



# CONTROLLER'S REPORT

## MEMBER BRIEFING

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## RISK MANAGEMENT

# Controller and Chief Compliance Officer: A Valuable Partnership

(Quick Code 091501)

Controllers are naturally concerned with risk—particularly when it comes to misuse of company funds. A key part of their job is to ensure that all the necessary financial controls are in place to prevent misuse of funds. That's why it behooves controllers to promote close teamwork with their companies' chief compliance officers (CCOs), stresses Michael Volkov, CEO and owner of The Volkov Law Group.

"Controllers and CCOs share a common purpose," Volkov explains. "They both want to ensure that all payments are properly made and documented. Both controllers and CCOs have a vested interest in making sure that money is used judiciously. They want to ensure proper access to company money by employees to avoid misuse as in the cases of bribery, conflicts of interest, theft, embezzlement, and kickbacks. They want to ensure that payments to vendors and third-party intermediaries are appropriate, that payments to charities and other organizations are not tied to foreign officials, and that payments for T&E expenses are also appropriate. Fraud, bribery, kickbacks, and other financial misconduct can have a direct impact on corporate ethics and compliance as well as on the bottom line."

However, while it makes sense that CCOs and finance leaders forge a true partnership to prevent corruption and misuse of funds, in recent surveys CCOs have reported that they do not have a strong working relationship with finance, Volkov notes. "They're typically not involved in the design and implementation of financial controls," he says. "That is a significant problem, as financial controls are the corporate mechanism for ensuring that money is used for proper activities."

The controller is in an ideal position to help forge a closer working relationship with compliance, Volkov points out, noting, "There are so many ways they can help each other out."

## Steps for the Controller

Volkov offers the following suggestions for controllers to forge a closer working relationship with the compliance officer:

**1. Invite the CCO into the finance department to make presentations to AP.** "The CCO is a great resource and can help educate accounts payable on such topics as fraud and money-laundering risks," Volkov points out. "The CCO can help AP understand what to watch out for when it comes to paying vendors."

**2. Team up to build due-diligence systems for third-party payments.** "With third-party payments, companies may sell a service to one company but be paid by another," Volkov says. "Companies are realizing that 15 percent to 20 percent of the money they collect is from someone they don't know. Accounts receivable people often say they are nervous about it. They don't know whether the money might be proceeds from crime and corruption, and

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**THE CONTROLLER'S REPORT**  
PO Box 7437 Portland, ME 04112-7437  
207-842-5557  
fax: 203-516-2396  
e-mail: customerservice@iofm.com  
controller.iofm.com

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by accepting it your company would be committing an offense."

"Controllers can work with their CCOs to establish due-diligence systems to make sure third-party payments are legitimate," he continues. "They can confer with the CCO when then have a question such as, 'Why are we getting money from company Y when we sold the products to company X?' They can work together to document that companies X and Y are properly affiliated, the payment has been authorized, and the arrangement has been made for legitimate business reasons."

The same thing can occur in reverse, Volkov adds. "AP may get an invoice from a company in Australia although the goods were purchased from a company in China. Controllers may want to know, 'Why are we paying this person?' It's a great opportunity to bring compliance into the conversation to make sure there isn't something illegal going on, such as a money-laundering operation."

**3. Collaborate with the CCO in designing financial controls.** "Controllers can get valuable input from CCOs when designing financial controls," Volkov explains. "For example, they can work out ways to prevent conflicts in segregation of duties in payment processes. I advise controllers not to wait till an internal auditor finds a problem and puts it in a report. Work with your CCO to identify and eliminate conflicts. Two heads are always better than one."

Another area where CCOs can help is in the design of controls for vendor verification. "Every controller's goal is to make sure no company money gets into the hands of a sham vendor," Volkov says. "Both the controller and CCO have a vested interest in making sure there is a

legitimate invoice before any vendor is paid."

**4. Invite CCOs to finance meetings.** "When there is a meeting of the senior finance team—controller, internal audit, and CFO—give the CCO a seat at the table," Volkov advises. "The CCO can help finance problem-solve and assist in working out ways to safeguard company money."

**The bottom line:** "Compliance professionals need a seat at the financial table, especially given the new COSO framework," Volkov emphasizes. "COSO, the Committee of Sponsoring Organizations of the Treadway Commission, is a joint initiative of five U.S. private sector organizations, focused on business ethics, fraud, and financial reporting, among other related issues. COSO has established an internal control model companies can use for assessing their own internal control systems. Since fraud and bribery are specific issues for focus, CCOs are a natural partner for controllers and finance leaders in this area. CCOs can help finance by offering insight and suggestions on financial controls to promote the company's interest in its ethics and compliance program. It's a win-win situation that will make everyone's job easier."

**Editor's Note:** Michael Volkov has more than 30 years of experience in practicing law. A former federal prosecutor and white-collar defense attorney, he has expertise in areas of compliance, internal investigations, and enforcement matters. He is a regular speaker and is frequently cited in the media for his knowledge on criminal issues, enforcement matters, compliance, and corporate governance. His blog "Corruption, Crime & Compliance" is at [www.blog.volkovlaw.com](http://www.blog.volkovlaw.com). □

## PROCESS IMPROVEMENTS

# Open the Door to a Better Close

(Quick Code 091503)

Any controller who has burned the midnight oil leading up to the monthly close deadline will attest that the close process can be fraught with errors, delays, and rework. But there are steps controllers can take to close the books in an efficient, accurate, and timely manner, says Elizabeth Milne, Product Marketing, SAP, who specializes in close process improvement.

"Consistency and control are the biggest problems—especially when you are using multiple, manual spreadsheets," Milne says. "When a number is changed in one spot on one spreadsheet, it must be changed in

the same spot on every other spreadsheet, which often doesn't happen. So it is extremely difficult to manage changes."

"You also have to have a clear, traceable audit trail of where all the numbers originated, but the audit tool within Excel doesn't always work great," she points out. "The result is that you can't trust your numbers. Every controller wants to be able to say the numbers are correct—in the interest of accuracy as well as compliance—before they sign off on the close, but they can't be sure of this if their close process has not been optimized."

**Getting it Right**

Milne advises controllers to take the following steps to optimizing the close process:

**Measure where you are now.** "Measuring the current close process is the first step to improving it. As Peter Drucker said, 'What gets measured gets managed,'" Milne notes. "Controllers need to take a benchmark of the close process and see where they are so they have something to measure against."

What specifically can you measure? "There are a number of key performance indicators (KPIs) for the close process," Milne explains. "One commonly used KPI is 'number of days to close books.' Another is 'number of days to produce financial report.' However, these are not necessarily the best metrics to use because they don't tell you a lot. It's better to use more detailed metrics."

Metrics she recommends include the following:

- Number of FTEs working on the close;
- Number of restatements produced;
- Number of times you had to reopen and reclose the books;
- Cost of audits; and
- Cost to finance department of closing the books and what percentage of revenue that represents.

**Analyze each of the four steps of the entity close management process.** The SAP breaks these steps down as (see exhibit):

1. **Accounting**/closing the books (general ledger, sub-ledgers, leasing, revenue accounting)
2. **Entity close management** (intercompany reconciliation, account reconciliation, entity close management)
3. **Corporate close** (consolidation of all entities and notes management)
4. **Reporting and disclosure** (reporting and analysis, disclosure management)

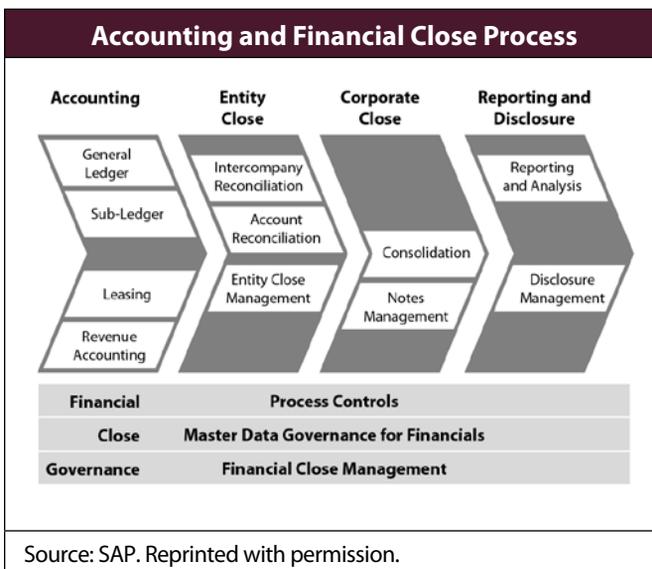
"There is also financial close governance for this whole process, which includes process controls and managing master data," Milne adds.

To analyze, measure, and optimize each of the four steps of the close process, controllers need to plan, execute, monitor, and analyze, she explains:

- **Plan.** "In planning, controllers want to think through the steps they and their teams take to close books," Milne says. "They need to run different batch jobs,

collect numbers for end of period, come up with lists, compare different divisions, etc. The goal is to plan out all the steps that must be taken for the close process to be well organized."

- **Execute.** "At the execution step, controllers and their teams need to methodically follow each of the steps they came up with in the planning stage. They need to establish the close date and dates for each task to be completed—such as executing batch jobs, posting manual journal entries, getting approvals, and running workflows," she says.
- **Monitor.** "Throughout each step of the close process, controllers need to monitor the process to keep tabs on who is finished with what steps, who is running late, who is causing bottlenecks, etc.," Milne explains.
- **Analyze.** "This is where controllers must determine what worked well and what didn't for each step of the close process. Where were the holdups? Why did one entity or division close more quickly and efficiently than another? Benchmark within the organization to see where the best practices are and how they can be used to bring improvement throughout the enterprise," she advises.



"This is also where you want to think about how to optimize every part of the close process. The goal is to centralize, standardize, and automate. Find ways to implement tools that will improve efficiency, such as scheduling tools that run on the ERP system that monitor batch jobs—such as calculation of depreciation," Milne continues. "But keep in mind that while there is a lot of technology out there, none of the financial close software is 'plug and play.' Everyone's processes are different. You have to configure the software to meet your needs. That's

why it's so important to clearly understand and measure all the steps in your close process and then optimize that process before you introduce automation tools."

Milne adds that Gartner, Forrester, and Ventana all analyze and review different tools for close management and provide impartial opinions on vendors.

**The bottom line:** "Controllers must optimize—as well as continuously improve—the close process, or they may

end up frequently pulling their hair out and working weekends," Milne notes. "An ineffective close process causes a lot of stress and can drain a controller's and finance team's quality of life—as well as drain company money."

**Editor's Note:** Elizabeth Milne manages the accounting and financial close portfolio for SAP Product Marketing. To read her blogs on close process improvement, go to: [www.digitalistmag.com/author/elizabeth-milne](http://www.digitalistmag.com/author/elizabeth-milne). □

## PAYMENTS

# P-Cards and Payment Fraud: Be Wary (But the Risks Are Lower Than You Might Think)

(Quick Code 091502)

P-cards and other commercial cards are gaining widespread momentum as a convenient method of allowing employees to pay for purchases on behalf of their companies, yet there are still many concerns about risk. To gain some insights about the real level of risk—and how companies can mitigate it—*Controller's Report* interviewed Terri Brustad, CPCP, Manager of Content Services at the NAPCP, a membership-based professional association committed to advancing Commercial Card and Payment professionals and industry practices worldwide, and P-card industry veteran Lynn Larson, CPCP, of Recharged Education LLC, an organization that offers resources focused on P-Cards and other Commercial Cards.

Larson and Brustad offer the following advice for controllers who are concerned about p-card fraud and other risks:

**1. Keep it in perspective.** "Organizations need to remember that all payment methods have risks—and P-cards and commercial cards offer many protections that others do not," Larson stresses.

Brustad agrees. "In the mid-1990s, when P-card programs were getting their start, there was much skepticism," she acknowledges. "Since then, however, you could say that P-cards have become a taxpayer's best friend in that they provide the transparency the public desires. Also, the efficiencies P-Cards bring to an organization allow for annual cost avoidance savings, which ultimately means that resources normally directed to the traditional check payment and procurement processes can be shifted elsewhere within the organization."

**2. Put effective controls in place.** "While it is natural

to be concerned about card fraud, establishing effective controls greatly reduces the risk," Larson says. "However, controllers should keep in mind that *more* controls does not necessarily equate to *better* controls. You need to determine what the right controls are for your operation and focus on those."

"When an organization has the right controls in place, P-cards are less risky than cash, check, wires, or money orders," Brustad notes.

**3. Establish clear policies.** "Card policies and procedures need to be clear and as specific as possible," Larson says. "Do not leave things open to interpretation or employees are liable to make up their own rules."

**4. Enforce card policies.** "One of the best things organizations can do is to consistently enforce their card policies and procedures," Larson says. "Organizations that experience internal fraud tend to be ones that are lax with their rules."

**5. Know what to watch out for—and educate your company's managers.** "In 2014, a Harris County, Texas, man used his company credit card to make personal gasoline purchases totaling more than \$18,000," Larson recalls. "The man, a truck driver for a local company, was filling the gas tanks of family and friends in exchange for cash. His boss became suspicious after noticing the average monthly fuel cost increased by as much as \$4,000. The boss looked into the situation and discovered that purchases of unleaded gas were being made—but the company vehicles used diesel."

It's important for controllers to keep an eye out for suspicious purchases on company cards, and advise managers whose employees use cards to also keep a

watchful eye on purchase activity. The sooner fraud is detected, the faster you can stop a money drain and nip the behavior in the bud.

"According to the *2014 Report to the Nations on Occupational Fraud and Abuse* by the Association of Certified Fraud Examiners (ACFE), the median amount of time between when this type of fraud commences and when it is detected is 18 months," Larson says. "That's a long time to have such behavior persist undetected—and that's why effective internal controls are so vital."

Brustad adds that the NAPCP's *Fraud Prevention and Detection* report concludes that media reports of fraud related to the use of P-cards and other commercial cards rarely mention the benefits of these card payments or the control gaps within the organization that allowed the fraud to occur. "Publicity associated with fraudulent incidents could lead one to conclude that such crime is significant within card programs," Brustad says. "In

reality, industry research—on P-cards in particular—has consistently shown that fraud tends to represent less than one-half of one percent of P-card spend."

"Fraud is not the epidemic problem that some people, especially those lacking an understanding of P-cards, believe it to be," says Brustad. "Furthermore, when P-card fraud does occur, it rarely causes the end-user organization to lose money. Controllers should keep in mind that the vast majority of fraud and misuse occurs within a small percentage of end-user organizations that do not have effective controls in place," she concludes.

**Editor's Note:** The Association of Certified Fraud Examiners (ACFE) study is available for free download at: [www.acfe.com/rtn/docs/2014-report-to-nations.pdf](http://www.acfe.com/rtn/docs/2014-report-to-nations.pdf). There is a wealth of additional information on p-card fraud and other aspects of p-card management available to NAPCP members at: [www.napcp.org](http://www.napcp.org), as well as at [www.recharged-education.com](http://www.recharged-education.com). □

## FINANCIAL ANALYSIS

# Boosting the Controller's FP&A Savvy

(Quick Code 091505)

Financial planning and analysis (FP&A) is a fast-growing function in finance, thanks to the bottom-line benefits that accurate planning and analysis can bring to an organization. Some companies are creating "FP&A Controller" positions or involving their controllers in FP&A initiatives—and the ones that aren't should be, suggests Mary Driscoll, Senior Research Fellow, APQC, since controllers can offer great expertise in supporting the FP&A effort.

However, controllers and finance teams are often unable to play a role in FP&A due to their myriad other finance duties, Driscoll points out. "In our survey of 130 finance executives, only 40 percent rated their companies' FP&A capabilities as effective. One impediment cited by two-thirds of survey participants is that their finance teams are always bogged down by their basic financial duties such as tracking budget targets versus actuals. They don't have the time to assist with FP&A activities such as evaluating the potential outcomes of pricing options."

### How Controllers Can Play the Part

"Obviously, the participation of controllers and other key members of the finance team would help boost the effectiveness of FP&A efforts," Driscoll adds. Here are some key ways controllers can aid the FP&A cause:

**Believe in the value of FP&A.** "Controllers will be more willing to make room for involvement in FP&A activities if they see the value and deeply believe that by playing a role—such as providing good, reliable financial data—they will help the company boost shareholder value," Driscoll suggests. "This is, in fact, an increasingly important way that controllers can directly influence financial performance—improving the company's ability to allocate resources dynamically."

When controllers believe in the value of FP&A, they will also support investments in technology that can facilitate analysis efforts. "When I talk to FPA people, they tell me that sometimes what holds them back is not having easy access to data they need to provide analysis in a timely manner," says Driscoll. "If, for example, a controller doesn't believe it is important to invest in software that will improve the ability to extract data from multiple sources, FP&A efforts will be like trying to use a 1940 Ford to win the Indy 500."

**Network with other controllers.** "I advise controllers to talk with controllers at companies that have winning FP&A strategies," she adds. "Find out what those strategies entail and how these controllers contribute."

"Respondents whose organizations use scenario analysis reported having better aligned and more agile

business strategies. Over the next year or two, I predict that greater numbers of controllers and their finance teams will be getting involved in these successful methodologies," Driscoll concludes.

### MASTER THE EIGHT SKILLS OF FP&A EXCELLENCE

"Controllers who are tapped to play a role in FP&A would do well to master the eight skills APQC has identified as being essential qualities for FP&A excellence," Driscoll advises. These skills are as follows:

1. **Deep knowledge of accounting and performance management.** "To be effective at financial analysis, someone needs to have a strong background in managerial accounting as well as advanced forecasting techniques," Driscoll says. "While traditionally accountants look backward, effective FP&A requires looking backward, forward, and sideways at the business. You need to use historical accounting information as a guide, but understand that it is only one piece of the bigger picture."
2. **Strong grasp of business strategy, functions, markets, and risks.** "Budgeting is the starting point for everything that happens in FP&A. To be effective at annual planning, the FP&A professional must have a strong grasp of every functional area in the organization," Driscoll stresses. "You have to understand every function's internal and external drivers, the resources that are required to meet expectations, and the risks inherent in that functional area, as well as any relevant marketplace dynamics."
3. **Mastery of systems, analytical tools, and data management.** "This entails the ability to use software applications that are standardized across the enterprise and designed to model, predict, and compare options for resource allocation," Driscoll explains.
4. **Ability to design reports and self-service tools that business managers will use.** "The finance team needs to be able to educate nonfinancial personnel about ways in which economic profit is created or destroyed," Driscoll says.
5. **Versatile and polished communication skills.** "This means the ability to deliver presentations that are clear and understandable to top management. It requires being able to present financial insights about pending trends in operating performance including myriad revenue and cost scenarios. These insights must be relevant, well-informed (etc.)—as well as concise so they are accessible to management, Driscoll points out.
6. **Customer service orientation.** "This entails supporting the internal customer's decision-making with the best available information while providing guidance that will help management achieve the business's economic goals," Driscoll says.
7. **Insatiable desire to solve business puzzles.** "Successful FP&A involves a keen, ongoing willingness to identify drivers and obstacles to business performance," Driscoll says.
8. **Use rolling forecasts and scenario analysis.** "Our survey showed clearly that using rolling forecasts of revenues and operating margins helps people better anticipate—and respond to—marketplace trends and other factors that will affect the business," Driscoll says. "A significant 94 percent of respondents whose businesses use rolling forecasts said their business analyses were effective, compared to only 50 percent of those that do not use rolling forecasts."

**Editor's Note:** For more information on FP&A, go to: [www.apqc.org/knowledge-base/documents/financial-planning-and-analysis-influencing-corporate-performance-stellar-p](http://www.apqc.org/knowledge-base/documents/financial-planning-and-analysis-influencing-corporate-performance-stellar-p). □

## FINANCIAL LEADERSHIP

# Solid Decision-Making Requires Instinct and Information

(Quick Code 091506)

To gain insights on how controllers are making decisions—and compare the "gut feel" versus "hard facts" approaches to decision-making—*Controller's Reports* spoke to finance executives Albert Antoine, Chief Financial Officer, Southeast Milk, Inc.; and Bob Sefton, Controller, Nomacorc.

### Background

A recent study by Epicor Software Corporation, based on interviews conducted with more than 1,500 finance leaders in 11 countries, including the United States and Canada, revealed that nearly half (46 percent) rely on "gut feel" and instinct to make business decisions instead of basing decisions on internal data—often because they do not have quick access to such data. According

to the study, this inability to access the right financial information is having a direct impact on business performance, with 45 percent of respondents indicating that insufficient data hampers timely decision-making, and that inaccurate information is the main cause of organizational mistakes.

The Epicor study found that the more finance leaders rely on empirical data for decision-making, the greater the chances of higher profitability—and that "increasing profits" is the top 2015 business objective for 46 percent of respondents. Furthermore, 72 percent of respondents that do rely on empirical data for decision-making as opposed to instinct, report greater profits.

**The other side of the coin:** While the Epicor study did

reveal that finance leaders recognize the importance of data visibility and accuracy, it also makes a case for best-practice decision-making being a blend of hard facts and emotions.

"Instinct, intuition, and even emotion were considered by a significant number of respondents to have a valid role in decision-making, with the most effective CFOs knowing when to use their instincts to guide and add value in the way numbers alone cannot achieve, as opposed to just using it to fill information gaps left by inadequate processes and infrastructure," points out Malcolm Fox, Epicor Software's vice president of product marketing financial management and services industry solutions.

### Sefton's and Antoine's Input

Controller Bob Sefton definitely finds that there are times he needs to rely on "gut feel" and instinct to make work-related decisions. "This goes hand-in-hand with whether it is a quick decision or long-term decision," he points out. "For quick decisions, experience and general knowledge will prevail and drive the gut instinct."

"The decision process is also a function of how critical the decision is and how much consequence can be forthcoming if the decision turns out wrong," Sefton adds. "When it's a long-term decision with higher consequences, then the more you want to be able to rely on specific data."

Albert Antoine agrees. "It is not uncommon to make decisions without all the data you need (or think you need)," he notes. "So, you rely on the data that is available, your experience, and the counsel of other experienced colleagues."

Do these gut-feel decisions usually work out? "Yes—these decisions generally work out due to experience and confidence in the process," Sefton says. "The odds are usually 50/50 that the decision will be right in any case, but technical knowledge will reinforce the decision-making to improve the odds."

"Most of the time the decision works out because while it may not be based on perfect knowledge, when you access all the sources that *are* available, they will usually lead you to the best solution," Antoine says.

### Finding Data

Since instinct combined with information is the ideal combination for solid decision-making, where do Sefton and Antoine find the data they need to make decisions?

"More often than not, I generally have the data I need to make decisions, and if not I actively seek it out from

other sources," Sefton says. "These sources include other departments (cross-functional teams), research and third-party sources. Spreadsheets are a helpful tool as long as they can summarize and sort key data in a way that makes sense," he adds.

"Data can provide relevant information to make the best informed decision, which could lead to the most valued-added choice. Depending on the importance of the decision and the timing required, I use a combination of sources for data, including application software, spreadsheets, other managers/departments, outside professionals in the relevant field, and/or online research," Antoine says. "Most of the data I use comes from internal sources like our ERP system and/or fellow employees."

The Epicor study found that the level of collaboration between finance leaders and other departments has increased significantly in recent years. Around half of those surveyed (52 percent) report that decisions are often made collectively, involving people from outside finance.

### Data Visibility

Only about half of the finance leaders Epicor surveyed felt they had "good visibility" of financial information, including such key data as overall and business unit performance, product line performance and profitability, sales and labor costs, sales forecasts, raw material costs, and customer profitability.

Sefton and Antoine agree that "data visibility" is crucial. "Good 'data visibility' means being able to access data when needed," Antoine says. "With today's information technology and communications capabilities, generally controllers can obtain lots of helpful data."

"Keep in mind that the 'visibility' of data is only as good as the due diligence put forth to seek out all forms of data to make an informed decision," Sefton stresses. "It's important for controllers to be aware that often the 'data visibility' provided by others is what they *want* you to see, and could omit key important data sets. This could result in an ill-informed decision."

**The bottom line:** Decision-making requires a balanced approach. Reliance on 'gut feel' versus empirical data can work out for many controllers who are experienced and know their businesses. "Being overly conservative may put organizations at a competitive disadvantage if CFOs don't have the confidence to allocate maximum resources for customer service, sales, marketing, and innovation (new product development, partnerships, etc.)," says Epicor's Fox. □

## SIX TIPS FOR DECISION-MAKING SUCCESS

Here are six tips to aid controllers in effective decision-making:

1. **Become a data expert.** "The secret to success is to constantly review your data and understand the source of the information. Review data on a regular basis—this will help you understand trends," says Bob Sefton, Controller, Nomacor. "Establish benchmarks to measure against. Every controller wants to improve profitability, and data can help them do just that in the same manner as a key measurement matrix can drive continuous improvement."
2. **Understand your business.** The better you understand your business—the way it operates, its challenges, its products and services, market, and strategic goals—the better you will be at making decisions, Sefton suggests.
3. **Regularly involve yourself in your company's decision-making process.** "The key to being a good decision-maker is to be involved regularly," Sefton notes.
4. **Hone your sleuthing skills.** "Know whom to ask and what questions to ask" Sefton advises. "Ask thought-provoking questions to get to the information you need."
5. **Be willing to go with the most informed and timely**

**decision you can make.** Never avoid a decision because you feel you don't have every possible bit of relevant data. "Objectively collect all the information available (given your time constraints) and make an informed, timely decision," says Albert Antoine, Chief Financial Officer, Southeast Milk, Inc. "Remember, indecision is also a decision and will lead to consequences." Some of those consequences might include weakening your reputation, failing to act on a revenue-generating opportunity, or neglecting to fix an operational problem that is causing a money drain.

6. **Know when to (and when not) to rely on your gut.** "Simply put, relying on gut instinct requires experience and confidence," Sefton says. "Experience is the best teacher. Controllers who do not have a great deal of experience will need to rely on other sources of data and should not rely as much on gut instinct, as this could cause them to make poor decisions that could damage their professional reputations. Also, you have to weigh the potential consequences of your decision. The greater the consequences, the less you should rely on instinct and the more you should rely on data."

However, on the flip side, overconfidence can cause organizations to miss market expectations, or even outspend revenues," says Epicor Software's Malcolm Fox. "The fact is, you can never have too much information."

## SCENARIO PLANNING

# Tips to Polish the Controller's Crystal Ball

(Quick Code 091504)

While no company would demand that its controller predict the future with pinpoint accuracy, most organizations do expect controllers to play an active role in scenario planning—and with excellent reason.

"Scenario planning allows a company to be agile," points out Moshe Kravitz, Director of Financial Planning & Analysis at IDT Consumer Phone Services, (Newark, NJ), a telecommunications-energy company. "Companies that are agile are in a position to respond quickly to changing conditions because they already have a plan in place to avoid looming danger or capitalize on business opportunities." Kravitz has the following words of wisdom for controllers involved in scenario planning:

**Start simple.** "Create a simple working model to begin with. You can add complexity later on," Kravitz advises. "Identify one or a few drivers with high sensitivity to variance and spend more time doing analysis and collecting data on those particular drivers. Also, don't aim for 100-percent accuracy of your assumptions; aim for 70-percent accuracy instead. The difference between 70 percent and 100 percent could be the difference between actionable information and analysis paralysis. The final

30 percent of accuracy in most cases would not change your decisions anyway."

**Keep the team small.** "Generally it's the finance people who do all the modeling, so the scenario planning team should actually be pretty lean. The controller, or team, can consult as needed with IT, HR, sales, etc.," Kravitz points out. "Of course for large, global scenarios, you would need more input from more areas of the enterprise."

**Establish the drivers.** "We don't know the future and we can't know it. But we can determine what the drivers are for any projection—revenue drivers, cost drivers, regulatory influences, staffing components, resource requirements and constraints, etc.," Kravitz explains. "For every scenario, ask, 'What would need to happen for this particular scenario to take place?' That will help you identify your drivers for that scenario."

**Avoid random stretch goals.** "When scenario planning, don't just say, for example, 'We want to increase sales of this product by 25 percent,'" Kravitz advises. "Look at prior performance both internally and in your industry. Look at resources, staffing, and industry and economic

trends to put your goals into context and see if conditions actually support the assumptions you are making. This will allow you to set goals that make sense."

**Use KPIs to monitor actuals for all drivers.** "An important part of scenario planning is implementing a dashboard of customized KPIs that measure the drivers you've identified for a particular plan," Kravitz points out. "This will allow you to monitor, track, and adjust the plan as necessary if a KPI goes above or below what you established for your target performance level for that driver."

**Rank your scenarios.** "It's a good idea to use the 'insurance principle'—probability times magnitude, the likelihood that it will occur multiplied by the size of the event if it does occur," Kravitz says. "It is an imperfect but simple way of evaluating the impact of a particular scenario and comparing its significance against other scenarios."

**Consider factors affecting volume, sales, and revenue.** "When scenario planning for a new product or service, always look at sales in terms of your existing customer base, in terms of a potential extended customer base, new revenue from add-on sales and cross-selling, etc., because of the availability of this new product or service," Kravitz says. "Other factors to look at include staffing, additional risk exposure because of extended time and conditions being covered, and how future production might impact existing inventory."

**Consider software solutions.** Some companies find it beneficial to implement software solutions that will provide scenario planning, Kravitz points out. "Solutions are available that work at the corporate, global level all the way down to the individual customer level. For example, one telecom company implemented customized software that sits on the desk of every customer service

rep. The system uses strong predictive analytics to build scenarios in real-time that provide options for the rep to offer the customer. That allows every customer interaction to become an opportunity to cross-sell, to up-sell, and to enhance customer retention and loyalty," he explains.

- **The system works like this: A customer calls in with an issue.** The predictive analytics built into the system have been set up such that if a customer calls with that particular issue, the rep should offer certain specific things in response. A customer might call in wanting to cancel a contract. The system would tell the rep to offer X service or Y hardware for free.

"These solutions use a profitability model that looks at each customer by volume of business, tenure, and expected lifetime value," Kravitz explains. "This helps companies determine how much it is worth for them to hold onto each customer, and then provides scenarios that allow them to do that in real time."

**Don't be intimidated by scenario planning.** "Most controllers have certainly done scenario planning—perhaps not in a formal sense but they have worked with aspects of it," Kravitz notes. "They just have to take what they already know and formalize it into a complete scenario approach. With time and effort, any controller can become more adept at anticipating and envisioning the future, analyzing options, making decisions, and becoming more agile in responding no matter in what direction the metrics may turn.

"Controllers bring great value to the scenario-planning process," says Kravitz. "They see the broad corporate picture, know the competitive landscape, and understand the interworkings of all financial dimensions and drivers of the business. Controllers know the right questions to ask to get people thinking analytically so no important

## CONSIDER THE 'UNTHINKABLE'

Not every scenario plan has to be completely "realistic." Sometimes having a plan for an eventuality that seems virtually impossible can put a company in a unique position to reap huge rewards.

"A classic corporate example of this was related by Peter Schwartz in *The Art of the Long View*," Moshe Kravitz notes. "When he was working for Royal/Dutch Shell in the 1980s, they used scenario planning to analyze financial investments in multibillion-dollar projects—mining oil and natural gas from the Black Sea."

"They looked at all the drivers—political, cultural, scientific, and economic," Kravitz continues. "To try to anticipate the 'unthinkable' scenarios and play out what effect they would have on this business decision, they examined all of their assumptions. Oil prices were steadily rising and control in the former Soviet Union was very tight. There was a limit to what resources were let out into the free market. It was

'unthinkable' that the political and economic structure would change."

Still, Schwartz and his team explored the scenario that would exist if the Soviet Union's economy actually weakened and it was forced to release more natural gas into the free market. They also looked at what would happen if OPEC, too, began to weaken, causing oil, which had been increasing in price, to turn into a commodity with a fluctuating price. And as a result, the company put into place a contingency plan that allowed it to jump on the golden opportunities that presented themselves when, in fact, those "unthinkable" assumptions came true.

"They didn't know the future better than anybody else," Kravitz notes. "But the advantage you get from scenario planning is that when one of those 'unthinkable' assumptions comes true, you already have a plan for what you will do. This is what allowed Royal/Dutch Shell to begin trading oil as a commodity before anyone else could get a similar plan up and running."

stones are left unturned. Finally, controllers are in the best position to see how a potential change might influence working capital, credit, and revenue subject to taxation.”

**Editor's Note:** Moshe Kravitz developed his skills in Forecasting and Risk Mitigation in his actuarial roles at CNA Insurance and Buck Consultants. In his current role

he is focused on Modeling and Profitability. Kravitz has taught in many venues: classroom, adult education, staff training and online webinars. He is also a certified career coach who specializes in the analytics and finance fields and in strategy and positioning for professionals changing industries or careers. Moshe can be reached at Moshe.Kravitz@IDT.net 

## COMPLIANCE

# Update on the New Revenue Recognition Standard

(Quick Code 091507)

By Lisa M. Starczewski

The new Revenue Recognition Standard, which converges U.S. Generally Accepted Accounting Principles with the International Financial Reporting Standards, will significantly change the way companies recognize and report on revenue. Regardless of whether a company will see a change in its revenue number, it will need to grapple with the new approach to revenue recognition and update its systems, processes, and controls to function within the new standard. Every company, therefore, needs to examine its contracts and business models with new eyes.

The ultimate goal of the Revenue Recognition Standard is a more useful set of financial statements for investors. The Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) have eliminated industry-specific guidance in hopes of achieving actual comparability in financial statements. The desired outcome is consistency with respect to revenue recognition across industries and transaction types.

In order to achieve this, however, the standard must be successfully implemented, which requires a shift in the way that accounting and auditing professionals approach revenue recognition, as well as consistent, effective oversight of the process. The Boards have committed significant time and effort to identifying and responding to implementation issues to avoid inconsistency in its application.

### Developments Controllers Need to Understand

Here are the key developments of which controllers need to be aware:

**The revenue guidance continues to evolve.** The FASB and IASB are responding to constituents and to issues raised by the Transition Resource Group (TRG). Both the

FASB and the IASB recently deferred the effective date of the new standard, although companies may choose to apply the original effective date.

In addition, the FASB issued a proposal amending the guidance on the identification of performance obligations and accounting for licenses. We will see additional proposals from the Boards over the next few months (additional practical expedients on transition, as well as possible guidance on principal vs. agent, presentation of sales taxes, collectibility, and noncash consideration).

**With a few minor exceptions, the standards issued last year were fully converged.** However, the Boards are taking different approaches in their responses to the implementation issues that have been identified. As the Boards issue new proposals, companies that apply both U.S. GAAP and IFRS need to pay close attention to areas of potential divergence. There is little doubt, at this point, that the wording in the two versions of the standard will be different. The FASB standard will likely include more specific guidance with respect to application of the principles. The question becomes whether these differences will lead to differences in practice.

**These amendments are further complicating the process for companies that have to reassess.** However, the changes being made to the Standard are welcome ones (in that they are simplifying and clarifying certain aspects of the guidance). Companies should be paying close attention to the Board proposals as well as the work that the TRG is doing and should be closely communicating with accounting and auditing consultants to stay on top of developments.

**The timetable for implementation will vary.** The variations will depend on whether the effective date is delayed and what transition method a company chooses to apply. If a public company applies the deferred effective date and the full retrospective transition method, the company will restate contracts for 2016 and 2017 to

show comparative financial data. If this is the case, the company will need to have systems and processes in place to capture necessary data beginning January 1, 2016 (which would also be the date of the cumulative adjustment).

### Details to Keep in Mind

Here are some of the key factors/changes financial controllers need to keep in mind going forward:

- One of the greatest challenges in a principles-based standard is the increased reliance on professional judgment to determine the proper accounting.
- There are significantly expanded disclosure requirements that companies need to begin focusing on. For example, companies need to begin to determine the categories into which they will disaggregate revenue.
- With respect to the specific guidance in the standard, the most impactful provisions vary across industries. In some industries (e.g., healthcare), determining whether and when a contract exists may present unique challenges. In others (e.g., software), identifying performance obligations and allocating transaction price may prove to be the most difficult steps.
- Industries that rely heavily on licensing (e.g., media & entertainment) will face the task of determining whether licensing revenue is recognized over time or at a point in time.
- If the most recent FASB guidance is finalized, companies applying U.S. GAAP will be required

to label licensed IP as either symbolic (over time recognition) or functional (generally point in time recognition).

### No 'One Size Fits All'

There is no "one size fits all" when it comes to assessment. Each company's unique business models and varying types of customer arrangements will lead to its own nuanced application of the principles in the new standard. There is no shortcut to what could be, for many companies, a long and arduous process.

Implementing the new standard will be a heavy lift for many companies. A delayed effective date may serve as a temptation to delay or take a break from the work that needs to be done—but companies should resist this temptation and continue on in their efforts.

**Editor's Note:** Please note that while the information we are reporting on is accurate as of our print date, additional changes may have occurred—or will occur—in the months to come. Lisa M. Starczewski, Counsel at Buchanan, Ingersoll & Rooney (Philadelphia) and Special Consultant to Bloomberg BNA, focuses her practice on corporate and pass-through tax planning, leasing, and installment sales. Lisa has written several articles on the new revenue recognition standard, including on how attorneys can and should be reacting to these new rules and helping clients understand and implement them. She is a frequent speaker at webinars and Continuing Legal Education (CLE) sessions on tax and financial accounting issues. Starczewski received the Tax Management Distinguished Author Award and is a member of the Tax Management U.S. Income Advisory Board. □

### A CHECKLIST FOR CONTROLLERS

According to Lisa Starczewski of Buchanan, Ingersoll & Rooney, controllers who are leading the compliance process for the new revenue recognition standard should ask and answer the following critical questions:

1. **Which transition method is best, from both a business and investor standpoint, for our company?**
2. **Have all the right players been included as part of our internal cross-functional team?** (These players should include tax, legal, finance, IT, sales, internal audit, and investor relations.)
3. **How is our company managing contract selection and data collection in its assessment process?** Also, how is the finance staff being trained to identify key terms and conditions?
4. **Is our company thinking broadly, beyond financial accounting, in terms of impact?** For example, are we looking at debt covenants? Incentive/bonus compensation arrangements? Potential tax implications?
5. **What additional oversights and internal controls might we need with respect to the judgments that will be necessary under the new standard?**
6. **How should our company handle the significant educational burden that the new standard imposes?** Specifically, how will professional staff be trained? How will potential impact be communicated to investors?
7. **To what extent can, or should, our external auditors be involved with assessment and implementation?**
8. **Are we having discussions with our auditors regarding how disclosures will be audited under a principles-based standard?** What level of detail will be necessary to adequately document judgments under the new standard? What changes will be necessary to capture the right information?
9. **Have we created an effective internal process for monitoring and assessing changes in the standard as they develop?**
10. **Have we considered engaging outside counsel to review contractual relationships and terms and conditions?**

**BENEFITS REPORTING**

# How to Report Health Savings Accounts (HSAs) on the Form W-2

(Quick Code 091508)

**By Raeann Hofkin, CPP**

Health Savings Accounts (HSAs) were created in 2003. They are available for employers of all sizes, and for individuals covered by a high-deductible health plan. HSAs receive tax-preferred treatment for money saved for medical expenses.

More employers are offering HSAs in an attempt to control healthcare costs and more employees are opting for the HSA option as they take on more responsibility for their own healthcare decisions. HSAs are portable, allowing employees to have complete control over the assets. What is not spent rolls over year after year, earning tax-deferred interest.

In addition, HSAs are simple to use because there are no claims to be reviewed—the employee just needs to keep the receipts. Basically, HSAs have lower insurance premiums while maintaining the security of quality major medical coverage.

**How HSAs Work**

HSAs work in conjunction with high-deductible health insurance. The contributed dollars can be used to pay health insurance deductibles for qualified medical expenses, including those not covered by the health insurance plan, such as dental or vision care. Any funds withdrawn for non-qualified medical expenses will be taxed at your income tax rate plus a 20 percent penalty if the patient is less than 65 years of age. Once the deductible has been met, health insurance pays the remaining covered expenses in accordance with the terms and conditions of the particular plan.

An eligible employee, his or her employer, or both may contribute to the employee's HSA. For both calendar years 2015 and 2016, the annual limitation on HSA deductions for an individual with self-only high-deductible health plan (HDHP) coverage is \$3,350. For an individual with family coverage under an HDHP, the annual limitation on HSA deductions for 2015 is \$6,650; in 2016, the limitation will be \$6,750. The limit is increased by \$1,000 for eligible individuals age 55 or older at the end of the tax year.

For both 2015 and 2016, the minimum annual deductible is \$1,300 for self-only coverage or \$2,600 for family coverage. Annual out-of-pocket expenses (deductibles,

co-payments, and other amounts, but not premiums) may not exceed \$6,450 for self-only coverage or \$12,900 for family coverage for 2015; this will be increased in 2016 to \$6,650 (self) and \$13,100 (family).

**How HSA Contributions Are Reported**

As Health Savings Accounts (HSAs) gain popularity, the confusion for W-2 reporting grows. Incorrect reporting of HSA contributions on the W-2, box 12, code W, will prevent employees from filing correct federal, state, and local tax returns. Employees rely on code W to complete the IRS form 8889, which is attached to the individual's income tax return. Therefore, errors in reporting amounts on the W-2, box 12, code W, are to be corrected via the W2C process.

Employer contributions to an HSA are excluded from wages subject to federal, Social Security, and Medicare taxes. Employee contributions are pretax and therefore also excluded from wages subject to federal, Social Security, and Medicare taxes.

**Forexample:** If the employer's contribution was \$500 and the employee's pretax contribution was \$6,000, report a total of \$6,500 on Form W-2, Box 12, Code W.

As long as the *total* annual employer and employee contributions to the HSA do not exceed the annual limits (see chart), they are not required to be reported on the W-2 in boxes 1, 3, or 5—however, they *must* be reported in box 12, Code W. □

Health Saving Account (HSA) Contribution Limits 2015 & 2016*			
	2015	2016	
<b>Self</b>	\$3,350	\$3,350	No Change
<b>Family</b>	\$6,650	\$6,750	\$100 increase
<b>Annual High-Deductible Minimums</b>			
<b>Self</b>	\$1,300	\$1,300	No Change
<b>Family</b>	\$2,600	\$2,600	No Change
<b>Out of Pocket (deductible &amp; co-pays)</b>			
<b>Self</b>	\$6,450	\$6,650	\$100 increase
<b>Family</b>	\$12,900	\$13,100	\$200 increase
*The limit is increased by \$1,000 for individuals aged 55 or older at the end of the tax year.			

# NEWS BRIEFS

## Quick Code 091509

### NETWORKING TIPS FOR CONTROLLERS

Networking with colleagues is a great way for controllers to stay on top of changes in their industries, benchmark successful finance-management techniques, and raise their professional profiles. What's the best way to keep in touch with your colleagues? A recent Robert Half Management Resources survey of 270 finance leaders reveals that when it comes to business networking, e-mail is the communication channel of choice for busy finance executives.

When asked, "How do you prefer to network professionally?" respondents answered as follows:

How Do You Prefer to Network Professionally?		
	2015	2012
E-mail correspondence	75%	42%
Networking online (social media)	9%	11%
Attend professional events, meetings, conferences	8%	33%
None/don't network	8%	10%
Other/don't know	0%	4%
	100%	100%

When asked, "What is the primary purpose of your professional networking activities?" the responses broke down as follows:

What Is the Primary Purpose of Your Professional Networking Activities?		
	2015	2012
Grow business	67%	38%
Keep up with industry news and developments	31%	49%
Recruit new talent	2%	2%
Find a new job	0%	1%
Other/don't know	0%	10%
	100%	100%

The survey shows that finance leaders' networking preferences are changing; three years ago, e-mail correspondence, while the top choice, was less popular than today. On the other hand, the preference for attending professional events has declined significantly.

"With the growing demands of busy work and travel schedules, email is an effective way for executives to stay connected to their teams and professional networks," notes David King, Canadian president of Robert Half Management Resources. However, "professionals shouldn't discount the value of in-person events as a way to build relationships and give you access to new contacts, in ways technology doesn't allow. Being a visible part of your industry's community both online and offline will go a long way in enhancing company credibility, and broaden your exposure to business insights and trends which can be then used to promote your own business's growth."

Robert Half Management Resources advises finance leaders to take these steps to broaden their connections and enhance their professional visibility:

- **Build a presence at industry events.** Consider delivering a presentation or facilitating a workshop at a national or chapter meeting or a conference. You will establish yourself as a "thought leader" and open the door to meeting valuable business contacts.
- **Mentor others.** If you share your expertise, you'll not only gain personal satisfaction but also help develop strong finance professionals who could serve your company in the future.
- **Volunteer with philanthropic and community organizations.** In addition to helping those in need, you'll expand your network and gain insights into diverse perspectives.
- **Serve in a leadership position outside the company.** By taking on roles in business and community groups, you'll demonstrate your leadership skills and may meet people who can provide value to your company.
- **Engage with your alma mater.** This will allow you to help prepare the "next generation" of finance professionals while enhancing your company's connections with professors and career centers. Your contributions could also build interest in your

## NEWS BRIEFS

company's brand, resulting in increased profits down the road.

**Editor's Note:** For more information, go to: [www.roberthalf.com/management-resources](http://www.roberthalf.com/management-resources).

### MORE COMPANIES LOOKING AT U.S. SITES FOR FINANCE OPERATIONS

The diminishing gap in labor costs—combined with lower turnover rates, greater business knowledge, closeness to customers and headquarters, and state tax incentives—is driving many companies to look at locating finance, IT, and other business services operations in the United States, according to research by The Hackett Group, Inc., an enterprise benchmarking and best practices implementation firm.

The Hackett Group's research provides detailed rankings for more than 30 cities based on a weighted mix of factors. Top 10 cities in the research are: Syracuse, NY; Jacksonville, FL; Tampa, FL; Lansing, MI; Grand Rapids, MI; Atlanta, GA; Allentown, PA; Green Bay, WI; Richmond, VA; and Longmont, CO.

Previous research by The Hackett Group found that the number of new business services jobs moving offshore has declined steadily over the past few years and will continue to do so, as companies reach the practical limits of the type of work in these areas that can be effectively offshored.

"Companies are realizing that the U.S. is becoming an increasingly viable option for elements of their service delivery organization, and we're seeing real growth in this sector, with nearly 700 U.S. centers of excellence, shared service centers, and global business services operations now up and running," says Jim O'Connor, Hackett Group Principal and Global Finance Executive Advisory Practice Leader. "Labor and operating costs are still high in the U.S. compared to Eastern Europe, Latin America, and Asia. But the gap is shrinking, and there are significant other benefits. In more and more cases, those benefits outweigh the additional cost. In addition, the public response to offshoring has made keeping jobs 'at home' an attractive option for U.S. companies."

O'Connor adds that, "Even if companies are using offshore centers, the U.S. is an essential part of almost any service delivery network for American companies, particularly when the work is complicated,

knowledge-based, or requires a high level of communication with customers and internal clients, or when fast turnaround or extensive collaboration is a critical element. U.S. centers are also ideal for transforming, improving, and standardizing processes before they are moved elsewhere."

**A case in point:** Verizon Communications is one company that recently decided to locate business services operations domestically. Verizon has consolidated nearly 1,500 finance operations staff into two U.S. service centers over the past two years. A variety of options were considered before the company decided to consolidate those finance staffers, from more than 300 U.S. locations, into the two service centers located in Lake Mary, Florida (near Orlando) and Tulsa, Oklahoma.

"By keeping our finance operations in the U.S., we've derived an array of benefits," reports Karan Mehra, Verizon's director of corporate-finance restructuring. "Talent was perhaps our primary deciding factor. We wanted to make sure we could recruit the quality talent that we needed, and that we could put strong training and development in place. Our goal was to build bench strength to support succession plans, so that our staff had the ability to learn new skills and develop professionally."

"We also saw a wide range of other benefits," Mehra continues. "By staying domestic, we got instant buy-in from both our clients within Verizon and throughout the finance organization itself. We have also been able to maintain complete control over our finance operations and processes, which can be difficult to do when you move offshore. And finally, avoiding extended travel times when visiting our service centers has been a significant advantage."

**Editor's Note:** A complementary abstract of the Global Location Guide Book of Numbers Research, "Optimizing Decisions on Business Services Locations," is available with registration at: [www.thehackettgroup.com/research/2015/sourcing-guide/](http://www.thehackettgroup.com/research/2015/sourcing-guide/).

### THE CONTROLLER'S CALENDAR

IOFM's *Controller's Conference & Expo*, September 9-11, The Westin O'Hare, Chicago, IL. For more information go to [www.iofm.com/controllers-conference](http://www.iofm.com/controllers-conference).

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