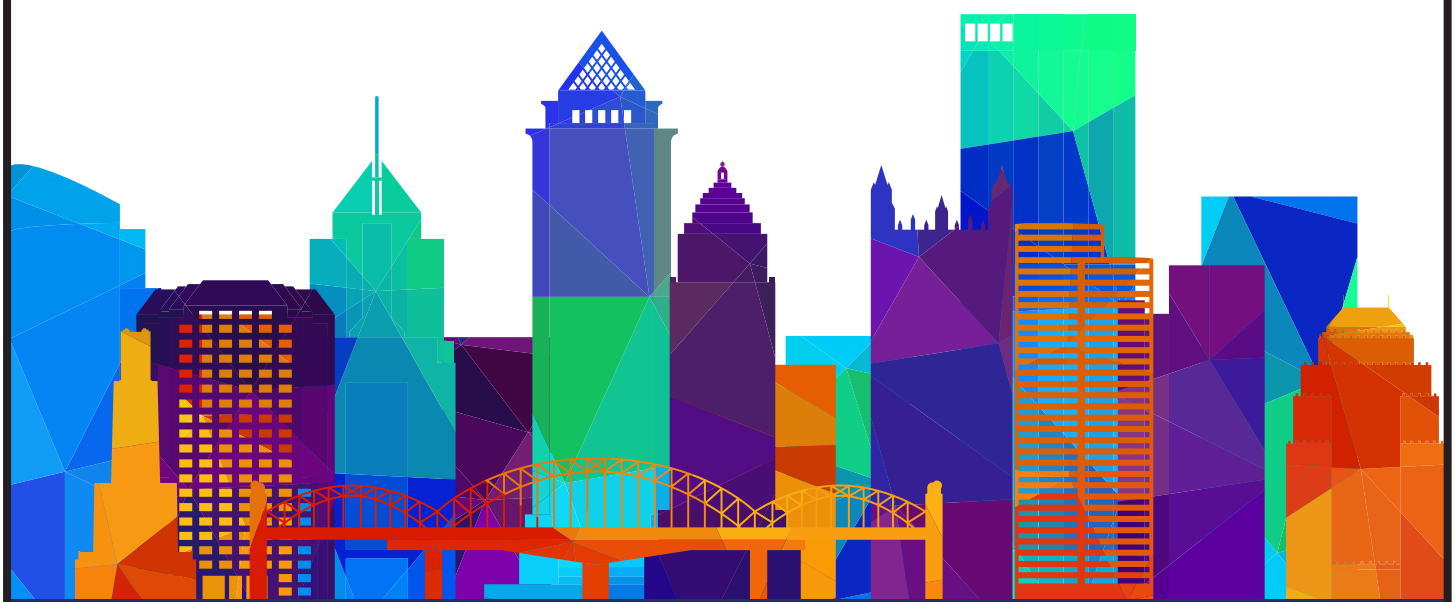
The Effective Use of Financial Experts: When and How to Utilize Them in Your Case

presented by the GYF Business Valuation & Litigation Support Services Group

Grossman Yanak & Ford LLP
Certified Public Accountants and Consultants



Grossman Yanak & Ford LLP

Headquartered in Pittsburgh, Grossman Yanak & Ford LLP is a regional certified public accounting and consulting firm that provides assurance and advisory, tax planning and compliance, business valuation, ERP solutions and consulting services. Led by six partners, the firm employs approximately 70 personnel who serve corporate and not-for-profit entities.

Our firm was founded in 1990 on the idea that the key to successful, proactive business assistance is a commitment to a high level of service. The partners at Grossman Yanak & Ford LLP believe that quality service is driven by considerable involvement of seasoned professionals on a continuing basis. Today's complex and dynamic business environment requires that each client receive the services of a skilled professional with a broad range of experience and knowledge who can be called upon to provide efficient, effective assistance.

Grossman Yanak & Ford LLP combines a diversity of technical skills with extensive "hands-on" experience to address varied and complex issues for clients on a daily basis. We pride ourselves on bringing value-added resolution to these issues in a progressive and innovative manner. Our ability to produce contemporary, creative solutions is rooted in a very basic and ageless business premise – quality service drives quality results. Our focus on the business basics of quality technical service, responsiveness and reasonable pricing has enabled the firm to develop a portfolio of corporate clients, as well as sophisticated individuals and nonprofit enterprises.

Our professionals understand the importance of quality and commitment. Currently, the majority of the professional staff in our Assurance & Advisory Services and Tax Services Groups hold the Certified Public Accountant designation or have passed the examination and need to complete the time requirements for certification. Each of our peer reviews has resulted in the highest-level report possible, attesting to the very high quality of our firm's quality control function. The collective effort of our professionals has resulted in our firm earning an exemplary reputation in the business community.

Grossman Yanak & Ford LLP…Quality You Deserve!

401 Liberty Avenue • Three Gateway Center, Suite 1800 • Pittsburgh, PA 15222
Phone: 412-338-9300 • Fax: 412-338-9305 • www.GYF.com

GROSSMAN YANAK & FORD LLP
Certified Public Accountants and Consultants

GYF CLE Course Offerings

The following courses have been presented by our professionals:

- *The Business Valuation Process*
- *Understanding Standards of Value and Levels of Value*
- *Income Approach to Business Valuation*
- *Market Approach to Business Valuation*
- *Cost/Asset Approach to Business Valuation*
- *Quantification and Application of Valuation Discounts*
- *S Corporations vs. C Corporations: Understanding Valuation Differences*
- *Special Purpose Valuations: ESOPs & Buy/Sell Agreements*
- *Special Purpose Valuations: Estate & Gift Tax Planning*
- *Economic Damages: Lost Profits Determinations*
- *Attorney's Guide to Financial Statements*
- *Marcellus Shale: Income Tax & Valuation Issues Related to Landowners*
- *Family Limited Partnerships: Realities of Estate Planning with FLPs*
- *Business Entity Selection & Structuring Transactions*
- *Fraud & Forensic Accounting*
- *Navigating the New Tax Laws: Recent Changes & 2013 Planning*
- *Intangible Assets: Identification, Valuation and Controversial Issues*
- *Understanding ESOPs and Their Use In Exit Planning*
- *Advising Individual Tax Clients for 2013 and Beyond*
- *Analyzing Financial Statements and Their Impact on Value*
- *Exit Planning: Considerations and Steps for Exiting a Business*
- *Planning in a Changing Tax Environment*
- *Law Firm Economics*
- *Corporate Divorce*
- *The Ins and Outs of Non-Cash Compensation*
- *International Taxation*
- *Thorny Issues with Applying the Income Approach in a Legal Setting*
- *Tax Reform or Tax Calamity? – A Closer Look at the Tax Cuts & Jobs Act*
- *Privately-Held Business Valuation in the Wake of the Tax Cuts & Jobs Act*
- *Economic and Legal Considerations in Equity Owner/Shareholder Oppression*

Materials from these presentations can be downloaded at https://gyf.com/resources/documents/

Robert J. Grossman, CPA/ABV, ASA, CVA, CBA

Bob heads our firm's Tax and Business Valuation Groups. He has nearly 40 years of experience in tax and valuation matters that affect businesses, both public and private, as well as the stakeholders and owners of these businesses. The breadth of his involvement encompasses the development and implementation of innovative business and financial strategies designed to minimize taxation and maximize owner wealth. As his career has progressed, Bob has risen to a level of national prominence in the business valuation arena.

His expertise in business valuation is well known, and Bob is a frequent speaker, regionally and nationally, on tax and valuation matters. Bob is a course developer and national instructor for both the American Institute of Certified Public Accountants (AICPA) and the National Association of Certified Valuators and Analysts (NACVA). He has served as an adjunct professor for Duquesne University and Saint Vincent College. He has also written articles for several area business publications and professional trade journals.

After graduating from Saint Vincent College in 1979 with Highest Honors in Accounting, Bob earned a Masters of Science degree in Taxation with Honors from Robert Morris University. He is a CPA in Pennsylvania and Ohio and is accredited in Business Valuation by the AICPA. Bob also carries the well-recognized credentials of Accredited Senior Appraiser, Certified Valuation Analyst and Certified Business Appraiser.

A member of the American and Pennsylvania Institutes of Certified Public Accountants (PICPA), Bob has previously chaired the PICPA Pittsburgh Committee on Taxation. He has also served as Chair of the Executive Advisory Board of NACVA, its highest Board; as well as Chair of NACVA's Professional Standards Committee and its Education Board.

Bob received NACVA's "Thomas R. Porter Lifetime Achievement Award" for 2013. The award is presented annually to one of the organization's 6,500 members, who has demonstrated exemplary character, leadership and professional achievements to NACVA and the business valuation profession, over an extended period.

Bob is a member of the Allegheny Tax Society, the Estate Planning Council of Pittsburgh and the American Society of Appraisers. He has held numerous offices in various not-for-profit organizations. Bob received the PICPA Distinguished Public Service Award and a Distinguished Alumnus Award from Saint Vincent College.

Bob and his wife, Susie, live in Westmoreland County. They have two grown children.

Melissa A. Bizyak, CPA/ABV/CFF, CVA

Melissa, a partner in the firm's Business Valuation & Litigation Support Services Group, has practiced in public accounting for more than 21 years. She has significant experience addressing business valuation and tax-related issues for privately-held concerns and their owners.

Her business valuation experience is diverse, including valuations of companies in the manufacturing, oil and gas and technology industries. These valuations have been performed for various purposes such as financial reporting, equitable distributions, buy/sell transactions, dissenting shareholder disputes, Employee Stock Ownership Plans (ESOPs), value enhancement and gift and estate tax purposes. Melissa also provides litigation support services, including expert witness testimony.

After graduating from the University of Pittsburgh in 1994 with a B.S. in Business/Accounting, Melissa spent two years with a local accounting firm in Pittsburgh. She joined Grossman Yanak & Ford LLP in 1997.

Melissa is a certified public accountant and is accredited in business valuation and certified in financial forensics by the American Institute of Certified Public Accountants (AICPA). She has also earned the AICPA Certificate of Achievement in business valuation. Additionally, Melissa carries the credential of Certified Valuation Analyst, conferred by the National Association of Certified Valuators and Analysts (NACVA).

Her professional affiliations include the AICPA, the Pennsylvania Institute of Certified Public Accountants (PICPA) and the Estate Planning Council of Pittsburgh. She is a member and previously served as the Chair of NACVA's Executive Advisory Board. Melissa has written business valuation course-related materials and serves as a national instructor for NACVA. She has also authored articles appearing in professional publications.

Melissa is a graduate of Leadership Pittsburgh, Inc.'s Leadership Development Initiative. She serves on the Board of Directors of the Children's Museum of Pittsburgh and is a member of the Executive Leadership Team for the American Heart Association's "Go Red for Women" initiative. Melissa is also a mentor for women business owners through Chatham University's MyBoard program. She was one of four female CPAs in the State of Pennsylvania to be honored in the PICPA's "Women to Watch" awards in 2017.

Melissa resides in the South Hills of Pittsburgh with her husband and their two sons.

GROSSMAN YANAK & FORD LLP
Certified Public Accountants and Consultants

Brad W. Matthews, CPA/ABV, CVA

Brad has focused his career on providing valuation and litigation support services since joining Grossman Yanak & Ford LLP in 2011. His experience includes financial statement and historical financial trend analysis, financial modeling, and business risk assessment, as well as performing calculations required for the preparation of business valuations and other consulting projects.

Brad has served clients in many industries including manufacturing, professional services, financial services, engineering, construction, retail, management consulting, oil and gas, and technology. He has played a significant role in providing business valuation services for a range of purposes including gift and estate tax planning, Employee Stock Ownership Plans (ESOPs), marital dissolutions, corporate divorce/shareholder disputes, financial and tax reporting, buy/sell transactions, and general business planning. Further, his litigation support experience includes the determination of lost profits and economic damages arising from various disputes.

Brad graduated from the University of Pittsburgh, earning a double major in Accounting and Finance with a minor in Economics. Brad is a graduate of Class XXIV of Leadership Pittsburgh Inc.'s Leadership Development Initiative (LDI) program that hones the leadership skills of high-potential young professionals.

He is a certified public accountant (CPA) and has earned the Certified Valuation Analyst (CVA) designation conferred by the National Association of Certified Valuators and Analysts (NACVA).

In his spare time, Brad enjoys golfing, following Pittsburgh sports and spending time outside with his family. He lives in the North Hills with his wife, Alexis.

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

CHAPTER I – INTRODUCTION

The practice of law, as each of today's participants well know, is by its very nature, a complex and challenging undertaking. The sheer breadth of the practice of law forces specialization and focused attention on specific areas of law, and only over time is practitioner expertise fully attained. However, as with all professions, the body of knowledge is constantly evolving, leading to a constant process of learning and relearning, making the ability to stay current a further challenge.

Perhaps the most challenging aspect of law, however, is the successful integration of the knowledge and expertise of parties from "non-law" disciplines into the representation of clients in a legal setting. The need to integrate the opinions of outside experts into the legal matters posed by clients often requires a steep learning curve for attorneys unfamiliar with the particular nuances of the profession and expertise which the expert brings to bear.

Most efforts undertaken in conjunction with legal matters center on evidentiary considerations. While the sources of such evidence are too broad to address in this brief program, there are four traditional types of evidence – real, demonstrative, documentary and testimonial. Rules of evidence, both state and federal (depending on the venue in which the matter will be filed), govern its admissibility.

Federal Rules of Evidence set the basic prerequisites of admissibility as relevance, materiality and competence. Under these rules, if evidence is found to be relevant, material and competent, and it is not barred by an exclusionary rule, the evidence will be found to be admissible.

Despite the steep learning curve and challenges of integrating the opinions of experts, it is a matter of necessity and a process which cannot be avoided. In the Notes of Advisory Committee on Proposed Rules, under Rule 702*, Testimony by Expert Witnesses*[1], it is noted, "An intelligent evaluation of facts is often difficult or impossible without the application of some scientific, technical, or other specialized knowledge. The most common source of this knowledge is expert witnesses, although there are other techniques for supplying it."

The use of an expert can bring substantial weight to the matters before the court in any legal proceeding, whether it be scientific, technical or specialized knowledge. It is also important to note that these same experts can provide assistance in a variety of other roles, including a "non-testifying" consulting expert role in a matter entered in court.

[1] Federal Rules of Evidence, Rule 702.*Testimony by Expert Witnesses* (Pub. L. 93-595, Jan. 2, 1975, 88 Stat. 1937; Apr. 17, 2000, eff. Dec. 1, 2000; Apr. 26, 2011, eff. Dec. 1, 2011.)

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

Today's program will focus on the successful use of financial experts. The authors and speakers today often play a role in matters of dispute requiring a potential appearance in court to express an opinion. In fact, that involvement is how we are most often utilized in cases handled by our clients. We have also been engaged as consulting experts, where our role is one of working as advisors to legal counsel in their roles as advocates for their clients.

As will be discussed later in these materials, the scope of services offered as consulting experts is broad and can include any and all financial services necessary to assist counsel with building their case. The key difference between the two roles, which will also be discussed in more detail in these materials, is the "objectivity and independence" requirement associated with a testifying expert witness engagement versus the "advocacy" role intended in a consulting engagement.

In addition to matters before the court, financial experts can play a significant role in assisting legal counsel in a variety of transactional matters and dispute resolution. These non-court services include:

- Transaction assistance for corporate attorneys facilitating the purchase or sale of a business
- Valuation and economic services related to disputes regarding buyouts of departing shareholder and equity owner departures
- Valuation for purposes of adding shareholders and equity owners
- Assistance in the determination of value and economic structures for shareholder exit planning, including employee stock ownership plans (ESOPs)
- Assistance with international transactions requiring determination of appropriate royalty and licensing rates for intangible asset transfers and intercompany transfer pricing applications
- Assistance with development of value-based compensatory payment mechanisms under the Internal Revenue Code and valuation and economic matters related to tax authority disputes and challenges

Though each project is subject to the sensitivities of its own facts and circumstances, each of these services will be addressed further in these materials to give participants a better understanding of the types of services available in conjunction with your representation of your clients.

The effective use of financial experts in any matter with legal implications (which, indeed, is almost every matter), is predicated upon a process that requires several steps, including:

- Identification of the financial and economic issue(s) that oblige the expert to opine
- A search for the most appropriate financial expert (given facts and circumstances of the case)

- Working with the financial/economic expert prior to engagement to discern those general procedures that might be possible, given available time and case status (where does discovery stand, for example)
- Determining the expectations of those issues that counsel would look to have addressed in the course of the assignment

In conjunction with communicating the issues that counsel would look to have addressed in the course of the assignment, it is important that he or she realize that such direction is generally welcome, but not controlling, in the event of the provision of objective and independent expert services. There is no room, whatsoever, for legal counsel influence on the opinions of the expert if he or she is being requested to testify in court.

Once the expert is engaged, the process of managing the engagement for which he or she was hired should take front and center. The best results stem from an organized process and regular communication with legal counsel. In addition, it is imperative that discovery be as comprehensive as possible, as the credibility of any financial expert will be evaluated based upon the expert's interpretation of the factual information at the core of the matter. The most difficult aspect in the provision of expert financial and economic services is the limitation imposed by incomplete documentation and financial information. Avoiding this shortcoming requires great experience and deftness in the construction of document requests for use in discovery.

The most difficult element that the authors encounter in these types of engagements is the lack of adequate time to facilitate the best possible outcome. To be sure, the authors would not agree to an assignment without at least minimum adequate time in which the work can be conducted in accordance with our professional standards. However, providing ample time allows for the opportunity to offer more in-depth assessments of case strategy as it is being developed as well as to provide time for both counsel and the expert to fully digest the outcomes of the work being undertaken and the findings as they are developed.

Ensuring that counsel undertakes the identification, selection and utilization of his or her financial expert through a timely and careful process that allows for management of the expert's work without compromising his or her objectivity and independence will lead to the best results for both legal counsel and his or her client.

Today's program is intended to outline that process and help participants better understand how the use of the right financial expert, when deemed appropriate, can lead to a better transaction or case outcome with the optimum financial impact.

To that end, the program has been separated into the following chapters:

I. Introduction
II. Identification of Financial and Economic Elements of the Matter
III. Understanding the Role of Financial/Economic Experts
IV. Identification and Selection of the Financial and/or Economic Expert
V. Engagement Protocols and Management
VI. Preparation for Depositions and Trial/Expert Testimony
VII. Case Illustrations
VIII. Concluding Remarks

We greatly appreciate the opportunity to have you as our guest today. We understand that your time is very precious and we are honored that you would spend part of your day with us. It is the hope of the authors and presenters that you will gain some new knowledge and are better prepared to serve your clients.

Have a great day!

CHAPTER II – IDENTIFICATION OF FINANCIAL AND ECONOMIC ELEMENTS IN THE MATTER

In today's increasingly complex business environment, it is crucial for financial expert professionals to be able to perform sophisticated financial analyses and communicate their findings clearly to a largely nonfinancial audience. The American Bar Association best expresses the role of an expert:

> *"A financial expert's main role is to educate, by helping the attorney and the court, to understand the financial aspects of a case during evidence gathering, trial preparations, possible mediation and in court at trial. Therefore, the expert's ability not only to understand the issues but also to communicate them clearly and in understandable language is paramount."*[2]

Qualified financial experts can assist legal counsel in a wide range of financial and economic assessments, including those attendant to potential litigation and in matters unrelated to litigation. These types of assistance include, but are not limited to the following:

- Business valuation
- Damages assessments including lost profits
- Fraud and forensic investigation
- Marital dissolutions - assembling and valuing certain marital assets and liabilities
- Personal injury awards
- Evaluation of operations
- Transaction analysis
- Loan compliance and covenant testing
- Business viability and business plan feasibility

The aforementioned work can be undertaken by accountants, fraud examiners, tax professionals, turnaround experts, asset appraisers (real estate and equipment), business valuators and consultants (typically industry specific). Additionally, the authors have observed on occasion, in a legal setting, members of academia (professors of economics and finance) may be involved. Determining the relevance and what type of expert is required depends on the questions or issues involved in the case. As will be noted throughout this material, there can be one or more financial experts engaged to assist legal counsel. The following summaries are areas in which a financial expert may aid legal counsel.

[2] Bart, D. *Successful Use of Financial Experts*. American Bar Association. October 31, 2018. https://www.americanbar.org/groups/litigation/committees/expert-witnesses/articles/2018/fall2018-successful-use-of-financial-experts/

Business Valuation

Most often at the heart of many transactions or disputes is the value of a privately held business or interest therein. Valuation experts are engaged to answer the question – what is the business or particular equity interest worth? It is of primary importance for members of the legal community to have an understanding of the role a business valuator can assume in a given project. Business valuation experts can perform many functions including the following:

Advising legal counsel or a client on a business valuation independent of a controversy related to the subject valuation.

These valuations can be prepared in the context of sales, mergers, acquisitions, spin-offs, incentive stock options, corporate and individual income tax planning, as well as estate and gift tax planning and financial restructuring. The majority of business valuations are performed for clients in everyday business transactions that do not become the subject of controversy. One reason that some transactions do not lead to controversy is that the event is supported by a qualified (and credentialed) valuator who provides a well-reasoned (and documented) report.

Providing an opinion of value that will be used before the Internal Revenue Service in an examination or an appeal at the Appellate Division.

A different type of civil controversy, appraisers are often called upon at the examination stage to provide an explanation of the valuation determinations included on previously-filed gift tax and estate tax returns. Most controversies relating to valuation of assets, including equity interests, are resolved at this level based on the taxpayer providing adequate support for the transaction. Most often, the support is encapsulated in a "qualified" appraisal prepared by a qualified appraiser.

Assisting legal counsel out of court in understanding technical issues and preparing for a case that may lead to potential litigation.

This role would entail educating legal counsel regarding various valuation approaches and/or methods and providing counsel with adequate understanding of the issues and the tools to be more effective in developing forward-looking case strategy and how best to facilitate resolution to the best interest of the client. Such services and assistance often include assistance with legal proceeding preparation, including preparation of challenges to opposing testifying expert's reports, opinions, and if helpful, the preparation of deposition and/or cross examination questions. This "consultative" expert role will be discussed in greater detail in the following chapter.

Testifying in court relative to an opinion that will be included in a trial record.

Business valuators, including the authors, are often called upon to testify as experts on valuation matters. For some practitioners, serving as an expert witnesses is a major part of their practice. In almost every case where a business appraiser is called upon to testify as an expert witness, the appraiser is being asked to offer an opinion of value – usually the value of some type of business interest or intangible asset. The role of "testifying expert" will be discussed in greater detail in the next chapter of these materials.

Each aforementioned tasks requires slightly different and nuanced skills from the valuation expert. Therefore, it is of the utmost importance that the expert should be selected based upon the "purpose" for which the services are required, as well as the "specific skills and knowledge" of the professional.

Integral to every business valuation conclusion or opinion is the purpose for which the value is being produced. Oftentimes, nuances to the business valuation process are predicated upon the purpose for the valuation and failure by the valuator to consider these nuances can have a profound effect on the conclusion. It is, without exception, critical to the value conclusion that the purpose be matched with the appropriate procedures to produce a correct result.

The question of purpose is always one of facts and circumstances. Generally, legal counsel provides the valuator with his or her perceived purpose, which then serves as the basis for the valuator's selected procedures, methodologies, etc. Once legal counsel provides the purpose, the specific valuation mechanics associated with completing the engagement to meet that specific purpose should be discussed. This discussion ensures that there are no misunderstandings of the meaning of the conclusion or opinion of value produced by the expert.

A sample of just a few of those purposes for which business valuations may be prepared include:

- Estate and gift tax planning and compliance
- Employee Stock Ownership Plan (ESOP) stock purchases
- Marital dissolution/equitable distribution proceedings
- Minority shareholder disputes
- Buy/sell agreement trigging events
- S corporation built-in gain computations
- Transactional litigation
- Bankruptcy
- M&A activity – purchase/sale of a business

Note that purpose, especially in the context of financial or economic matters with a potential to expand into a litigation setting, often requires tweaking after conversations between attorney and valuator due to the availability and quality of appropriate records, selected dates of valuation and the acceptability and credibility of certain procedures, approaches, methodologies and calculations within any jurisdiction.

Further, within these varied "purposes" for obtaining a business valuation, it is necessary for the valuator to consider a number of technical items that might influence both the work and the conclusion of value, including:

- What is the appropriate standard of value?
- Is the premise of value a going concern premise or, alternatively, liquidation?
- Is it appropriate or permissible to apply discounts for lack of control and/or lack of marketability?

By way of example, assume that the purpose of engaging an expert is to provide legal counsel with an opinion of value of a fractional interest in an operating company in connection with a shareholder oppression suit. Here the standard of value pursuant to statutory requirements is fair value. Unlike fair market value, fair value generally does not include application of valuation discounts.

In addition to carefully defining the purpose of the valuation, legal counsel must also determine the date of valuation. Value is a "point in time" assessment, and it is important to understand that the date of valuation, or the "as of" date, is a single date. Thus, the determination of that date is critical to the usefulness of any business valuation.

Excepting practice in litigation or family law, identifying the date of valuation is generally a rather matter-of-fact issue. There are however, additional considerations in selecting the most appropriate date of valuation. Often these are predicated upon practical matters such as the availability and quality of financial information from which the valuator can apply their procedures.

An example of this type of consideration may be the circumstance where a date of valuation of October 20th is desirable as the exact date of the action at the center of the controversy. However, this date may not be absolute in that there may be quarterly financial information deemed to be more readily available and of a much higher quality as of September 30th than the later date. Generally accepted business valuation procedures allow for estimating value changes over the intervening 20 days in this example, but suffice to say that they are broadly based and far from absolute. In cases such as these, so long as both sides stipulate, and no major events have occurred in the intervening days, the earlier quarter end date would most often be selected.

Note that the date of valuation should not be confused with the date of the report, which generally coincides with that date on which the field work on the engagement was completed.

Again, it is NOT the responsibility of the business valuator to set the date of valuation. As discussed above, most business valuators will be open to discussing the date of valuation and providing professional insight. However, at the end of the day, legal counsel must provide that date for which he/she wishes to obtain a conclusion or opinion of value.

As can be observed, it is critical for legal counsel to be knowledgeable of the specialized skills necessary for an appraiser or valuator to complete specific engagements. Financial experts in this area should be credentialed in business valuation, and therefore, the expert's work product should be prepared in accordance with professional standards.

Damages/Lost Profits/Business Interruption

Financial and economic experts have a specific role in cases involving damages. Damages can be caused by a variety of means, including breach of contract, intellectual property infringement, a natural or man-made disaster, or any event that causes a real or perceived negative impact on value. In these matters, it is important that the expert evaluates whether the damage analysis is linked to the wrongful event(s) in question and properly analyze the economic damages. If the financial expert cannot explain how damages flow from the cause of action, the expert's opinion may be discredited and add the risk of exclusion in court

In the context of seeking compensatory damages for lost profits, a plaintiff must demonstrate the following key elements to enable a recovery of lost profits:

- That the lost profits were directly caused by opposing parties' wrongful actions,
- The lost profits were a foreseeable consequence of the defendant's wrongful conduct, and
- The lost profits can be determined and proven with reasonable certainty.

Economic damages include lost "net" profits, which are defined as lost revenues less the avoided cost, and are usually included as an element of economic damages in a litigation matter. Typically, net lost profits are computed by estimating the gross revenue that would have been earned "but for" those circumstance which are found to have caused the losses had not occurred. This amount is then reduced by the avoided costs, or those costs which were not incurred because of the lost revenue.

Lost revenues – Avoided costs = Net lost profits

Generally, once the fact of lost profits has been established with reasonable certainty, less certainty may be required in establishing and proving the amount of lost profits. Often courts have found that the amount may be somewhat uncertain or inexact, so long as the determination is based on a "reasoned conclusion" or by a "reasonable estimate."[3]

Dates are always a major consideration in the determination damages or lost profits. In the calculation of damages, there are three specific points in time that are important to understand and consider. These include the time of the damages event, the date of resolution, and the date at which the incurrence of further damage ends. The damage period is generally deemed to run from the time the damage occurs to the time the damage ends. This can be almost any length of time, and the damage period can sometimes be permanent. Thus, it is critical for the financial expert to understand the timeline that will drive the determination of the financial and economic damages in the matter.

As noted above, damages can be permanent. In such cases there will likely be a determination that the subject business or asset has sustained a permanent loss of value. Typically, in these instances, a valuation will be performed to quantify the loss of value of the subject business or asset.

At the end of the day, the calculation of damages is simply the projection of what would have happened if the damage did not occur ("but for"), less the actual results that occurred following the damage.

Each lost profits situation is nuanced, different and unique. The specific facts and circumstances surrounding the economic damages calculations govern the approach and methods employed. It is imperative that the financial expert clearly defines the facts and assumptions on which he or she has based the calculations.

Often encompassing a knowledge of accounting (both historical and forensic), tax, economics, finance, statistics and business valuation, these determinations can become exceedingly complex, depending on the facts and circumstances surrounding the case.

The authors have often worked with legal counsel to make each of these determinations. While certain events, such as plant fire, are easily determinable in setting the start date to the damages or lost profits calculation, other causes of alleged damages are not so clear. Where we have participated in assignments regarding a breach of contract, for example, it can be very difficult to determine the start date and the end date with any degree of precision until procedures are applied to identify these events.

[3] *Hill v. Republic of Iraq*, 328 F. 3d 680 (D.C. Cir. 2003)

The job of the financial and economic expert, then, is to provide the attorney with an analysis that is as accurate as possible, prepared with a focus on clarity and simplicity, and on an independent and objective basis. All specific procedures undertaken in the process must be in the hands of, and at the discretion of the financial expert to protect his or her objectivity. The calculations should be credible and serve to aid a trier of fact in the particular matter. The expert's calculations should provide relevant and reliable information and use approaches, methodologies and analytical procedures that specifically relate to the given situation. Finally, all work performed by the financial expert must be undertaken with an eye first to the possibility of deposition, and then to presentation in a court of law in the event an explanation needs to be communicated in such a venue.

Fraud/Forensic Analysis

Forensic assistance in any case, as will be discussed below, is an entirely different skillset than that required in providing the types of expert services discussed above. Generally, forensic services require an in-depth look at history via the financial records and operating activities of the abused business entity or individual. The result is almost always an extremely cumbersome and costly process of information gathering and detailed analysis to fully opine on the degree of malfeasance.

Forensic accounting expert insight may be valuable in a variety of cases. A forensic accounting expert witness may provide an expert opinion on matters such as accounting malpractice, fraudulent insurance claims, embezzlement, employee theft, financial reporting fraud, occupational fraud, kickbacks, tax returns, fraudulent financial statements, malpractice and other forms of white collar crime.

Often, in the consideration of fraud, certain phrases and concepts will be encountered. A brief (not intended to be all-inclusive) example of these might include the following:

- Unfair advantage by unlawful or unfair means
- Knowingly making false representations
- Intentional deception resulting in injury to another party
- Intentional and successful deployment of cunning, deception, collusion or artifice used to cheat or deceive another person, whereby, that person acts upon it to the loss of his/her property and to his/her legal injury
- A deception, intended to wrongfully obtain money or property from another who acts on the deceptive statements or acts, believing them to be true
- Intentional perversion of the truth to mislead someone into parting with something of value

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

From the point of criminal law, fraudis most often defined as a criminal deception, whereby, the use of false representations results in an unfair advantage or harm of another's interest.

Fraud experts rely on financial statement analysis to detect much of the fraud that they encounter. Financial statement analysis is paramount in discovering and proving any major discrepancies in various accounts. In order to perform these procedures, fraud examiners and external auditors perform various analytical examinations, such as analyzing trends and ratios, to determine if an account is misstated. Analytical procedures allow for a broader approach to fraud examination without an auditor having to obtain a business' financial records.

Detailed test work is deployed when there is determined to be a greater risk of fraud in an organization. Fraud experts will ask the client to retrieve certain records as evidence for suspected fraud. Detailed test work is entirely reconstructive, which allows auditors or fraud experts to review supporting detail and trace every transaction that comprises an account. The timing of detailed test work can also trigger discovery of fraudulent activity. Whether procedures are performed during the middle or end of the client's fiscal period may be dependent on the nature of the client.

Fraud experts and auditors also utilize evaluations of internal control within the organization. This process can be accomplished through review of documented control procedures, interviews with management, staff and employees who directly handle the financial obligations of the organization, and testing of various controls to determine their effectiveness. Controls related to check signing, segregation of duties and transaction approvals are commonly documented control procedures tested by fraud examiners. Testing internal controls can provide a gateway to vulnerable areas that may be more susceptible to fraud.

The primary purpose of a fraud expert's investigation is to gather evidence. Evidence can be obtained and maintained in various forms, which include documentary, client testimonial, observational, and any other physical evidence. The fraud expert will use this evidence in constructing a case to support or refute a specific claim.

The cost of a forensic assignment can vary widely, but it can be cost beneficial where the amounts lost to the malfeasance are suspected to be material and recovery is available through repayment by the perpetrator or via insurance settlements.

Shareholder Disputes and Shareholder Oppression

The most common type of controversy matter dealt with by the authors is that of alleged shareholder oppression. The role that we most often undertake in these matters is the determination of the financial effects of the alleged acts. At times, these calculations are undertaken in a means similar to damages calculations. In other circumstances, the effects are measured through the use of multiple valuations in an attempt to prove the loss of value attributable to the equity ownership interest held by the plaintiff shareholder (equity ownership interest holder), both before and after, the alleged oppression. Sometimes, the determination of the financial effects of the alleged oppression are made via a combination of both of these calculations.

There are various types of shareholder disputes. Shareholder disputes can be due to a disagreement with the majority shareholder's actions, a shareholder wishing to exit the relationship, or the minority shareholder claiming that the actions of the controlling shareholder were either fraudulent, illegal or oppressive. Typically, these situations arise when there is an imbalance of power between controlling shareholders/equity owners and minority owners or a deadlock amongst equal owners.

The type of dispute influences the assignment(s) that are requested of the financial expert. Often, financial experts are sought to provide business consulting, accounting, audit, tax and valuation services. Therefore, the financial expert needs to have a clear understanding of the type of dispute, including whether or not it is a circumstance of pending or threatened litigation, in order to assist legal counsel with the determination of what services may need to be performed. The financial professional will work closely with legal counsel to provide assistance regarding the services that might be employed in a particular project based on specific facts and circumstances.

In the case of a shareholder dispute, the financial expert can assist with performing a valuation of the subject interest, as well as performing forensic services related to the suspected fraudulent, illegal, or oppressive actions. The financial expert may also quantify economic damages. Economic damages calculations in these matters may include appraisals to quantify loss of business value or lost profits. The process generally requires a team of professionals led by legal counsel and requires a specific, strategic plan of action.

Most often, the key element facing both the departing and controlling shareholders, just as with a marital dissolution, is the valuation of the subject equity interest under consideration and the terms under which the matter will be successfully resolved. Very often, the most difficult element of the process is to find a value that the both sides can agree upon.

This process can be as simple as determining the value in compliance with a "previously-agreed-upon" valuation formula set forth in shareholder agreements adopted at the inception of the business. Or, it can be so complex as to require the use of multiple business valuators on each side conducting an in-depth analysis and then later deferring to a third, independent valuator to reconcile differences and make the final decision. Even then, many of these cases end up in formal litigation with judges and triers of fact making the final determination.

Given the fluidity and dynamics of equity owner split-ups, the authors have rarely observed success in resolving these matters in short order. That is not to say that such instances do not exist. However, the complexity of the economic determinations and the complexities of the legal process, combined with the dynamics of betrayal and mistrust (real or perceived) tend to exacerbate an already-difficult situation. In such cases, the time required to accomplish fair and equitable resolution can be significant.

Shareholder/equity owner oppression can take place through a variety of actions by those in control. Actions found to constitute such include but are not limited to: generally oppressive and abusive conduct; withholding of dividends; restriction or preclusion of employment in the company; payment of excessive salaries to majority equity owners; the withholding of information on the operations of the business; misappropriation of corporate assets; denial of appraisal rights to dissenting shareholders/equity owners; failure to hold shareholder equity owner meetings; and, exclusion of minority owners from having a meaningful role in corporate decision-making.

Aiding members of the legal community in determining the economic effect of alleged majority equity owner oppression against a minority equity owner is at the heart of the role played by financial experts. Services extend to both plaintiffs and defendants. To understand how this role is fulfilled, it is first necessary to briefly discuss the various remedies available in such actions.

Generally, the remedies in an oppression proceeding are most often reduced to an economic platform comprised of a monetary resolution. These remedies often include the determination of monetary damages resulting from actions taken by the majority equity owners that ultimately served to misuse corporate assets and/or unjustly enrich majority equity owners. Though it is the experience of the authors that many of these determinations involve a specific matter calculation (such as addressing excess economic enrichment actions including excess compensation, rent or other corporate expense), sometimes the actions can only be measured in terms of shareholder/equity owner value before and after the alleged majority equity owner's oppressive actions.

Valuations in this context are generally intended to assist counsel and their client(s) in assessing the estimated economic impact of the alleged action. To make this determination, depending on the controlling state law statutes, the general goal in remedying such matters is to ensure that the plaintiff minority equity owner is returned to the same financial position he/she was at prior to the alleged oppressive action(s) by the majority equity owners.

Members of the business valuation community are usually required in such circumstances to adopt a "fair value" standard of value. For these purposes, fair value is generally defined by statute in each respective jurisdiction, and must be respected.

The authors continue to see a broad range of majority equity owner activities being challenged through claims of oppression. The breadth of such claims appear to affect businesses of all sizes, and the authors are not able to identify any discernible trend related to the growth in the number of these cases other than minority owner perceptions.

Any dispute among shareholders, partners or members that involves acts of oppression can result in an expensive and time-consuming process of litigation or dispute resolution. As has been discussed, parties to such affairs end up disputing each other's conduct and the "fair value" of their equity interests. The resulting expense is not only the prospect of a buy-out order at fair value, which can represent substantially more than fair market value (due principally to the non-recognition of discounts for lack of control and/or lack of marketability), but also the expense of valuation experts, forensic accountants and, of course, legal representatives.

Marital Dissolution

Many divorce cases involve complex financial issues. These issues require the engagement of a financial professional. This is especially relevant in a case where there is a wide discrepancy between the earnings capabilities of the spouses.

In a divorce proceeding, a financial expert may also assist in coordinating financial information and performing net disposable income calculations to quantify support. They may aid in the preparation of financial statements or the statement of marital assets and liabilities. A financial expert can be instrumental in researching and explaining an asset's net worth. They may even quantify the value of stock-based compensation, such as restricted stock awards or certain compensation under employee stock purchase plans.

One area in which the authors have extensive experience is collaborative resolution of financial issues related to marital dissolutions. Whether the financial matter is the subject of significant controversy or not, we have successfully resolved such matters by working with counsel and opposing counsel and their expert in a "non-court" setting to resolve the matters efficiently and cost-effectively.

Personal Injury

In a personal injury case, financial experts will focus on matters concerning damages, such as quantifying the present value of future lost wages and benefits. A financial expert may also assist in discovery, identifying what documents will be needed to evaluate the economic loss. In a personal injury case, an individual is entitled to recover any and all monetary losses caused by the injury. This may include damages such as lost wages and benefits, as well as pain and suffering. Often juries struggle with quantifying pain and suffering, so the amount quantified for economic loss may be utilized by the jury as a base.

Analysis/Rebuttal of Opposing Expert

A rebuttal can be a key part of discovery, exposing flaws and weaknesses in the opposing expert's work and opinions. Differences in facts and shortcomings may be exposed, which allow the reliability and credibility of the opposing expert to be challenged. The financial expert may attack the numbers and calculations in a report and/or the overarching conceptual approach. A powerful rebuttal can be pivotal for a case, even leading to settlement.

Expert Testimony at Trial

Financial experts can also assist in preparing for and attending mediation, arbitration, and/or trial, including attending depositions, providing expert testimony, and assisting with cross examination of opposing experts. Financial experts may also provide charts or other illustrations to utilize in trial to help highlight certain analyses or conclusions for the court.

Concluding Thoughts

This chapter presented a general overview of the financial and economic elements of a matter requiring the attention of a financial expert. Financial experts can help legal counsel and their client by answering a variety of questions based on the specific facts and circumstances of the project or case.

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

The decision to retain a financial expert can be impacted by certain economic factors of the case including the amount of money at stake, likelihood of success, cost of the expert versus the perceived benefit, and whether or not the case can be successful without an expert.

The authors of this material have become involved in matters that were proceeding without a financial expert on the basis that the case could be successful without involvement of an expert. Occasionally, this can lead to insufficient time to develop complete conclusions or opinions, resulting in a less favorable outcome or leaving money on the table

Financial experts should be capable of explaining their methods, underlying data, procedures, ethical issues, interpretations, and terminology. They should also be able to explain potential weaknesses, questions they may face, questions for the opposing expert and expected answers, and liability & damage theories. The basis for the expert's conclusion must be clearly understood by both the attorney and expert.

CHAPTER III – UNDERSTANDING THE ROLE OF FINANCIAL/ECONOMIC EXPERTS

Federal Rule of Civil Procedure 26(b) provides for two very different types of experts to assist counsel with trial preparation – an expert identified as one whose opinions will be presented at trial, versus an expert employed only for trial preparation.

In a matter that has the likelihood of developing into a civil or criminal case, the first decision facing legal practitioners is exactly what type of expert is required to accomplish the objectives of the legal strategy. When litigating any case requiring the assistance of an expert, it is important to find the right type of expert as early in the case as possible. This expert may need to prepare for discovery and depositions and can help the attorney prepare his or her discovery requests and questions for opposing witnesses. In more complex cases, it is often a good idea to retain an expert as a consultant to help prepare the case, in addition to hiring a second "testifying" expert witness.

Generally, if the circumstances surrounding a case are clear and the strategy well defined, the decision to engage a "consulting" or a "testifying" expert can be undertaken early in the case history. There is no question that a decision to engage an expert of any type should be made as early as possible.

However, more often than not, an attorney will not know for certain if he or she is going to put the expert on the stand in either a civil or criminal case. It is entirely possible that, after reviewing the documents provided through discovery and other open case file contents, the expert might conclude that the opposing expert came to the proper conclusion, or that the opposing expert came to the right result, even though he or she relied on incorrect or incomplete information or an improper technique to arrive at the conclusion. In circumstances such as these, counsel may decide that there is not a need for the expert to testify.

On the other hand, preliminary assessments of factual detail and information gathered through the preliminary discovery process are not always fruitful and definitive. In the experience of the authors, each case is a journey with additional factual information being gathered throughout the course of the matter's resolution. Unless the case file being reviewed by the expert is totally complete and not expected to be supplemented in any way, it may be impossible to immediately discern whether the opposing expert's opinions are challengeable in court.

Further, it is not unusual for the expert's final conclusion with respect to opposing counsel's work product to differ from the one reached in the expert's initial review of the case file. The ongoing process of financial, economic and legal research can ultimately lead to a differing conclusion.

Finally, legal strategies often tend to be somewhat malleable and go through an evolutionary process as a result of changes in facts and circumstances as more information becomes available and as counsel has more time to contemplate case strategy and direction. The most appropriate approach, then, to addressing the type of expert required at the front of a case is to ensure that legal counsel maintains as much flexibility as possible in engaging the expert.

The fundamental difference between a consulting expert and a testifying expert is one of absolute independence and objectivity. To express an opinion as a "testifying" expert, one has to maintain an objective attitude toward all information provided and reviewed. In a perfect sense, the testimony of an independent testifying expert would be the same whether he is engaged by counsel on behalf of plaintiff or defendant.

The other primary difference between a consulting expert and a testifying expert witness is the requirement of designation before the court. A consulting expert does not have be designated. An attorney can retain the consulting expert for his or her advice and guidance and to ensure their confidentiality. Consulting experts cannot be deposed nor retained by the opposing attorney. The authors have observed legal counsel engaging additional experts within the financial and economic services community to avoid their engagement by opposing counsel. Generally, such an approach requires major litigation, as the cost to carry additional consulting experts can be prohibitive.

On the other hand, an expert witness must be designated. Once the expert has been designated as a testifying expert, he or she can be subpoenaed for deposition, or he or she may be obligated to report other discoverable materials, as once designated, the expert's files become subject to Subpoena. An expert slated to be independent and testify is still able to perform most of the functions of a consulting expert; however, his or her level of confidentiality is tempered slightly by the fact that he or she may be compelled to provide certain information to the other side. The benefit of being an expert witness, of course, is that he or she can testify at trial in front of a judge or jurors and offer expert opinions directly to the finders of fact.

A consulting expert is not limited to remaining in that role through the entire life of the matter under contest. It is possible and, in fact, common, to retain an expert to consult on a case and then, just prior to the deadline for declaring the expert as a witness, designate them as such. In the authors' experience, this strategy is often used as a means to limit opposing counsel's access to a witness until the last possible moment. In those situations where an attorney has engaged multiple consulting experts, this strategy might also allow for the creation of some doubt and confusion as to which of the consulting experts might eventually be appointed as testifying experts.

It is noteworthy that the process does not work as efficiently in reverse. A testifying expert can, of course, be withdrawn from a case, but it rarely occurs without ramification. Withdrawing a testifying expert witness can have an impact on the credibility of the case perceived by jurors or triers of fact in certain situations. Questions are certain to arise as to why would one want to change a testifying expert to a consulting expert. Importantly, the added critical benefit of confidentiality of a consulting expert is lost if the expert had already had his or her deposition taken or reports disclosed.

It is not mandatory that a party calls a particular expert witness at trial, even if he or she has been previously designated as a testifying expert. At times, the authors have noted that legal counsel will name several witnesses, but will only call one or two in an effort to generate some level of uncertainty to opposing counsel. This strategy can require opposing counsel to spend their trial preparation time focusing on unknown outcomes and possibly prepare and take potentially lengthy depositions of expert witnesses, only to find that they are not called at trial.

The most significant element of an appointment of a testifying expert is the admissibility of that particular expert's testimony and opinions. Rules of evidence in any particular jurisdiction set the protocol and requirements for admissibility. In the Commonwealth of Pennsylvania, testimony by expert witnesses is governed generally by Rules 702 through 705 of the Pennsylvania Rules of Evidence[4] (Pa. R.E.) Pursuant to Pa.R.E,

> A witness who is qualified as an expert by knowledge, skill, experience, training, or education may testify in the form of an opinion or otherwise if:
>
> (a) the expert's scientific, technical, or other specialized knowledge is beyond that possessed by the average layperson;
>
> (b) the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue; and
>
> (c) the expert's methodology is generally accepted in the relevant field.

These rules differ in several important areas from the Federal Rules of Evidence. Pa.R.E. 702(a) and (b) impose the requirement that the expert's scientific, technical, or other specialized knowledge is admissible only if it is beyond that possessed by the average layperson. Pa.R.E. 702(c) differs from F.R.E. 702 in that it reflects Pennsylvania's adoption of the standard in *Frye v. United States*, 293F.1013 (D.C. Cir. 1923).

[4] Article VII. *Opinions and Expert Testimony,* Pennsylvania Rules of Evidence (Pa.R.E.) 702

The rule applies the ''general acceptance'' test for the admissibility of scientific, technical, or other specialized knowledge testimony, consistent with prior Pennsylvania law. The rule rejects the federal test derived from *Daubert v. Merrell Dow Pharmaceuticals, Inc.,* 509 U.S. 579 (1993).

Note that Pa.R.E. 702 does not change the Pennsylvania rule for qualifying a witness to testify as an expert. In *Miller v. Brass Rail Tavern, Inc.,* 541 Pa. 474, 480-81, 664 A.2d 525, 528 (1995), the Supreme Court stated:

> The test to be applied when qualifying a witness to testify as an expert witness is whether the witness has any reasonable pretension to specialized knowledge on the subject under investigation. If he does, he may testify and the weight to be given to such testimony is for the trier of fact to determine.

Pa.R.E. 702 does not change the requirement that an expert's opinion must be expressed with reasonable certainty. Pa.R.E. 702 states that an expert may testify in the form of an ''opinion or otherwise.'' Much of the literature assumes that experts testify only in the form of an opinion. The language, ''or otherwise'' reflects the fact that experts frequently are called upon to educate the trier of fact about the scientific or technical principles relevant to the case.

The primary consideration when selecting a testifying expert that can meet counsel's needs in driving forward a legal strategy that aids in the successful resolution of his or her client's matter is ensuring that any testimony to be offered by that expert complies with these Rules of Evidence. Thus, it is imperative that the selected expert possess the requisite scientific, technical or other specialized knowledge to express an opinion. The qualification as an expert must have come from knowledge, skill, experience, training or education in order to testify.

As an aside, it is important to remember that both the Federal and Pennsylvania Rules of Evidence impose a legal obligation to disclose to opposing counsel critical information related to the expert and his or her expected testimony.

In civil cases in federal court, the duty to disclose is addressed in Federal Rule of Civil Procedure 26, "Duty to Disclose." In federal court, the expert must be disclosed 90 days before the trial date, unless the judge has set another timeline. Fed.R.Civ.Pro. 26(a)(2) requires disclosure if the expert will present evidence under Federal Rule of Evidence 702, 703, or 705. The disclosure must include a report, written by the witness, which includes:

- A comprehensive statement, covering all of the opinions the witness intends to express
- The basis and reasons for those opinions

- The facts the witness considered when forming their opinions
- Any exhibits the witness intends to use to support, summarize or otherwise advance the testimony
- Expert qualifications, which include all publications authored by the expert over the past year
- A list of all cases wherein the witness testified during the prior four years, either in a trial or during a deposition
- An accounting of the witness's compensation, both for the review of the file, trial preparation, and testimony

Pennsylvania Rules of Civil Procedure differ from the federal rules, and require the use of interrogatories to discover the identity of experts, the subject matter they intend to testify to, the substance of the facts and opinions the expert will testify to and a summary for the basis of the opinion.

Pennsylvania Rules of Civil Procedure, Rule 4003.5. Discovery of Expert Testimony. Trial Preparation Material, provides:

(a) Discovery of facts known and opinions held by an expert, otherwise discoverable under the provisions of Rule 4003.1 and acquired or developed in anticipation of litigation or for trial, may be obtained as follows:

(1) A party may through interrogatories require

(A) any other party to identify each person whom the other party expects to call as an expert witness at trial and to state the subject matter on which the expert is expected to testify, and

(B) subject to the provisions of subdivision (a)(4), the other party to have each expert so identified state the substance of the facts and opinions to which the expert is expected to testify and a summary of the grounds for each opinion. The party answering the interrogatories may file as his or her answer a report of the expert or have the interrogatories answered by the expert. The answer or separate report shall be signed by the expert.

As noted earlier, once opposing counsel has been informed of the name of the expert, the ability to retract the appointment is likely to provide opposing counsel with the ability to explore at trial the reasons for such a change. The perceived message sent by such a change, of course, is that the departing testifying expert does not have an opinion that corresponds with the legal trial strategy developed by counsel.

In Summary

From a practical standpoint, in the authors' experience, reference is rarely made to the type of expert role that we are expected to fill in the engagement. The engagement letters that we submit simply note that we will, "provide expert business valuation (economic damages calculations, etc.) services, and that these services, while conducted at the request of legal counsel, will be undertaken on an independent and objective basis. In this assignment, all procedures required to complete the engagement will be determined by Grossman Yanak & Ford LLP, and those conclusions and opinions we develop as a result of these procedures will be solely our own."

Such language is designed to allow us the opportunity to work for legal counsel as the engaging party, thereby, affording the protection of privilege while permitting us to offer consultative services in the period leading up to notification of testifying expert witness. The thought behind this protocol is to allow engaging counsel to better understand the expected opinions that we might offer as a result of our work. This understanding, then, allows counsel to decide whether he or she wishes us to continue forward and prepare a formal report and to prepare to testify.

The key element of moving from a consulting expert role to one of testifying expert is to ensure that those services rendered as a consultant are conducted on an objective basis, and that no procedures are undertaken that could be perceived as acting in a posture of advocacy for counsel's client or his or her legal strategy.

CHAPTER IV: IDENTIFICATION AND SELECTION OF THE FINANCIAL/ECONOMIC EXPERT

The authors of these materials often speak with members of the legal profession that have experienced less-than-desirable results with respect to experts. These negative experiences are due primarily to the fact that they engaged financial, economic or forensic experts ultimately lacking in some aspect of those skills necessary to the matter at hand. It goes without saying that, first and foremast, requisite technical skills are necessary to make any ultimate determinations and provide a credible opinion at some future point in the matter. Just as important, however, is the ability for the expert to understand the case itself, whether it be one in litigation or a non-controversy assignment, such as offering an opinion on tax structure.

Additionally, technical expertise in any discipline is useless without an ability to communicate the information clearly and concisely in an effective manner. The authors have observed many cases in which opposing experts were unable to effectively communicate the findings resulting from the work they had undertaken in the assignment. We observe this limitation in both written reports and verbal communications. Nowhere is this issue more critical than in a controversy matter heading to court.

The need for, and selection of, a financial expert in any legal matter, whether or not related to potential litigation, will depend on the facts and circumstances of each individual case. In order to best leverage the knowledge and experience of a financial expert, legal counsel should employ a framework which will allows for the selection of the most appropriate expert for the project.

This chapter will address the four main questions that must be answered in considering the use of financial, economic and forensic experts:

1. Is a financial expert needed for the case?
2. What different types of experts might be used to effectively move the matter forward?
3. What type of process can counsel employ to screen potential expert?
4. How should the financial expert ultimately be selected?

Necessity of a Financial Expert

The most basic issue requiring consideration in determining whether a financial expert is needed for a particular case is, whether the inclusion of a financial expert's opinion will increase the likelihood of a favorable outcome for the client. Often, the answer to this question is "yes," however, there are many additional issues to consider when determining whether and how to use a financial expert.

Effective Use of Financial Experts: When and How to Utilize Them in Your Case

In a matter that is transaction-oriented, such as non-litigation assignments including valuation for estate and gift tax purposes, assistance with tax structure in a business sale or purchase transaction, etc., experts generally serve to supplement the expertise of the engaging attorney. Thus, in these cases, the primary criterion in evaluating the need to look to an outside expert is simply whether the attorney's assignment requires an element of technical knowledge or expertise on any particular matter beyond that available within the engaging attorney's skillset or from others in his or her firm.

On the other hand, in matters of controversy and potential litigation, rules governing the admissibility of evidence must be considered in conjunction with the assessment of areas within the case where an expert could bring credible and relevant assistance to the court and trier of fact. Financial experts can help simplify complex issues for the trier of fact as well as legal counsel. As financial, economic or forensic issues within a case become increasingly complex or frequent, the argument for the retention of a financial expert increases. An expert's purpose is to analyze, simplify, and educate. If a financial issue cannot be easily understood, inclusion of a financial expert might be the best alternative and should be strongly considered.

Limitations inherent in the case should also be considered when determining whether a financial expert is engaged. Will the financial expert have complete access to necessary information in order to form a credible opinion or properly perform their procedures? Any financial expert that carries professional credentials will require the ability to review information sufficient to form and substantiate an opinion.

Oftentimes, the authors have been involved in preliminary discussions with counsel to help to determine the need for an expert and the type of expertise demanded by the fact pattern of the case. Most often, attorneys clearly understand the facts and surrounding circumstances related to the matter at hand and how they preliminarily assess the legal strategies that they plan to employ in the representation of their clients. Those elements most often discussed include nuanced financial, economic and/or forensic principles and how that nuanced understanding can work to drive a work product, and possibly testimony, that will move the case forward. If such a finding results from those discussions, the use of an expert is generally the proper route to take.

In conjunction with the determination of whether a financial expert is needed at all, legal counsel must also determine the type of financial expert required. This, again, will be driven by the facts and circumstances of the particular case, the strength of the argument with and without the testimony of an expert, and the resources available to bring an expert onto the team. If a specialized financial expert is needed, more time will be required to find an expert that meets the case's specific needs.

Expert Specializations

Business Valuation/Business Appraisal Expert

In many instances where a case involves equity ownership assessments related to a business, a valuation or appraisal expert will serve to address many of the complex issues associated with equity interest valuations. Shareholder oppression cases or general shareholder disputes almost always require the expertise of a business appraisal specialist as the primary issue will be to determine the value of the dissenting shareholder's ownership interest.

This need to determine value can spill into the divorce arena as well. If one spouse is a business owner, oftentimes the equitable distribution calculation will require a valuation of that spouse's ownership interest. In many divorce cases, both spouses hire their own valuation experts.

While buy-sell agreements are intended to define how a shareholder's ownership interest is to be valued, poorly written, dated or vague agreements can cause dispute between the parties. Valuation experts can be utilized to determine a value of the subject ownership interest in accordance with the agreement. Additionally, some buy-sell agreements are drafted with language that states the value must be determined by a qualified appraiser. In this instance, disagreements may arise in the selection of an expert that is acceptable to all parties.

Valuation experts may also be utilized to assist in an estate and gift dispute. This assistance can take the form of a valuation expert defending their report against IRS inquiry or consulting with legal counsel in defense of a previously filed estate and gift tax return. Valuation experts are also commonly asked to perform services outside of the traditional framework of business appraisals. Often, valuation experts have backgrounds in the accounting and tax arenas, which can allow for the leveraging of this additional expertise.

Forensic Expert

Forensic accounting experts use investigative and analytical skills to evaluate financial information. Often forensic accounting experts are relied upon when there is a presumed impropriety within a company's financial statements. Unlike an audit, in which accountants review a company's financial statements on a *test basis*, forensic accountants analyze significantly more transactions (sometimes every transaction) in order to interpret and communicate their findings.

If there is suspected fraudulent activity within a business' financial statements, forensic experts are utilized to investigate whether such issues exist. These issues can include tax fraud, money laundering or any other manipulation of financial statements. The work of a forensic expert is extremely detailed and can take a significant amount of professional time.

General Financial Expert

In certain circumstances, a financial expert may not need to have specialized credentials. However, an expert should always be vetted to determine whether he or she is the best fit for any particular case. In the next section, we will discuss the credentials that are carried by financial experts and how legal counsel can use these credentials to find qualified financial experts as well as prove to the court or trier of fact that an expert is capable of forming an opinion or analysis relevant to the case.

In many scenarios, a general financial specialization is all that is needed for an expert to assist in a case. For example, in a lost profits case, many issues can be handled by an expert that has general accounting or tax experience. A financial expert is expected to be able to identify the benefit stream that was lost by the damaged plaintiff and quantify the impact of the loss of income. Other examples of where general financial specialization can meet the needs of legal counsel include:

- ***Deposition or trial preparation*** – if legal counsel requires assistance in the formulation of deposition, direct or cross examination questions that need not be reviewed by an expert within a specific discipline (ex. deposing a tax preparer or bookkeeper)
- ***Personal injury cases*** – when the issue is the plaintiff's lost wages and future benefits
- ***Marital dissolution*** – financial experts can assist in calculations related to equitable distribution, alimony, or child support

Expert Evaluation and Screening

The evaluation and screening process should be focused on determining whether the expert is qualified. That qualification is built upon a foundation of general education, specific discipline training and, importantly, experience in matters similar to that in the current case. An essential element in assessing qualification is the understanding of the professional credentials awarded the expert and the underlying requirements for attaining those designations.

Engaging an expert carrying professional credentials is critical to establishing that the financial expert is credible. The type of analysis that the financial expert will perform in conjunction with the case should determine which professional credentials are desired. As such, the role of the financial expert must be clearly defined before the evaluation and screening process begins.

After determining a clear understanding of the role that a financial expert will need to fill as it relates to any particular case, focus shifts to finding a financial expert that is qualified to assist legal counsel. While the selection of a financial expert will ultimately be determined by a number of factors (professional experience, experience within the specific jurisdiction, availability, cost, etc.), the critical element to consider when choosing a financial expert is the credentials held by the available experts.

Professional Credentials of Financial Experts

Financial expert credentials are awarded by a number of membership organizations. Each credential carries specific prerequisites, examinations and ongoing recertification requirements. As credentials relate to a specific knowledge base, which can be similar between membership organizations, we will present the credentials grouped by type and then by membership organization.

General Credentials for Financial Experts

Pennsylvania Institute of Certified Public Accounts (PICPA) or other state board of accountancy

The PICPA is Pennsylvania's membership organization for Certified Public Accountants. The PICPA provides many resources to its members including training and continuing education. The PICPA also sets the certification and education requirements for its members.

Certified Public Accountant (CPA) – The CPA designation is the most recognizable designation for accountants. The designation requires a broad understanding of accounting concepts. Unlike many credentials that will be discussed, the CPA credential is issued at the state level, and each state has its own set of education and experience requirements that holders must meet. The CPA designation is the gold standard in the accounting profession.

- The CPA designation proves that an individual is knowledgeable in a diverse range of accounting topics. As a general designation, the body of knowledge required for an individual to obtain the CPA designation is immense.
- **Requirements:** Candidates must pass all four parts of the uniform certified public accounting examination, meet work experience as well as continuing education requirements. CPAs must also maintain active membership in their state institute.

CFA Institute

The CFA Institute is the credentialing organization that offers multiple credentials geared toward the investment management industry. The organization provides educational materials and training to its members and also developed the ethical codes and standards for the charter holders.

Chartered Financial Analyst (CFA) – The CFA credential is awarded to investment and financial professionals and covers a wide range of investment and analytical topics. The credential is offered internationally by the CFA Institute. The CFA credential is considered one of the highest distinctions in the investment industry.

- CFA charter holders are experts in investment research and analysis. Many CFAs become portfolio managers and financial analysts.
- **Requirements:** to become a CFA charter holder, one must pass three exams (Level I, II and III) and meet minimum work experience or higher education requirements. CFA charter holders must also maintain membership with the CFA Institute.

Valuation Credentials for Financial Experts

American Institute of Certified Public Accountants (AICPA)

The AICPA is the national membership organization of Certified Public Accountants in the United States. As the CPA credential is awarded at the state level, the credential is not required for membership, nor is membership required for CPAs. The AICPA issues multiple valuation related credentials.

Accredited in Business Valuation (ABV) – Initially, only CPAs could obtain this credential, however, in 2018 the AICPA began to allow qualified finance professionals that obtain a minimum threshold of valuation-related experience to qualify for the ABV designation. Individuals carrying the ABV designation as well as the CPA designation will display their credentials as "CPA/ABV". As of 2016, approximately 2,800 individuals hold this designation.

- The ABV credential is business-valuation specific, requiring candidates to demonstrate a considerable amount of knowledge and experience in the appraisal of equity instruments.
- ABV credential holders specialize in determining the value of a business or an ownership interest in a business.
- ABV credential holders may work for a consulting firm, within a CPA firm, or in businesses that regularly analyze the value of businesses.
- **Requirements:** To obtain this credential, a candidate must pass a two-part examination and provide proof of experience and competence by way of continuing professional development and a minimum threshold of valuation experience.

Certified in Entity and Intangible Valuation (CEIV) – The CEIV designation is designation is available through multiple valuation organizations including the AICPA, the American Society of Appraisers and the Royal Institution of Chartered Surveyors.

- The CEIV credential was designed to address fair value measurements for businesses, business interests, intangible assets, certain liabilities and inventory for financial reporting purposes.

- Individuals carrying the CEIV credential perform valuations for financial reporting purposes, primarily for public companies that submit filings to the SEC or privately held companies that prepare financials in accordance with generally accepted accounting principles.
- **Requirements:** to obtain the CEIV credential, candidates must pass multiple examinations and meet certain eligibility requirements. To maintain the credential, individuals must participate in an ongoing monitoring program, maintain membership with the AICPA (or other credentialing organization), perform a minimum of 1500 hours of work related to fair value measurement every five years, and complete mandatory continuing education.

Certified in the Valuation of Financial Instruments (CVFI) – Although the CVFI credential is awarded by the AICPA, applicants need not be a CPA to qualify as long as they fulfill the requisite education and experience requirements.

- The CVFI credential is granted to individuals that demonstrate expertise in performing and/or reporting on fair value estimates of financial instruments for financial reporting purposes.
- Individuals carrying the CVFI designation are experts in valuing financial instruments which have traditionally proven to be difficult to value (examples include derivatives, mortgage-backed securities, credit default swaps, complex bonds, and securitized debt).
- **Requirements:** applicants must have over 3,000 hours of experience related to fair value estimates for financial instruments over a five-year period and must pass an online exam.

National Association of Certified Valuators and Analysts (NACVA)

The NACVA is a national credentialing organization, which offers multiple credentials and certifications within the valuation disciplines. The organization enforces standards of ethical conduct among its members and provides training, education and literature related to appraisal techniques, best practices and current developments.

Certified Valuation Analyst (CVA) – The CVA credential is the largest of the valuation-specific credentials. As of 2016, approximately 5,500 individuals hold the CVA designation.

- The CVA credential is awarded to applicants who have a wide degree of general valuation knowledge and experience.
- The credential is primarily focused on equity valuation, covering fundamentals, techniques and theory, and the broad approaches to business valuation.
- **Requirements:** individuals must be a member of the NACVA and must complete a five-day training program, pass a written examination and finish a rigorous business valuation case study. Additionally, three personal and three business references are needed.

Accredited in Business Appraisal Review (ABAR) – Since 2016, the NACVA has not taken applications for the ABAR credential and is evaluating the credential for redesign. There are approximately 100 designees carrying the ABAR credential to date.

- The ABAR credential was designed for business valuators whose work involved the review of valuation reports and analysis performed by others and was attained by individuals whose practice includes appraisal review and quality assurance.
- **Requirements:** were similar to those required to obtain the CVA credential.

American Society of Appraisers (ASA)

The ASA is an international organization representing appraisal professionals across multiple disciplines, including: business valuation, gems and jewelry, machinery and technical specialties, personal property, real property and appraisal review.

Accredited Member (AM) – The AM credential requires the least amount of experience of all of the available valuation credentials offered by the ASA, requiring two to five years of experience.

- The AM credential is designed for professionals who perform valuations in a wide range of specialties. This includes business valuation, as well as other appraisal disciplines.
- **Requirements:** An applicant must have a college degree and two years of full-time business appraisal experience. An applicant must also complete four courses (three days each) with the successful completion of one half-day exam following each course or the successful completion of one all-day exam. Additionally, an applicant must submit two appraisal reports to a Board of Examiners for review as evidence of professional capability.

Accredited Senior Appraiser (ASA) – This designation is earned by individuals who have met all of the AM requirements, and have an additional five years of full-time appraisal experience.

Fellow of the American Society of Appraisers (FASA) – The FASA is the highest honor bestowed by the American Society of Appraisers. An individual could become a FASA if he/she has met all of the above requirements and has been voted into the College of Fellows on the basis of technical leadership and contribution to the profession and the ASA as a whole.

Certified in Entity and Intangible Valuation (CEIV) – co-developed by the ASA, the AICPA, and the Royal Institution of Chartered Surveyors. Requirements to earn the CEIV credential through the ASA are the same as noted under AICPA, with continued membership in the American Society of Appraisers.

Institute of Business Appraisers (IBA)

In 2008, the NACVA acquired the assets of the IBA and continued to support two business valuation credentials. These certifications are no longer awarded to new applicants, however, credential holders that continue to meet their requirements are recognized as being in good standing.

Certified Business Appraiser (CBA) – The CBA designation is earned by an individual who has met the requirements for education and business valuation experience.

Master Certified Business Appraiser (MCBA) – the highest professional designation in the industry, recognizing extraordinary competence of a few highly skilled and experienced individuals.

Forensic Credentials for Financial Experts

American Institute of Certified Public Accountants (AICPA)

Certified in Financial Forensics (CFF) – The CFF credential is only awarded to certified public accountants, leveraging the vast accounting knowledge obtained through the CPA credentialing process. As of 2016, there were approximately 3,300 CFF credential holders.

- CPAs holding the CFF credential specialize in forensic accounting. CFF holders can apply forensic accounting skills in a variety of service areas.
- The CFF body of knowledge includes laws, courts and dispute resolution; engagement planning and preparation; information gathering, preservation and analysis; expert reports and testimony.
- **Requirements:** Applicants must hold a valid CPA license, pass a written exam, and meet business experience and education requirements. CFF holders must also maintain active AICPA membership and meet continuing education requirements.

National Association of Certified Valuators and Analysts (NACVA)

Master Analyst in Financial Forensics (MAFF) – The MAFF credential is intended to prove an individual's credibility within the financial litigation services arena.

- The MAFF credential requires applicants to have already earned another credential in one of eight specialty areas, as well as provide proof of foundational experience
- **Requirements:** To earn the MAFF credential, an individual meet basic and foundational experience requirements, which include involvement of 20 matters or 2,500 hours of financial forensics experience and holding at least one other credential in a specialty area. They must also pass an examination focusing on financial forensics, and provide professional references.

Association of Certified Fraud Examiners (ACFE)

The ACFE is the national membership organization of fraud examiners. Founded in 1988, the ACFE is the largest anti-fraud organization that provides its members with anti-fraud training and education.

Certified Fraud Examiner (CFE) – The CFE credential combines knowledge of complex financial transactions with an understanding of methods, law, and how to resolve allegations of fraud.

- Credential holders are trained to identify the warning signs and red flags that indicate evidence of fraud.
- **Requirements:** applicants must meet minimum academic and professional requirements, maintain active membership in the ACFE, and pass a four-section electronic exam.

Other Credentials for Financial Experts

Certified Turnaround Professional (CTP) – The CTP designation is granted by the Turnaround Management Association (TMA), which provides benchmarks for practical experience, knowledge and ethical conduct.

- Individuals with the CTP designation specialize in assisting distressed companies.
- **Requirements:** to obtain the CTP credential, candidates must pass a three-part examination on management, law, finance and accounting, have five years of consulting experience, with a minimum of three years focused on corporate renewal, provide three client case studies and names of individuals who can verify the work, and submit to a background check.

Certified Management Accountant (CMA) – The CMA designation is awarded by the Institute of Management Accountants.

- CMAs possess specialized knowledge in the areas of cost and financial accounting, finance, investment analysis, performance management, technology and analytics, and risk management.
- **Requirements:** to obtain the credential, applicants must pass a two-part examination, fulfill education and experience requirements, and meet continuing education requirements.

Overview of Credentials

Understanding the credentials available to financial experts and the weight each carries is critically important to the selection of the proper financial expert. Many credentials are awarded for expertise in a specialized area of practice. As such, it may be wise to look to experts carrying multiple credentials.

The CPA credential may be seen as a requirement for any financial expert that must speak on accounting-related topics. Experts carrying a CPA credential have set themselves apart from those non-CPAs in being able to understand, interpret and stay current on accounting concepts.

The primary credentials that are obtained in the valuation arena are the ABV (from the AICPA) and the CVA (from the NACVA). The CVA credential is more commonly seen as it had a wider pool of potential applicants for many years, while the ABV designation could only be obtained by professionals carrying the CPA credential. Only a select number of ASA credentials are seen in the market as the experience requirements and prerequisites make them more difficult to obtain.

In the forensic accounting space, the CFE designation is the gold standard for fraud detection. CFEs, however, may not have as diverse a knowledge base as individuals holding the CFF designation. Only CPAs are eligible to obtain the CFF credential, proving the expert has both a diverse and thorough understanding of accounting and forensic related matters.

Other Considerations in the Expert Evaluation and Screening Process

In addition to reviewing a financial expert's professional credentials, additional items must be considered. Each of these considerations can impact what experts are chosen to assist legal counsel.

Title and Position

One should look to the prospective expert's current position and his/her job title as the starting point for determining the propriety of engaging that professional as an expert. While the information gleaned from this first look may be cursory and definitely requires follow-up, it is often helpful to know how that individual holds himself or herself out to the public.

Websites often contain detailed information on senior professionals. Another common source for this preliminary assessment information may come from searching for that person's LinkedIn profile. Most often, when the authors try to gather information on opposing experts, we are able to locate from these sources such items as general experience, education, and work history. Other significant information found on these sources includes professional credentials and, of course, job title and current position. A more comprehensive effort will be required from the engaging attorney to investigate the prospective expert's experience and history in similar matters.

Experience

To be sure, the proper education and training is important to the development of a credible expert opinion. However, nothing replaces a history of experience that encompasses the same types of matters that are currently faced by counsel in any current matter. This experience can be usually

found on the expert's curricula vitae. It is incumbent upon the engaging attorney to test that CV, looking for confirmation of the information included therein, either through references provided by the expert or through peer confirmation.

History as a Financial Expert

Legal counsel must also find out whether the financial expert has previously encountered a Daubert[5] challenge. While not all states (including Pennsylvania, which uses the *Frye* decision[6]) have adopted the federal rules of evidence or invoke a Daubert standard, consideration must be given to the financial expert's previous opinions or material that they have authored to determine whether it could negatively impact the case.

Conflicts of Interest

It is best practice to verify that an expert and their firm are free from conflicts of interest. Similarly, it is not uncommon for an expert to be contacted by attorneys representing parties on opposite sides of a controversy. In such instances, questions may arise as to the expert's perceived independence.

Will the Expert Testify?

Legal counsel must determine whether the expert will serve as a testifying expert, or whether the expert will serve in a consulting role. As a testifying expert, caution must be taken as to ensure no questions arise as to the expert's independence. As a testifying expert, all procedures and analysis are at the discretion and judgment of the expert, and cannot be dictated by legal counsel. As a consulting expert, legal counsel, after proper guidance from the financial expert, can take the lead in the determination of the calculations and analyses that should be performed to best support the case.

Selection of an Expert

Once the financial expert's role is clearly defined, the type of expert determined, and experts have been evaluated and screened to determine whether they meet the threshold level of qualifications, care must be taken to select the best candidate from the pool of qualifying experts. The final phase of the selection process must include an interview of the potential expert, either in person or over the phone or videoconference. It must be determined early in the process whether the expert is able to effectively communicate their thoughts and opinions to others.

[5] *Daubert v. Merrell Dow Pharmaceuticals, Inc.,* 509 U.S. 579 (1993)
[6] *Frye v. United States,* 293 F. 1013 (D.C. Cir. 1923)

CHAPTER V – ENGAGEMENT PROTOCOLS AND MANAGEMENT

Among the primary goals of financial, economic and forensic experts in a controversy setting is the performance and delivery of services that are in compliance with applicable legal, regulatory and professional standards. To that end, it is critical that at the outset of each project careful consideration is given to building a team with the appropriate specializations, experience and knowledge.

The nature and complexity of the services that are requested of these experts continues to increase. As a result, the authors of these materials have participated on a variety of multi-disciplinary teams with specialized education and training. For example, the work undertaken in connection with the assessment of damages for a company operating in the oil and gas industry, included a petroleum engineer as well as our firm to competently and effectively complete the assignment.

There will also be times where a second expert unrelated to the financial and economic aspects of the engagement is necessary to educate not only the attorney directing the case, but also the financial or economic expert. By way of example, the authors completed a damages case related to the value of patented medical technology intended to detect cancer more quickly and earlier in women. A medical technology specialist was engaged by counsel to ensure that both she and our Firm, as independent experts, were able to understand the many detailed aspects of the technology. The work of the medical technology expert was critical in our Firm's ability to properly analyze the technology and produce a credible opinion.

It is imperative to address both administrative and procedural issues at the outset of the engagement. Having a proper understanding of specific facts and circumstances of the case and what is being requested of the financial expert by legal counsel will lay the groundwork for setting expectations.

This chapter will address certain protocols generally followed by a financial expert as well as the management of this type of engagement. It is imperative to manage the engagement in a way that maximizes the benefits of employing the expert as well as satisfies the objectives of the assignment.

Timing of Engagement

To be sure, it is the preference of financial experts to be engaged by legal counsel as early on in the process as possible. It is the utmost concern of the expert to have fair and complete access to all of the pertinent facts and information necessary to perform an independent and objective analysis. Financial experts seek to understand if any limitations exist with respect to access to documents and individuals with whom experts seek input and information.

Understanding that cost considerations come into play, engaging financial experts early in the process will enable their participation in preparing discovery requests by articulating what is needed to prepare their analysis. Additionally, financial experts can provide assistance to legal counsel in preparation for depositions and hearings.

There are instances wherein experts are called to assist legal counsel and there is insufficient time to prepare a complete and defendable analysis. In these situations, financial experts will attempt to work with legal counsel to provide a workable solution or they may determine that time will not allow the preparation of a suitable work product in compliance with professional standards.

Conflict Checks

Financial experts specialize in objectivity, as they are called to maintain an attitude of independence and impartiality in order to ensure unbiased analysis and interpretation of the evidence. When contacted by legal counsel relative to a potential engagement, one of the first matters that is addressed is to ensure that the financial expert is free from conflict. Even before background information on the particular case or issue is shared, a conflict check should be undertaken. Just like a law firm, the conflict check should be part of the intake process.

Financial experts who are routinely engaged to assist legal counsel, including Grossman Yanak & Ford LLP, typically have a system in place to complete such a task. Databases are maintained and should include past, current and potential clients with whom the financial expert's firm has had or currently has a relationship. A good contact management system should prove helpful in this area. Of course there is still an opportunity for human error, so efforts should be made to communicate with all partners and managing members of the financial expert' firm to ensure no conflicts exist, as the databases and lists maintained by the firm may be missing information or have not been updated.

Results of conflict checks performed should be articulated to legal counsel in writing. Engagement (or retainer) letters typically include a statement that the financial expert and his/her firm is free from conflict.

Any time a potential conflict exists, an expert's obligation is to disclose the nature of the conflict to the attorney, so the attorney can determine whether it is truly a conflict and if they can proceed with the engagement. Courts and triers of fact may disqualify experts from testifying if conflicts come to light.

Identifying the Client

At the beginning of the engagement, it must be determined for retainer (or engagement) letter purposes who will be the expert's client. Is it internal or outside counsel for the company or individuals subject to investigator or party to the matter at issue? If counsel is the client, the work of the financial expert is generally protected from discovery by opposing parties as long as legal privilege is granted by the engaging attorney. As such, the financial expert will not share findings or provide opinions to parties that are not similarly granted privilege with respect to the expert's work.

It is common practice for the authors of this material to not only address the engagement letter to the engaging party (i.e. legal counsel), but to also identify the client in the body of the letter.

There will be discussions with legal counsel regarding the extent that the work undertaken by the expert is protect by legal privilege as it may influence communications, the manner in which work is directed, documented and disclosed. Additionally, the financial expert should confirm communication and documentation protocols and other aspects of the work that should be treated and labeled as "privileged" to aid in identification and protection.

Confidentiality and Privilege

Upon appointment and execution of the engagement (retainer) letter, document and information flow will commence. It should go without saying that the financial expert is expected to preserve client confidences. Upon performing work on the engagement, the financial expert will uncover facts that may harm the client's position, in addition to facts that may benefit the client's position. Legal counsel requires this information as well because they will need to determine how to address it in their case. Advance notice of weak or harmful information, will assist legal counsel in formulating case strategy.

Expert testimony has embedded itself as a pivotal component of nearly every lawsuit. There is hardly an action pursued without the guidance or opinion of an expert. In the instance of litigation, financial experts should at least be knowledgeable of preservation of the attorney-client privilege and the work product doctrine embodied in Federal Rule of Civil Procedure 26, including amendments[7], as well as applicable procedures in the relevant court or jurisdiction. This extends to what can be shared with both testifying experts and consulting experts.

[7] Federal Rule of Civil Procedure 26(a)(2) was amended effective December 1, 2010. The amendments are intended to change pre-amendment law as to testifying experts.

As noted previously, financial experts can be engaged by legal counsel as testifying or consulting experts. If it has not been determined whether the expert will testify, legal counsel will exercise caution in what is shared with the expert. It has been the authors' experience that legal counsel prepares in advance what information or evidence they want the expert to consider.

If the role of the financial expert will be strictly interpretive, and the expert will not testify, it is likely that everything shared among the expert, the attorney, and the client will be protected by the attorney-client privilege. A consulting expert in this instance is acting as an arm of the attorney, will likely fall within the scope of the attorney-client privilege, rendering the communications among the consultant, the attorney, and the client privileged.

Confidentiality and privilege should be understood and respected at the outset of the engagement. The financial expert must understand the fluidity of matters addressed by legal counsel and seek input in any areas of uncertainty. Additionally, the financial expert should have internal procedures in place to protect documents and evidence shared by legal counsel as well as to avoid unnecessary written communications between expert and counsel.

Legal Counsel – Expert Communication

Communication between the financial expert and legal counsel is critical; however, both expert and counsel should be mindful of discovery implications in connection with all written materials. This includes expert billings related to the engagement.

Once engaged, the expert should ensure that they have an adequate understanding of legal counsel's preferences for communications. Regular meetings between the attorney and the expert will be necessary to maintain a clear understanding about the issues, the documents being requested and the analysis being performed.

In federal cases, and those jurisdictions that follow federal rules, drafts of expert reports are protected work product. There is protection for communications between experts and attorneys, except those that (1) relate to compensation, (2) identify facts or data provided by counsel and considered by the witness, or (3) identify assumptions provided by counsel and relied upon by the witness in forming his or her opinions.

Experts will communicate findings and opinions, or those expected to result from their work, to legal counsel as work progresses. This will allow legal counsel to develop case strategy as it relates to the financial/economic aspects as well as manage their client's expectations.

Ongoing communications are key to successful case management on the part of legal counsel as well as the expert. The expert should ensure that all options are properly vetted to provide objective opinions and insight to the trier of fact.

Managing the Engagement

Effective management of the engagement on the part of the financial expert requires careful oversight of the process undertaken, along with thoughtful communication between the expert, legal counsel and the client. In instances where the expert has a team of professionals devoted to the matter, the expert should provide adequate supervision through all stages of the engagement.

Effective project management includes leveraging work to lower-cost professionals without compromising a quality work product. The ultimate analysis and opinions of the testifying or consulting expert should be their own.

As cases evolve, the amount of information and evidence received can be voluminous. Information gathering, through discovery or other means, will be ongoing. The process of gathering, reviewing and analyzing information deemed to be relevant is time consuming and can lead to stops and starts in the experts work. As can be expected, there can be some inefficiencies in the process if the expert is waiting for critical data and then resumes work upon receipt of the information.

An electronic document management system can be maintained for ease of searching the population of documents provided. Documents should be labeled by bates number, as well as description, and organized by category or type. Effectively managing the inventory of documents provided to the expert will add efficiencies to completing the analysis and drafting the report or other deliverable.

A primary goal of the financial expert should be to provide objectivity. Experts perceived as a hired gun or mouthpiece will lose credibility and potentially jeopardize any work product or testimony. The successful financial expert will understand and manage all of the aforementioned items as a key member of the litigation team.

CHAPTER VI – PREPARATION FOR DEPOSITIONS AND TRIAL/EXPERT TESTIMONY

Perhaps the most significant element of expert services related to litigation is the actual testimony itself. Even if the matter is settled before trial, it is not unusual that the expert designated by counsel will have to provide an indication of his or her testimony through the process of a deposition.

Live testimony at trial, or through a deposition, is a critical aspect of the communication of the expert's findings. Without the offering of clear information related to the matter, the procedures undertaken in the course of the expert's assignment and the manner in which that information reviewed and analyzed within the procedures leads to the opinion(s) of the expert, the resultant benefit will be far less than it might have otherwise been. In this case, the usefulness of the expert to the accomplishment of the engaging attorney's legal strategy may be nullified.

Depositions and Expert Witnesses

Depositions, of course, are not quite as formal as testimony in a trial before a state or federal court. However, the authors of these materials have been advised many times by counsel to carefully respect the process of deposition as this process belies the ultimate testimony that an expert will be required to provide at trial.

Specifically, and as all participants in today's program realize, a deposition is the legal term for a formal, recorded question and answer session which occurs when the witness is under oath. A deposition generally serves two purposes. First, opposing counsel is trying, through a question and answer format, to find out exactly what the expert knows and how he/she will testify at trial, if that later becomes necessary. The process of deposing an expert is to allow opposing counsel to better prepare for future decisions in the case and to allow him or her the opportunity to prepare future legal strategies in full understanding of what he or she may encounter should the expert take the witness stand later in the proceeding. From the perspective of the expert and attorneys on each side of the matter, a deposition allows the experts testimony to be preserved for later use (either in motions to be filed with the Court or at trial).

Opposing counsel, as he/she asks questions at a deposition, will target the questions to obtain information that will help his or her client prove their case. The key to successfully navigating a deposition is to prepare with legal counsel. This preparation generally requires a meeting with the engaging attorney to review the expected questions and to ensure that the responses provided by the expert coincide with the work undertaken and the resultant findings from that work. Ultimately, it is these findings that lead to the experts conclusions or opinions.

It is important to ensure that the expert is mindful that the question and answer session encompassed in the deposition will be recorded in a formal transcript taken by a Court Reporter. Once completed, the transcript is generally provided to the expert at a later date for review in a written format for approval and, if necessary, correction. The final written deposition transcript will be available for attorneys on both sides of the case.

It is important that engaging counsel work with the expert to ensure a credible level of preparedness in offering responses to opposing counsel's questions. The authors have been advised on occasion that the best thing about a written deposition transcript is that there is no record of time lapse between the moment a question is asked and when the expert provides an answer. Likewise, physical demeanor by the expert in responding to a deposition question is not captured in a written deposition transcript.

While there is truth to those assertions, in the authors' experience, the attorneys taking the deposition are generally the same individuals who will lead the opposing side of the case, should it proceed. As such, by their very presence at the deposition, they have clearly identified those questions that might have caused the expert to show emotion. For this reason, it is important that the expert be as prepared as possible to answer all questions to the best of his or her knowledge, and that responses to the examining attorney's questions be provided in a clear and articulate manner with an even demeanor.

It is important for engaging counsel to remind the expert that opposing counsel is, through the deposition process, trying to assess the credibility and communication skills that will be evident in his or her testimony at trial. To that end, likeability and emotional bearing are important attributes for an expert at deposition.

It is also important that engaging counsel advise his or her expert to respond only to the very specific questions posed. While some experts are quite accomplished, it is not beneficial for them to try to demonstrate how smart they are during the deposition process. Short direct answers should be employed as a tactic, and information should be limited so the deposing attorney is left to his or her own devices in formulating those questions required to get the information they seek.

It is important to, again, note the formality of the deposition process. The responses provided by counsel's expert at the deposition, to the extent that they may be interpreted as being helpful to the deposing attorney's case, are very likely to rise again if, and when, the matter goes to trial. Should the expert respond differently to a similar question at trial, the result can be harmful and lead to the perception that the testimony is not reliable or credible. Thus, expert's responses in depositions are as important as later testimony at trial and must be treated as such.

The attorney whose expert is being deposed should listen to the questions carefully. This is easy to do at the beginning of the deposition, when minds are fresh and engaged. However, after an extended time period of questions and answers, perhaps after lunch and during the late afternoon hours, it is tempting to take a mental break and pay less attention to a question.

A good attorney conducting the deposition will realize the witness is most vulnerable at this time and will attack when least expected. If you find you have missed a question and the deponent is well on his or her way to giving an answer, don't hesitate to make a belated objection.

Further, there is no need for the expert to provide the basis for an expert's response unless directly asked by the deposing attorney. This additional information, if offered without being requested to do so, could serve to strengthen the position of opposing counsel.

In light of the formality of the deposition process, it is important that the expert respect the need to be as accurate as possible. To the extent necessary, he or she should ask questions that they do not understand, or find confusing, to be repeated or further explained. If the deposing attorney is asking for an answer on a schedule or exhibit, it is important that the expert request an opportunity to review the information prior to offering an answer.

Finally, the engaging attorney should work to close the deposition process at the end of the session. To this end, he or she should advise the expert not to offer to provide further information after leaving the deposition.

From the perspective of taking a deposition, the process is opposite the advice given when your expert is being deposed. In these cases, deposing counsel should use open-ended questions to try to get the witness talking. Make a list of what the witness says on an issue; exhaust the witness's recollection; and then go back and drill down. However, detailed outlines are generally not recommended as one of the keys to taking a good deposition is listening to the witness's answer. Deposing attorneys need to be prepared to follow up, deviate from any outline they might be using, and go back to the notes or outline after exhausting any follow up.

Expert Witnesses at Trial

Direct Examination

Having an expert who is prepared for a courtroom appearance could be the key to winning the case. In order to optimize the use of an expert, engaging counsel must prepare the expert for as many possibilities that may occur during a trial as he or she can. The more preparation, of course, the less likelihood of a surprise during the course of the trial, which could be devastating to the case.

An important consideration is not to begin trial preparation too early. The most effective preparation will be closer to the date of the expert's appearance, with the understanding that a sufficient amount of time will be required and likely vary from case to case, given the complexity of the matters before the court.

It is also important, if significant time has lapsed since the expert was queried at deposition, that the deposition transcript be read by both the expert and the engaging attorney. A fresh reading will ensure that the testimony to be offered at trial is consistent with the expert's responses in the deposition transcript.

As the trial date approaches, the assumption is that engaging counsel has "qualified" his or her expert. Refer back to Chapter III of these materials, when the Federal Rules of Evidence, as well as the Pennsylvania Rules of Evidence were discussed. Though Pennsylvania rules vary slightly, a quick look at Federal Rules of Evidence 702 provides that a witness qualifies as an expert based on their skill, knowledge, education, training and education. An expert may testify in the form of an opinion if the expert's scientific, technical or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue; the testimony is based on sufficient facts or data; the testimony is the product of reliable principles and methods; and the expert has reliably applied the principles and methods to the facts of the case.

If, in fact, the witness meets all of the above-noted criteria, he or she will be admitted as an expert. Once the expert is found to qualify as an expert witness, it is necessary to determine exactly what the expert is basing his or her opinion on. If engaging counsel's expert is basing his/her opinion on fact or data from the case that the expert was personally made aware of, there is a basis for your expert. Experts are also permitted to use information that is commonly used in their field of study that other experts would use.

As the primary role of the expert is to educate, if it is found that there is no basis for the expert's testimony and it will not help the jury understand the case, that expert will be disqualified, and the testimony become inadmissible.

As one might presuppose, preparation is the key element of a successful expert appearance in court. While this would seem logical to most participants in today's program, the authors have observed on several occasions an overly lax attitude in preparing for trial. As one might further presuppose, the results are measureable where adequate preparation is undertaken prior to the appearance.

By the actual trial preparation stage, the attorney(s) engaging the expert should be well aware of the strengths and weaknesses of his or her testimony. If such is not the case, it is imperative that engaging counsel take those steps necessary to come up to speed in understanding the procedures that were employed by the expert in forming his or her opinion, whether there are any particular strengths or weaknesses in the procedures applied, and the formulation of the opinion to be offered at trial. In those instances where the testifying expert expects challenge from opposing counsel, it is incumbent upon him or her to inform engaging counsel and to provide viable "counter arguments" by which the attorney engaging the expert can rebut challenges to the expert's testimony.

In preparing for direct examination of a financial, economic or forensic expert, focus should be on the educational aspects of the expert's testimony. To that end, preparation of direct examination questions should be developed to "walk" the trier of fact, or jury, through the entirety of the expert's work and the resulting opinion. Such a discourse, if conducted properly, will serve to accomplish a number of factors that should be deemed to be relevant to the determination and veracity of the expert's testimony.

Included in the factors clarified through a strong direct examination are the documents and information that were made available to the expert in the course of his or her preparation, either through discovery or otherwise; the professionally accepted financial and economic or forensic theory deemed appropriate by the expert in the conduct of the assignment; the propriety of the procedures and analytical assessments applied in the assignment and how they integrate the professionally accepted financial and economic or forensic theory; the veracity and propriety of the actual calculations; and, finally, how those calculations lead to the opinion of the expert. This "map" will allow the trier of fact or jury to follow in a logical manner.

Most often, the authors of these materials have been required to render a written report including all of the above. In such cases, the general discourse through the direct examination generally follows the flow of the report, as each of the above-noted factors are set forth therein. However, given the complexity of a great deal of the matters set forth in the report, it often becomes more beneficial to the case if the expert assists in drafting those questions that will comprise the direct examination.

If an expert has the experience of taking the complex minutiae included in the conduct of their engagement and reducing that information, in layman's terms, into an understandable discussion through the direct examination process, the preparation process can be made much more efficient for engaging counsel.

Physical practice of a direct examination is not always required, but larger and more sophisticated matters absolutely require live rehearsals. A failure to conduct such practice sessions could lead to a choppier direct examination and make it more difficult for the trier of fact or the jury to understand the information. If the direct examination is going well, the trier of fact or the jury should be focused on the expert during the course of the testimony.

Cross examination

Cross examination is the domain of opposing counsel and, as such, the expert cannot be as prepared for the cross examination as he or she might have been for the direct examination. However, if the expert is sufficiently experienced, he or she should be able to advise counsel on the strengths and weaknesses of the work that was undertaken in the assignment and the resulting opinion.

In these instances, having the expert assist with the development of potential challenges to his or her own testimony will allow engaging counsel to gain an understanding of how best to counter or rebut these challenges as the cross examination progresses. Such counter arguments should include strategic reinforcement by the expert on rebuttal as well as other avenues of defense, if available.

As with the direct examination, it is important to have a sense of the strength of the cross examination testimony so that any weaknesses identified can be readdressed on rebuttal offered through redirect.

Thoughts relating to instructing experts how to perform under cross examination vary. Note, however, the following common tips for successfully navigating a well-conducted cross examination.

- Make certain you fully understand the question and answer only when the expert is ready
- Do not provide rambling, lengthy and evasive answers – few answers are as powerful as a simple “Yes” or “No”
- Do not show hostility or sarcasm to opposing counsel; professionalism always carries the day
- Do not make a closing argument during cross-examination; if speeches are necessary, counsel will give them in closing or on redirect
- Do not stake credibility on some unimportant side issue; stick to an assertion in the face of strong contradictory evidence only if that assertion is critical to the case.

Also important in both the direct and cross examination is the need to avoid technical jargon and acronyms generally assumed to be known with the expert’s technical field or discipline. Using such language serves only to create an air of arrogance with respect to the expert, as well as cause confusion to the trier of fact or the jury.

Cross Examination – Opposing Expert

Greater effort is required, of course, with respect to the cross examination of opposing counsel's expert. In this matter, the expert engaged by the cross-examining attorney can provide an invaluable service. Utilizing the expert to review the case history as it relates to the opposing expert, perform a detail review of the report offered by that expert, review depositions transcripts, and attend the direct examination of this expert will allow for the development of concise and meaningful cross-examination questions that will serve counsel as a strategy for how best to attack the credibility and veracity of that expert's testimony.

The authors of these materials very often assist counsel with the development of arguments intended to disprove the propriety of opposing expert's testimony and opinions set forth therein. In addition, experts are able to provide counsel with draft questions for cross examination where those questions are focused on differing perspectives on financial, economic or forensic theory and the manner in which that theory has been interpreted by the opposing expert. Financial, economic or forensic experts are also able to provide questions directed at incorrect facts set forth by the opposing expert or errors in calculations and computations.

The critical element of assisting counsel in the development of draft questions to be used in across examination is to avoid adopting a posture of client advocacy as has been mentioned numerous times in these materials. As a testifying expert, the primary role of education must be conducted in an independent and objective manner, leaving room to advocate only for the expert's own opinion.

Concluding Thoughts

The use of financial, economic or forensic experts in a matter likely to proceed to court carries with it a need to assess early on, the capability of that expert to conduct the required assessment(s) and to render an opinion as to the matter at hand. Further, though, is the need to ensure that that expert will be able to qualify as an expert in the matter before the court, and that his or her testimony will serve to meet the relevance requirements necessary to be admitted as evidence in the matter.

Once the expert has completed the requested analyses, assessments and calculations and set them out in a formal report, if requested to do so, the next steps require that engaging counsel begin the process of preparing the expert to submit his or her work to the discovery process, from where he or she will begin the formal process of appearing at a deposition and/or trial. As the dates for these appearances approach, it is critical that counsel participate in a preparation process so that the expert's responses at deposition, and ultimately, trial, serve to move the engaging attorney's case forward to the benefit of the client.

CHAPTER VII – CASE ILLUSTRATIONS

This chapter presents a few cases in various courts and jurisdictions, in which the use of financial experts (or lack thereof) played a role in the ultimate outcome of the matter. These examples highlight the number of different ways in which financial experts will be relied upon in disagreements.
Note that the case law presented here is NOT intended to be a collection of all relevant cases on the topic, nor is it intended to present all of the issues and related findings in each matter. Rather, it is intended to provide some insight into the roles of financial experts, how the experts were utilized, what they analyzed, and how their analysis and expertise impacted the case. The participants in today's program should always undertake their own legal research to ensure adequacy of that process.

Majority Owners of a Restaurant Grilled for Not Reporting Cash Sales
Cortes v. 3A N. Park Ave. Rest Corp.
No. 13396/11 (October 24, 2014)

- Plaintiff, Porfirio Cortes, owned a 16.67 percent interest in Cabo, a Mexican restaurant in Rockville Centre, New York. Plaintiff purchased this interest in 2003, entering into a purchase agreement that gave the corporation the right to purchase Plaintiff's shares should he resign from his position with the Company. Plaintiff worked as day manager at the restaurant from 2003 to 2010.
- Defendants were majority shareholders, Angelo Ramunni and Dominick DeSimone. Ramunni controlled the corporation's finances, and DeSimone had a less active role in the management of the business.
- Plaintiff resigned from his position in 2010 as a result of long hours. Defendants offered to buy Plaintiff's ownership at the same price that he had originally paid. This arrangement was technically in accordance with the purchase agreement, which did not detail a pricing mechanism for the buyback of shares. This offer was rejected by Plaintiff.
- In 2011, Plaintiff filed a complaint against Defendants, accusing them of diverting millions of dollars of the cash receipts of the business, which were not reported on the corporation's financial statements. The tax returns regularly showed minimal profits.
- Defendants alleged that Plaintiff's mismanagement of the corporation was the primary cause for the poor profitability, and that the corporation became profitable after Plaintiff's departure because of the change in management.
- As the cash receipts went unreported on the corporation's financial statements, quantifying them became the primary issue at hand. This was estimated using the corporation's server reports, which are generated through the point-of-sale system, and detail both cash and credit card sales.

- During the trial, Defendants failed to produce sufficient financial information for the restaurant. Server reports were only retained by the corporation for one year. Defendants only produced 11 months of server reports
- Plaintiff procured the skills of a financial expert to calculate the unreported cash revenue of the business. The expert calculated this by using the cash to credit card payment ratio of a sample of the server reports.
- Based upon the sample, the financial expert concluded that 45.6 percent of revenue was paid by credit card, and 54.5 percent of the revenue was from cash sales. The cash to credit card payment ratio was applied to the automatic credit card bank deposits received by the restaurant to estimate revenue received in cash. In her decision, the Judge specifically noted that the court was satisfied that a rational basis existed for the expert's calculations.
- The financial expert opined that the restaurant's revenue was significantly higher than initially reported, determining that Defendants diverted in excess of $3.7 million in the form of cash receipts during the time period in question. The court ordered that Defendants pay this amount, plus interest, for a total of $5.0 million, back to the corporation.
- The court calculated the value of the corporation utilizing testimony from multiple experts. Using the cash to credit card payment ratio to quantify a normalized earnings stream for the business, the value was calculated by the court to be $3.2 million.
- To this figure, the court added $5.0 million, the judgment of the sums diverted from the business by Defendants, totaling a value of $8.2 million. After consideration of a 10 percent discount for lack of marketability, the court determined the fair value of Plaintiff's ownership interest to be $1.2 million.
- The court ruled that Defendants must buy out Plaintiff within 90 days to maintain operations of the business. Otherwise, the court ordered dissolution of the corporation by a liquidating trustee.

Court Finds Wife Should Have Known Better in Divorce Settlement
Kojovic v. Goldman
35 AD 3d 65, 823 NYS 2d 35 - NY: Appellate Div., 1st Dept. (October 19, 2006)

- Lora Kojovic and Neal Goldman were married in 1998. They filed for divorce in 2004.
- During their marriage, Husband was the chief executive officer and minority shareholder in a closely held corporation, Capital IQ, Inc., an information technology company.
- Wife, in the first two years of the marriage, worked as a securities analyst at Morgan Stanley and later pursued a career in acting.

- Shortly after filing for divorce, the parties exchanged financial information including lists of assets and statements of net worth. The parties decided not to conduct further discovery, and in late 2004, less than three months after divorce actions began, they settled the divorce pursuant to a comprehensive settlement agreement that was negotiated with the assistance of the parties' attorneys.

- Pursuant to the settlement, Wife received $1.15 million in cash, rehabilitative spousal support of $350,000 payable over four years, and certain other considerations. Husband retained, among other things, his minority shareholder interest in Capital IQ.

- Shortly after settling the divorce, Standard & Poor's (S&P) formally submitted a nonbinding expression of interest to purchase Capital IQ. One month following the divorce settlement, S&P bought Capital IQ for approximately $225 million. Husband received approximately $18 million for his minority interest.

- Subsequently, Wife commenced action for fraud, reformation, breach of contract and rescission of the settlement agreement, claiming that it was procured through fraud. Her allegation was based on Husband's misrepresentations as to the value of his ownership in Capital IQ as well as conversations that had taken place regarding the potential sale.

- Wife asserted Husband should have disclosed to her the value and the potential sale of Capital IQ, and that he concealed this information from her.

- The Court disagreed and found that by agreeing to the settlement, Wife had explicitly waived her rights to inquire into Husband's finances, including the taking of depositions and a forensic evaluation.

- The Court noted, *"Wife concedes, as she must, that the husband consistently and accurately disclosed the full extent of his minority interest in Capital IQ, an asset of speculative value at the time the settlement agreement was executed... That the wife now believes her husband privately harbored a more optimistic assessment of the potential value of his minority interest in that company, or even had additional information that he kept to himself, is irrelevant... wife has only herself to blame for her failure to inquire further. Such failure is not, however, a basis upon which to vacate the settlement."*

- The Court noted further, *"given her professional background and the advice furnished by her counsel and accountant, [she] should have been aware of the distinct possibility that Capital IQ would be sold. That she opted for an immediate and certain payout instead of the uncertainty of an eventual sale does not afford a basis for setting aside the agreement."*

Unclear Allocation of Damages Confuses Jury in Misrepresentation and Concealment Claim
Quick Pick Express, LLC v. Quick Pick Express, Inc./Kathy Javor, et al. v. Charles J. Stos, et al.
Cal: Court of Appeal, 2nd Appellate Dist., 4th Div. (April 22, 2008)

- Thomas Javor founded Quick Pick Express, LLC in 1989 by as a messenger service. By 2002, the company had four divisions – courier, trucking, warehousing and drayage – and had more than $4 million in annual sales.
- Thomas handled day to day operations while Kathy, his wife and co-owner, handled the financial aspects of the business. In 2002, the Javors decided to sell the company to help Kathy's ailing father run his real estate business.
- The owners provided a business profile of the company to Charles J. Stos and George T. Boyle. The documents presented the company as a growing, profitable business that was well established with a capable management team in place.
- The parties signed a letter of intent and began due diligence. During the due diligence process, the sellers provided the buyers with additional financial documents, but the buyers were not permitted to contact the company's employees, customers or vendors.
- The buyers and sellers, through the legal entities Quick Pick Express, LLC and Quick Pick Express, Inc. entered into a Purchase Agreement which provided for a purchase price of $1.5 million with $1,175,000 to be paid in cash and a note for $325,000.
- The terms of the note required the buyers to pay the sellers $325,000, plus interest, in 84 equal monthly installments.
- The note provided a clause that it could be offset if material facts relevant to the operation of the business were not disclosed or if material misrepresentations were made. The note also stated buyer must continue to make payments as required and only after an offset had been agreed upon by the parties or determined by arbitration or litigation, quantifiable amounts could be deducted from the principal of the note.
- After closing in July 2003, the buyers discovered multiple issues at the business, including unpaid creditors, uncompleted work and misrepresented expenses. Additionally, over $200,000 of accounts receivable were uncollectable, and an employee disclosed that a major customer (accounting for approximately 10% of sales) was about to terminate its contract, which was known by the sellers prior to the sale.
- The buyers contacted the sellers about the issues in attempt to resolve differences but, ultimately, they were not resolved so the buyers ceased payments on the note.

- Shortly thereafter, the buyers filed a complaint against the sellers alleging 13 claims for breach of contract (alleging approximately $1.8 million in "decreased sale value" and an additional $80,000 in damages, totaling approximately $1.9 million); one claim for intentional misrepresentation; and one claim for negligent misrepresentation. The complaint alleged $1.9 million in damages for each misrepresentation claim.

- The sellers cross-complained against the buyers, alleging failure to pay a promissory note.

- At trial, the buyers presented numerous witnesses to support their claim, including the testimony of Jason Engel, a forensic accountant. Engel quantified damages, but did not attribute the specific damages to different causes of action. Instead, he assumed the damages were the same for each claim and only differentiated between categories of damages.

- Engel categorized damages into: (i) out-of-pocket costs and lost assets, (ii) lost profits, and (iii) the difference in what the buyers paid for the assets versus what they were actually worth. Engel explained that each of these categories were distinct.

- Engel explained that the category of out of pocket costs and lost assets includes over-inflated assets, such as overstated accounts receivable, and unanticipated costs, such as payments the new entity made on bills owed by the old entity, or claims by customers against the old entity for which the customer was holding the new entity accountable. Engel provided a schedule of these damages, showing approximately $280,000 in out of pocket costs and lost assets.

- The second category of damages Engel identified was lost profits. He explained that this category of damages arises because the buyers are entitled to receive the benefit stream that was represented by the sellers when negotiating the purchase. He computed the lost profits by examining the financial statements that the sellers had provided and making adjustments to reflect what he found to be the true revenues and expenses of the company.

- The difference between the profit shown on the company's previous financial statements and the adjusted financial statement represented the lost profit. He explained that the business will continue to lose profits into the future and, therefore, he calculated the lost profits (using a net present value for future losses) for a period of five years, seven years, and 10 years. The minimum figure he calculated for his lost profits calculation was approximately $2,050,000.

- The third category Engel identified was the difference between what the buyers paid for the assets versus the actual value of those assets. Engel testified that the company only had value to the extent it had collectible accounts receivable and tangible assets.

- Engel opined that the company had no goodwill, which he defined as "the ability to earn money," because the company did not have a history of making profits and did not have the capacity to make profits based upon his adjustments to seller's financial statements.
- Engel determined the "difference in value" damages by calculating the value of the collectible accounts receivable and tangible assets and subtracting that sum from the $1.5 million, purchase price for those assets. Engel concluded the difference in value was approximately $1,150,000.
- In summarizing the damage, Engel explained the first category of damages, the out-of-pocket costs and lost assets, represented a "one-time" loss. He said requiring the sellers to pay the buyers $280,000 would put the buyers in the same position as if the sellers had given them the true value of the assets that they purchased.
- Further, Engel explained that the lost profits represented "a continuing loss of the business from year to year," and an award of those damages makes the buyer whole for the decreased benefit stream. The lost value analysis is an alternative to the lost profits analysis.
- The buyers asked the jury to award $280,000 in out-of-pocket costs and lost assets and either $1,150,000 in lost value or $2,050,000 (or more) in lost profits for each of the claims it asserted (breach of contract, intentional misrepresentation, negligent misrepresentation and concealment). The Jury struggled with completing the required forms which outline damage awards when providing their verdict as a result of confusion with allocating the categories of damages to individual claims.
- Ultimately, the Jury found against the buyers on the breach of contract claim, and in favor of the buyers on the negligent and intentional misrepresentation and concealment claims.
- The jury awarded the buyers $280,000 in out-of-pocket losses and lost assets on the intentional misrepresentation claim, and $480,000 in out-of-pocket losses and lost assets on the concealment claim. In addition, the jury found that Kathy Javor engaged in the conduct with malice, oppression or fraud, and awarded LLC $10,000 in punitive damages.
- Finally, the jury found in favor of the sellers on their breach of contract claim (relating to the buyers discontinuing payments on the note), and awarded damages in the amount of $370,000.
- On appeal, the sellers challenged the $480,000 award for concealment. On cross-appeal, the buyers argued against the Jury's finding that they breached terms of the note.
- Ultimately, the judgment was reversed and the $480,000 award for out-of-pocket losses and lost assets on the concealment claim was stricken.

Comingling of Funds Results in a Decision to Pierce the Corporate Veil for an Unpaid Debt
Steiner Electric Co. v. Leonard Maniscalco and Sackett Systems, Inc.
2016 IL App (1st) 132023 (March 2, 2016)

- Plaintiff, Steiner Electric Company (Steiner), an Illinois company, was in the business of distributing electrical products and services, including generators.
- Sackett Systems, Inc. (Sackett), incorporated in 1982, was a manufacturer and seller of battery storage systems. The company purchased supplies from Steiner.
- Delta Equipment Company (Delta), incorporated in 1972 for the purpose of selling and servicing batteries, eventually shifted its corporate focus to selling, installing and maintaining natural gas powered electric generators sold to Delta by Steiner.
- Leonard J. Maniscalco (Maniscalco), individually and through a revocable trust, was the sole owner of Delta and Sackett. He also owned the buildings from which Delta and Sackett operated.
- Steiner and Sackett's relationship began in 1989 and was described as being "mutually beneficial" until late 2008.
- Over time, Delta's financial situation weakened, as corporate records showed negative retained earnings from 2004 until it closed. Delta lacked funds to pay rent to Maniscalco and stopped paying Maniscalco's salary as an officer.
- By November 2008, Delta stopped paying invoices to Steiner and owed approximately $200,000 to Steiner. During the following months, Steiner made multiple offers to aid in resolving the debt, including extended payment plans, installment plans and restructuring of credit terms. However, no agreement was reached, and Steiner eventually filed mechanic's liens in December 2008.
- Maniscalco made the decision in late 2008 to close Delta. Delta was never able to repay the debt owed to Steiner before dissolving. Steiner then filed suit to pierce the corporate veil, such that Maniscalco and Sackett would be held liable for Delta's debt.
- Interestingly, in early 2009, shortly after Delta closed, Maniscalco's daughter and her husband started a new company, MPower, which sold the same natural gas generators that Delta had sold, and used Delta's customer list and sales data.
- In the matter, Steiner procured the services of a forensic accountant, John Bradley Sargent. Sargent reviewed various bank, financial and other records of Maniscalco, Delta and Sackett, spanning a five-year period, 2005 to 2009.

- After performing his forensic analysis, it was Sargent's opinion that Delta, Sackett and Maniscalco comingled funds to yield substantial tax benefits to Sackett. Specifically, Sackett was a profitable corporation, and Maniscalco and his accountant initiated a series of transactions that created the false appearance of management services/fees in order to minimize Sackett's tax burden.

- At trial, Maniscalco testified that he alone controlled and supervised all of Delta's financial matters. Maniscalco also testified that he periodically loaned money to the businesses but did not execute promissory notes.

- Evidence, gained though the forensic analysis, reflected hundreds of thousands of dollars being transferred between Delta and Maniscalco, and Delta and Sackett. Transactions included transfers without substantiating invoices, back-and-forth transactions, and personal withdrawals of funds without explanation.

- Sargent testified that the management fee scheme violated the Economic Substance Doctrine as codified in section 7701 of the Internal Revenue Code of 1986 [26 U.S.C. § 7701 et seq. (2012)], because the transactions had no meaningful impact on the economic positions of the parties, but only served to produce an income tax savings for Sackett.

- Sargent also testified that his analysis found multiple instances of commingling of funds, specifically a bank account held by both Delta and Sackett, which identified both companies as joint holders of the account, and detailed incoming and outgoing transactions by each entity.

- Sargent, in reviewing the information specifically related to the customers, who were subsequently being serviced by Maniscalco's daughter's company, MPower, estimated the value of the customer list to be upwards of $200,000.

- In 2009, Steiner won a default judgment against Delta for $226,686, representing the amount owed to Steiner before Maniscalco closed Delta, finance charges, attorney fees, expenses and other costs.

- However, since Delta no longer existed, Steiner attempted to collect the judgment by filing action against Maniscalco and Sackett, alleging that Maniscalco's various improprieties, both individually and through Sackett, rendered him liable for the Delta judgment.

- The trial court entered its order on June 18, 2013, holding Maniscalco and Sackett liable to Steiner for the Delta debt. The court stated that the management fee, which was discovered through Sargent's forensic analysis, resulted in comingling of funds. Additionally, the joint bank account between the entities and rental agreements that were not adequately memorialized further illustrated the communal nature of the corporations.

- The court stated, *"Mr. Maniscalco closed Delta when he became frustrated at Steiner's filing of liens. It was apparent to the court that Delta allowed the corporation to become dissolved in large part due to the potential debt problems it faced with Steiner, thus, taking the position that it could avoid its potential financial obligation to Steiner. The evidence further showed that Mr. Maniscalco had valued the customer service list and had taken consideration for same in prior corporate dealings. This interest in the customer service list was abandoned when Delta shut down and MPower was created. These inconsistencies on how the customer service list was treated further showed that Delta wanted to avoid payment to Steiner."*

Experts Battle for Value in a Texas Divorce
Sandra Graves v. Michael Tomlinson, Bryan Rice, Hartman Leito & Bolt, LLP and Rice Stewart Faris & Co.
329 S.W.3d 128, Tex. App. (November 30, 2010)

- Sandra Graves, Wife, and Michael Tomlinson, Husband, were married in 1997. When they married, Husband was engaged in farming and ranching, and Wife was a licensed home and community-based services program provider for the Texas Department of Aging and Disability Services.
- During their marriage, Wife formed three businesses, which served different purposes providing home and community-based services for mentally handicapped and disabled persons in group homes, foster care, and supported home living:
    1. Sandra Graves d/b/a All The Little Things Count, a sole proprietorship
    2. All The Little Things Count, LLC
    3. All The Little Things Country, a non-profit organization
- Wife filed for divorce in June 2005. The value of the marital assets, including Wife's businesses, became a focus of the divorce proceedings.
- Husband hired a financial expert and a forensic accountant to value Wife's businesses. The financial expert valued the entities, and the forensic accountant normalized the accounting records.
- In the normalization process, Husband's forensic expert analyzed the financial records to identify expenses that were charged to the business that were personal in nature, expenses that were non-recurring in nature, and excess compensation that was paid to the owner.
- Husband's forensic expert reviewed detail of the financial transactions of the entities in order to differentiate personal expenses from business expenses. The inclusion of personal expenses in the financial statements would serve to decrease income and, ultimately, value.

- Husband's financial expert valued all three entities together as one after consideration of the intercompany transactions, noting that each could be viewed as a division of one single entity.

- Husband's expert determined the value under the income approach was $4.1 million, the value under the market approach was $6.2 million, and the value under the asset approach was $1.5 million. Placing the most weight on the income approach and some weight to the market approach, the weighted average value of the three combined entities was determined to be $3.5 million, after deducting $1 million for Wife's goodwill. Husband's expert applied no weight to the asset approach.

- Wife's valuation expert considered all three commonly accepted valuation approaches: the asset approach, the market approach, and the income approach. Wife's expert also valued the entities separately, as they were different legal entities.

- Wife's expert believed that no businesses were sufficiently comparable to utilize the market approach. In addition, Wife's expert believed the income approach could not be used because it is rooted in the company's projected cash flows. If Wife were to leave, so would the customers, eliminating any possible future cash flows.

- Wife's expert relied solely on an asset approach for his valuation, determining the LLC had a value of $400,000. Wife's expert applied a 50% discount for lack of marketability, to arrive at a value of $200,000 for the LLC. Wife's expert used the asset approach to value the sole proprietorship at ($87,000) and accorded the non-profit no value.

- After consideration of the testimony of both Husband's and Wife's experts, the jury determined a value for each of the three entities individually. The jury determined the value of the LLC to be $1,250,000 and the value of the sole proprietorship to be $19,000. The jury accorded no value to the non-profit.

Disgruntled Employees Sabotage Business After Sale Through Employment at Competitor
Fairway Dodge, LLC v. Decker Dodge, Inc.
924 A.2d 517 (N.J. 2007)

- The owner of Fairway Dodge, a family owned and operated car dealership, desired to sell the dealership in the early 1990s. Fairway Dodge had a good reputation and client base, making it a desirable acquisition target.

- The owner's daughter, Kate Fair, and her husband, Timothy Morgan, who were long-time Fairway Dodge management employees, disapproved of the sale.

- After the sale, Fair, Morgan and an additional employee of Fairway Dodge, Diane Kennedy, resigned from their positions to work for a competing dealership, Decker Dodge.

- Before leaving the original dealership, but after being hired by the new dealership, Fair cancelled Fairway Dodge's contract from a key referral source of customers, and rejected a shipment of highly profitable vans.

- Further, Fair and Morgan returned to the Fairway Dodge premises after business hours and made a backup tape of the computer system, which included the customer and sales lists and the sales and service history of vehicles and automotive parts. She then provided this to a computer service company (Reynolds) to install on the computer system of her new employer.

- Since Reynolds required consent from Fairway Dodge for the installation, Fair falsely represented herself as still holding her previous position and sent Reynolds a letter on Fairway Dodge's letterhead that gave permission to access the information.

- Ronald Sumner acquired Fairway Dodge in 1995 from Fair's mother. Immediately after the acquisition, business began to plummet. Sumner later learned of Fair's and Morgan's actions and filed a complaint seeking injunctive relief and damages against Decker Dodge, Fair, Morgan and Reynolds.

- The next month, the parties entered into a consent order in which it was agreed that Decker Dodge would remove Fairway Dodge's information from its computer system and refrain from soliciting Fairway Dodge's customers. However, in the following month, Decker Dodge mailed a solicitation letter informing the public of Fair's and Kennedy's move to Decker Dodge. As a result, the court found that Defendants violated the court order.

- Sumner later added Susan Decker Bibbo and Ronald Bibbo, owners of Decker Dodge, as well as Kennedy, to the suit. Sumner alleged unlawful interference with prospective advantage, breach of the duty of loyalty, conspiracy and racketeering. He also claimed violations of the Computer Act.

- The court granted partial summary judgment in favor of plaintiff against Fair, Morgan and Decker Dodge for violation of the Computer Act, but dismissed the racketeering claims.

- Sumner also dismissed the complaint against Reynolds through a settlement agreement. The parties agreed to a consent order dismissing the complaint without prejudice and permitting Fairway Dodge to re-file the complaint within one year.

- Fairway Dodge then filed action against Decker Dodge, Bibbo, Decker, Fair, Kennedy and Morgan, alleging conspiracy to interfere with Fairway Dodge's prospective economic relations, breach of the duty of loyalty, misappropriation of property, and violation of the Computer Act. The matter was tried before a jury.

- At trial, Mark Koenig, a certified public accountant specializing in forensic accounting and valuation, acted as Fairway Dodge's financial expert.
- Koenig reviewed the business records provided by both dealerships and other relevant evidence. Koenig also used a specific industry calculation for goodwill.
- Koenig opined that Fairway Dodge suffered damages of $850,497 ($627,798 lost profits and $222,699 lost goodwill). Koenig estimated that total damages from defendant's actions amounted to $1,813,890.
- Koenig's calculations were based upon multiple critical assumptions including Fairway's client base would have shown loyalty to the dealership resulting in recurring revenue, and that Fairway would experience similar profit margins, which included the highly profitable vans.
- Defendant's financial expert, Karen Frankel, testified that she disagreed with Koenig's assumptions including the assumptions that: Fairway Dodge's clients would have remained loyal; the assumed profit margins could be achieved; and Koenig's goodwill evaluation.
- Defendants also presented a list of former Fairway Dodge clients who were prepared to testify that they purchased their Decker Dodge vehicle without any solicitation by defendants. However, the trial court did not permit those witnesses to testify for "lack of competency." Later an Appellate Court would find that the testimony of these clients should not have been denied, as it may have resulted in a lesser damage figure calculated by plaintiff's expert.
- The jury returned a verdict in favor of Fairway Dodge. The jury found that all defendants conspired to commit a wrong against plaintiff; all defendants interfered with plaintiff's economic relations; Fair, Kennedy, and Morgan breached their duty of loyalty to plaintiff; and Bibbo, Decker and Kennedy violated the Computer Act.
- The jury awarded Plaintiff compensatory damages on the common law claims against Defendants totaling $1,920,250. The jury also awarded punitive damages to Plaintiff totaling $130,000.
- Subsequently, the court awarded Plaintiff $525,628.26 in attorneys' fees, $16,429.82 for costs of investigation pursuant to the Computer Act, and $853,184.85 in prejudgment interest.
- On appeal, it was found that insufficient evidence existed to find that the defendants violated the Computer Act, and, as noted, that failure to admit witness testimony may have undermined the damages calculations of Plaintiff's expert. The Supreme Court of New Jersey affirmed the Appellate Court's decision.

CHAPTER VIII – CONCLUDING REMARKS

The use of a financial, economic or forensic expert in any legal undertaking, whether the matter is one of controversy and likely to move through the courts or one requiring some type of expertise beyond that available to the engaging attorney through his or her own education and experience, can be a valuable asset in resolving the issues at hand. However, as has been demonstrated through today's presentation, the use of external experts and the integration of outside expertise and skillsets, requires a substantial effort by the engaging attorney to optimize the overall impact of the expert's presence in the matter.

The precarious and unpredictable nature of matters of controversy makes careful use of independent experts a paramount consideration. As has been discussed herein, consideration of an expert's capability and experience, independence and objectivity, education and qualifications, technical processes, communication style and admissibility, and credibility must all be factored into the engagement of such a professional to ensure that the client that is being represented is able to obtain the most articulate and issue oriented expertise available to advance his or her position.

Even after consideration of all of these factors, it is still imperative that legal counsel take all steps necessary to ensure that they have a thorough understanding of the work expected to be undertaken by the expert and the manner in which the results of that effort will be communicated. While the engaging attorney, ultimately, has no involvement in the selection of procedures undertaken by the expert, if he or she is slated to be designated an expert before the courts, it is still possible at the outset and throughout the selection process to discuss the matter with the expert. This discussion allows the attorney to gain a sense of the manner in which the expert would undertake the assignment and how he/she might preliminarily see those steps and procedures leading to a conclusion or opinion.

Due care must be exercised in making the decision as to which expert best fits the needs of the case before the court as the use of an expert can be costly and the value must be assessed on a cost/benefits basis in light of the materiality of the case. It is unnecessary to tell those in today's audience that the costs of litigation are profound and that such matters are even more costly with the incorporation of experts into the case. Thus, it is essential to get the expert that bests fills the need of the case.

In areas not related to controversy, the authors believe that, excepting the nuances of controversy work, the same diligence should be used in engaging experts. We have worked predominantly for, and with, members of the legal community to aid clients with services related to business acquisitions and dispositions, corporate reorganizations, corporate finance and transaction analysis, loan compliance matters, cash flow planning, forensic and fraud investigation work, business viability assessment and

business plan feasibility, qualified benefit plan development, damages and lost profits for insurance settlement purposes, transfer pricing matters, contract compliance assessments, management evaluation and director and officer liability issues.

In each of these areas, Grossman Yanak & Ford LLP is able to match highly qualified and experienced professionals to accommodate those special skillsets that are required to offer members of the legal community the finest services available for their clients.

The professionals at Grossman Yanak & Ford LLP hold numerous professional designations, including:

- Certified Public Accountants (licensed in Pennsylvania and elsewhere)
- Accredited Senior Appraiser (American Society of Appraisers)
- Certified Valuation Analyst (National Association of Certified Valuators and Analysts)
- Certified in Financial Forensics (American Institute of Certified Public Accountants)
- Accredited in Business Valuation (American Institute of Certified Public Accountants)
- Certified Business Appraiser (Institute of Business Appraisers)

Our Firm has extensive experience in matters of controversy and has been successful at resolution development through mediation, as well other out-of-court processes. In addition, we are very active in matters of controversy brought before the courts and have worked in both state and federal court on many occasions. We have worked more predominantly in civil matters, but also have experience in the criminal sector of litigation.

Should you encounter a matter in your practice that may require the use of an expert, we would greatly appreciate your consideration of our Firm. Bob Grossman and Melissa Bizyak are always happy to discuss the matter on a general basis to better aid in your understanding and the way in which we might approach the services required to assist you in your case. Please feel free to contact either of them at any time.

Again, we understand you are busy and we are honored that so many of you would take time from your practices to attend today's program. We hope that each of you was able to add a little more knowledge to your personal repertoire and that you have a better understanding of financial, economic and forensic experts than you did prior to your attendance. Thank you!

Bob Grossman	Melissa Bizyak	Brad Matthews
412-338-9304	412-338-9313	412-338-2227
grossman@gyf.com	bizyak@gyf.com	bmatthews@gyf.com