Ownership Costs versus Commercial Service Costs

The Scenario

A company, based in Stanford, Connecticut, provided printing services to the Department of Defense. The company was a small, family-owned business with a branch office in Pittsburgh, Pennsylvania. The president, an avid pilot, owned and operated a private airplane. The president would fly the plane between the two offices, instead of taking a commercial flight. The president charged 100 percent of the cost of ownership and operation of the airplane to the company’s indirect accounts.

The auditor decided to perform a cost benefit analysis to determine whether the plane’s depreciation, operational cost, and other related expenses did not exceed the normal cost of comparative commercial airline travel. The auditor requested supporting documentation for the private airplane such as total cost, depreciation schedule, a copy of the flight plan, and the business reasons for the trips. The flight log contained the date, route, destination, and length of each trip. The auditor determined the cost of owning the plane was reasonable when compared to commercial service. However, upon review of the flight log, the auditor discovered that in addition to traveling between the Connecticut and Pittsburgh offices, the president detoured to Las Vegas, California, and Canada. The company was unable to substantiate business reasons for trips to locations where the company did not have offices. The auditor determined that a significant percentage of airline costs were not related to official company business, and therefore were not allowable.

General Comments / Lessons Learned.

Although some fraud indicators may be obvious, many are very subtle, as illustrated in this scenario. Therefore, it is important that an auditor have knowledge of the industry, company, and applicable laws and regulations when performing their work. When private ownership of an asset is involved, an auditor should compare the cost associated with the ownership and use of the asset to the cost of leasing, renting, or using a commercial service. The auditor should use this information to determine whether the costs were reasonable and allowable.

FRAUD INDICATORS

- Small company using privately or company owned assets versus rentals, leases, or commercial services.

- Lack of adequate support or explanation for a privately owned asset used for company operations.