



Forensic Accounting, Business Valuation and Consulting

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**The Burden of Proof:
Lost Profits and Economic Damages**

by Michael J. Mard, CPA/ABV/CFF, ASA

Note: Portions of this article are excerpted from a recent article by Michael J. Mard published in The Licensing Journal

An attorney and friend, who long ago taught me the most about the reality of trials and litigation, once said civil litigation and particularly damages is like a three-legged stool: the plaintiff has to prove liability, damages and collectability. If one leg is not there, the stool falls over. We would now add the top or seat of the stool is the Rules of Evidence such that all three legs have to be proved to a reasonable certainty based on a preponderance of the evidence. The reality of a plaintiff's situation centers on the task of proving to a reasonable certainty all three legs of the stool within the confines of the Rules of Evidence. This can be very difficult.

Causation

A claim for lost profits and economic damages must be proven relevant. There must be a cause and effect, a premise, a link between the alleged action by the defendant and the measured impact. The liability must link to the damage amount. It is the plaintiff's lawyer's responsibility to assure this causation of liability is established by the evidence. Sometimes this is straightforward (perhaps with a trade name violation) and sometimes very difficult (perhaps with a product liability or professional malpractice claim). In any event, causation should not be assumed and the evidence may or may not be able to be established by the damages expert (generally an economist, accountant or appraiser). Paraphrasing one Court's ruling in favor of a defendant's motion for summary judgment: The plaintiff must establish THAT specific train caused THAT specific spark igniting THAT spe-

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Hot Topic: Damages

“Bullet Holes vs. Bullet Proof”

Key Issues in Cross-examination

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cific dried grass leading to THAT fire resulting in the destruction of THAT defendant's business. Causation is an area that varies with the facts and circumstances of a specific case. Additional discussion is beyond the scope of this article. Suffice to say the issue should be discussed at length by the plaintiff and counsel.

Reasonable Certainty

The fact of damages must be

separated from the amount of damages. Perhaps a tort has occurred in which defendant damages have not occurred. Of course certain venues allow a claim of statutory damages (copyright law comes to mind) but that too is beyond the scope of this article. The determination of reasonable certainty rests with the court. Evidence might first establish that damage has occurred but the measure of the amount of damage does not rise to the level of "reasonable certainty." Given the nature of measurement, lost profits would normally be based on a reasoned conclusion including the expert's use of reliable factors in the calculations. Speculative and problematic evidence normally is excluded. I will often tell clients that lost profits are profits that are lost. You (client) must first lose established profits before you can make a claim to recover such lost profits.

Conclusion

Competent professionals, in-

cluding lawyers, economists, accountants, appraisers and other witnesses, must use appropriate judgment in applying the facts and circumstances to a specific claim.

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ACCOMPLISHMENTS

On September 30, Michael Crain (Ft. Lauderdale office) will complete six years of service on the American Institute of Certified Public Accountants (AICPA) Forensic and Valuation Services Executive Committee. His first three years were spent as an ex officio member when he was chairman of the AICPA's business valuation committee. The executive committee is one of only a few AICPA bodies who are authorized to issue professional standards and speak on behalf of the profession.

Getting the Most From Your Expert

By Michael J. Mard, CPA/ABV/CFF, ASA and Deanna Muraki

A Message to Lawyers:

Valuation experts have become a necessary part of most corporate litigation, from shoring up a defense in an estate tax filing claim to proving lost profits and business damages. In most cases, it is the attorney's job to locate a valuation expert. It has become more common for experts to be retained directly by the client—in fact, many experts require it. However, it is you, the attorney, who will be held accountable for the entire cost of litigation, including fees of the expert. Therefore, managing the assignment includes your management of the expert, even if the expert's agreement is directly

with the client. The following sections highlight several key areas that will assist you in this task.

Know the Applicable Standards

Broadly, familiarize yourself with the standards the expert is obligated to follow. You do this by asking your expert for two or three broadly accepted pronouncements, periodicals, aids, or books. For example, all CPAs who perform business valuation services must adhere to the American Institute of Certified Public Accountants Standards for Valuation Services No. 1, published in 2007. For Federal cases, the expert's report

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Look for one of FVG's professionals at these upcoming events:

FCG University - Atlantic City, 9/9-10
Knowledge Congress webinar - 9/23
NACVA/IBA Congress on Fair Value -
Seattle, 9/27-28

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must conform to Rule 26 of the Federal Rules of Civil Procedure. In addition, you should closely review the expert's Curriculum Vitae and Record of Testimony.

Broad Parameters

The lawyer has an obligation to oversee; that does not mean micro-manage. You should confirm with the expert that all material information produced in discovery, including depositions, has been appropriately considered by the expert. In large cases, there should be mechanisms established to reconcile document controls between you and the expert. You should share philosophies with the expert, whether conservative or aggressive, and be aware of whether the expert's reputation is that of consistency. It is, of course, the expert's job to aid the Court, not advocate for a client.

Know also that an experienced expert can provide insight into the nuances of the valuation methodologies. There is a reason they are considered to be experts—listen to them!

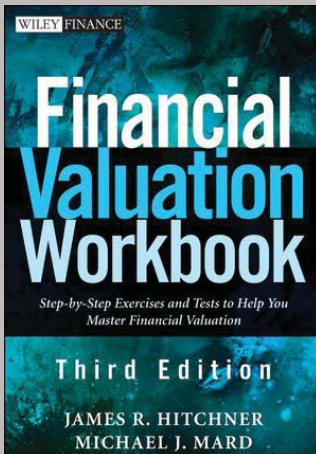
You should obtain a rough fee estimate from the expert. Keep in mind, though, that any fee estimate will be broad—it is virtually impossible to foresee all events that may unfold during the litigation process that might necessitate additional work from the expert, such as attending depositions or assisting in developing interrogatories.

Review

You should plan to spend some time with the expert as the assignment progresses. You and the client should review the expert's work product for factual input (not professional judgment). Remember, if a draft report is issued, it is discoverable.

Conclusion

Managing the valuation expert requires planning, monitoring collected data, and reviewing the expert's work product. This process will go far in informing your client and managing your case. At the end of the litigation, there should be no surprises related to the presentation of your case or resulting fees. By working closely with the expert, your client will benefit. ~~



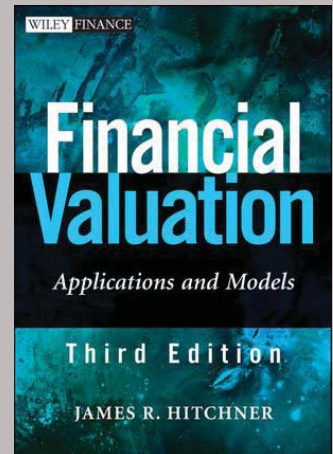
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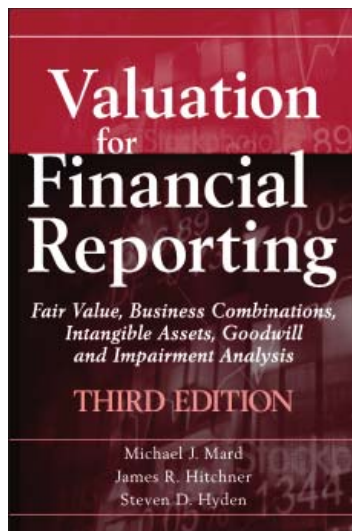
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Valuation for Financial Reporting

3rd Edition

This 3rd edition from valuation experts Michael J. Mard, James R. Hitchner, and Steven D. Hyden provides the most current guidance to date on Fair Value for business combinations and impairment promulgated by the FASB.

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