

University of Mississippi

eGrove

---

Newsletters

American Institute of Certified Public  
Accountants (AICPA) Historical Collection

---

6-1988

## Accountant's Liability Newsletter, Number 14, June/July 1988

Rollins Burdick Hunter Company

American Institute of Certified Public Accountants. Professional Liability Insurance Plan  
Committee

Follow this and additional works at: [https://egrove.olemiss.edu/aicpa\\_news](https://egrove.olemiss.edu/aicpa_news)



Part of the [Accounting Commons](#)

---

INSTITUTE OF  
PUBLIC ACCOUNTANTS  
SERVICES  
BUREAU OF THE AMERICAS  
NEW YORK, N. Y. 10036-8775

# ACCOUNTANT'S **LIABILITY** NEWSLETTER

For Reference  
Do Not Take  
From the Library

AICPA Professional Liability Insurance Plan

Number 14: June/July 1988

## MERGER MANIA — WATCH YOUR TAIL

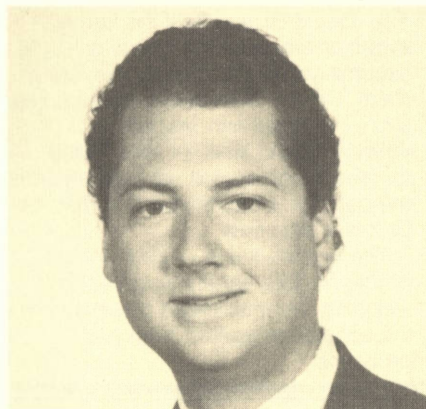
BY F. KYLE NIEMAN  
Underwriting Manager  
Crum & Forster

It seems that every time you pick up a newspaper there is an article about a merger or acquisition. The accounting profession has not been immune to this "Merger Mania."

Mergers appeal to small practices because these firms may become stifled in terms of growth, and also because of attractive benefits programs offered by larger firms. On the other side of the coin, larger, established firms see the acquisition of other accounting practices as a means to open branch offices which provide opportunities for growth. Unfortunately, the topic of professional liability insurance often is not considered until

after the merger is completed. Ignoring the impact of a merger agreement upon insurance coverage can be costly in both merging parties.

(Continued on page 2.)



F. Kyle Nieman

## NEWLY FORMED AMERINST INSURANCE COMPANY ADDS STABILITY TO AICPA PLAN

Well over a year's work by members of the AICPA Professional Liability Insurance Plan Committee and Rollins Burdick Hunter was rewarded in early February, 1988 as the stock offering for AmerInst Insurance Group, Inc. was successfully concluded. A total of 2,624 accounting firms and sole practitioners purchased 343,357 shares to raise \$8,583,925, well above the minimum floor of \$7,500,000 necessary to activate this company. AmerInst was formed for the purpose of adding stability to the AICPA sponsored professional liability insurance plan.

AmerInst will achieve this objective by initially reinsuring AICPA Plan policies issued by Crum & Forster, the primary Plan underwriter, with effective dates of April 1, 1988 and later. AmerInst will not have any liability for policies with effective dates before April 1, 1988.

According to the Professional

Liability Insurance Plan Chairman, Norman C. Batchelder, "We believe that, by having a member-owned company reinsuring the lead underwriter of the basic plan, we will be in a better position to maintain access to the commercial insurance market. Underwriters as a rule are very favorably impressed when a group is willing to put up its own money and share the underwriter's risk."

Mr. Batchelder additionally commented, "We believe that AmerInst will provide an additional element of stability to the AICPA program in both rate levels and policy forms. Insurance rates come from what an underwriter thinks will happen to the risks he has assumed and while the AICPA program, unlike many others, bases these assumptions on actuarial studies, we believe that AmerInst, as a participating underwriter, will weigh against these estimates becoming overly conservative."

In addition to helping maintain access to the commercial insurance market and exercising a stabilizing influence on accountant's professional liability insurance forms and rates for the benefit of all AICPA Plan insureds, the company was formed to act as a cushion for its investors in the event of another crisis in the professional liability insurance marketplace. If another such crisis occurs, AmerInst intends to devote its resources exclusively to the benefit of its investors.

The current business plan of the company does not contemplate dividend payments in the near future. AmerInst intends instead to use any underwriting profit and investment income earned as a reinsurer of the AICPA Plan to strengthen the company's surplus and position.

AmerInst Insurance Company has been issued its Certificate of Authority by the State of Illinois, its domicile. AmerInst has appointed Continental Illinois National Bank as its investment advisor and the Bank will also provide custodial services. Additionally, AmerInst has selected the firm of Liscord, Ward & Roy to provide actuarial services. The First National Bank of Chicago acts as AmerInst's Transfer agent and Registrar.

In short, AmerInst is in business.



**AmerInst  
Insurance  
Group,  
Inc.**

This Newsletter is prepared by Rollins Burdick Hunter, administrator of the AICPA Professional Liability Insurance Plan as a service to the accounting profession to alert you to loss-prevention/risk management considerations in your accounting practice. It should not be regarded as a complete analysis applicable to your particular situation or used for decision making without first consulting your own firm's legal counsel. The Newsletter is furnished free to practice units insured under the AICPA Professional Liability Insurance Plan.

## Merger Mania

(Continued from page 1.)

Through the AICPA plan, various merger scenarios are addressed on a regular basis. Merging firms that are both insured through the AICPA plan can revise their coverage by contacting Rollins Burdick Hunter **in advance** of the planned merger.

One important issue to consider when contemplating a merger is continuity of coverage, i.e. maintaining prior acts coverage. Most professional liability coverages are written on a "claims-made" basis. This means that coverage is afforded for claims made against the insured and reported to the carrier within the policy period. As far as claims-made coverage is concerned, the important date is when the insured is **made aware** of an incident leading to a claim, not when the incident took place.

Most claims-made policies contain a prior acts endorsement. This endorsement indicates a date, which usually represents the date the insured began carrying uninterrupted claims-made coverage. Any alleged act, error or omission taking place before this date will not be covered, even if the claim is made during the policy period. The importance of prior acts coverage is that frequently the acts, errors or omissions giving rise to a claim precede the claim by several years.

If your firm is acquiring or merging with a firm that has not carried insurance, you, as a partner of the merged firm, may be liable for work performed by that firm during the uninsured period in their coverage. This will hold true, even though 1) this work was performed prior to the merger date and 2) prior to the merger your firm carried continuous claims-made coverage.

Another concern to a firm considering a merger or acquisition is the claims experience of the firm being acquired. When you purchase a firm with a severe claims background this firm **and** all of its attributes become part of your firm, in the eyes of the

insurer. This could potentially lead to an increased premium or worse yet, future claims stemming from the claim-prone entity. Therefore, prior to negotiating the contract, it is important that you request all claims information pertinent to the acquired firm to facilitate your decision whether the addition of the entity is worth the risk. You should determine if the firm is aware of any potential claims or circumstances that may evolve into a claim. Finally, learn about the acquired firm's practices with respect to collections and suits for fees. Suing for fees is considered risky, as it opens the door for a countersuit that may be filed at a later time.

The bottom line is — don't inherit problems. Use careful judgment in weighing the anticipated benefits from the acquisition against potential problems.

---

### *Ignoring the impact of a merger agreement upon insurance coverage can be costly . . .*

---

Caution should be the rule of thumb not only for firms buying another practice, but for those considering selling their practices, since many merger agreements include a provision excluding prior acts coverage for the acquired firm. Where such an agreement exists, the acquired firm should consider purchasing extended reporting period coverage, also known

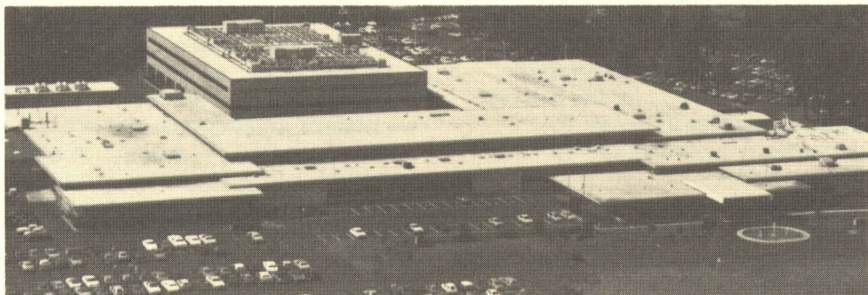
as "tail" coverage, which, provides coverage for claims-made during a given period of time after the policy expires. Unfortunately, tail coverage provided in today's professional liability policies is restricted in length (usually to one year) and in some cases will not be available at all.

To illustrate the restrictiveness of a short tail, even if you have a one year tail and a claim is made against you after that year has elapsed, no coverage will be available. Once again, the benefits of the additional year of claims reporting must be weighed against its cost and the perceived possibility of a claim within the reporting period.

In view of the short reporting period, in the event your firm is acquired, you are better off negotiating with the acquiring firm and their insurer, the acceptance of your firm's prior acts coverage. By doing so, you will retain the continuity of coverage established by your firm.

In conclusion, whatever role your firm plays in a merger or acquisition, plan ahead. Before entering into an agreement, make sure you understand the impact that the change in your firm's status will have on insurance coverage. Make sure to contact Rollins Burdick Hunter before the agreement is finalized, and allow Rollins Burdick Hunter sufficient time to determine the necessary action to be taken.

Don't jeopardize your firm's coverage. Make insurance coverage a top priority in all merger or acquisition negotiations.



The Trevoze, Pennsylvania plant, headquarters for the administration of the AICPA Professional Liability Insurance Plan.



## BALANCE SHEET

Responses to our readers comments and questions.

BY NORMAN C. BATCHELDER, CPA,  
CHAIRMAN  
AICPA Professional Liability Insurance  
Plan Committee

From Arthur C. F. Pratt, CPA, Sisters,  
Oregon:

*In one of the Accountant's Liability  
Newsletters, you mentioned two rules  
which I would like your help on:*

**1. Use engagement letters on  
every engagement.**

As you know, the vast majority of all CPAs would think it a crime to prepare any sort of financial statement without an engagement letter, but the vast majority of all CPAs do not use an engagement letter for tax returns.

**Response:**

*The initial engagement letters for individual tax returns often causes apprehension on the part of the CPA, but clients readily accept and appreciate them, by and large. A sample individual tax return engagement letter is included on this page. There is no standard letter. Each firm must develop its own, in consultation with the firm's attorney, preferably. Some attorneys recommend clauses requiring arbitration in the event of disputes and clauses regarding collection costs, among others. A claims attorney once observed that he had never seen an engagement letter help a defendant's case, but that the lack of one frequently hurts the defense.*

**2. Never represent, or appear to represent, both sides of the transaction.**

I have been hired by one side to prepare the tax returns for both sides of the transaction. If, however, either side were to negotiate and need representation concerning a

revision of the present contract, I would only represent the side that is presently paying me. I would make it very clear, both in writing and verbally to the other side, that I

would be representing the side that has been paying me. Would I get in trouble?

(Continued on page 4.)

## Sample Engagement Letter

This letter confirms the arrangements for our services.

We will prepare your federal and state income tax returns for 1988 from information you furnish us. Unless you specifically object (see bottom of page), we may use a computer processing service located outside our office. We will not audit or otherwise verify the data you submit, although we may ask you to clarify some of it for us.

We will resolve questions involving application of tax rules in your favor, if there is a reasonable justification for doing so.

We are available to answer your inquiries on specific tax matters and to consult with you on income and estate tax planning should you wish us to do so.

We will bill you for the above services as our efforts are incurred plus out-of-pocket expenses, after the returns are completed. Our invoices are due and payable upon presentation. Balances unpaid within 30 days will have a FINANCE CHARGE assessed on the unpaid balance computed at a periodic rate of 1.5% per month, which is an ANNUAL PERCENTAGE RATE of 18%.

Your returns are, of course, subject to review by taxing authorities. In the event of an examination, we are available to represent you. You may appeal any adjustments proposed by an examining agent. Our fee for these services will be billed to you, plus out-of-pocket costs, as our efforts are incurred.

If the above fairly sets forth your understanding, please sign the enclosed copy of this letter and return it to us in the enclosed return envelope. Please indicate in the space provided below the date by which you expect to give us your information.

We are pleased to have you as a client and we will do our best to render satisfactory service to you.

Sincerely,

APPROVED BY: Client \_\_\_\_\_  
Date \_\_\_\_\_

I (We) will submit my (our) 1988 income tax information to you no later than \_\_\_\_\_, 1989. If, for some unforeseen reason, the data is not complete at that time, I (We) will submit whatever is ready and will send you the balance of it as soon as it is possible to do so.

I (We) authorize you to use an outside computer processing service for the preparation of my (our) tax returns should you elect to do so. (If you object to such processing, please line out the preceding sentence).

## BALANCE SHEET

(Continued from page 3)

### Response:

From the facts you presented, you apparently prepared returns for your client, and another party, presumably a buyer, accepted them. Your further explanation that you would clearly state to the other party, orally and in writing, that you were representing only your client indicates that you understand the danger and, hopefully, would not get into trouble. You don't have to be wrong to get into trouble these days, so appearances can be as important as the actual, factual situation. Many lawyers echo this recommendation and many are most adamant about it.

From Windsor L. Anderson, CPA,  
Warren, Ohio:

1. **Never sue for collection of a fee unless the suit is based on a promissory note, and then consider that a lawsuit may still be too risky.**

Mr. Batchelder strongly emphasized never to sue for collection of a fee for fear of a countersuit. We believe that this issue has been overstated and question the economic substance of such a statement. If our clientele knew that our own professional society was advocating the reluctance to collect fees, we would certainly incur additional bad debts. All too often in our profession we find clients who do not realize the economic value of a CPA's services and would relish the opportunity to beat us out of fees. This reluctance to legal action for collections by our profession can only hurt ourselves in lost revenues, to which we are entitled.

### Response:

*The first thought that strikes me is the astounding fact that over 90% of the claims in the AICPA Plan are first-time claims. Most CPAs that have not had a claim believe that*

*since they haven't had a claim and don't even know anyone who has had a claim, they will never have a claim. That fateful day when a CPA receives service of a writ is a traumatic day indeed. The CPA will experience anxiety, loss of income through time spent with attorneys, disruption of day-to-day business, and the chances of having a claim in any one year are approximately 6½%. Second, roughly 10% of the claims arise because the CPA has sued for a fee and the common reaction by clients is to countersue for malpractice. If the client thought that the CPA was a tough collector and untouchable, then his lawyer soon advises him to the contrary. The relatively small amount involved in the suit for fees seems paltry in relation to the potential bonanza that the client can realize from a*

*... over 90% the claims in the AICPA Plan are first-time claims*

*malpractice claim. His lawyer knows that the CPA will probably settle, because the costs of defense are so high and the prospect of winning in court is usually questionable when viewed from the vantage point of hindsight, even in a well-executed engagement. Thus, in addition to winning a large settlement, the client can force his ex-CPA to dine on humble pie — all brought on because the CPA sued him for a fee.*

2. **To settle or not to settle, that is the question.**

It was interesting to us to note that only 5% of the claims actually go to trial. This indicates to us that all too often the insurance carriers are too quick to offer a settlement in order that trial cost, which you indicate averages \$150,000, may be saved. We question whether this practice is beneficial to our profession in light

of the increase in claims being made. If easy settlements are made outside of the court system, what is left to stop the assertion of meritless claims and negative affect this has on our profession? We believe that a strong stand by the insurance companies not to offer out of court settlements and to litigate these

In court, a molehill of a deficiency in an engagement can easily be made into a mountain of a transgression . . .

claims is far better in the long-term to our profession and to the insurance industry itself.

### Response:

*Insurance companies care about overall program stability, which is measured by the plans loss experience (premiums paid to claims incurred). To minimize premium increases, claims control is a vital function of the insurance company. The insurance company will do what is best to minimize claims costs and keep premiums down, which may involve settling a dispute over costly prosecution. In many cases meritless claims are pursued, so that future claims of that nature do not arise. In every case under the AICPA Professional Liability Insurance Plan, a claim will not be settled without the consent*

(Continued on page 6.)

## THIS IS YOUR NEWSLETTER

If you have any particular topics or issues you'd care to have addressed, please let me know. Send your suggestions to Barbara J. Frantz, AICPA Professional Liability Newsletter Editor, Rollins Burdick Hunter, 123 North Wacker Drive, Chicago, IL 60606



## KNOW YOUR PLAN ADMINISTRATOR

*The AICPA Professional Liability Insurance Plan is administered by RBH Direct Group from a state of the art insurance processing and customer service facility located in Trevoze, Pennsylvania. A total of 42 people, not including data processing support personnel, are dedicated exclusively to the AICPA Professional Liability Insurance Plan. This staff works closely with Crum & Forster's underwriting department to process almost 14,000 quotes annually and to deliver timely, helpful service to Plan insureds and applicants.*

*Though every person who works on the Plan is key to its success, three people in particular have major responsibility for seeing to it that AICPA members are properly served.*

### **Robert Parker**

Robert Parker is the RBH Direct Group Vice President in charge of the overall administration of the Plan. He ensures that the administrative management and underwriting/service function of the Plan run smoothly and efficiently. He is also involved in all aspects of the Plan include marketing, pricing, working with account representatives on renewing large or difficult renewals and assisting with consumer inquiries ranging from coverage questions to claims handling issues.

Robert is an attorney who joined Rollins Burdick Hunter in May of 1987 after two and one half years of heading up a \$200,000,000 professional liability program for another national insurance program. He is an insurance professional with fifteen years in the business having insurance brokerage experience, hands on litigation experience defending both insureds and insurers and professional liability underwriting expertise.

### **Michael J. Chovancak**

Mike is the RBH Direct Group Assistant Vice President in charge of the underwriting/service function of the Plan. He manages ten account representatives and seven additional service personnel devoted exclusively to the AICPA Professional Liability Insurance Plan. Working with the Plan's insurance company, Crum & Forster, his staff is responsible for the

review and analysis of the respective applications and supporting data. In addition, Mike's staff is responsible for providing premium quotations to Plan members and applicants in a timely manner.

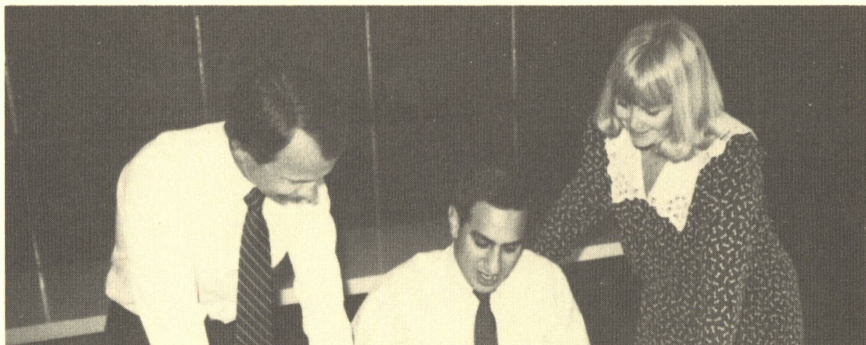
Mike transferred to Rollins Burdick Hunter Direct Group from a sister company where he had gained nine years of underwriting experience.

### **Tensie Miller**

Tensie Miller is the Assistant Vice President responsible for administrative

management of the Plan. In this capacity, she directs the daily activities of Policy Issuance, Accounting, Data Entry and Mail/File. In addition, she acts as liaison with Data Processing to meet the computer and system needs for all aspects of the Plan.

Robert, Mike, Tensie and their staffs are concerned that Plan insureds and applicants receive the highest level of professional treatment. If you have any questions or problems, you should feel free to call them at 1-800-221-3023.



Left to right: Michael Chovancak, Robert Parker and Tensie Miller.

## GUIDELINES FOR LIABILITY INSURANCE

How much professional liability insurance should a firm buy? The answer depends upon a number of factors from the area of practice to the legal and judicial climate in your geographical location. The chart below shows the percentage distribution of professional liability insurance limits by staff size of firms presently involved in the AICPA Plan. As would be expected, smaller firms typically carry lower limits.

The Plan Administrator has noted that in the last 6 months of 1987, there had been a tendency for firms to increase their limits. In June of 1987,

40.5% of all Plan participants carried a \$250,000 limit and 35.7% had a \$1,000,000 limit. By year end, however, 36.2% of Plan participants had a \$250,000 limit while insureds with a \$1,000,000 limit had increased to 39.2%.

In choosing its limits of liability, firms should recognize that defense costs have been placed within the overall limit of liability. These costs, which have historically amounted to almost 40% of all paid loss, effectively reduce the amount available to settle a claim or to pay a judgment.

### AICPA Professional Liability Plan Percentage Distribution of Limits By Staff Size As Of 1/1/88

Staff Size	Limits				
	\$250 M	\$500 M	\$1 MM	\$2 MM	\$3 MM
1-2	61.6%	18.7%	18.5%	0.7%	0.5%
3-4	50.0%	22.9%	26.2%	0.7%	0.2%
5-10	30.9%	27.7%	39.3%	1.6%	0.5%
11-25		19.8%	74.7%	4.1%	1.4%
26-50			85.0%	11.2%	3.8%
51-100			64.2%	14.4%	21.1%
101-150			75.0%	18.8%	6.2%
151 +			40.0%	—	60.0%



## Balance Sheet

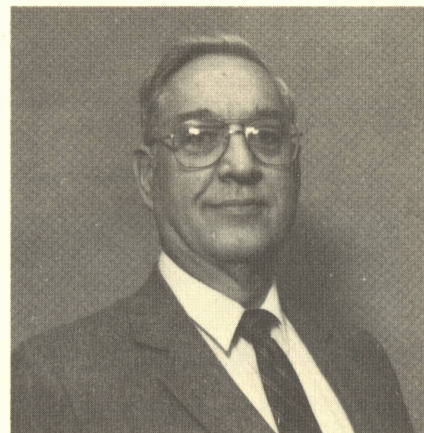
(Continued from page 4.)

of the insured (subject to a maximum of what the settlement amount would have been).

Remember, in court a molehill of a deficiency in an engagement can easily be made into a mountain of a transgression. Under the AICPA plan, if it appears that it will cost less to settle, than to defend and the insured agrees to settle, the case will probably be settled out of court. This type of a system creates favorable loss experience and stabilized premiums.

Thanks to Mr. Pratt and Mr. Anderson for their thoughtful and pertinent letters. Your Committee encourages readers to submit questions or comments as well.

— Norman C. Batchelder, CPA  
AICPA Professional Liability Insurance  
Plan Committee



## AICPA LIABILITY PLAN

## LATE BREAKING NEWS

Do you have a question about your professional liability insurance plan? We want to answer all Plan questions and we will be at the following AICPA and state CPA Society meetings to talk with you and other AICPA members.

### Show

AICPA Practice Mgt. Conf.  
Midwest Accounting Show  
AICPA Small Firms Conf.  
AICPA Annual Meeting  
AICPA Practice Mgt. Conf.  
Florida St. Soc. Acct. Show  
AICPA Small Firms Conf.  
Connecticut Tax Forum

### Dates

July 19-21 Boston  
Aug. 17-19 O'Hara Expo. Ctr.  
Aug. 25-26 Denver  
Oct. 2-5 Los Angeles  
Oct. 17-19 Las Vegas  
Late Oct. Orlando  
Nov. 3-4 Washington, D.C.  
Dec. 5-6 Southington, CT.

### Location

## 'NEW, ATTRACTIVE PREMIUM FINANCING AVAILABLE'

We are pleased to announce that effective January 1, 1988, a new professional liability premium finance plan has been arranged through Whirlpool Leasing Services, Inc. — Insurance Finance Division. Monthly payments are available at a very attractive annual percentage rate of 9.95% **regardless of your premium size.**

Whirlpool Leasing Services, Inc. is a subsidiary of Whirlpool Acceptance Corporation, which in turn is a subsidiary of The Whirlpool Corporation established in 1911 which has net sales in excess of \$4 billion.

We believe the financing program is with a company committed to giving its customers, AICPA Plan insureds, good service and a well priced product. For more information, please contact The Plan Administrator, Rollins Burdick Hunter, at 1/800-221-3023.

## AICPA PROFESSIONAL LIABILITY INSURANCE PLAN COMMITTEE

Norman C. Batchelder, *Chairman*  
New Hampshire Society of CPAs, Bedford, NH  
Leonard A. Dopkins  
Dopkins & Company, Buffalo, NY  
Joseph B. Dresselhaus, Lincoln, NE  
Robert B. Geis  
Geis, Buhrdorf & Company, Denver, CO  
Terry L. Hothem  
Miller, Wagner & Company, Ltd., Phoenix, AZ  
Ronald S. Katch  
Katch, Tyson & Company, Northfield, IL  
Charles B. Larson, St. Joseph, MO  
Gelon E. Wasdin  
Wasdin, Darnell, Penland and Holmes, P.C.  
Bremen, GA  
James D. Winemiller  
Blue & Company, Indianapolis, IN  
**Staff Aide:** William C. Tamulinas  
**Plan Administrator:** Rollins Burdick Hunter  
C.J. Reid, Jr.  
Robert M. Parker  
**Plan Underwriter:** Crum & Forster  
Managers Corporation (Ill.)  
Kyle Nieman  
Dennis Bissett  
**Newsletter Editor:** Barbara J. Frantz

## AICPA Professional Liability Insurance Plan Committee

c/o Newsletter Editor  
Barbara J. Frantz  
Rollins Burdick Hunter  
123 North Wacker Drive  
Chicago, IL 60606

*The contents of this newsletter do not represent an official position of the AICPA Professional Liability Insurance Plan Committee.*