



Filing Season Finds: Wednesday, March 7

For March 6, 2018, our forensic accounting red flag comes from a financial services firm with a hidden (and confusing) non-operating expense.

We pulled this highlight from yesterday's research of 129 10-K filings, from which our [Robo-Analyst](#) technology collected 18,042 data points. Our analyst team used this data to make 2,644 forensic accounting [adjustments](#) with a dollar value of \$153 billion. The adjustments were applied as follows:

- 1,128 income statement adjustments with a total value of \$15 billion
- 1,088 balance sheet adjustments with a total value of \$72 billion
- 428 valuation adjustments with a total value of \$67 billion

Figure 1: Filing Season Diligence for Tuesday, March 6th

	Filings Parsed	Data Points Collected	# of Adjustments	Total Value of Adjustments (\$Billions)
Filing Season Day 11	129	18,042	2,644	\$153
Filing Season Total	1,258	196,075	31,150	\$11,716

Sources: New Constructs, LLC and company filings.

We believe this research is necessary to fulfill the [Fiduciary Duty of Care](#). Ernst & Young's recent white paper, "[Getting ROIC Right](#)", demonstrates how these adjustments contribute to meaningfully superior models and metrics.

Today's Forensic Accounting Needle in a Haystack Is for Financial Services Investors

Analyst Peter Apockotos found an unusual item yesterday in CBIZ Inc.'s (CBZ) 10-K.

On [page 25](#) of the footnotes (page 65 overall), CBZ disclosed a \$12 million gain (24% of net income) on the investments in its [deferred compensation plan](#). At first glance, it looks like this item is non-operating income and that we need to reduce reported pre-tax income by \$12 million to get to the true operating cash flows ([NOPAT](#)).

However, the company clarifies its treatment of these deferred compensation gains on [page 22](#). CBZ includes the \$12 million gain under "Other Income" on the income statement, a line item we already exclude from our NOPAT calculation. In addition, the company records an offsetting \$12 million increase to operating expenses. As a result, reported net income is unaffected, but reported operating income is significantly understated.

In 2017, CBZ's reported operating income increased by just 1%. Our adjustments reveal that NOPAT actually increased by 14%.

This adjustment shows the importance of combining our Robo-Analyst technology with human subject matter experts. A sophisticated analyst that didn't have the technology to rapidly identify this item would have to rely on the company's understated operating income. An unsophisticated analyst that did have the technology to find this data point might mistake it for non-operating income and make an adjustment in the wrong direction. To get it right, you need have both man and machine working at a high level.

This article originally published on [March 7, 2018](#).

Disclosure: David Trainer, Peter Apockotos, and Sam McBride receive no compensation to write about any specific stock, sector, style, or theme.

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To fulfill the Duty of Care, research should be:

1. **Comprehensive** - All relevant publicly-available (e.g. 10-Ks and 10-Qs) information has been diligently reviewed, including footnotes and the management discussion & analysis (MD&A).
2. **Un-conflicted** - Clients deserve unbiased research.
3. **Transparent** - Advisors should be able to show how the analysis was performed and the data behind it.
4. **Relevant** - Empirical evidence must provide [tangible, quantifiable correlation](#) to stock, ETF or mutual fund performance.

Value Investing 2.0: Diligence Matters: Technology is Key to Value Investing With Scale

Accounting data is only the beginning of fundamental research. It must be translated into economic earnings to truly understand profitability and valuation. This translation requires deep analysis of footnotes and the MD&A, a process that our [robo-analyst technology](#) empowers us to perform for thousands of stocks, ETFs and mutual funds.



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