philly.com

Posted on Thu, Jul. 17, 2003

Bucks firm notified it is in default amid dispute over quarterly report

DVI Inc. and an outside auditor, Deloitte & Touche, disagreed over accounting procedures. DVI's shares fell 10 percent.

By Todd Mason
Inquirer Staff Writer

A Bucks County medical-equipment leasing firm said yesterday that it had been notified it was in default on a bond agreement as a dispute with its outside auditor snowballs.

Shares of the company, DVI Inc., of Jamison, fell 47 cents, or 10 percent, to $4.23 yesterday on the New York Stock Exchange. A year ago, the stock was trading above $16.

Deloitte & Touche L.L.P. resigned June 2 as auditor for DVI after a clash over whether the accounting firm had finished its review of DVI's latest quarterly financial results.

Things got worse for DVI after the Securities and Exchange Commission sided with Deloitte June 27, rejecting DVI's filing for the three months ended March 31.

"It looks like management really didn't understand what it would be like in the market with an auditor resigning," said Matthew D. Gallino, an analyst with Fitch Ratings who downgraded DVI bonds last month.

John F. Schoenfelder, a DVI vice president, said: "We were faced with a filing deadline, and we either filed or we didn't file."

DVI is asking the bond trustee, Minneapolis-based U.S. Bank, to reconsider the default notice. Failing that, the company has 60 days to address the notice. DVI said the bank claimed it was in default over the filing of the quarterly report.

On June 30, the company said it had hired UBS Securities to explore "strategic alternatives," including the sale of all or part of DVI's business. Originating and packaging medical-equipment leases for sale as securities, DVI manages $2.8 billion.

Yesterday, Standard & Poor's Rating Service downgraded DVI debt by one notch to a lower "junk" status, saying the default notice could trigger similar notices on agreements stipulating that DVI stay out of default on its debt.

Fitch lowered DVI bonds last month by one notch to a lower "junk" status on worries that the auditing stain could linger after DVI replaces Deloitte.

"Any auditor that comes in may have to audit three years of financial statements" to gain confidence in DVI's numbers, Gallino said.

The accounting issues in dispute surface indirectly in a series of SEC filings. Schoenfelder would not elaborate on the filings.

In the rejected quarterly report, DVI said it asked Deloitte to review the accounting treatment of transactions involving a radiology clinic in Corpus Christi, Texas. A restatement would trim 2002 fiscal-year earnings by 34 percent, a cut of $1.4 million, or 9 cents a share.

But Deloitte wanted more documentation, including affidavits from people outside the company, so DVI filed the report with Deloitte's disclaimer, saying: "We do not accept their characterization."

In a June 17 letter to the SEC, Deloitte said it wanted to look at a series of transactions between 1999 and 2002. Deloitte said in the letter that it wanted DVI to disclose that the accounting firm found fault with the company's accounting procedures.

Deloitte said it warned DVI to consult with a lawyer "regarding these matters, including the propriety of management's certifications" that the March 31 quarterly report was accurate.

Investors have paid little attention to finer points of accounting disputes after the Enron scandal, said Steve Erickson, a consultant to the accounting industry who is based in Las Cruces, N.M.

"The moment there's a dispute with an auditor, it sends up a red flag," he said. "It creates all kinds of speculation."

Contact staff writer Todd Mason at 215-854-5679 or tmason@phillynews.com.
