The best bits by FAR

Introduction

Welcome to the Autumn edition of FAR Consulting's quarterly newsletter.

In this edition of the newsletter we are pleased to announce that Simon Paley, a senior and experienced forensic accountant will be joining us in the Midlands (See below).

Following the recent widespread flooding, we also include a couple of articles looking at the impact of business interruption. In the first article Phil Southall looks at the practical steps that should be taken by a business that suffers an interrupting event, and in the second, “Evidence! Evidence! Evidence!” I consider the key decisions that need to be taken to ensure any losses are fully recovered. We look at this from the perspective of retailers.

In our final piece, the first of three exploring pension losses in personal injury claims, “Pension losses… it’s all Greek to me!”, we take a look at the types of pension schemes that there are. Over the course of the next two newsletters we then consider how losses are calculated.

Yours sincerely
Greg Lacey, Managing Director

FAR continues to expand


Simon Paley

We are pleased to announce that Simon Paley has joined the team as Forensic Accounting Director.

Simon, who has been at Ernst & Young for the last 16 years, is our most senior level hire to date.

This is a very significant appointment for our Midlands operation and for the business as a whole. Simon is a hugely experienced forensic accountant with wide ranging expertise. We are thrilled at having yet another experienced and highly respected expert in our ranks. He has a major role to play as we continue our expansion and increase our market presence.

On his decision to join the team, Simon Paley said: "I was happy at Ernst & Young but when the management team at FAR outlined their plans for the business, I knew it was time to make the move."

"FAR Consulting is a young and dynamic business with exciting growth plans. In the current marketplace our business model also provides us with a significant competitive advantage."

FAR Consulting provides forensic accounting services direct to corporate clients, law firms and individuals.

As well as providing the "traditional" expert witness service, uniquely within the UK, we also provide in-house forensic consulting services to a range of lawyers, insurers, insurance brokers and other firms of accountants. This service enables additional flexibility, ensuring advantages to both solicitors and end clients throughout any forensic assignment.

We operate as a virtual business, employing a number of experienced forensic accountants who all work remotely. Because we don't have any overheads as such, we are able to price our services very competitively, but perhaps more interesting than that, it means that we are also able to provide in-house accounting support to law firms on a consultancy basis.

FAR CONSULTING

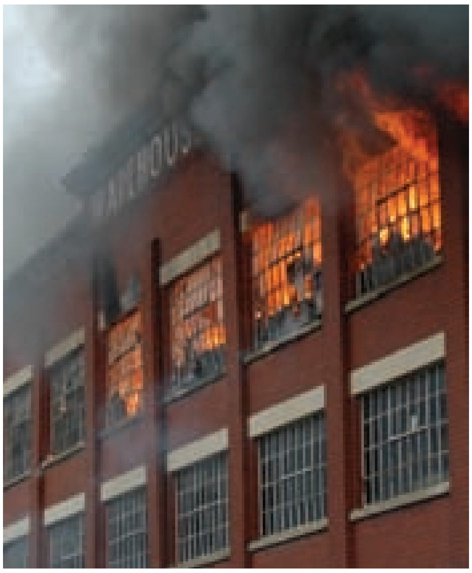
FAR Consulting Limited, PO Box 555, Stockport SK4 3WF. Tel: 0161 431 6263 Email: info@farconsulting.co.uk Website: www.farconsulting.co.uk

Bases also in Birmingham and Liverpool

Business Interruption

The steps you should take to bring a successful claim

Phil Southall explains...



Interruption to businesses can occur for many reasons. One such incident would be the flooding which has affected large parts of the country recently. However, whatever the timing or cause of the interruption there are always two common factors:

- it is always a major inconvenience to the business, which can often impact upon profitability and the individual employees within the company; and
- from the forensic accountant's point of view, the task is more or less the same. Our role is to establish how the business was performing prior to the incident, and assess how it would have traded were it not for the interruption.

The key to bringing a successful claim is evidence evidence EVIDENCE! Therefore, if you or any of your clients have been affected by the recent flooding, or any other interrupting event, and are considering preparing (insurance) claims, then the following checklist, summarising the key things to be considered at the outset of preparing a claim, may be of use.

Establish "the team"

1.1 Establish the claim team consisting of an individual/a small number of key individual(s) responsible for liaising with:

- external advisors (solicitors, accountants, loss adjusters etc);
- internal "ground level" staff regarding the disruption, essentially requesting, collating and presenting information to external advisors;
- senior management - keeping them informed of developments; and
- overseeing recording of all "management"/internal time spent (see below).

1.2 If a number of departments/sites are affected, it may be beneficial to have one person collating all departmental/"on-site" information. This may usefully reduce the number of lines of communication, and can be used to effectively remove certain responsibilities from the key individuals.

What to do immediately

1.3 If a simple set of procedures is established as soon as possible after the interrupting event, the task of collating the information and evidence can be substantially improved and effort reduced. Whilst such processes should be designed not to interfere with the operation of the business at this time, it will enable the business to recover faster once the situation has "normalised", as management can focus their time and effort in driving the business forward once more, safe in the knowledge that the information necessary for supporting their claim has already been successfully captured.

1.4 The key individual(s) should take responsibility for designing these procedures, which should be designed to capture:

a) all material damage information regarding:

- buildings;
- other assets, such as machinery, vehicles, furniture, fixtures and fittings etc;
- IT and telephone equipment, plus any associated infrastructure costs (network charges);
- consumables, such as stationery and marketing materials; and
- (if appropriate) staff personal assets held on site.

b) all additional personnel cost information for own staff, including overtime, any temporary staff and any contractors/specialists required, and also including any **management time**.

This can be something as simple as timesheets or diary entries that are kept/sent to key individual(s) on a weekly/monthly basis to evidence the amount of time spent dealing with the disruption and subsequent claim, particularly where they have been redeployed or reallocated as a result of the disruption, or when work has been deferred/cancelled. The time recording should continue into the preparation of the claim phase, particularly for key individual(s).

c) all other additional cost information, together with documentary evidence of the cost where possible (e.g. invoices/receipts):

- relocation costs – such as additional rent, utility costs, logistics costs etc;
- replacement/rectification costs for items damaged;
- travel, accommodation and subsistence costs;
- additional financing costs;
- additional security costs;
- disposal costs (if appropriate, e.g. if specialist disposal of equipment is required); and
- external advisors costs

d) other financial documentation, particularly relevant if bringing a claim for consequential losses, including:

- information from loss adjusters, insurers, advisors etc both "verbal" and written (which may be used to support business decisions made);
- any penalties or charges e.g. payable for late deliveries;
- any adjustments made to the accounts or targets, which affect bonuses;
- and evidence of cost savings e.g. if overtime curtailed etc;
- evidence of specific lost orders; and
- historical management accounts, budgets/forecasts/cash flows/targets.

This only refers to data/reports that are already readily available or can easily be retrieved, and no new documentation out side of normal financial reporting documentation should be created in this regard.

e) all other relevant documents such as:

- minutes of meetings;
- correspondence with advisors or third parties; and
- any accounting entries/adjustments (see below).which any third party reviewing the claim will expect to have sight of.

1.5 Therefore, it is best to bring the claim to the attention of all employees likely to be affected by the claim as soon as possible to ensure:

- time is recorded appropriately and accurately;
- information is provided on a timely/contemporaneous basis; and
- all subsequent internal reporting (e.g. minutes of meetings) is consistent with the claim.

1.6 Depending on the extent of disruption it may be beneficial if a separate cost code or codes is/are added to the accounts to capture specifically "disruption" related expenditure. This will make their subsequent identification easier, as other margins/metrics should remain unchanged throughout this unusual trading period.

Evidence! Evidence! Evidence!

Following a business disruption after a flood there are a number of key financial decisions for retailers to make in order to ensure optimal recovery of losses. Greg Lacey summarises the issues that arise and the decisions to be made in order to avoid any unnecessary criticism from any third party liable for the disruption.

The first point to bear in mind is that at all times the independent retailer must attempt to mitigate the loss to the business. It is necessary to do this not only for obvious commercial reasons but also in order to be able to expect to recover all of the losses suffered from any third party, including an insurer. In order to demonstrate this it will come down to evidence.

Assuming a temporary closure, the first issue to consider is what should be done in the short-term with stock and staff?

For retailers with multiple stores it may be possible to transfer both stock and staff to other sites. Single site retailers will need to consider options for alternative (temporary) sites. These decisions will take account of factors such as the nature of stock (e.g. perishable goods, high end fashion garments), demand against supply of stock and the mobility of staff at the affected store. Obviously if stock has been damaged it goes without saying that an inventory should be taken of all damaged stock, as well as the remaining good stock. This will be a primary concern for loss adjusters.

Any steps that are taken to mitigate the loss should be looked at in terms of whether the benefit to the retailer exceeds the cost. Costs affected should be recorded and evidence retained – typically these costs will include:

- additional logistics costs (destocking/restocking);
- staff overtime costs or savings, at the affected store and any stores receiving re-deployed staff;
- (sales related) staff bonuses, both at the affected store, and at stores receiving any staff and/or stock or local to the affected store;
- incremental warehousing costs;
- additional financing charges;
- cost of management time dealing with the disruption; and
- any external advisers' costs.

In the case of any disruption that causes the store to temporarily close, the next issue to address is when should you re-open?

Where all stock has been removed, restocking can cause logistical problems and can complicate the decision of when to re-open. It can be a fine line between escaping criticism for re-stocking too early and opening prematurely, and being criticised for delaying opening until a full-stock profile is in place.

The decision when to re-open may also be dictated by the terms of your insurance cover. For many, policy terms may mean that the recoverable loss period ceases once the store has re-opened, however, realistically depressed trading conditions may continue a long time after re-opening which will mean profits may not have recovered before the insured period ceases. For some, therefore, it may come down to deciding whether it is worth re-opening at all!

Any "cost/benefit" analysis undertaken to support the decision when to re-open should be documented and evidence retained in order to justify the decision later on. If the decision is made in good faith and you have evidence to support this, this will go along way to protecting your position.

Once trading "normally" again the full extent of any potential claim can be considered. Collating the information and evidence necessary to support a claim can be an onerous task. It is therefore important to document and retain as much information/ evidence as possible during the disruption.

In assessing any loss of revenue suffered, it is appropriate to look at how the business was performing prior to the disruption and assess how it would have performed had the disruption not occurred. This may be complicated by having to take account of transferred sales to other stores (or a pick up in online sales).

Single site retailers will need evidence regarding the affected store's sales and gross margin over previous years, and/or budgets/ projections, in order to assess what its performance would have been but for the disruption. Multiple site retailers should also consider obtaining this evidence, along with actual results over the affected period, for any comparable stores within its portfolio. Notwithstanding the specific damage caused by flooding, it will be necessary to consider the impact that the poor weather might otherwise have had. This is obviously easier to do for multiple site retailers, as other stores' performance will provide some guidance on this.

Finally, to assess the benefit from transferred sales, turnover and gross margin information may be required for other local or online stores within a retailer's portfolio.

Most reasonable costs should be recoverable, including management time and any external advisers' costs; however, it is important to record these costs as you go along.

If the decisions taken to minimise the effects of the disruption are correct and are fully supported by underlying evidence, it should be possible to recover all the losses successfully from any third party liable for the disruption. If unjustified decisions are taken, and there is insufficient evidence to substantiate the losses claimed, it may be that not all of the losses suffered will be recoverable.

FAR Consulting is an independent firm of forensic accountants specialising in providing advice and dealing with loss claims on behalf of companies and individuals. Their clients include a number of the UK's leading retailers, law firms and insurance companies.

Οι συνταξιοδοτικές απώλειες... αυτό είναι όλα τα ελληνικά σε με!

(or "Pension losses… it's all Greek to me!")

In this, the first of three articles, Greg Lacey aims to provide a rough guide to pensions and pension losses, a sort of "Essential phrases and basic vocabulary" if you will. We try to explain the different types of pension schemes and more importantly, what to look for when dealing with a pension loss claim. In this quarter's newsletter we look at the basic types of pension scheme and their key features. Over the course of the next two newsletters we shall consider how to assess the loss for a "defined contribution scheme" and a "defined benefit scheme".

The basic types of pension

Pension loss calculations can often appear complex. However, the basics should be straightforward once you have established what sort of pension scheme you are dealing with. As well as the state pension, there are generally two types:

- defined contribution schemes, also known as money purchase schemes; and
- defined benefit schemes, otherwise known as final salary schemes.

I think it fair to say that dealing with defined contribution schemes is potentially simpler, at least conceptually, than dealing with a defined benefit scheme. So let's look at defined contribution schemes first.

Καθορισμένα σχέδια συμβολής

or "Defined contribution schemes/ money purchase schemes"

Members of a "defined contribution/money purchase schemes" contribute a proportion of their salary into an investment intended to create a fund from which an annuity is purchased on retirement. Basically, you save cash and this then forms a fund from which, on retirement, you then buy an annuity, which pays you an annual income for the rest of your life.

These types of scheme may be classed either as "personal schemes" or "occupational schemes" – the difference between the two is that one is operated by your employer, whilst the other will be set up and operated by individuals in a personal capacity. Typically employers will pay contributions into an occupational scheme, although sometimes they will also pay into a personal scheme, although this is rarer. If you are really lucky your employer will pay into a scheme without requiring you to contribute, although quite whether the level of their contribution is sufficiently generous so that you then do not need to contribute anything additional is an entirely different matter.

The size of the fund, or "pot", available on retirement is determined by the level of contributions made during the working life of the scheme member and the investment returns achieved over the life of the fund. It is therefore the member who shoulders the risk of receiving a lower than anticipated pension if insufficient contributions have been made, and/or the investment returns are lower than projected.

The pension will often be index linked in some way, meaning that once the member starts drawing the pension it will increase in value each year to take account of inflation. Most schemes are index linked on the basis of the Retail Prices Index ("RPI"), which itself is outpaced by average earnings, which means as time goes by pensioners enjoy a lower increase in pension than those still working. Which in reality means that the standard of living achieved by a pensioner on retirement will stand still and will most certainly be outpaced by that for someone still working.

A member of a defined contribution scheme will often also have the choice to opt to make provision for a spouse's pension, which means that on the death of the member, his or her spouse will continue to receive a pension benefit, albeit at a reduced level to that paid to the member, typically this is half or two thirds the rate paid to the pension scheme member. By making provision for a spouse's pension the member's overall pension payable on their retirement will also be reduced to take account of the fact that the accumulated pot will have to fund an additional pension payable to the spouse. (NB: the spouse's pension can often be overlooked in loss of dependency and earnings claims, but can add considerable value to a claim).

Καθορισμένα σχέδια οφελών

or "Defined benefit schemes/final salary schemes"

A "defined benefit scheme" is an occupational scheme (i.e. will be run by employers), and is designed to give a member the right on retirement to a pension for life that is usually dependent on two factors:

- the value of a member's final salary at the time of retirement; and
- the number of years service completed with that employer by the member.

Again, these schemes also usually make provision for indexation (see above).

There is usually a requirement that a member contribute towards the scheme, but the actual level of contribution is irrelevant in determining the final pension that will be received as the pension received does not depend on the amount contributed, or the investment performance of the pension fund itself. If there is any shortfall in the funding of the scheme, it will fall to the employer to make up the difference.

From an employee's perspective a defined benefit scheme is often seen as preferable to a money purchase scheme, the reason being that the final pension is a known amount, and any risk in funding the pension is borne by the employer. Conversely, from an employer's

perspective the money purchase scheme is usually more preferable as the employer is not liable to top up any shortfall in funds, and furthermore there is no need to disclose any pension fund shortfall in the company's accounts. As a result of this, defined benefit schemes in the private sector have fast been closing to new members, albeit they still remain commonplace in the public sector.

You will have seen lurid headlines over the past few years concerning pension deficits at many leading companies in the UK. The deficits have arisen due to increasing mortality rates, the poor performance of the stock market and companies in the past having taken contribution holidays when stock market returns were sufficiently high to indicate schemes at that time were overfunded. Improving stock markets have now left these deficits much smaller than they once were. Due to the closure of many private schemes, you are more likely to come across defined benefits schemes in the context of public sector employees such as nurses, members of the armed forces, police and fire services and Council employees.

The approach to assessing the pension loss is different depending on whether you are dealing with a defined benefits scheme or a money purchase scheme. In our next newsletter we explain the approach to assessing losses from a defined contribution scheme, the issues to look out for and also look at a worked example. In the following quarter's newsletter I shall do the same for defined benefit schemes.

www.farconsulting.co.uk forensic accounting and risk consulting

FAR Consulting - Key contacts

Greg Lacey
Managing Director

Greg, a Chartered Accountant, has specialised in forensic accounting for over ten years. Greg has represented many of his clients at mediations and as an expert witness. He has prepared reports as an expert, a single joint expert or court appointed expert. He has experience of high profile cases involving contract and pricing disputes, completion accounts disputes, product recalls and royalty disputes, gained whilst acting for a number of high profile clients across a broad spectrum of sectors.

Direct line: 0161 431 6263
Mobile: 07788 914 188
Email: greg.lacey@farconsulting.co.uk

Phil Southall
Forensic Consulting Director

Phil is a Chartered Accountant with eight years of post qualification forensic experience during which he spent over two years working as an in-house forensic accountant at a national law firm. His almost unique experience in this role and extensive forensic background make him ideally placed to advise on settlement strategies, using “decision analysis”techniques, which analyse a client’s potential costs, risks and rewards of being involved in litigation.

Direct line: 0121 384 7270
Mobile: 07782 300 312
Email: phil.southall@farconsulting.co.uk

Simon Paley
Forensic Accounting Director

Simon Paley is notionally based in Birmingham. Before joining FAR Consulting, he worked in Ernst & Young's forensic accounting team.

Simon has over 10 years' forensic experience, principally in commercial and contractual disputes, with a particular interest in insurance claims. He also has a broad experience advising clients on purchase price adjustment mechanisms, completion accounts, breach of warranty claims and other transaction-related disputes.

He has provided advisory and expert witness services to clients involved in disputes across a wide range of industries and has experience of most forms of dispute resolution.

Direct line: 0121 459 3826
Mobile: 07747 864 074
Email: simon.paley@farconsulting.co.uk

Teresa Morrison
Forensic Accountant

Teresa is a law graduate and qualified as a certified chartered accountant in 2002. After working for a small practice specialising in preparing accounts from source data, gaining significant experience of reporting on incomplete records, Teresa chose to specialise in forensic accounting.

Teresa has experience of business interruption claims acting on behalf of a number of major high street retailers and breach of fiduciary duty claims, including a multi-million pound claim involving several household names.

Mobile: 07747 864 075
Email: teresa.morrison@farconsulting.co.uk