOU LAST REVIEW YOUR INTERNAL CONTROLS?

When did you last review your internal controls? Most dealers answer with “never” or “right after we discovered embezzlement.” The Association of Certified Fraud Examiners (ACFE) estimates that \$994 billion is lost annually to employee theft and fraud. Small businesses average losses of \$200,000 per occurrence. Fraud takes place every day in small businesses just like yours.

Most employees who commit fraud or embezzlement do not begin their employment with the idea of stealing from their employers. The characteristics of the majority of people involved in embezzlement schemes are counterintuitive. Instead of acting and appearing “untrustworthy,” the individuals typically are long-term employees above suspicion, which is how they get in a position to perpetrate the fraud.

The 2008 ACFE Report to the Nation on Occupational Fraud and Abuse reported that

✓ In 52% of the cases, the employee had been with the organization for more than 5 years.



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- ✓ Although almost 40% of fraud is committed by nonmanagerial employees, fraud committed by managers is twice as costly.
- ✓ Less than 8% of the perpetrators had convictions prior to committing their frauds.

A multitude of different reasons eventually drives an employee to steal, but three factors are commonly present in cases of fraud: financial pressure, opportunity and rationalization. These three factors make up the fraud triangle (*see figure on page 2*).

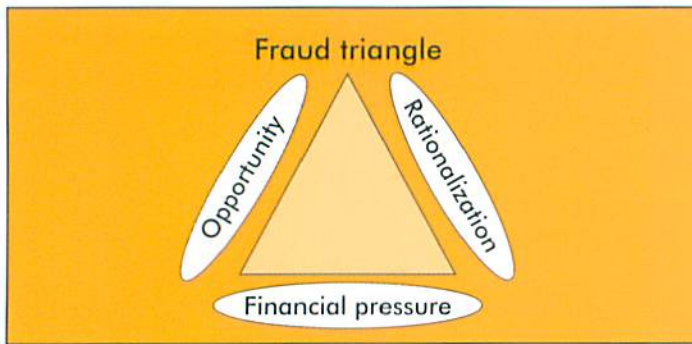
Financial pressure is the base of the fraud triangle. Financial pressure may arise from a variety of circumstances. It is not uncommon for perpetrators to have gambling debts, addiction to drugs, a failed marriage, large education costs,

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SPRING 2009

**IRS COST SEGREGATION
RULINGS**

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medical bills or simply to be living above their means. Regardless of the specific reason, all employees involved in embezzlement have a need for cash beyond their ability to earn it. After a fraud has been detected, it is not uncommon for management to realize that red flags that should have alerted them to the possibility of fraud were present.

Opportunity is the second side of the triangle. Opportunity refers to the employee's belief that his or her risk of being detected is reduced to a tolerably low level. Because the employee does not want to get caught, opportunity is an extremely important part of the fraud triangle. Even if the employee is under financial pressure, a belief that the chance of being detected is great will likely deter the employee. Conversely, if the employee has opportunity with little risk of being discovered, the employee is more likely to steal from the employer. Poor internal controls, sloppy recordkeeping and too much trust create the perfect opportunity for employee theft.

Rationalization is the third side of the triangle. Most people have a need to reconcile their behavior with commonly accepted morality, decency and trust. Many embezzlers are employees who believe that they are underpaid, underappreciated or who have been passed over for a promotion. A common rationalization is, "I didn't really steal. I just took what was owed to me because I am underpaid." Management should constantly be on alert for employee behavior that could be a red flag for potential employee theft.

Fraud occurs every day and may be occurring at your dealership. What can you do to determine if an employee is stealing from you? Many business owners believe that the year-end audit or review by an independent CPA firm will discover fraudulent activity in the dealership. However, fraud is more

commonly discovered by internal audits and controls rather than an external audit. According to the 2008 ACFE report, employee fraud is typically uncovered in the following ways:

- ✓ **Tips (46%)**—Tips are the single most effective technique for detecting fraud. Tips can come from a number of sources, including customers and vendors, but having an internal whistleblower program continues to be highly effective in detecting fraud. It is important to mention that with a whistleblower program, you need a policy that prohibits retaliation against a whistleblower.
- ✓ **Accident (20%)**—Studies indicate that luck comes into play in a fifth of the fraud detected.
- ✓ **Internal audits (19%)**—A good internal audit program can be highly effective in uncovering fraud.
- ✓ **Internal controls (23%)**—Effective internal controls will uncover fraud at times. There are no statistics indicating the effectiveness of internal controls to deter fraud from being committed. But strong internal controls create an environment that increases the chances a fraudulent scheme will be detected.
- ✓ **External audit (9%)**—Because a CPA's engagement is not designed to uncover fraud, it is unusual for a year-end audit or review to uncover embezzlement.

It is impossible for you to look at your employees and know who is stealing from you. Your judgment of who may be committing fraud is influenced by preconceived notions of the individual's character. The typical profile of an embezzler is one of a trusted employee, married, well educated and well respected within the company.

Fortunately, there are many ways you can reduce the risk of a significant fraud being perpetrated at your dealership. Implementation of sound internal controls can reduce the risk of your dealership being the victim of a significant embezzlement. All corporate officers with fiduciary responsibility over the assets of the company should understand the internal control procedures that have been put in place to properly safeguard company assets and demand strict adherence to those procedures. When did you last review your internal controls? ↵

IRS COST SEGREGATION RULINGS

Jerome Bressler, CPA, CVA
Mountjoy & Bressler, LLP

The IRS has issued technical guidance to assist its field examiners in determining whether dealership cost segregation studies set forth the correct depreciation period for different components of the dealership's facilities.

Cost segregation or building studies segregate facility components into different asset classes. These asset classes can result in some facility costs being depreciated over shorter periods (e.g., 5 or 7 years) than the traditional 39 years used for buildings and improvements. In September 2007, the IRS sent a letter to NADA requesting its comments on a draft chapter on automobile cost segregation studies that the IRS intended to add to its broader Cost Segregation Audit Technique Guide.

In November 2007, NADA provided the IRS with comprehensive comments on the draft that were prepared on NADA's behalf by the AutoCPA Group. After considering NADA's comments, the IRS final-

ized the new chapter and incorporated it into the IRS Cost Segregation Audit Technique Guide. One of the key components of this chapter was the inclusion of the use of an engineer to determine the breakdown of the various asset classes.

The substantial tax savings that cost segregation studies can provide will be safer if the study includes the use of an engineer. Otherwise, the savings may be reversed if the IRS can successfully dispute the breakdown of the dealership facility into its separate components. Please contact your local AutoCPA Group member to assist you in properly applying the savings provided by cost segregation. ↗



NADA 2009 CONVENTION

As you can imagine, this year's NADA attendance was not quite what it usually is. Many dealers and vendors decided to forgo this year's event to conserve resources.

Despite the lower-than-usual dealer attendance, the convention was a magnet for the domestic automotive manufacturers. A who's who of Ford, General Motors and Chrysler leadership were present. And their message was clear: We're here to stay, and you should be as well. There is always a "but" though, and this year's was that dealers must become profitable. If dealers cannot become profitable, they need to reevaluate their commitment to the industry.

So how do you survive and become profitable in this economy? As many articles in recent issues have discussed, dealers need to get back to basics—"blocking and tackling," to use a football term. The NADA convention was full of vendors and seminars



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Albin, Randall & Bennett, CPAs

covering these topics and more. As usual, the selection of seminars offered at NADA was a great mix of topics to help dealers improve their operations. Seminars addressed improving service profitability and salesperson performance, hiring and retaining good people, structuring pay plans that work and ways to sell more vehicles on the Internet, to name a few.

Arguably the most inspirational moment of the convention was the Sunday morning featured speaker, Chris Gardner, whose life story was made into the film *The Pursuit of Happyness*, starring Will Smith. Gardner made an impression on those who heard him speak, and he left many in tears. He spoke about the struggles he faced being homeless, raising his son alone and working to break a tradition of failure in his family. And in the end he

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NADA 2009 CONVENTION

(continued from page 3)

made his listeners realize that they can accomplish anything, including surviving and prospering, if they believe in themselves and control that which is within their control.

It was great to see those dealers who attended the convention. We enjoyed speaking with you at our booth and sharing ideas for the upcoming year. Everyone I spoke with from New Orleans was elated that the NADA convention was held there. It was a shot in the arm that the local business community really needed. We wish all of you a prosperous 2009 and hope to see you in Orlando for NADA 2010. ☺

For assistance, please call 1-800-4AUTOCPA or see our website at www.autocpa.com. Headlights is prepared by the **AutoCPAGroup** for the clients of its members. We are required by IRS Circular 230 to inform you that the advice contained herein (including all attachments) is not intended or written to be used for the purpose of avoiding any penalties that may be imposed under Federal tax law and cannot be used by you or any other taxpayer for the purpose of avoiding such penalties. © 2009 Headlights

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