MERCER CAPITAL
Business Valuation & Financial Advisory Services

IN THIS ISSUE

Value Matters™

Issue No. 6, 2013

The Defining Elements of a Valuation Engagement

They Are More Important Than You Think

In the valuation world, literary success and technical competency are often estranged. However, when the two do meet in the same document, the valuation report is readable, understandable, the analytics are replicable, and the reader recognizes the subject company or interest.

It all begins with understanding and explaining the defining elements of the valuation engagement correctly, which is a step in the valuation process that cannot be overlooked or given cursory treatment. If the business appraiser gets this wrong or fails to properly explain the elements in his or her report, you might receive a work product that doesn't satisfy your intended purpose.

Business valuation is defined as "the act or process of determining the value of a business enterprise or ownership interest therein" (ASA Business Valuation Standards). Business valuations can be among the most hard to understand documents for readers. Sadly, few valuations provide the reader with a clear, concise definition of what the report proposes to do and what its conclusions represent. What are the parameters of the report? Who is the client? Why does the report exist? What definition of value is used in developing the report conclusion? The answers to these and other important questions can have incalculable influence on virtually every aspect of the development and documentation of a business valuation report.

Providing the valuation report reader a well-defined set of report parameters (defining elements) starts with defining the valuation engagement–done by the client and the valuation practitioner. The first call to the valuation professional often originates from an attorney, accountant, company financial officer or other trusted advisor. Although business owners are increasingly aware of the valuation professional's role, most private entity owners have rarely experienced the valuation engagement process.

It is incumbent upon the valuation professional to work with the client or referral source to clearly understand and record these defining elements. A valuation professional that does not invest the time necessary at the beginning of an engagement to understand the defining elements of that engagement can put the engagement at risk.

The Defining Elements of a Business Valuation Engagement

The defining elements of a business valuation assignment and the resulting work product include the following primary definitions, concepts, and terms. These defining elements should foreshadow the content and organization of the valuation report.

The client
The subject entity
Entity type
State of entity organization or incorporation
Principal business location of the subject entity
Description of the subject interest
Standard of value
Premise of value
Level of value
Date of the valuation
Purpose and intended use of the valuation
Scope of the work product

Many of these individual concepts have been the focus of stand-alone publications and occasionally the source of heated debate within the profession, in courtrooms, and in academia. This article provides a relatively consensus perspective with some specific insight and caveats.

Remember, the defining elements of a business valuation are not solely up to the appraiser to determine. The appraiser works with the retaining client to inform and educate about the defining elements of the valuation.

Figure 1 is a sample of the Engagement Description and Assignment Definition used in Mercer Capital engagement letters and reports. It should be present in every full business valuation report.

Figure 1: Engagement Description and Assignment Definitions

Client Name	Referral Law Firm, PLLC
Business Name	Client Company, Inc.
Type of Entity	S Corporation
State of Incorporation	Anystate
Principal Business Location	Anytown, Anystate
Business Interest Under Consideration	Shareholder Smith's 900 shares (90%) of common stock
Standard of Value	Fair market value
Premise of Value	Going Concern
Level of Value	Controlling Interest Basis
Effective Date	January 1, 20xx
Purpose and Intended Use	Management and shareholder succession
Scope of Work (ASA Defined)	Appraisal

The Client

Defining the client of a business valuation engagement seems a self-evident requirement. In fact, virtually all professional valuation standards require the disclosure of the client who requisitioned the appraisal. From the appraiser's standpoint, this is an obligatory disclosure that recognizes specifically who is commissioning the work. However, from the client's perspective, and depending on the purpose for the valuation assignment, this could be a question requiring thoughtful consideration. It is common in the gift and estate tax environment for the legal counsel of a shareholder or estate to be the party who retains the business appraiser. Alternatively, appraisers also frequently encounter a family wealth advisor or accountant as the referring party for valuation services. As a general rule, appraisers should inquire about exactly who is doing the retaining and who will be paying the fees.

The Subject Entity and Entity Type

Most business valuations involve the appraisal/analysis of an entity that owns, manages, operates, or otherwise uses a collection of assets to achieve the business objectives of the entity. The nature of the entity can be important when assessing the unique attributes, financial or otherwise, of the legal form of the entity. There are numerous types and thematic variations on entity form. The relative strengths and weakness of entity type are beyond the scope of this article. However, from a valuation perspective, there are some key considerations that should come to mind regarding how the valuation is developed and what form the work product may take as a result of the type of entity involved. The following provides an overview of the most common business entity types

Sole Proprietorship

A sole proprietorship is a business owned by a single individual. Many small businesses are owned and operated as sole proprietorships. The revenue, expenses and profits, as the case may be, are ultimately reported on the sole owner's individual income tax return. From a valuation perspective, a sole proprietorship presents numerous challenges primarily related to the division of personal and business income and expense.

Partnership

A partnership is a business entity owned by two or more individuals. This entity structure is common for service-related businesses such as legal, medical, financial, and other professional service firms. This entity form is also a common vehicle for the pooling and collective management of family assets. Generally, a mutually agreed upon partnership agreement governs various rights, obligations, and limitations of each partner. The attributes of a partnership can vary by state regarding formation, dissolution, financial matters, and other significant aspects of the operation of the business. Partnerships usually provide a mechanism for the securitization of assets and liabilities and the corresponding sharing of the risks and rewards associated with the assets and liabilities of the entity. Income is shared on the basis of percentage ownership unless otherwise specified in the partnership agreement.

There are various types of partnerships, including general partnerships, limited partnerships and limited liability partnerships. Partnership types are differentiated by the extent to which individual partners have legal, financial, management, or other rights and obligations. The composition and features of a partnership agreement can differ from state to state. From a valuation perspective, ownership interests in partnerships are valued using the same tenets employed in the valuation of corporate ownership interests, while taking into consideration the specific attributes of the partnership interest.

The appraisal of a partnership interest can be greatly affected by the specific features of a given partnership agreement. It could be important to understand how a specific partnership agreement comports with the partnership law in the state of its organization. Certain features in a partnership agreement may not be enforceable if such features are considered too onerous or restrictive in the context of applicable/overriding state laws.

Limited Liability Company

Limited liability companies (LLCs) have grown in prevalence and offer a hybrid of characteristics associated with partnerships (i.e., flow-through or pass-through of income for taxation at the ownership level) and corporations (i.e., limited liability). There are variations of LLCs much as there are variations of partnerships. LLCs usually are governed by an operating agreement. As with a limited partnership, but not necessarily a general partnership, organizational documents are filed with the secretary of state in which the entity is established. The owners of an LLC are referred to as members. Valuation treatments are often similar to those of a partnership. One potential variation between LLCs and other flow-through entities is the differentiation of income allocation. Some LLCs provide for income allocations based on a formula or other construct different than ownership. This can have significant influence on how value is allocated to a particular ownership interest.

S Corporation

An S corporation is a corporation that has elected to be taxed under subchapter S of Chapter 1 of the Internal Revenue Code. S corporations provide the benefits of partnership taxation treatment while offering limited liability to the owners of the entity. Alternatively referred to as small business corporations, S corporations have various requirements, including a limitation on the number of shareholders (100), the composition of capital stock (only common voting and common nonvoting), and U.S. citizenry for stock owners.

C Corporation

A C corporation is a chartered, separate legal entity having its own rights, privileges, and obligations that are distinct from those of its owners. The characteristics of a corporation include limited liability of its owners, legal recognition as if it were an individual under law, free transferability of shares, governance by articles of incorporation and bylaws, oversight by a central board of directors, and subjugation to corporate and/or securities laws at both the federal and state levels.

The ownership interests of a corporation are comprised primarily of two main forms of stock: preferred shares and common shares. Both of these share types have numerous variations that may relate to ownership rights, financial remuneration, and other prerogatives.

Entity Distinctions and Their Tax Treatment

The type of the entity, in tandem with the specific type and size of the subject ownership interest being valued in an appraisal, can establish a variety of expectations and/or requirements for the content of the report and the specific methods and treatments employed by the appraiser. Regardless of the specific entity form, a broader understanding of what the entity does and how it operates is important in assessing the scope of the methodology employed in the valuation.

To some appraisers and report users, the most significant aspect of the entity type relates to its treatment under tax law and, correspondingly, its tax treatment for purposes of developing a valuation. Partnerships, S corporations, and limited liability companies are income pass-through entities. This refers to the fact that the entity's income is passed through to the individual owners of the business and then taxed as personal income. Not all states relieve pass-through entities from taxation. However, for the most part, pass-through income avoids the so-called double taxation that owners of C corporations incur in order to realize returns on their ownership interests (i.e., corporate income taxes at the entity level followed by dividend taxes at the shareholder level).

> There is significant consensus within the business appraisal profession that the income of a pass-through entity should be tax affected ...

There is significant consensus within the business appraisal profession that the income of a pass-through entity should be tax affected and/or that valuation mechanics should be adjusted in some fashion to recognize that entity income, regardless of entity type, brings with it a tax liability that is economically realized by the owners of the business. Most appraisers capture entity income taxes as if the entity was a C corporation. Others use various methods that in some fashion attempt to align the income stream of the entity with an appropriate present value discount rate. Not surprisingly, there have emerged a variety of treatments that have served to confuse and distort the economics.

Certain Tax Court rulings have modified or eliminated tax effects on the income streams of pass-through entities. The majority of financial and valuation professionals find these rulings economically untenable.

The Standard of Value

Fair market value is the standard of value used for virtually all tax matters in the U.S. According to the American Society of Appraisers, fair market value is defined as:

> The price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing buyer and a hypothetical willing seller, acting at arm's length in an open unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts. (Note: In Canada, the term "price" is replaced with the term "highest price."

Internal Revenue Service Revenue Ruling 59-60 provides additional clarifications to the definition of fair market value:

> Court decisions frequently state in addition that the hypothetical buyer and seller are assumed to be able, as well as willing, to trade and to be well-informed about the property and concerning the market for such property.

Figure 2, borrowed from *Valuing a Business, 5th Edition* (Pratt/Niculita, McGraw-Hill, 2007), provides an overview of the standard of value typically employed for valuations developed for numerous purposes.

Figure 2: Matching the Standard of Value to the Purpose of the Appraisal

PURPOSE OF VALUATION	STANDARD OF VALUE UTILIZED
Gift and estate taxes, charitable contributions	Fair market value
Purchase or sale	Can be fair market value but most often is Investment value reflecting unique circumstances and/or motivations
Marital dissolution	Varies greatly by state and may include hybrid consideration of fair value and fair market value
Buy-sell agreements	At the discretion of the agreeing parties; requires agreement at a point in time and proper wording in the agreement documents; often multiple value definitions depending on the nature of the triggering event of the agreement
Dissenting shareholder actions	Fair value in most states; may be specified by statute and/or derived from case law in each jurisdiction
Minority oppression actions	Often fair value; likely consistent with dissenter actions
Employee stock ownership plans	Fair market value (promulgated by U.S. Dept. of Labor)
Ad valorem (property) taxes	Fair market value
Going private	Fair value in most states
Corporate or partnership dissolutions	Fair value
Antitrust cases	Damages quantified according to case law and jurisdiction
Other damage cases	Damages quantified according to case law and jurisdiction
Bankruptcy	Fair market value but can vary; must consider premise of value for various assets of the bankrupt estate
Financial reporting	Fair value, pursuant to the accounting codification standard for which the report is developed

Premise of Value

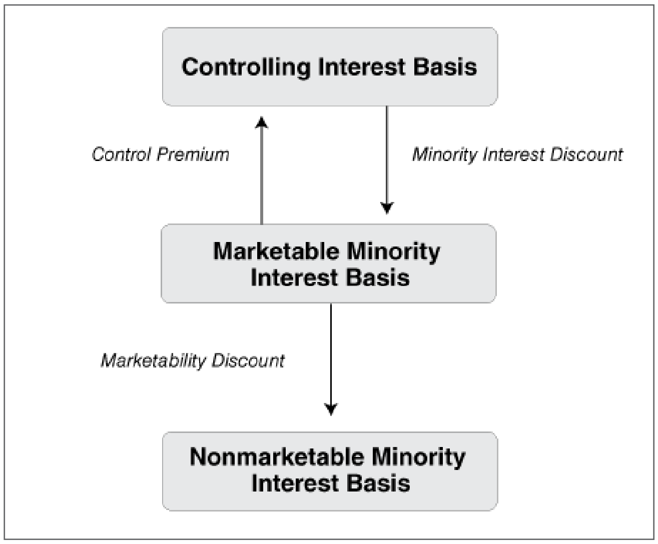
The standard of value is directly impacted by the underlying premise of value. An appraiser's premise of value is either that of a going-concern value or liquidation value. Going-concern value assumes that the business enterprise is expected to continue to operate into the future. Conversely, liquidation value is defined as the net amount that would be realized if the business is terminated and the assets are sold. Liquidation can be either orderly or forced.

Level of Value

Valuation theory suggests that there are various "levels" of value applicable to a business or business ownership interest. The levels of value can be described as:

- **Controlling interest basis** (levels) refers to the value of the enterprise as a whole. The controlling interest level of value is considered to include two components, the financial control level and the strategic control level.
- **Marketable minority interest basis** (level) refers to the value of a minority interest, lacking control, but enjoying the benefit of liquidity as if it were freely tradable in an active market. The marketable minority level of value is also on an enterprise level of value, meaning that it is developed based on 100% of the expected cash flows of the enterprise.
- **Nonmarketable minority interest basis** (level) refers to the value of a minority interest, lacking both control and market liquidity.

Figure 3: The Traditional Levels of Value



While Revenue Ruling 59-60 is the definitive ruling regarding the valuation of business interests for estate tax and gift tax purposes, the only guidance with respect to the debated concepts surrounding control premiums, minority interest discounts, and marketability discounts is contained in a single sentence of this section.

While the guidance is limited, the Ruling does appear, on balance, to embrace the conventional wisdom of valuation that suggests there are three basic levels of value. The actively traded stock of a public company is the implied reference point in this discussion. That is the middle level of value that can be described as that of a marketable minority interest in Figure 1.

The nonmarketable minority interest is the lowest level of value. The marketability discount is the difference between the value of a subject minority interest if it enjoyed ready marketability and the value of that same interest lacking marketability. In practice, this discount is generally expressed as a percentage of the marketable minority value.

The highest level of value is called the controlling interest level of value. Analogous to the marketability discount, the control premium is the difference between the value of a subject interest that exercises control over the company and the value of that same interest lacking control (but enjoying marketability). In practice, the control premium is generally expressed as a percentage of the marketable minority value. When the difference is expressed as a percentage of the controlling interest value, it is referred to as a minority interest discount. Both the concept of the control premium and that of the marketability discount have been addressed in numerous studies by appraisal professionals and by the various courts.

Two oft-forgotten concepts are important in the discussion of valuation discounts and premiums. The first is that no premium or discount has any meaning apart from a well-defined base value to which it is applied. A marketability discount has no meaning apart from a marketable minority interest value to which it is applied. Likewise with a control premium. In the same way, a minority interest discount is meaningless in the absence of a controlling interest value.

The second is that valuation discounts and premiums are ultimately outputs of, not inputs to, a well-reasoned valuation. Discounts and premiums are shorthand ways of describing differences in value attributable to economic differences between related subject interests. They are not, and cannot be treated as, the source of valuation differences. Investors evaluate the worth of a particular interest by reference to the expected cash flows, growth potential, and risk characteristics of that interest. Varying expectations among interests lead to discounts and premiums.

...valuation discounts and premiums are ultimately outputs of, not inputs to, a well-reasoned valuation ... [t]hey are not, and cannot be treated as, the source of valuation differences

Levels of value can coexist, with one shareholder owning a controlling interest, one a marketable minority interest, and one a nonmarketable minority interest. The appropriate level of value often depends on the purpose of the valuation. Stakeholders do not get to choose their level of value; there are typically clear guidelines about which level of value applies to which circumstance. Understanding the three primary levels of value is critical to the valuation process from the standpoint of the professional, the client, and other stakeholders.

State of Entity Organization or Incorporation

Identifying the state in which the subject entity of an appraisal was formed is critical. In appraisals for gift and estate tax purposes, the distinctions may only relate to state income tax rates. In other valuation engagements, such as litigation support, the state in which an entity was formed may have a bearing on the applicable definition of value for the appraisal as well as on the underlying valuation methodologies and treatments employed. Dissenting shareholder rights, corporate damages, marital dissolution, securities fraud, and so forth may all have unique requirements under applicable state and federal law. The state of formation is a relatively simple fact, but the state of formation can have significant domino effects on other defining elements in a valuation engagement.

Principal Business Location

Business location typically refers to the primary office and operational facilities of a business enterprise. For entities with a minimal operational footprint, the primary location may simply relate to the location of a post-office box or some other address used in the legal documentation to organize the entity. For many service, manufacturing, and contracting businesses, the principal location often identifies the main office and primary working location of the business. Users of appraisal reports should be curious from the beginning about the physical scale of the business as suggested by the geographic breadth of facilities and markets. Most appraisal reports will provide a summary of the subject entity that identifies the scale of the business by revenue, locations, or other attributes. This, in turn, should set an expectation about the possible scope of the information to be presented and the range of possible valuation methods employed to value the business or business interest.

Years of valuation practice have brought us in contact with an array of owners and managers of differing business models in a wide range of industry classifications. Preparers and users of valuation reports should expect to see a reflection of the broader business, market, and economic realities that surround every business in the report. Some information, such as location, is simply factual and for the record. However, context is often the most important feature a report user should understand. A simple fact like location can be a vital element of the report, both to its content and its development.

Description of the Subject Interest

What ownership interest (or security) does the appraisal purport to be valuing? As with other defining elements, this aspect of the assignment definition can suggest the nature, breadth, and sequence of adjustments and methodologies, as well as many other features the user might encounter in the report. Knowing the specific security and subject triggers the need to understand all the features of that security from an economic perspective, as well as from a rights and obligations perspective.

Business valuations may, in fact, not be business valuations if the subject interest is of a nature or class that can be valued without a valuation of the entire business. For example, the exercise to value a preferred stock interest usually is very different than valuing a common stock interest. The former could involve a relatively finite analysis, while the later could involve a top-down analysis whereby the total expression of value (whatever that might be) is divided and/or allocated among the various classes and ownership interests.

The majority of business valuations involve the expression of value for common stock ownership interests in a corporation. Obviously, with the knowledge of the entity type, the nature of the ownership or other security interests in the total capital of a business should come into view. There is a long list of possible business ownership and security interests. At the most basic level, the capital structure of a business consists of equity and debt. Identifying every possible security underlying every entity type is beyond the scope of this article. However, the following list provides the most frequently encountered equity interests by class and/or subtype.

C Corp	Common stock, voting common, nonvoting common, restricted stock, preferred stock (in numerous forms), derivatives such as options, warrants and futures
S Corp	Common stock, voting common, nonvoting common
LLC	Member(ship) interest (e.g., managing, non-managing), assignee interest
GP	Partner, equity partner, income partner, assignee interest
LP	General partner, limited partner, assignee interest

There are a plethora of debt securities as well. Closely held private businesses often have relatively simple, albeit sometimes high-dollar, debt financing. Most debt on the balance sheet of closely held businesses is assumed to be market priced, as long as the debt is from a third party lending institution and/or the terms and features of the debt are comparable to lending markets. There are often cases in which shareholders or other related parties provide debt financing whether directly to the business or via some level of personal security and/or nonbusiness collateral. In some cases, the business may have loan assets derived from lending to shareholders or to other entities such as joint ventures, real estate holding entities, and so forth. It is not uncommon to encounter debt securities on the personal balance sheets of business owners. As a rule of practice, appraisers should review and understand the nature of debt in a business entity and to apply adjustments and considerations that capture or reflect the value of such debt, on whatever side of the balance sheet the debt falls.

Purpose and Intended Use of the Valuation

The purpose for which an appraisal is performed drives the valuation methodology. Various purposes have various applicable statutory, regulatory, and jurisdictional considerations. For example, a valuation for estate tax purposes would need to consider case law, rulings, and regulations. The standard of value would be fair market value. On the other hand, a valuation for divorce purposes would need to consider state law, case history in the state, and may not use fair market value as its standard of value.

If the purpose is not considered, the entire valuation could be meaningless. This makes it imperative that the purpose is known and stated and that the use of the valuation is expressly limited to specific users for the purpose stated. Frequently, this is stated in a limiting conditions section of the report.

Figure 4: When Do Business Owners Need a Valuation?

OWNERSHIP TRANSFER MATRIX	Partial Sale/Transfer	Total Sale/Transfer
Voluntary Transfer	ESOP Outside Investor(s) Sales to Insiders/Relatives Combination Merger/Cash Out Going Public Gifting Programs Buy-Sell Agreements	Sale of Business Stock-for-Stock Exchange w/Public Co. Stock Cash Sale to Public Co. Installment Sale to Relatives/Insiders ESOP/Management Buyout Liquidation Buy-Sell Agreements
Involuntary Transfer	Death Divorce Forced Restructuring Shareholder Disputes Buy-Sell Agreements	Death Divorce Forced Restructuring Bankruptcy Shareholder Disputes Liquidation Buy-Sell Agreements

Statements clarifying that the report is only to be used for its stated purpose are intended to prevent, for example, a gift tax appraisal being used in a divorce case. A gift tax appraisal may include a marketability discount, which may or may not be appropriate for a divorce in a given jurisdiction. This is just one of many hypothetical instances in which values would not be the same for a given share of stock, depending on the purpose of the appraisal. Therefore, it is imperative that the purpose be clearly known prior to beginning the engagement, clearly stated in the report, and expressly limited for use pertaining to the stated purpose.

The purpose for which an appraisal is performed drives the valuation methodology

Users of valuation work products must appreciate that an appraiser crafts a business valuation report for a defined purpose, for a specific set of users, and using a value definition that may be specific to the purpose of the report. Thus, use of a valuation report by some other person or entity for some other reason than for its original intent could be fundamentally inappropriate and likely forbidden under the engagement letter of the provider. Valuation reports produced for corporate purposes or for financial reporting purposes would likely have the wrong foundation and underlying analysis than a report required for gift and estate tax purposes or for marital dissolution (and vice versa).

Figure 4 provides many of the common purposes for which valuations are rendered.

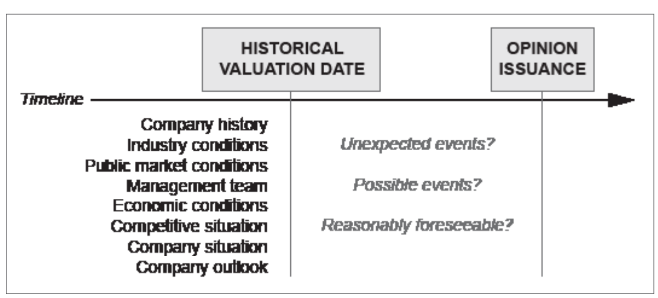
Date of the Valuation

Specifying the date for which a valuation is effective is perhaps the most important defining element for an appraisal report. Most appraisals are performed for a specific reason requiring a valuation date specific to the date of effect for a transaction or some other event. For example, the date of appraisal for an estate tax filing will be either the date of death, or, if so elected, the alternative valuation date, which is six months subsequent to the date of death. The annual valuation date for an employee stock ownership plan (ESOP) will typically be defined in the ESOP plan document or some other regular annual date determined by the trustee. However, the valuation date for many other events and purposes may not be so clear.

Establishing the effective date (referred to as the as-of date) of an appraisal report sets the stage on which the valuation will play out. It provides the overarching context in which the subject interest of the appraisal is interacting with and being affected by the internal (specific to the appraisal subject) and external (market, regulatory, etc.) environments to which it is exposed.

There is significant consensus in the valuation profession that the as-of date defines a boundary between observable, measurable history and hypothetical expectations of the future. Most appraisals do not occur in real time with the valuation date. Rather, most are performed well after a defined valuation date, at a point in time when post-valuation events, information, and other subsequent matters are observable but which may have been only remotely plausible to expect at the

Figure 5: Event Timeline for a Typical Valuation Engagement



valuation date. Figure 5 provides a timeline of considerations and events in the context of the due diligence and development for a typical valuation engagement.

The date defines the timing for the underlying information that will be reviewed. As shown in Figure 5, the scope of such information spans every aspect of the documentation and analysis that comprise a valuation report. The as-of date establishes the point in time from which future expectations may be reasonable to postulate but which remain unknown to the investor at the valuation date.

Taking heed of the various business valuation standards and practices, most appraisers and courts employ a standard of considering what was known or reasonably knowable at the valuation date. That a specific event occurred at a time subsequent to a valuation date renders that event no more relevant to the valuation than would have been reasonably foreseeable or considered as part of a continuum of possibilities that could have been expected to occur. There is, and likely will remain, debate on this critical matter. However, the various standards and guidance appear clear about what an appraiser should and should not consider in a given valuation exercise.

The direct or indirect reliance on subsequent events in appraisal opinions represents a particularly seminal challenge in valuation and one of the most opportunistic circumstances for abuse in the valuation process.

Scope of the Work Product

According to the American Society of Appraisers Business Valuation Standards, the "nature and type of the engagement must be defined. An acceptable type of engagement will generally be one of the three types [appraisal, limited appraisal, or calculation]."

Upcoming Industry Events

The senior staff of Mercer Capital attends and presents at numerous industry and professional conferences. If you are attending as well, please let us know so we can connect with you.

Heckerling Institute on Estate Planning

January 13 - 17, 2014
Orlando, FL

Matt Crow, President, **Tim Lee**, Managing Director, **Nick Heinz**, Senior Vice President and **Barbara Price**, Senior Vice President, will attend this event. Mercer Capital will also be exhibiting. Visit us at booth 408.

Matt Crow » crowm@mercercapital.com
Tim Lee » leet@mercercapital.com
Nick Heinz » heinzn@mercercapital.com
Barbara Price » priceb@mercercapital.com

Acquire or Be Acquired Conference

January 26 - 28, 2014
Arizona Biltmore Resort, Phoenix, AZ

Matt Crow, President, **Jeff Davis**, Managing Director, and **Andy Gibbs**, Senior Vice President, will present the topic "Acquisitions of Non-Depositories by Banks" on January 27. Mercer Capital will also be exhibiting.

Matt Crow » crowm@mercercapital.com
Jeff Davis » jeffdavis@mercercapital.com
Andy Gibbs » gibbsa@mercercapital.com

Step Up Your Game: Effective Business Appraisal Reporting Webinar

February 7, 2014
Webinar sponsored by BV Resources

Tim Lee, Managing Director, will co-presenting with L. Paul Hood, Jr., Esq.
leet@mercercapital.com

Professional Member Forum of the ESOP Association

February 25, 2014
New Orleans, LA

Tim Lee, Managing Director, will be attending this event.
leet@mercercapital.com

Banks with ESOPs Seminar sponsored by the ESOP Association

February 26, 2014
New Orleans, LA

Tim Lee, Managing Director, and **Andy Gibbs**, Senior Vice President will be attending and Tim will be speaking.

Tim Lee » leet@mercercapital.com
Andy Gibbs » gibbsa@mercercapital.com

Omissions & Commissions: Errors, Challenges & Solutions in Business Appraisal Reports Webinar

February 28, 2014
Webinar sponsored by BV Resources

Tim Lee, Managing Director, will co-presenting with L. Paul Hood, Jr., Esq.
leet@mercercapital.com

NCEO 2014 Annual Conference

April 8 - 10, 2014
Atlanta, GA

Tim Lee, Managing Director, and **Nick Heinz**, Senior Vice President, will be attending this event.

Tim Lee » leet@mercercapital.com
Nick Heinz » heinzn@mercercapital.com

AICPA/AAML Conference on Divorce

April 24 - 25, 2014
Las Vegas, NV

Chris Mercer, CEO, will be speaking in three sessions. He will present a general session on April 24 on "The Five Really Big Issues in Business Valuation." In addition, he will participate on the following panel discussions: "The Great Debate on the Future of Marketability Discounts" and "Hot Debate on the Hot Topics in Business Valuation."
mercerc@mercercapital.com

Users and reviewers of business appraisal reports should:

- Confirm the identity and scope of the report you are reviewing
- Understand the scope of analytical development and documentation required of such a report
- Review the report for its compliance with all respective governing standards.

Keep in mind that not all valuations are appraisals and not all appraisals are the same.

As a consumer of services, confirm what standards of performance and documentation you will receive from the provider you retain.

Conclusion

The importance of defining the valuation engagement is paramount for both practitioner and client on a business service level. The devil is certainly in the details.

Mercer Capital provides objective valuations for tax compliance. Our opinions of value are well-reasoned and thoroughly documented, which provide critical support for any potential challenge. We pay attention to detail and place a premium on communication with clients and other pertinent stakeholders during the valuation process.

To discuss a valuation issue in confidence, contact us at 901.685.2120.

Timothy R. Lee, ASA
Managing Director
leet@mercercapital

Article adapted from the book *A Reviewer's Handbook to Business Valuation: Practical Guidance to the Use and Abuse of a Business Appraisal* by L. Paul Hood, Jr., and Timothy R. Lee (John Wiley & Sons, New Jersey, 2011)

Customary and Not-So-Customary Services in the Litigation Arena

We have worked with many attorneys over the last 30 years on a broad range of projects for purposes ranging from gift and estate tax to financial reporting to employee stock ownership plans (ESOPs) to fair value determinations. In addition, a growing number of assignments have been related to litigation support. As such, this article relates our experience in the litigation support arena and highlights not only those services well known to attorneys, but other services that business valuation professionals can provide with which some attorneys may not be as familiar.

Customary Services

Customary services a business valuation professional can provide in a litigated situation are summarized below:

- Valuation in U.S. Tax Court
- Consultants in litigated matters
- Valuation in corporate dissolutions
- "Fair value" determinations in dissenting minority shareholder situations in numerous states
- Corporate tax matters
- Buy-sell agreement litigation
- Estimates of damages and lost profits
- Valuation in marital dissolutions
- Bankruptcy matters
- Formal appraisal review under Standards Rule 3 of Uniform Standards of Professional Appraisal Practice
- Determining value in condemnation situations
- Securities fraud
- Analysis of complex business issues from a valuation perspective
- Numerous other matters

Not-So Customary Services

Attorneys familiar with valuation-related litigation understand that an expert for one side is often called upon to review or critique the report of the expert on the other side. In other cases, an independent business appraiser is retained to provide the needed review and analysis, either for attorney preparation or for rebuttal at trial. We mention these customary services as a prelude to less customary services listed below (over the years, we have worked with many attorneys to provide these additional services):

- Analyzing the work of other experts to ascertain reasonableness (or not) prior to filing litigation
- Preparation of preliminary damages analyses, or developing initial damages theories, prior to the filing of damages litigation
- Preparation of questions to assist counsel in the deposition of expert and/or appropriate fact witnesses
- Developing follow-up questions based on counsel's deposition preparation ("If the response is ___, then ask ____.")
- Assistance in developing discovery requests

We or any other business valuation professional cannot provide these services unless we are retained in time. It is frustrating as an expert to be retained after the discovery has closed or after the depositions of fact and expert witnesses have been taken.

What are the benefits of these not-so-customary services?

- Making the attorney's job easier and leveraging his or her expertise
- Developing realistic expectations for damages and/or value in the preliminary stages of litigation (and assisting with managing client expectations)
- Enhancing the understanding of the strengths and weaknesses of the opposing expert's position(s)
- If appropriate strategically, pointing out errors or logical problems in the opposing expert's work at the deposition stage
- Enhancing the prospects of timely settlement

Whatever your needs in the litigation arena, please do not hesitate to contact us if you have questions or desire to have initial discussions in complete confidence.

Z. Christopher Mercer, ASA, CFA, ABAR
Chief Executive Officer
mercerc@mercercapital

Mercer Capital's
Litigation Support Services

Mercer Capital offers credible and trusted opinions to assist with a variety of tax-related controversies and disputes.

Mercer Capital brings analytical resources and over 30 years of experience to the field of dispute analysis and litigation support. We assist clients through the entire dispute process by providing initial consultation and analysis, as well as testimony and trial support.

Mercer Capital has been engaged by some of the premier professional firms in the country, including national, regional, and local law firms and their public and private clients, trust departments of financial institutions, and governmental agencies such as the Internal Revenue Service, Federal Deposit Insurance Corporation, Resolution Trust Corporation, Department of Labor, and Department of Justice.

Our professionals have been designated as expert witnesses and have testified in federal and state courts and before various regulatory bodies, including U.S. Tax Court, U.S. Federal District Court (several jurisdictions), County and State Courts (numerous states), U.S. Bankruptcy Court, state regulatory bodies, and the American Arbitration Association.

Contact Chris Mercer (mercerc@mercercapital.com) or Tim Lee (leet@mercercapital.com) at 901.685.2120 to discuss your needs in confidence.

Recent Transaction

GAVION
Memphis, Tennessee

acquired

CSG

CSG Holdings, LLC
Memphis, Tennessee

Mercer Capital issued a fairness opinion on behalf of CSG Holdings, LLC

In addition to our corporate valuation services, Mercer Capital provides transaction advisory services to a broad range of public and private companies and financial institutions. Contact us to discuss your needs in confidence.

Tim Lee
leet@mercercapital.com
901.322.9740

Nick Heinz
heinzn@mercercapital.com
901.685.2120

Karolina Grabowicz, CPA Joins Mercer Capital Analytical Staff

Mercer Capital is pleased to announce the addition of Ms. Karolina Grabowicz, CPA to our professional staff as a Financial Analyst.

Ms. Grabowicz is a Certified Public Accountant and holds a Bachelor of Arts degree and a Masters of Science degree from Rhodes College.

Prior to joining Mercer Capital, Ms. Grabowicz was employed by Ernst & Young as an Audit & Assurance Services Senior Auditor.

In her capacity as a Financial Analyst at Mercer Capital, Ms. Grabowicz will provide business valuation and financial consulting services to public and private companies and financial institutions across the nation.

Mercer Capital News

Do You Subscribe to Mercer Capital's Industry Quarterlies?

Having built a substantial client base in various industries, we have formalized our research efforts to provide a regular, detailed overview of pertinent issues and relevant current events. These industry newsletters offer a quarterly perspective on valuation issues pertinent to various industry groups and sectors. Each issue includes a segment focus, market overview, mergers and acquisitions review, and more.


Mercer Capital's
FinTech Watch
4th Quarter 2013

NEW FinTech Industry

FinTech Watch focuses on one FinTech segment each quarter, including payment processors, technology, and solutions companies.

Each issue examines general economic and industry trends as well as a summary of M&A and venture capital activity for the segment.

Industries Currently Covered

- Asset Management Industry (quarterly)
- Depository Institutions (via monthly Bank Watch newsletter)
- Business Development Companies (quarterly)
- Construction (quarterly)
- FinTech (quarterly)
- Insurance (quarterly)
- Medical Device (quarterly)

Subscribe

Mercer Capital

Mercer Capital's ability to understand and determine the value of a company has been the cornerstone of the firm's services and its core expertise since its founding.

Mercer Capital is a national business valuation and financial advisory firm founded in 1982. We offer a broad range of valuation services, including corporate valuation, gift, estate, and income tax valuation, buy-sell agreement valuation, financial reporting valuation, ESOP and ERISA valuation services, and litigation and expert testimony consulting. In addition, Mercer Capital assists with transaction-related needs, including M&A advisory, fairness opinions, and strategic alternatives assessment.

We have provided thousands of valuation opinions for corporations of all sizes in a variety of industries. Our valuation opinions are well-reasoned and thoroughly documented, providing critical support for any potential engagement. Our work has been reviewed and accepted by the major agencies of the federal government charged with regulating business transactions, as well as the largest accounting and law firms in the nation on behalf of their clients.

Contact a Mercer Capital professional to discuss your needs in confidence.

Contact Us

Timothy R. Lee, ASA
901.322.9740
leet@mercercapital.com

Matthew R. Crow, CFA, ASA
901.685.2120
crowm@mercercapital.com

Travis W. Harms, CFA, CPA/ABV
901.322.9760
harmst@mercercapital.com

Nicholas J. Heinz, ASA
901.685.2120
heinzn@mercercapital.com

Z. Christopher Mercer, CFA, ASA, ABAR
901.685.2120
mercerc@mercercapital.com

Mercer Capital
5100 Poplar Avenue, Suite 2600
Memphis, Tennessee 38137
901.685.2120 (P)

www.mercercapital.com

VALUE MATTERS™. This newsletter, published 6 times per year, addresses gift & estate tax, ESOP, buy-sell agreement, and transaction advisory topics of interest to estate planners and other professional advisors to business. For other newsletters published by Mercer Capital, visit www.mercercapital.com.