

## **The ERS Fiduciary Test™**

### **Seven Steps to Honoring Your Duty**

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Fiduciaries must answer seven key questions about a company's financial condition before investing. These uncover critical aspects of its health, earnings quality, durability, liquidity, growth, and risks. A fiduciary's duty is to protect client interests, avoiding speculative decisions that could jeopardize financial security.

#### **1. What Are the Company's Revenue Growth Trends?**

Analyze revenue trends from quarterly financial statements to reassess assumptions about long-term growth and recalculate the company's Net Present Value (NPV). This ensures decisions reflect the company's latest financial trajectory.

#### **2. How Have the Company's Profit Margins Changed?**

Profit margins (gross, operating, and net) reveal cost efficiency and profitability trends. Changes must be incorporated into the NPV model to reflect shifts in operational efficiency, pricing power, and shareholder value creation.

#### **3. How Does the Company Use Debt?**

Debt-to-equity ratios and other leverage metrics highlight financial risks. High leverage increases vulnerability in downturns, while low leverage and strong cash flows indicate stability. Selecting stocks with lower risk is essential.

#### **4. Are Free Cash Flows Quantified and Recalculated Quarterly?**

Analyze quarterly free cash flow and update the NPV accordingly. This aligns investment decisions with the company's latest cash generation ability and financial health, reducing risks for clients.

#### **5. What is the Company's REVENUE TO EQUITY CONVERSION RATE™?**

This measures a company's ability to convert revenue into liquid, tangible assets. Companies generating higher cash from revenue build "economic equity," enabling R&D, seizing opportunities, and rewarding shareholders. Weak tangible equity signals greater risk.

#### **6. What Are the Sources of the Company's Equity?**

Determine how much equity comes from IPOs, secondary offerings, or Additional Paid-In Capital versus operational cash flow. Companies reliant on external financing dilute shareholder value, while those funded by earnings are more sustainable.

#### **7. What is Their Insider Ownership?**

High insider ownership aligns management with shareholder interests. Insider buying signals confidence in the company's prospects, while heavy insider selling raises concerns.

### **Conclusion**

Fiduciaries must deeply understand a company's financial health, profitability, and risks. These questions go beyond superficial metrics, ensuring decisions are grounded in data-driven analysis and align with the fiduciary duty to act in clients' best interests.