Forensic Accounting Today

Newsletter of Ron J. Anfuso, CPA/ABV, An Accountancy Corp.

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Issue 69

Serving all of California

Ron's Corner

In issue 68 of ***Forensic Accounting Today***, I briefly discussed a case involving reasonable compensation in which I prevailed. This was a complex case involving the purchase of several accounting practices by Petitioner both before and after the couple's date of separation.

I have decided to devote this and at least one following newsletter to a detailed presentation of this case. Because it has not been published, I've chosen anonymous names for the parties and used fictitious dates and numbers.

I think you will find this case, which I'll call *Lawler versus Lawler*, informative. Complicated cases such as this inspire and stimulate me because I have the confidence and energy to draw on all my knowledge and skills to prepare and present logical conclusions that typically result in favorable decisions by the courts.

Cases such as this one require a more thorough knowledge of forensic accounting and pertinent case law. They also require the ability to discern, critically think and correctly apply the right forensic accounting principles based on the facts of the case. Then, should the case go to trial, it requires testimony that is so on target it becomes difficult to successfully challenge. This case is especially demanding because proceedings concerning reasonable compensation require both objective and subjective logical conclusions.

In this case, I represented Respondent. I refer to Petitioner's forensic accountant as "*The Other FA*."

Should you have questions concerning this case or reasonable compensation, I welcome you to contact me.

Ron

Determining Reasonable Compensation

(Part 3)

John Lawler Versus Carol Lawler (Respondent)

Presented by Ron J. Anfuso, CPA, ABV, CFF, CDFA, FABFA

John and Carol Lawler were married in September of 1992. The parties separated for the final time on November 30, 2017.

Petitioner worked at home as a CPA. In 2007, although he continued practicing as a CPA, he began working primarily as a business development consultant, and then began acquiring other accounting firms.

Prior to their separation, Petitioner had acquired the *Lancaster Accounting Firm*. Petitioner testified he paid \$3 million—\$300,000 came from personal savings, \$2.5 million from a bank loan, and the seller carried back \$200,000. The loan was secured by the assets of the practice and guaranteed by the parties. Petitioner had a limited guarantee, which required the lender to review the practice's assets and then to look to Petitioner for repayment, but not to Respondent. Respondent was aware of the opportunity to purchase the practice and knew she needed to sign documents.

After physical separation but prior to the parties' stipulated date of separation, Petitioner's firm purchased the *Stamford Accounting Firm* (in 2016). Then in 2018, the firm bought the *Roxford Accounting Firm*. The Stamford's purchase price was \$1.3 million. Petitioner made a \$70,000 down payment, received a bank loan of \$900,000 and a carry-back loan of \$330,000. His \$70,000 came from a business line of credit.

Petitioner testified that he gained about 600 new clients through the acquisition of Stamford and retained

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approximately 60 percent. From Roxford, Petitioner gained roughly 750 new clients and maintained about 80 percent.

Petitioner made a $200,000 down payment for the Roxford firm from a client loan of $250,000. The balance was used for working capital. The purchase price was set at 15 percent of the revenue received by Petitioner from former Roxford clients for a period of seven years. In 2020, the amount received was $180,000 and about $340,000 in 2021. Petitioner did not book this as a liability or equity. When questioned why, he testified that he keeps the books on a *cash* rather than an *accrual* basis of accounting.

After the date of separation and less than a week before the trial began, Petitioner's firm acquired the *Gould Accounting Firm*. The terms of purchase were $150,000 down and 18 percent of gross receipts from Gould's clients over the next five years.

Stipulations Agreed to for the Trial

- The date of separation was November 30, 2017
- The date of trial valuation for Lancaster, Lawless, Roxford and Stamford (LLRS) was established as November 30, 2021. However, the parties also stipulated that the issue of alternative valuation would be heard at the time of trial. The Other FA's position was that the business should be valued as of November 30, 2017, while my position was that the business should be valued as of the date of trial (November 30, 2021).
- The Petitioner's cash flow available for support each month was set at $225,000.

My Testimony Concerning the Date of Valuation

I testified that the business is most appropriately valued at the date of trial because valuing at the date of separation is only appropriate when the personal efforts of the in-business spouse are the primary reason for any increase in value. The facts of this case indicate that LLRS's revenue came from the work of multiple CPAs and staff who bill and generate income for the firm, not just from Petitioner. My understanding was that as of December 31, 2021, there were about 28 separate accountants billing hours for LLRS.

Furthermore, I testified that there was no way to capture the community property borrowing power without using a date-of-trial valuation. This was because the existing community property company was leveraged to get the SBA loan for the Stamford acquisition. Also, the company was leveraged to get a client loan to acquire the Roxford firm, and the company was leveraged to acquire the Gould firm, which did not involve a loan.

The court found that my reasoning "was persuasive" and the date of valuation was set at November 30, 2021.

Positions to Be Addressed

Petitioner's stance was that the business was partially community and partially separate. He believed the business should be allocated to him at a value of $2,364,000 based on a valuation date of December 31, 2017. Petitioner's alternative position was that LLRS should be valued as of the date of trial at $3,125,000 and awarded to Petitioner at that value.

Respondent's position was that the business was entirely a community asset and should be allocated to Petitioner at a value of $4,100,000.

In the next issue of ***Forensic Accounting Today***, we will consider the positions taken by the forensic accountants and provide the rulings by the court.

For an explanation of these titles, please visit our website or request a copy of Issue 3 of* ***Forensic Accounting Today**.*