

“Understanding Business Valuations Reports”

Alpha Kappa Psi

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This Presentation can be downloaded from:

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The Basic Elements in a Business Valuation Report should answer the following questions:

- What is being Valued? Enterprise Value versus an equity value - Control versus minority equity interests
- How it is being valued? Standard of Value: Fair Market Value (Revenue Ruling 59-60); Fair Value (State Statute or SFAS); Investment Value (“Value to Whom”); etc.
- What is the premise of Value?: Going Concern or Liquidation.
- What is the stated purpose of the valuation? Tax purposes (Requires Revenue Ruling 59-60), sale or purchase of a business, marital dissolution, merger, SFAS financial reporting compliance i.e., testing goodwill impairment, purchase price allocations, ESOP.

Typical Report Contents

- 1 Executive Summary
- 2 Introduction
- 3 Economic Analysis
- 4 Industry Analysis
- 5 Financial Analysis
- 6 Approaches and Methods
 - 6.1 Considered but not Used
 - 6.2 Used
- 7 Valuation Methodologies
- 8 Valuation Adjustments: Discounts and Premia
- 9 Reconciliation of Findings
- 10. Reasonableness Tests
- 11. Opinion of value
- Exhibits
 - Exhibit A
 - Exhibit B
- Appendix
 - Sources Relied Upon:
 - Curriculum Vitae

Practical Considerations for CPAs when Relying on Business Valuation Reports

Caveats for the CPA

- A business valuation report provides an opined value as of
- a **specific date**.
- The opined Value depends on:
 - the facts and circumstances of the specific case,
 - the applicable statutory authority and judicial precedent within the relevant jurisdiction.
 - the application of the informed judgment of the valuator
- The purpose of the valuation engagement will require the selection and application of a specific “Standard of Value.”
- Different Standards of Value can yield radically different valuations of the same enterprise, and/or interest being valued as of the same valuation date.

ASSUMPTIONS AND LIMITING CONDITIONS

Some are boilerplate and found in most business valuation reports

- **All** should be carefully read by users
- Disclose and clearly explain any *special limiting conditions* or *hypothetical assumptions* included in the methodology utilized

Examples of assumptions and limiting conditions

The opinion of value is valid only as of the Valuation Date

Regulatory compliance is assumed to exist as of the Valuation Date

Management estimates concerning the value of machinery and equipment were used in the valuation

Managerial integrity and abilities existing as of the valuation date are reasonably assumed to continue

Limitations on the use and distribution of the valuation report

All documents provided to the valuator have been duly authenticated according to judicial requirements

NATURE OF METHODOLOGY USED IN A BUSINESS VALUATION REPORT

- Is there sufficient information on which to form a basis for an opinion?
- Is the information and methodology Relevant?
Your analysis needs to be **probative** of your opined conclusion.
- Are the Methods Reliable?
Your analysis must rely on the same “tools of the trade” relied upon by other experts in your field
- Does the methodology reference the recognized body of knowledge?
Your methods must be those used by other experts when dealing with similar fact patterns and circumstances

The AICPA Code of Professional Conduct

- The AICPA *Code of Professional Conduct and Bylaws* applies to all services rendered by AICPA members. The following sections of the Code of Professional Conduct have particular applicability to the practice of business valuation services:
- Rule 102, *Integrity and Objectivity*
(AICPA, *Professional Standards*, vol. 2, ET sec.102.01)
- Rule 201, *General Standards*
(AICPA, *Professional Standards*, vol. 2, ET sec. 201.01)
- Rule 202, *Compliance With Standards*
(AICPA, *Professional Standards*, vol. 2, ET sec. 202.01)
- Rule 301, *Confidential Client Information*
(AICPA, *Professional Standards*, vol. 2, ET sec. 301.01)

VALUATION SERVICES AND APPLICABLE PROFESSIONAL STANDARDS

- *AICPA Statement on Standards for Valuation Services SSVS1 – June 2007*
- *Rule 302, Contingent Fees*
(AICPA, *Professional Standards*, vol. 2, ET sec. 302.01)
- *Rule 501, Acts Discreditable*
(AICPA, *Professional Standards*, vol. 2, ET sec. 501.01)
- *Rule 101, Independence*
(AICPA, *Professional Standards*, vol. 2, ET sec. 101.01 and 101.05 for Non-Attest Services)

VALUATION SERVICES AND APPLICABLE PROFESSIONAL STANDARDS

- Professional competence includes, among other things, identifying client needs, applying an analytical approach, and being knowledgeable about the technical areas involved in the valuation engagement.
- As a result of *Daubert v. Merrill Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), and *Kumho Tire Company, Ltd. v. Patrick Carmichael*, 526 U.S. 137 (1999), the practitioner should consider that the **reliability and relevance** of the expected testimony is likely to be subjected to careful judicial scrutiny before it will be allowed to be presented at trial. When deciding whether to accept a litigation services engagement, the practitioner should consider whether it is likely that he or she has the knowledge and skills necessary to provide a reasonable basis to present relevant and reliable testimony on the issues to be presented in the particular case.

Professional Competence

- Practitioners should undertake only those valuation services that they reasonably can expect to complete with professional competence.
- Consequently, practitioners may be unprepared to meet client needs adequately in every area and in every phase of litigation engagements.
- To comply with this standard in providing valuation services, practitioners may need the assistance of other individuals with the required education and experience.

Some Useful Links:

AICPA Forensics and Valuation Services Center

- <http://fvs.aicpa.org/Resources/>

Federal Rules of Evidence

- http://www.law.cornell.edu/rules/fre/#article_vi

Listing of IRS Rulings:

- <http://www.taxlinks.com/rulings/findinglist/revrulmaster.htm>
- Online Dictionary & Thesaurus
- <http://www.websters-online-dictionary.org/>

Thank You for your Attention And Good Luck!!

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