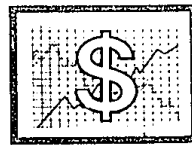


Business

Marilyn Fitchett editor/591-2300



(FHC)

Account-ability

CPA firms face liability issues as malpractice rates balloon

By Philip A. Sherman
special writer

"With respect to the _____ process, there's nothing wrong with it. It's just like airplanes. They're basically sound vehicles that fly thousands and thousands of miles every year. That doesn't mean something won't occasionally go wrong or the pilot occasionally won't make an error."

If you fill in the blank with a reference to the medical profession, it probably would fit but wouldn't necessarily be correct in this case. The quote, from Jerry Hepps, is about the occasional mistake professionals make that turns into a huge malpractice lawsuit.

The profession he's referring to is accounting, one of the latest, relatively speaking, to join the duck-and-cover world of ostensibly serving clients while hoping like crazy they won't turn around and sue in the event of an error.

Hepps is the partner in charge of professional standards at Plante & Moran in Southfield, one of the area's top five accounting firms that does the books for a wide variety of companies. He sees recent mounting criticism of mistakes in what's commonly termed "the auditing process" as unfair, particularly for himself, his company and his colleagues.

"The auditing profession really provides useful services by providing credibility in financial reporting. Who else could do it?" Hepps said. In answer to his question, some might say they'd rather do it themselves.

THAT'S EVIDENCED by inquiries as recently as 1985 by Congress, probing for answers to the

'Liability is true throughout the country, not just in our profession. Costs are up and we have more litigation. They're (clients) prone to sue because we have relatively deep pockets.'

— Harold Dubrowski
of Grant Thornton

question of who is liable when an audit is incorrect. An article in Management Accounting magazine cites the number of lawsuits filed against CPA firms and attaches a dollar amount to requested damages — \$2 billion. The article says errors great or small have cost the country's eight largest accounting firms almost \$180 million to settle audit-related cases and notes "another major CPA firm has paid \$137 million in judgments and settlements over the last five years."

What does it mean? For one thing, charts tracking liability insurance costs for accounting firms have lines that start at the floor and go through ceiling vents. Harold Dubrowski, managing partner of Grant Thornton of Southfield, said he knows of one small firm whose \$100,000 policy used to cost \$5,000 and went up to \$34,000 in one year.

Hepps said accounting firms vigorously apply quality control standards to the point of having peer reviews every three years. The reviews at this time are voluntary — Hepps noted Plante & Moran just completed its third — but there is talk of making them mandatory. Hepps is an executive committee member of the Division for Firms, an SEC arm, he said, "formed back in the '70s after a lot of heat from Congress about accounting firms."

EVEN IN A TIME of increasing litigation, Dubrowski sees most firms growing, not necessarily due to the auditing process but rather due to what he called "peripherals."

"Accounting firms offer three standard products: the compilation, which just compiles numbers with no analysis; the review, which is analytical with no testing; and the audit, which is analytical, includes outside testing and opinion," Dubrowski said. "But the area that's really making money is consulting, human resources and strategic planning."

Dubrowski said consulting is the highest growth area in the profession, and cited Arthur Anderson's consulting department as an example, calling it the "single largest in the world." He said consulting is a big seller because it teaches time-saving techniques through computers and couples those with more efficient statistical acrobatics.

"But liability is true throughout the country, not just in our profession. Costs are up and we have more litigation. They're (clients) prone to sue because we have relatively deep pockets," Dubrowski said, which has the effect of making firms scrutinize high-risk clients before signing them up. He defined high-risk, for example, as one with which a firm has had no previous experience.

Hepps' view of the malpractice problem can be likened to that of the medical profession. Basically, a few doctors are being negligent or their patients while the overwhelming majority are practicing their profession with skill and dignity. "We're still going to run into pilot error occasionally, but few cases result in court decisions where auditors have done a good job. For each one, thousands have gone on without one problem."

Chamber boss promotes southeast Michigan

Attorney Richard C. Van Dusen, as the newly elected chairman of the Greater Detroit Chamber of Commerce, sees improvements in education and the crime situation as keys to improving southeast Michigan as a place to live and do business.

Van Dusen, a Bingham Farms resident and chairman of the law firm of Dickinson, Wright, Moon, Van Dusen and Freeman, was elected chairman in June and will serve a one-year term.

"The importance of elementary and secondary education, particularly in Detroit, will be a critical issue along with the improvement of the crime situation and improvement of Detroit and southeast Michigan's image," Van Dusen said.

"We have now embarked on a program to improve the quality of education and reduce the dropout rate and improve that system which needs help," said Van Dusen of Detroit Public Schools.

PROMOTING A greater understanding of Detroit and southeast Michigan is a vital chamber goal, said Van Dusen.

"We work on improving understanding on the part of business and civic leadership from outside Michigan with their counterparts in southeast Michigan," he said. "It promotes southeast Michigan and a greater understanding."

The chamber recently hosted visits from a number of outside legislators and has sponsored visits from business and civic leaders in Grand Rapids, Kalamazoo and Marquette in the past.

On the legislative calendar, Van Dusen says the chamber will be tackling the issue of product liability.

"We are very interested in seeing improvement in the law regarding product liability so producers are not hauled into court every other day," he said.

The 3,700-member chamber is also opposed to proposed parental leave legislation.

"Legislation has been offered in Lansing which would



BILL PARKER/Staff photographer

Richard C. Van Dusen: "We are very interested in seeing improvement in the law regarding

product liability so producers are not hauled into court every other day."

be extremely burdensome, especially for small businesses," he said.

He says the chamber is not opposed to maternity leave, but the proposals are so draconian in their effect that it would be extraordinarily burdensome for some

care of a child or the serious illness and care of dependent.

All employers of two or more employees are included and must provide each employee of more than one year with up to 180 days of parental leave. Sixty days at full pay with benefits continued at the employer's expense and 120 days unpaid with benefits continued at the employee's expense is required.

The employee would also be restored to the position held prior to the leave upon a return to work.

Van DUSEN SAYS the chamber has, from time to time, addressed social issues, specifically hunger.

The chamber took a major leading role in providing food for the hungry," he said.

Project Pride, another chamber program, helps keep neighborhoods clean by aiding in various cleanup activities, including removal of abandoned cars.

One of the chamber's activities is Leadership Detroit, which involves more than 50 young potential leaders in programs designed to acquaint them with the business, social and government structure in Detroit and also leadership in the area, says Van Dusen.

Van DUSEN has been on the chamber board of directors since 1982. The board is made up of 54 business leaders who represent a cross section of business interests including manufacturing, retail, service, utility and health care.

His former positions in the chamber include assistant treasurer, vice chairman of government affairs and first vice chairman. He also served as chairman of the headquarters committee and the chamber's 1987 Mackinac Island legislative conference.

No stranger to politics, Van Dusen ran George Romney's campaign for governor in 1963 and served Romney in his first year in office.

In 1969 he took another leave from law to serve for three years as undersecretary of the Housing and Urban Development Department in Washington, D.C., under Romney.

BIDCOs: hybrid financing

By Philip A. Sherman
staff writer

An alternative financing device for growth businesses, falling between commercial bank loans and venture capital investments, is making its debut in the Michigan market.

The product is referred to by its acronym, BIDCO — Business and Industrial Development Corporation.

The first BIDCO conference, for decision makers interested in starting BIDCOs, played to a packed room at Detroit's Westin Hotel earlier this week. The conference generated enough excitement in the financial community to draw its audience from 21 states.

"What we're really talking about here is creating a new industry," said Steve Rhode, director of policy and program development for Michigan Strategic Fund, which sponsored the conference. The Michigan Strategic Fund is the catalyst behind BIDCOs, which at an overview work like this:

● As a given, businesses have a problem securing loans to expand because of the risk involved. Rhode said commercial loan institutions — banks — are heavily regulated and take a low-risk lending position because of their debt-to-equity ratio, which he pegged at 15-1.

● On the other end of the line is the venture capitalist, who is low on

'We don't want to do mom and pop shops because they can't offer a good return to investors and shareholders.'

— Ronald Bieleke
of Arcadia BIDCO

debt, high on equity and engages in higher risk for a higher return. Rhode said most venture capitalists won't invest without hope of a 40-percent or greater return. Either scenario stifles the middle-weight entrepreneur in a growth position, he said.

● Enter the BIDCO, developed in California by financial heavyweight Derek Hansen and now exported to Michigan. A BIDCO takes up the slack by taking more risk than a bank, less than the venture capitalists and then offering hybrid repayment arrangements such as debt and equity mixes, Rhode said.

MICHIGAN ALREADY has three BIDCOs, which are private institutions. The Michigan Strategic Fund started each of the three with an initial \$2 million investment as an in-

centive for further investment from the private sector, according to Jim Paquet, BIDCO program manager. The idea, he said, is to spur growth by freeing up money.

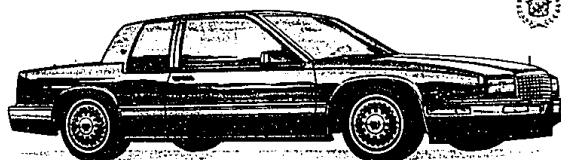
But BIDCOs do not appear to be a financing solution for start-up businesses. The heads of Michigan's three BIDCOs said during a panel discussion it was unlikely they would finance start-ups because of high failure rates.

Also, Paquet said the strategic fund merely stipulates a BIDCO do business in Michigan and aim at the middle market. That means other rules for obtaining BIDCO money can, and do, vary widely.

FOR INSTANCE, Gordon Areen, co-founder of Onset BIDCO in Farmington Hills, said the profile of a company they would likely invest in would include sales between \$500,000 and \$20 million. It must be within an hour's driving distance of his headquarters in Farmington Hills so he can maintain a "hands-on" management stature. The loan to such a company wouldn't exceed \$1 million on fixed interest based on the cost of money, would be repayable in five to seven years, and the typical loan would be between \$600,000 and \$700,000.

Please turn to Page 2

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