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Determining Actual Economic Loss Without a Forensic Accountant May Be a Gamble

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Annie Duke grew up in a highly competitive family, where family games around the dinner table were the glue that kept the family together. Being the youngest (her younger sister was too young to play) Annie spent a lot of time losing to her competitive parents and older brother. The experience frustrated the young girl who would often leave the table in a frustrated tantrum. But her experience would pay off.

Duke eventually attended Columbia University and majored in English and Psychology. After college, she decided not to follow in her parents' footsteps as teachers, and instead went on to the University of Pennsylvania where she worked on a doctorate in Cognitive Psychology. She eventually proposed marriage to her long time boyfriend and found herself playing poker to earn enough money to pay for their mortgage.

Duke had an uncanny ability to both read the players she was playing against, and weigh that against the possible outcomes of the cards sitting in front of her. She used that experience and talent to join the World

Series of Poker as one of the first female professional poker players, eventually beating some of the biggest poker legends in the world on her way to earning millions.

For many, poker is a game of luck, but Duke believes that her winnings at the poker table are a direct reflection of her experience and her ability to determine the most likely outcome based on what she sees.

While you'll never see a group of forensic accountants crowded around a table on ESPN, our work can draw a couple similarities to Duke and her poker-playing competitors when a case involves determining an insured's actual economic loss in a claim.

SURVEYING THE TABLE

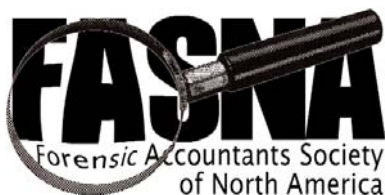
Every insurance claim involves calculating the actual economic loss to the insured. In some cases, this is as simple as determining what it will cost to repair an asset. In a lot of cases however, it's just not that simple. When we're called in to help determine actual loss, we're usually there to answer the question "what would have happened



Playing the Odds

Just like a professional poker player, forensic accountants face the challenge of figuring out the probability of each possible outcome based on limited information. However, while the poker player can only use the cues they gather from watching how their competitors play, an experienced forensic accountant can often uncover other information to help determine what most likely would have happened if a loss-causing event never occurred.

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CASEWORK EXPERIENCE

FASNA member casework includes, but is not limited to, cases involving:

- Inventory/property loss
- Employee dishonesty
- Business income loss
- Personal injury or wrongful death claims
- Truth in lending/truth in leasing
- Post judgement matters/ calculations
- Loss of income/earnings
- Divorce and fidelity claims
- Business valuation
- Expert testimony
- Fraud

INDUSTRY EXPERIENCE

FASNA member experience includes, but is not limited to cases involving:

- Auto dealerships and transportation
- Colleges and universities
- Construction, contracting, and engineering
- Financial/money management, trust, and estate
- Healthcare
- State and Indian tribal government
- Insurance claims
- Manufacturing
- Real estate
- Restaurant and hotel industries
- Retailing/wholesale

Determining Actual Economic Loss continued from cover



If you've ever watched a professional poker player, you'll notice that they often wear dark glasses and hats to prevent experienced competitors from gaining an advantage by reading their face. As forensic accountants, we too are trained to "read" people and look for clues that can often help determine if what someone is telling us is truthful.

if what happened didn't". Where do we start? Well, in poker terms, we start with a process that could be described as "surveying the table."

We start by taking a quick look at the broad landscape. What kind of business is the insured involved in? What's the industry like? What's the environment? Who are the managers and decision makers? What's the economy like? Inventory? Damage?

Next, we take a "business snapshot" of the insured as close to the loss-causing event as possible (whether that is a fire, storm, accident, or other loss-causing event resulting in a business income claim). Significant information can be gathered from this snapshot - and this information is extremely important in helping to determine actual economic loss.

For example, a company's inventory level just before the loss-causing event can provide hints about their current business status and plans for the future. A business with a higher than normal inventory level could mean slower than expected sales - or a ramp-up in preparation for higher expected sales in the near future. The insured's higher than normal cash position could indicate that they are preparing for an expansion - or could show that they are positioning themselves for a business slow-down. In both cases, gathering an early snapshot of the insured can be helpful when analyzed along with additional information later.

Finally, we gather additional information as needed to help support our calculations. This process can include everything from interviewing employees, vendors and

customers of the insured to looking at current financial documents to digging through detailed contracts and historical documents.

THE IMPORTANCE OF EXPERIENCE

Gathering information is only half the battle. Making sense of the information is where the experience and expertise of a good forensic accountant really pays off. By combining all of the information, we are able start putting together some of the most likely scenarios of what a company would have looked like if the loss event had never occurred.

Experience plays a huge role here because a lot of what we're really asked to do in cases of economic loss is to predict the future based on the past. What would sales have looked like if there wasn't a fire? What would the inventory have sold for if it could have been sold? What were the real intentions of management leading up to the loss occurrence? Is the loss recovery timetable reasonable? Was the business growing or slumping? Are there ways that the company could reduce the amount of the loss?

Like a battle-hardened poker player, an experienced forensic accountant can apply things we've seen in past cases that less experienced people might miss. Even things that may seem insignificant at the time - like accounting practices that the company may use for inventory or sales recording - can often have a significant impact in determining the actual economic loss.

And, when it comes to calculating the proper payout on a claim, is it really worth taking a big gamble?

NAVIGATING THE MAZE WITH *Experience*

Article provided by *Cremers, Holtzbauer & Nearmyer, P.C.*
FASNA Member

The Hampton Court Palace Hedge Maze covers a third of an acre of riverside gardens just outside of London along the Thames River. It is literally a walking maze created with walls of hedge-bushes. Its fame comes from the fact that it was originally planted in the late 1600s in honor of King William III, making it the oldest hedge maze in the world. As a popular tourist stop, the maze's half-mile of pathways befuddle inexperienced visitors. However, those who have been through the maze before know how to quickly navigate it and avoid the dead ends to find their way to the end point in the middle quickly.

So, what does this have to do with calculating actual economic loss? Well, in many cases, calculating business loss requires you to wander through endless piles of information, trying to sort useful information from dead ends. However, with experience, you learn tricks and insights that can give you a quicker, more direct route to the final destination. In a nutshell, experience pays.

For example, we have a lot of experience working with claims related to auto dealerships. Auto dealership claims can be much more complex than the average "main street" business. You have potentially huge inventory dollar values. Complicated looking factory formatted financial statements. Factory-financed expenses. Sales draws, commissions and bonuses based on performance and factory-to-dealer sales incentives.

And, on top of all that, you have subjective trends, consumer brand preferences, market and seasonal timing and factory rebate programs that can play a big role.

Knowing Where to Start

Gathering information is never a problem with auto dealership losses. The problem is that you can easily get overwhelmed with more information than you'll ever need. Auto manufacturers and financing companies have sophisticated business management software and systems that feed you more reports with more detail than you could ever possibly need.

Knowing what information is available and where to find it is the most important part of handling a loss for an auto dealership. Having handled dozens of these types of losses, it's easy for us to know exactly where to find the information we need -and how to quickly sort it out from everything else. This experience alone can often pay huge dividends in calculating claim losses.

Digging Into Data

If finding information is the easy part, determining how to use the information is the hard part. Did the damage to the dealership require a total shut down - or were some operations able to remain

By analyzing sales trends, we can often identify outside factors, like changes in consumer tastes that could affect a business' insurance claim.

open? If the showroom and new car lot were closed, but the service center was able to remain open because it was housed separately, that business income was still available to the dealership - thus, possibly not part of the loss.

Salespeople at dealerships are often compensated on draws/commissions -with bonuses paid at month-end based on sales performance. Depending on the exact compensation structure, compensation for these workers could be considered a direct or indirect cost due to the loss - and could be treated differently under a loss based on the exact structure.

Determining when a dealership actually incurred an expense is important. Even short suspensions in business for an auto dealership can lead to large business loss claims. However, policy limits on business income and monthly limits on indemnity can be lower than the claimed losses. Sometimes, that can result in "shifted expenses" where an unscrupulous dealer may try to show expenses that did not actually occur during the period of coverage.

Determining Actual Loss

Even after you've been able to sort through the data and determine the potential loss, there are other subjective factors that can still weigh heavily on a loss involving an auto dealership.

Competitive forces can quickly change sales forecasts. A manufacturer that promotes a low-interest financing plan can draw customers away from a competing dealership. The time of the year also affects auto sales at dealerships - as activity can ebb and flow as new models are released.

Trends in consumer taste can also have a big impact. A year ago, when gas prices were a dollar higher than they are today, gas-guzzling SUVs were difficult to sell, while new, flexible-fuel hybrids were gaining momentum. Dealers who maintained a high-inventory of SUVs were likely not selling at the same rate they were the year earlier. By analyzing sales trends, we can often identify outside factors that could affect an auto dealer's insurance claim.

Experience Matters

Think that's complicated? Now imagine working with a manufacturing company loss. They often face even more complex issues - like calculating the proper amount of manufacturing overhead absorbed into the cost of the products manufactured. If you're not working with someone who has experience with those kinds of analysis, you're entering a whole new maze.

With decades of experience, FASNA members can make it easier to help you determine the actual economic loss in a business loss. In fact, because we've handled losses ranging from hurricane damage to fraud investigations and fires to damages caused by blizzards, you'd have a hard time finding forensic accountants with more experience than FASNA members.

Give us a shot at your next challenge.

An experienced forensic accounting firm will have broad experience working with a variety of different kinds of niche companies. That experience can be invaluable in determining actual economic loss in a complex business insurance claim.

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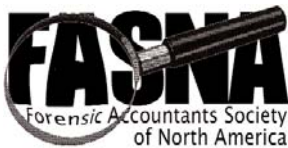
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