

Forensic Accountants Society of North America

# FASNA FORUM

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## The Burning Question

By Kevin S. Terry, C.P.A., Mellen, Smith & Pivoz, CPAs, PLC,  
FASNA Member Firm

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A view of the aftermath of the fire was devastating. The inside of the dealership was rubble and melted plastic equipment. However, it could have been worse. The new car sales area was destroyed, but because of the firewalls, the parts and service departments were left intact with minimal damage.

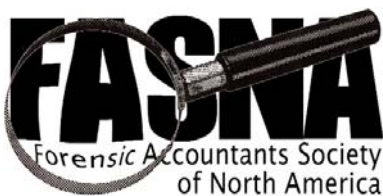
The owners of the dealership moved quickly to bring temporary trailers on site to house the sales operations, and the parts and service departments continued to function. A business interruption claim was filed and we were asked to review it.

Fortunately, this is not an everyday occurrence, but this is the type of claim that FASNA members review for insurance adjusters. There were some interesting aspects to the claim. First, the tragedy of September 11, 2001 occurred during the restoration

period of this claim. As you will recall, in the days immediately following 9/11, economic activity in this country slowed to a snail's pace. As for the automobile industry, within two weeks the US automobile manufacturers responded to this slow down with a series of "zero down, zero percent interest" programs. This gave the automobile industry an incredible shot in the sales arm. Our project was to review the sales (income) forecast of the dealership in light of the successive tragedy-spark in their business. Our ultimate objective was to help determine the loss that the dealership suffered as a result of the fire, as opposed to the loss that was a result of the economic downturn due to 9/11.

There is an amazing wealth of statistical information available for the automobile industry. We can obtain sales information by brand for the entire country or specific

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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
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- Healthcare
- State and Indian tribal government
- Insurance claims
- Manufacturing
- Real estate
- Restaurant and hotel industries
- Retailing/wholesale

## *The Burning Question continued from cover*

regions within the country. This information is updated regularly and is available for both new and used vehicles. Although the information is not as thorough for the parts and service departments, there is still a lot of comparative information available.

Accessing the information, applying that knowledge to the facts surrounding the claimant, and reporting to the insurance company on a monthly basis alone provided for an interesting claim.

For projection purposes, the dealership provided us with information related to sales and profits in the twelve-month period preceding the fire. At that point, we discovered some significant items in the historical information. In the summer before the fire, there had been a work stoppage that lasted approximately six weeks. This stoppage had a significant impact on the business operations of the service department. Revenue for this department was extremely low for the months that included this work stoppage. An adjustment had to be made to the numbers related to the historical activity of the service department to recognize lost revenue as opposed to delayed revenue. Once these adjustments were made, the information could then be used to project the loss for this department during the restoration period.

A second significant item that was discovered in the historical information was that the dealership was valuing its inventory at the lower cost or market (as we would expect). However, it was determining its cost using the "last in, first out" method. This methodology is perfectly acceptable under both gener-

ally accepted accounting principles as well as for tax purposes. Nevertheless, it has the potential of distorting results in the automobile industry when a particular vehicle is eliminated. This is exactly what happened in this fire loss claim.

During the year that ended immediately prior to the fire, certain models were eliminated by the manufacturer. At the year-end, the dealership adjusted its inventory, in accordance with its selected methodology, to reflect the elimination of the models no longer in production. Without going into an inventory accounting lesson, the result was a large increase in profit for the year. Since the dealership had given us its information on a monthly basis, the profit for the month of December of that year was extraordinary. In our analysis, we normalized the profit for the month so that it would not distort the lost income for the claim.

As mentioned earlier, we provided the insurance company with a calculation of the business interruption loss on a monthly basis during the restoration period. We met with the insured on more than one occasion during the process to review the calculations with him. While his public adjuster did not make the adjustments we made in calculating the loss for the dealership, the insured and the insurance company appreciated our willingness to review and explain our calculations with them. Although the insured and the insurance company had significant issues between them, they were both happy to have had an independent party help resolve the matter of business interruption.



# One Proud Papa

By Michael A. Pivoz, CPA, JD, Mellen, Smith & Pivoz, CPAs, PLC, FASNA Member Firm



Those of you that are parents likely remember a time when your rebellious kids actually listened to what you said and did as you suggested. Well, I had one of those proud parent moments recently. However, it was not with my kids, rather it was a defense attorney.

I have been preaching for a number of years to anyone in the business of claims and damages, that it is not enough to fight liability issues; you

must also fight damage claims. My mantra has been that if you only fight liability issues and you lose, the jury or the judge has only heard the claimant's version of damages and therefore, when an award is calculated, they are left with no alternative other than accepting that version. As a result of this, we are still seeing headlines that scream at us about huge awards that may not have been justified given the factual circumstances of the claim. Sometimes a judge will recognize this and adjust the award accordingly. More often, however, this is not the case.

There has been a lot of talk about Federal Tort Reform that would, in part, limit damages that can be awarded. This still will not eliminate the need for the damage expert. In Michigan, we have had tort reform in place for several years. Among other things, Michigan's tort reform has placed caps on the amount of non-economic damages that can be awarded in certain circumstances. For non-economic damages outside of those circumstances and for economic damages, the result of not presenting a damage expert remains the same. One-sided

evidence leads to a one sided result.

All of my preaching should not be misconstrued as a suggestion that the claimant's damage expert never presents a fair calculation. I am sure that it happens often. However, since the calculation of damages is more art than science, what is "fair" may be a dollar amount in a very wide range. It should come as no surprise that claimants' "fair" value of damage would most likely fall in the upper end of the "fair" range. More importantly, without your own damage expert, how do you know that the calculation is "fair"?

Now that I have convinced you to engage a defense side damage expert, where do you find one? Although many attorneys like to use economists, I think that a better option is to use a forensic accountant. A forensic accountant combines investigative skill learned in auditing with practical business skills developed in the every day accounting practice. Some of us even have an economics background. I have been told by several attorneys that they prefer the testimony of a forensic accountant. In their view, juries are more likely to accept the testimony of a forensic accountant as compared to an economist. Ultimately, isn't this what you are looking for in your damage expert?

What was my recent proud papa moment? About a week ago, I received a call from an attorney that I knew, but had never performed litigation services for. He asked me if I would serve as his expert in a wrongful death action he was defending. My pulse raced, my hands began to sweat, and of course, I agreed.

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