

# VALLEY LAWYER

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A Publication of the San Fernando Valley Bar Association



**Commercial Litigation and  
Forensic Accounting**

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## Finding an Expert

# Commercial Litigation and Forensic Accounting

By Chris L. Hamilton, CPA, CFE, CVA, DABFA

**A**N ARRAY OF CIVIL LAWSUITS are typically grouped into the category of commercial litigation, ranging from false advertising to breach of contract to unfair competition. For many businesses, commercial litigation is part of daily operations, in which they actively protect company rights and defend against frivolous lawsuits. Litigators advocate their client's interests through negotiations, pre-trial testimony of witnesses, mediation, alternative dispute resolution and trial. To do so effectively, a commercial litigator often seeks to gain expertise on the client's business and industry.

Litigators look for every legal and ethical edge to enhance their client's position, including the use of experts, in particular, those known as "forensic accountants." Forensic accounting is a specialty practice area of accounting, describing engagements that result from actual or anticipated litigation. "Forensic" means "suitable for use in a court of law" which, along with other forms of dispute resolution, is the expected outcome of forensic accounting engagements.

### Forensic Accounting

In many scenarios, it is very productive to involve a forensic accountant to analyze, interpret, summarize and present complex financial and business issues. An attorney should be able to rely upon his/her forensic accountant to provide objective and independent evaluation.

In particular, these services may include reconstruction of

accounting records, analysis of business transactions, document review and tracing. This work will then be communicated to the client via consultations, reports, exhibits and collections of documents. In legal proceedings, a forensic accountant may then prepare visual aids to support trial evidence and testify as an expert witness. Obviously, in order to effectively perform these services a forensic accountant must not only be familiar with legal concepts and procedures but must be able to clearly, persuasively and accurately present economic and financial evidence and opinions.

Presentation of the conclusions and the basis for the conclusions is often critical to the success of the engagement. There are a lot of experts who can do an adequate or even superior job in the analysis stage but cannot present the data in a form that is understandable and reasonable for a trier of fact to adopt.

Conversely, there are experts who tell a good story but do not have the analytical skills required. They either have others do the analysis and step in personally only to provide the testimony or they do scant analytical work and rely on their testifying skills to carry the day. Finding both skills in one expert brings efficiency to the damages phase of the case.

Regardless of the venue (jury trial, bench trial or arbitration), the ability to present the conclusions in an easily understood presentation that is backed up with substantial data not only can win the case, it can also assist in settling

the case before incurring the expense of a trial.

### Typical Business Cases

Forensic accounting can be a valuable resource for virtually any type of legal controversy related to business issues. Here are a few examples:

- **Bad Faith.** Although insurance companies owe a duty of good faith in dealing with the persons they insure, violation of that obligation occurs in commercial policies that can involve huge sums of money. Examples of bad faith include undue delay in handling claims, inadequate investigation, refusal to defend a lawsuit, threats against an insured, refusing to make a reasonable settlement offer or making unreasonable interpretations of an insurance policy. Forensic professionals provide objective and independent evaluation of the economic and financial issues involved in insurance claims/bad faith litigation.
- **Breach of Contract.** When a party fails, without a legally valid excuse, to live up to responsibilities under a contract, there are typically widely varying opinions between plaintiff and defense as to the damages incurred from the breach of contract. Forensic accountants investigate and analyze lost revenues, lost profits, lost opportunities and unjust enrichment.
- **Business Interruption.** Business interruption matters involve loss of income resulting from a temporary shutdown, destruction of property, fire or other peril. Typically, insurance coverage is purchased to protect against such business expenses and loss of income. Since insurance policies differ significantly as to their terms and conditions, forensic accountants are often asked to assist either the insured or insurer in the appropriate method of calculating the loss.
- **Fraud, conversion and misappropriation of funds.** Increasingly, businesses are being victimized by embezzlement and fraud, serious and costly crimes. When such crimes are detected,

litigation may be necessary for recovery of losses. Forensic professionals work assist in determining the extent of monetary loss or damages and to determine who committed the fraud. For example, the investigator may review or reconcile the company's bank accounts, identify payees, track electronic transfers and payments through the company's general ledger, and scrutinize documents supporting check disbursement, such as vendor invoices and expense authorization. They also utilize various investigative and analytical procedures to support criminal or civil actions against an individual(s), provide evidence for insurance claims, and uncover hidden assets in bankruptcy or divorce situations.

- Partnership/Shareholder/Officer/Director Litigation. A forensic accountant may play a significant role through an objective and independent evaluation of the economic and financial issues involved in partnership disputes and dissolutions. This involvement may

include assistance with technical and complex discovery issues, case strategy and investigation and analysis under several different scenarios.

- Trade Secret and Unfair Competition. Forensic accountants are typically engaged by either plaintiff or defense counsel to determine whether and how the theft occurred, the economic damages incurred, the financial benefit or loss incurred by competition and the value of the stolen asset. Such investigation involves calculation of projected lost sales and profits, customer retention analysis, reverse engineering gains by competitors and other quantifiable results of the alleged theft.
- Wrongful Termination. In wrongful termination cases, the plaintiff seeks to receive compensation for the economic loss sustained by the firing, most of which is typically lost earnings. A forensic professional might be retained by an employer or employee to provide objective

and independent evaluation of the economic and financial issues involved in such matters.

These are only a few of the many different scenarios in which commercial litigators can effectively utilize a forensic professional. Other common matters include commercial collection, debtor/creditor litigation, disputes concerning the sale or purchase of a business, dissolutions of corporations and partnerships, lender liability, product liability, trade libel and Uniform Commercial Code disputes.

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