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Claiming Contingent Liabilities and the Effect on Stockholder Wealth

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ABSTRACT

This research is a non-Accountant's view of the accounting practices over the past 15 years at closely-held Rollins, Inc.; the parent company of Orkin Exterminating, Inc. Many subtle interpretations and transactions are encountered following the recording of a \$117 million contingent liability in 1997. The contingent liability was for the "anticipated costs of re-inspections, repair obligations and associated labor, chemicals, and other costs incurred relative to termite work performed prior to December 31, 1997 (1997 10-K of Rollins, Inc.). The company essentially changed accounting practices to self-insure due to an abundance of lawsuits related to termite damage to homes under contract with Orkin Exterminating, Inc. The damage settlements had previously been expensed in the year they were paid. The study is particularly interested in the effect on stockholder equity that this strategy had over a long-term horizon.

Keywords: Orkin, contingent liabilities, Rollins, Inc., self-insurance