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Reading financial statements gives a competitive advantage

By Christopher J. Zinski

If you want to impress CEOs and other top executives, make it your mission to read and understand a company's financial statements. If done well, you will have them glued to your every word and impressed by your insightful questions. You also will learn what they value and find yourself in high-level strategic discussions in minutes. In addition, you will have almost no competition in the market place. This is particularly valuable with a new corporate client or a prospect you are trying to impress. My own experience is illustrative.

I recently returned to private practice after three years as General Counsel for a publicly-traded regional bank holding company. Based on my in-house experience, I would estimate that less than 5 percent of lawyers in private practice can read and understand balance sheets and income statements well enough to ask provocative questions. This knowledge gap makes it unlikely lawyers are able to speak "fluent CEO" and, thus, they are squandering an opportunity of a lifetime.

Being Financially Literate Impresses Prospective Clients

Financial statements present a treasure trove of insights into a company's well-being, business focus and future prospects. Imagine you are at your first meeting with the CEO of a prospective client and you start the lunch – even before the waiter delivers the bread basket and menus – by asking the CEO how his company was able to reduce its cost of goods sold by 12 percent last quarter compared to the year-ago quarter and whether he thinks he can keep that profit boosting trend going for several more quarters. You are guaranteed to impress that CEO a whole lot more with this question than by asking who he uses as his current counsel. With questions like these it won't be long before you will be replacing his current counsel because you are showing you have a better command of the CEO's business. Doing so shows you are a high-energy, financially literate lawyer, who devotes time educating himself on what matters most to the CEO – his profitability!

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A 90-minute read of a company's financial statements – provided you know what to look for – will yield multiple opportunities for increased business. Since returning to private practice two months ago I would estimate I have met with a dozen CEOs and C-suite

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executives. Without exception, all of these senior executives have wanted to meet with me again and in most instances wanted to hire me and the firm to help them with problems and issues that most lawyers in private practice cannot even spot.

Many lawyers lack confidence in business development, but all private practitioners have existing clients who would hire them for more work repeatedly if they were more financially literate. When you are armed with knowledge of how to read financial statements every interaction with your clients is a business development opportunity. How would you like to experience what it feels like to "pitch" an idea to a client and have them hire you on the spot? If you hope to impress CEOs and other senior executives, learning to do a critical read of a company's financial statements should be a priority. It is the gateway to new business.

An Illustration

I practice corporate and securities law with a particular expertise in representing financial institutions including banks. Since September 2008, I have noticed an increasing number of banks are heavily focused on protecting their deferred tax asset (DTA) from impairment. Why should a lawyer care about this highly technical accounting issue? Because I know, even without asking, that the DTA is keeping many bank CEOs awake at night. If the DTA is deemed "impaired," it gets written off (in whole or in part) and the charge goes directly to the bank's capital. Doing so in many cases will put the bank in a compromising capital position that creates problems for the CEO with her regulators, stockholders and even customers of the bank. If I can show an interest in something keeping the CEO up at

night and show I have mastered the technical aspects of the issue, I am starting to not only prove my expertise but, as the strategic conversation about defending the DTA continues as the bread basket is passed between us, I am acting as the company's lawyer even before getting hired.

Before I meet with a prospective bank client, I study its financial statements to learn the amount of the DTA. I also study the tax, GAAP-accounting and regulatory issues affecting the DTA so I can have an intelligent conversation with the prospective client about the threat of DTA impairment presented in that bank's particular circumstances. Armed with that insight, I am able to talk intelligently with senior leaders about how to defend the DTA against impairment challenges by the client's public accounting firm. This is the kind of issue that gets raised when the menus arrive and continues with the CEO over cappuccino as the lunch concludes. It is technical but central to the CEO's success and so captures her attention for a disproportionate period of time over the lunch.

But wait, it gets even better, because studying the financial statements can put you in a position to generate business in other ways. For example, DTA impairment directly affects the bank's capital position and will often lead naturally to a discussion about the bank's need for new capital. The amount of trust inspired to this point often leads to the CEO sharing her concern over her bank's capital position and whether she is planning a capital raise. Further probing reveals her views about impediments to a successful capital raise, such as a continuing negative trend in loan delinquencies, fears about diluting current stockholders or a board of directors in denial over the bank's problems or all of the above.

At this point in the discussion, you have no competition. And you get there in less than 90 minutes all because you show a profound understanding of the bank's financial statements. In less than two months back in private practice, I have had many bank CEOs frankly share their business concerns, which has provided me multiple opportunities to show my creativity in solving their strategic problems. This all naturally follows from a targeted question to the CEO about a technical and hot button accounting issue embedded in her company's financial statements. It is all about becoming a trusted advisor – and that is good for the client and good for your practice.