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TALES FROM THE GREEN EYESHAD
Financial Insights into the Surety & Fidelity Claims Handling

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I. YOU MIGHT BE A FRAUD VICTIM IF, ... (With apologies to comedian Jeff Foxworthy, author of "You Might be a Red Neck if,...")

- A. The salesman in the music store offers to sell you stock in the music store. (Tampa Tribune, March 25, 1998.)
- B. Your bookkeeper has not taken a vacation in 15 years.
- C. You do not destroy old or voided checks which contain account information.
- D. You do not destroy your credit card statements or old credit cards.
- E. Your bookkeeper arrives in a new Cadillac Seville.

II. Y2K? THE NEXT MILLENNIUM

- F. What is it?
 - 1. The "Year 2000" Problem, referred to by its shorthand name, Y2K, is a situation caused by the designers of early software. To save space in computer files when computer memory was expensive (remember when a super PC had 640k of ram and two, yes, two 5.25" floppy drives?), the data field that contained the year was limited to two digits. For example, 1984 was referred to as 84. Their rationale was that by the time the year 2000 arrived, this software will be obsolete and no longer in use.
 - 2. Well, guess what? That software designed in the seventies and early eighties, has been upgraded, enhanced, enlarged and improved, but not fixed. Even the latest versions of the two most popular spreadsheets, which can handle dates beyond 12/31/99, if the year is entered with four digits, handle the two digit dates differently. If you do not know how each version of the software works, problems could arise.
- G. What does it affect?
 - 1. The Y2K problem will affect any software application programmed with a two digit year field rather than a four digit year field. This includes the obvious programs that you use on your PC or mainframe computer, such as accounting software, spreadsheets, word processing and databases.
 - 2. The not so obvious applications include the programs that run the VCR, ATM machines, timers on locks such as bank vaults and any other date dependent

electronic equipment. Consider your normal day and make a mental list of the devices, programs, or other applications that rely on or report a date.

H. How can it be corrected?

1. The first step is a review of a business' software and hardware applications to determine the risk areas. This would include any internally developed spreadsheets.
2. Next, is a test of these applications to determine if they are Y2K compliant. Unless the software or hardware is relatively new, a good assumption is that it is not Y2K compliant. To avoid unnecessary expense, however, each existing application should be tested before it is replaced. Some farsighted developers made provision for this situation.
3. After a list of applications that need to be "fixed" has been made, it must be determined if an upgrade is available or if the program needs to be modified. This modification of programs can be very expensive because many older programs were written in COBOL, a computer language that is no longer popular. As such, software engineers experienced in using COBOL are not readily available, and those available are demanding premium fees. In addition, many of these older programs are not adequately documented, thereby requiring additional time to learn about the program before beginning the "fix."
4. Prudent managers should first determine Y2K compliance before any new software or hardware acquisitions
5. We can be comforted in the fact that December 31, 1999 falls on a Friday, so we'll have the entire weekend to work out a solution.

I. How does it affect the Surety?

1. Most contractors bonded by Surety companies have computerized accounting records. The obvious implication is that if their software is not Y2K compliant, then their accounting system will likely crash at the turn of the century (only 21 months away.)
2. If they are not able to process payroll, pay subcontractors and vendors timely, run management reports or track receivables, then they may become a client of the Surety's claims department. That is a client most Sureties do not need.
3. The Y2K compliance issue should be addressed now by the underwriting department rather than during the post mortem. Also the inquiries should be specific, tailored to the Principal's business and compliance should be verified by an independent party, rather than a generic questionnaire. One fill dirt supplier was a little miffed when he received a 12 page questionnaire asking for details on how his company has made his product Y2K compliant.

III. FRAUD INDICATORS IN CLAIMS HANDLING

- A. Aggressive billing practices of the Claimant.
- B. Claiming for materials, not specially manufactured, that were picked up at the Claimant's facility and not delivered to the Project site by the Claimant.
- C. Claimants documents are not "professional." For example, the invoices have a P. O. box, but do not have a corresponding street address, or the invoices do not have an address.
- D. Payroll reimbursement to Principal which has employees with no or only nominal withholding for one or more employees.
- E. Verbal Purchase Orders.

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Mr. Allen is a Certified Public Accountant licensed in the State of Florida. He is also a member of the American Institute of Certified Public Accountants and the Florida Institute of Certified Public Accountants, and is an associate member of the Association of Certified Fraud Examiners and the Construction Financial Management Association. He received his Bachelor of Arts, Cum Laude, with an accounting major, from the College of Business Administration at the University of South Florida in Tampa, FL.

Mr. Allen has a varied background in both the practice of public accounting and within the construction industry. He is a forensic consultant to the insurance industry in surety, fidelity, business interruption and lost income claims. He also has a public accounting practice. His public accounting experience includes auditor with in-charge responsibility for planning, supervision and review of assistant's work and preparation of financial statements on various audit engagements. Specific industries include for real estate developers, contractors, hotels/motels, colleges, and not-for-profit organizations, agricultural cooperatives and commercial enterprises. He also has prepared Federal and state income tax returns for corporations, partnerships and individuals.

Within the real estate and construction industry, Mr. Allen has been controller for various home building and land development companies within the Tampa Bay area. Responsibilities included full responsibility for financial statement preparation, construction lending coordination, financial planning, land acquisition feasibility studies, and internal audit of other home building divisions. In addition, he was responsible for supervising construction for single family homes, customer service and monitoring of land development expenditures in a large multi-use parcel of land zoned for single and multifamily homes and commercial uses. In addition, Mr. Allen was a shareholder in an architectural firm which designed major commercial and institutional buildings.