VSCPA FVS Conference
September 26, 2023

Valuation Update

Jim Hitchner, CPA/ABV/CFF

Financial Valuation Advisors

VPS Valuation Products and Services

FCG Financial Consulting Group

1

James R. Hitchner, CPA/ABV/CFF

- Managing Director, Financial Valuation Advisors Inc.
- CEO, Valuation Products and Services LLC
- President, Financial Consulting Group LLC
- Editor in Chief, *Hardball with Hitchner* publication
- 43 years in valuation services
- Former member of the AICPA task force on BV standards
- Inductee in the AICPA BV Hall of Fame
- Two-time recipient – AICPA Volunteer of the Year award
- Coauthored over 20 courses; taught over 60 courses
- Published over 150 articles; made over 400 presentations

2

2

James R. Hitchner, CPA/ABV/CFF

- **Editor and/or coauthor of the books:**
  - *Discount for Lack of Marketability Guide and Toolkit*, 2017
  - *Financial Valuation Applications and Models*, 4th edition, 2017
  - *Financial Valuation Workbook*, 4th edition, 2017
  - *PPC's Guide to Business Valuations*, 18th through 31st editions
  - *Hitchner • Pratt • Fishman, A Consensus View, Q&A Guide to Financial Valuation*, 2016
  - *Valuation for Financial Reporting: Fair Value, Business Combinations, Intangible Assets, Goodwill, and Impairment Analysis*, 3rd edition, 2011

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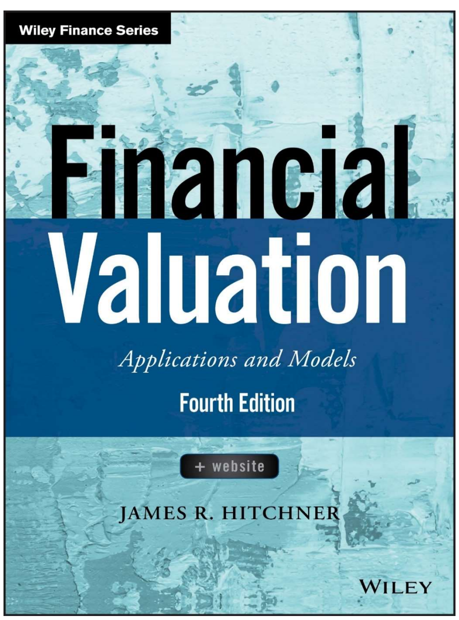

2017 (5th Edition 2023)

- **1300 pages**
- **Completely updated**
- **Coauthored by many of the top names in BV**

Jim Alerding	Jim Hitchner
Rosanne Aumiller	Vince Kickirillo
Jeff Balcombe	Mark Kucik
Neil Beaton	Eva Lang
Melissa Bizyak	Harold Martin
Marcie Bour	Ed Moran
Jim Budyak	Ray Moran
Carol Carden	Kate Morris
Stacy Collins	Shannon Pratt
Larry Cook	Ron Seigneur
Don Drysdale	Stacey Udell
Ed Dupke	Sam Wessinger
Jay Fishman	Richard Wise
Chris Hamilton	Don Wisehart
Tom Hilton	Kevin Yeanoplos

https://www.wiley.com/en-us/Financial+Valuation%3A+Applications+and+Models%2C+%2B+Website%2C+4th+Edition-p-9781119312314

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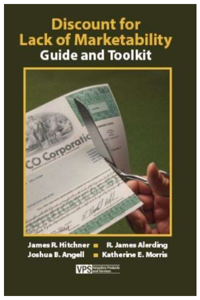

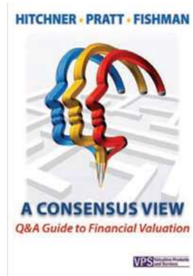

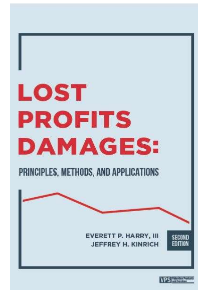

Discount for Lack of Marketability Guide and Toolkit
James R. Hitchner
R. James Alerding
Joshua B. Angell
Katherine E. Morris

A Consensus View Q&A Guide to Financial Valuation
James R. Hitchner
Shannon P. Pratt
Jay E. Fishman

Lost Profits Damages: Principles, Methods, and Applications
Edited by
Everett P. Harry III
Jeffrey H. Kinrich

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Learning Objectives

- The participant will learn about:
  - The guideline company transactions method – a fresh look, including a blockbuster court case
  - Key issues on selecting guideline public companies, e.g., is one enough?
  - Grabowski's new research on whether long-term growth rates are too high
  - Bad vs. good language in reports – you won't believe what you see
  - How to use both the new and old glossaries of business valuation terms – yeah, it's complicated
  - The IRS, appraisers, and penalties – Watch out!
  - Poll results – Who's doing what?
  - Advanced expert testimony tips

 7

7

Joseph Jones v. A Town Smoke House & Catering Inc. et. al., Circuit Court of Waynesboro, Virginia, CL19000199-00

Shareholder Oppression and Use of the Guideline Company Transactions Method

Quite the Whopper

 8

8

Oldie but Goodie Skit
Guideline Company Transactions Method

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,
Circuit Court of Waynesboro, Virginia, CL19000199-00
Shareholder Oppression — Background

- Jones was a 1/3 shareholder in a restaurant business that also provided limited catering services.
- Jones filed litigation alleging shareholder oppression and retained an expert to determine the “fair value” of his shares.
- In 2015, Virginia amended the shareholder oppression statute. The amended statute permits a company to purchase a shareholder’s interest in lieu of liquidation. Further, in determining fair value under the amended statute, minority status and marketability may be considered.
- A Town exercised this option and retained Keiter to determine the fair value of Jones’ interest. Jones retained an Adverse expert to also determine the fair value of Jones’ interest.
- The matter was tried before a judge in a bench trial.

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,

§ 13.1-749.1. Election to purchase in lieu of dissolution.

D. If the parties are unable to reach an agreement as provided for in subsection C, the court, upon application of any party, shall stay the proceedings under subdivision A 1 of § 13.1-747 and **determine the fair value of the petitioner's shares as of the day before the date on which the petition under subdivision A 1 of § 13.1-747 was filed** or as of such other date as the court deems appropriate under the circumstances. **The determination of fair value shall include consideration of all relevant facts and circumstances, including, unless the court determines it would be unjust or inequitable to do so, (i) the petitioner's minority status, (ii) the marketability of the petitioner's shares, (iii) the relevant terms of any shareholders' agreement, and (iv) if the court finds that the value of the corporation has been diminished by the wrongful conduct of controlling shareholders, the petitioner's proportionate claim for any compensable corporate injury.** In determining the fair value, the court may, in its discretion, select an appraiser to appraise the fair value of the petitioner's shares and shall assess the cost of any such appraisal to the parties, to the corporation, or both, as the equities may appear to the court.

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,

Adverse Expert's Application of the Transaction Method

- Adverse expert selected transactions based upon key words and SIC codes (the industries included both restaurants and catering businesses).
- Selected transactions that occurred over past four years (no explanation).
- Selected transactions that were greater than $1 mil. in sales.
- Selected transactions that were asset sales (no stock sales).
- Used both a revenue multiple and seller's discretionary earnings ("SDE") multiple.

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,

Failures of Adverse Expert

- Adverse expert selected transactions based on SIC code, business description, revenue size, transaction date, and asset sales. Adverse expert **failed to consider other qualitative and quantitative characteristics in assessing the comparability of the acquired companies**.
- Adverse expert **failed to consider the motivation of the buyers and sellers**.
- Adverse expert **failed to consider terms** for any of the selected transactions.
- Adverse expert **failed to consider whether the transactions were all cash deals or included an earn out**.
- Adverse expert **selected companies that included both restaurants and catering businesses. However, A Town's catering business made up only three percent (3%) of total sales.** Adverse expert's comparables included companies with roughly 50% of sales from catering, which increased the valuation of those comparable companies.
- Adverse expert **used a revenue multiple and SDE multiple. Despite a significant difference in the resulting values (the revenue multiple resulted in a value that was 2.2X higher than the value derived using the SDE multiple), the multiples were weighted equally.**

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,

Court's Opinion

"The market-based approach requires the appraiser to identify publicly traded companies in a similar line of business to the company being valued (guideline publicly traded company). **The merger and acquisition approach compare actual sales of similar companies to the subject company.** Martin rejected both these methods as he was unable to identify a sufficient sample of comparable publicly traded companies to calculate the value of the corporation. **Martin also rejected the merger and acquisition method because he was unable to find directly comparable companies that would have provided a reliable comparison for valuation. Martin therefore rejected the market base approach since this methodology requires finding comparable companies similar in qualitative and quantitative characteristics to the subject company.** On the other hand, [Adverse expert] did utilize the market-based approach to arrive at his valuation of $958,00.00. Pl. Ex. 2, Exhibit 2-K. [Adverse expert] then blended the two methodologies (capitalization of income and market-based approach) to arrive at his final opinion of value. Pl. Ex. #2 at 49." [Emphasis added.]

Joseph Jones v. A Town Smoke House & Catering Inc. et. al.,

Court's Opinion

"**The Court finds that the market-based approach in this case is a less reliable methodology for valuation of A Town**. Market based valuations are most often used to value a business that will be sold whereas the income methods are utilized to value stock in a corporation as a going concern. In this case, **[Adverse expert's] selection of comparable companies did not include relevant considerations such as the motivation of the buyers and sellers** (i.e. if the sale was between a willing buyer and seller versus a forced sale). [Adverse expert's] analysis **did not include consideration of the terms of the sale** for any of the comparable companies. [Adverse expert] **did not analyze whether the comparable sales were all cash deals or included an earn out** (i.e. and up from price with a higher price paid if certain benchmarks are met). **The databases relied upon by [Adverse expert] do not include that necessary information. Further, [Adverse expert] selected companies that included restaurants and catering businesses. However, in this case, the corporation's catering business made up only three percent (3%) of total sales. [Adverse expert's] comparable included companies with roughly 50% of sales from catering which increased the valuation of those comparable companies. Finally, [Adverse expert's] market-based approach used revenue multiples versus company profitability which does not provide an accurate basis for valuation."** [Emphasis added.]

15

15

Guideline Public Company Method
Can You Eat Just One?

- What is the desired number of guideline public companies (GPCs) that should be used in the guideline public company method (GPCM)? Is there a minimum number of "good" GPCs required to provide meaningful guidance in a valuation? What is that number?
- Can you rely on just one guideline public company if it compares well to the subject company?
- Is it better to have many GPCs that are just somewhat comparable, or is it better to have fewer GPCs that are more comparable?
- Why is size an important screening criterion?
- Can you use the GPCM when valuing smaller-type businesses? Should you check for GPCs even when you don't think you will find any? Isn't it a waste of time? [Testimony Skit]

16

16

Guideline Public Company Method
Can You Eat Just One?

- What are some of the more common valuation multiples that can be used? Is invested capital/EBITDA the best multiple?
- Is it better to use equity multiples vs. invested capital multiples?
- When you select the multiple to apply to the subject company, is it based on an average or something else?
- What is a fundamental adjustment that is sometimes applied to multiples?
- Are revenue multiples reliable?
- If you apply a multiple to a pre-tax earnings parameter like EBITDA or EBIT, is the value a pre-tax value?

 17

17

Cost of Capital Benchmark Data – December 31, 2019, 2020, 2021, and 2022

	2019	2020	2021	2022
• U.S. 30-day Treasury bill[1]	1.48%	0.08%	0.06%	3.95%
• U.S. five-year Treasury note[2]	1.69%	0.36%	1.26%	3.99%
• U.S. 20-year Treasury bond[3]	2.25%	1.45%	1.94%	4.14%
• Aaa corporate bond[5]	3.04%	2.23%	2.71%	4.70%
• 30-year conventional mortgage[6]	3.74%	2.67%	3.11%	6.27%
• Baa corporate bond[7]	3.90%	3.11%	3.37%	5.87%
• Prime rate[4]	4.75%	3.25%	3.25%	7.50%
• Large-cap stock ($29 billion - $2 trillion)[8]	11.04%	11.25%	11.39%	11.54%
• Micro-cap stock ($2.2 million - $452 million)[8]	17.67%	17.73%	17.92%	17.93%
• Small-cap stock ($2.2 million - $190 million)[8]	19.80%	19.90%	20.04%	20.04%
• Subdecile category 10b ($2.2 million - $95 million)[8]	22.67%	22.73%	22.98%	22.95%
• D&P size category 25 ($9 million - $385 million)[9]	23.35%	22.98%	23.09%	23.37%
• Subdecile category 10z ($2.2 million - $47 million)[8]	24.97%	25.02%	25.55%	25.62%
• VC Bridge/IPO[10]	20%-35%			
• VC second stage/expansion[10]	30%-50%			
• VC first stage/early development[10]	40%-60%			

 18

18

1 https://fred.stlouisfed.org/series/TB4WK
2 https://fred.stlouisfed.org/series/DGS5
3 https://fred.stlouisfed.org/series/DGS20
4 https://fred.stlouisfed.org/series/DPRIME
5 https://fred.stlouisfed.org/series/DAAA
6 https://fred.stlouisfed.org/series/MORTGAGE30US
7 https://fred.stlouisfed.org/series/DBAA
8 Duff & Phelps *2022 Cost of Capital Navigator*, CRSP Deciles Size Study –Supplementary Data Exhibits, all data from 1926 to 2021, large cap is decile 1, micro-cap is deciles 9 and 10, small cap is decile 10.
9 Duff and Phelps *2022 Cost of Capital Navigator, CRSP Deciles Size Study and Risk Premium Report Study – Supplementary Data Exhibits*, Resource Library, all data from 1963 to 2021.
10 *Valuation of Privately-Held-Company Equity Securities Issued as Compensation, Accounting & Valuation Guide,* 2013, American Institute of Certified Public Accountants, p. 148. (2019, 2020, 2021, 2022)

Grabowski on Long-Term Growth Rates … and Other Stuff

"Typical Way to Estimate Long-Term Growth Is 'Flat Wrong,'" Says Grabowski[1]

- "During the latest BVR "Power Panel" webinar, which had a 'Festivus' theme, Roger Grabowski (Kroll) aired his bugaboo about how analysts typically estimate long-term growth for the terminal value in a discounted cash flow analysis." [Power Panel: Festivus Edition, BVR webinar, Dec. 9, 2021, featuring Jay E. Fishman, Roger Grabowski, and Z. Christopher Mercer; recording at: sub.bvresources.com/TrainingEventPast.asp?WebinarID=1680.]
- "Many analysts use long-term real GDP growth plus expected inflation in their terminal values, but that **'is just flat wrong,'** he stresses." (p. 1)
- "GDP includes both existing firms and new firms, whose growth is driven by acquisition.
- 'Firms such as Amazon, Apple, Qualcomm, and NVidia—businesses that did not exist 20 years ago—drive GDP growth, so you can't assume your subject company will grow at the rate of GDP,' Grabowski says.
- Therefore, the expected long-term growth rate should reflect 'organic' growth, so the effect of the acquisitions should be backed out.
- For their research, Grabowski and Abbott removed the growth in years when the firms made significant acquisitions and/or conducted significant divestitures." (p. 4)

1 "Typical Way to Estimate Long-Term Growth Is 'Flat Wrong,' Says Grabowski," *Business Valuation Update*, vol. 28, no. 2 (February 2022), Business Valuation Resources, LLC, pp, 1, 4–5.

Grabowski on Long-Term Growth Rates … and Other Stuff

- "The implication is that an existing business will grow by an amount less than overall GDP growth.
- By how much? Grabowski cites research that estimates real long-term growth in aggregate corporate earnings at 3%, with 2% attributable to new companies. [Bradford Cornell, "Equity Growth and Equity Investing," *Financial Analyst Journal*, vol. 66 (1), pp. 54–64.]
- Therefore, the long-term average real earnings for existing businesses (i.e., organic growth) is equal to 1%, or one-third.
- This means an established, mature company will, on average, grow at the rate of one-third of real GDP plus inflation." (p. 5)
- "Their research also found significant differences across industry groups in nominal organic and real (inflation-adjusted) organic growth in revenues, EBITDA, and EBIT (see the exhibit). The chart (next slide) highlights the median organic growth rates in nominal and real terms in the 20th year after each firm went public."

Organic Growth Rates–Long-Term Steady Growth
Nominal and Real (Median Growth Rate in Year 20 After IPO)

Industry	Revenue Growth Rate		EBITDA Growth Rate		EBIT Growth Rate	
	Nominal	Real	Nominal	Real	Nominal	Real
Energy	9.00%	6.00%	4.20%	1.10%	–1.60%	–4.60%
Materials	6.50%	3.10%	3.40%	zero	–0.20%	–3.70%
Industrials	8.10%	4.50%	5.30%	1.80%	2.60%	–1.10%
Consumer Discretionary	7.90%	4.40%	6.40%	2.90%	4.50%	1.10%
Consumer Staples	8.30%	4.80%	8.00%	4.60%	7.30%	4.00%
Health Care (incl. Pharma, etc.)	11.20%	8.50%	5.50%	2.80%	4.30%	1.60%
Information Technology	9.50%	6.80%	–1.50%	–4.40%	–6.70%	–9.50%
Communication Services	7.80%	4.40%	6.30%	2.80%	5.30%	1.80%
GDP Growth 1950–2008:	Nominal = 6.39%		Real = 2.93%		Implicit GDP Deflator = 3.46%	

Source: From Shannon Pratt's ***Valuing a Business*** 6th ed., Chapter 12, "Income Approach: Forecasting Economic Income"

Bad Report Language

YOU CAN'T MAKE THIS UP

23

23

Careful Careful Careful

- Why is everything:
  - It is critical
  - It is extremely
  - It is significantly
  - It is substantially
- Why is everything:
  - It appears
  - It seems
  - It can be argued
  - It cannot be ruled out
  - It is more likely than not
  - It is possible

24

24

Often-Seen Sentences

"Often, an appraiser will find **wide differences of opinion** as to the fair market value of a particular stock."

"ABC Firm does not **guarantee** the value. Valuation is an **art** as well as a science and, by its very nature, **cannot be precise**."

"**Reasonable appraisers can differ** in their value conclusions."

New Report Reviews

- I applied the Discounted Cash Flow method **as appropriate** in my analyses as detailed in this report.
- In my valuation of [ABC], **I did not incorporate any buyer-specific synergies. As such, the standard of value I applied to value the EV of [ABC] is Fair Market Value.**
- The level of economic benefit that is **most typically utilized** is distributable cash flow.
- In my application of the GPC method, I was able to find public companies that **were comparable enough** so as to make the results implied by the GPC method **relevant for consideration** in my conclusion of value with respect to [ABC]. **[WORDY]**

New Report Reviews

- **It is commonly recognized that sole reliance on the DCF method can result in a misinformed conclusion**, especially if market data exists on which to conduct a form of the Market Approach. In fact, **a recent court case noted that "The DCF methodology has been subject to criticism for its flexibility; a skilled practitioner can come up with just about any value he wants."**
- **It is my opinion in addition that an estimate of the value of [ABC] based on multiples derived from transactions involving other companies does not value [ABC] as a going concern** operated by its current management with its usual business practices and policies and is thus inconsistent with my understanding of the definition of fair value under [State] law.

New Report Reviews

- **There are additional factors that adversely affect the value of [ABC] by increasing its risk profile or reducing its expected future cash flows that are not included in my quantitative analysis.**
- In my DCF model, the **forecast period ends in 2020, the last year that [ABC's] cash flows are forecast to be positive. Without any other information available, I assume that at that point [ABC] maximizes its value by unwinding its cash and working-capital positions**, with inventories sold and accounts receivable and accounts payable resolved.

New Report Reviews

- I base my discount rate on the Capital Asset Pricing Model, which is the **most common model** for estimating discount rates and is **widely taught in graduate and undergraduate finance and economics courses**.
- From the equity beta of [Comp] and the median equity beta of [ABC's] industry group, I calculate asset betas of approximately 0.77 and 0.88.
- **It is likely that [ABC's] discount rate, which is unobservable, is in this range.**
- **To be conservative**, I assume that a discount for lack of marketability equals the lower-bound median estimate of 35%.

New Report Reviews

- **It is possible that completed transactions of shares of [ABC] could provide some information that is relevant for this proceeding. I understand that there was a completed transaction of shares of [ABC], but I have not studied this transaction.**
- **Under the income approach, a discounted cash flow ("DCF") analysis is generally used.**
- This report constitutes our **affirmative opinion** of the fair value of …
- **This report is also responsive to both parties' expert reports.**
- **Our services in connection with this engagement relate to expert valuation services as opposed to services performed as an advocate for any party.**
- Our business valuation considered **all the pertinent factors** outlined in the aforementioned business valuation standards issued by the AICPA, the factors outlined in Rev. Rul. 59-60, as well as other factors, including but not limited to …

New Report Reviews

- Immediately below are the **more salient and pertinent** background data and information.
- Following are the **more salient and pertinent** industry data and information.
- We believe the following constitute the **most pertinent** known and knowable facts/information …
- Immediately below are the **key** normalization adjustments …
- We **believe the following risk factors justify such a significant cost of equity …**
- Pursuant to the ***Statement*** *on Standards for Valuation Services* (SSVS) of the American Institute of Certified Public Accountants **the valuation analyst is expected to disclose subsequent events and assess the extent to which these subsequent events were known, knowable, foreseeable**, etc. as of the valuation date.

 31

31

New Report Reviews

- **Thank you for the opportunity to be of assistance in this matter.**
- The analyst's compensation is fee-based or is not contingent upon the outcome of the litigation, **if applicable**, or any other factors.
- **The analyst has relied upon the work and opinions of industry experts.**
- **There are two primary methods within this approach, the capitalization of earnings and the discounted future returns methods.**
- **Based on our analysis, we believe a weighted average of the last full five years of adjusted earnings would be the most appropriate basis upon which to project future cash flows.**

 32

32

New Report Reviews

- To determine reasonable compensation, **we relied upon one of the most commonly referenced and relied upon sources of compensation information, Economic Research Institute ("ERI").**
- After summing all of the individual components of the equity discount rate, the concluded **equity discount rate was for each year** is as follows:
  - 2014 – 16.23 percent (1.44% + 6.21% + 6.58% + 2.00%)
  - 2015 – 20.23 percent (1.44% + 6.21% + 6.58% + 6.00%)
  - 2016 – 24.23 percent (1.44% + 6.21% + 6.58% + 10.00%)
  - 2017 – 28.23 percent (1.44% + 6.21% + 6.58% + 14.00%)
  - 2018 – 32.23 percent (1.44% + 6.21% + 6.58% + 18.00%)
  - **ARE YOU KIDDING ME?**

New Report Reviews

- We have performed a valuation engagement … **to assist you** in the above-described litigation.
- The value included in this report is based upon the premise that the entity will **maintain its character and integrity as a going concern**.
- [Valuation Firm] has been retained to provide a summary conclusion of value, as defined in the ***Statement*** *on Standards for Valuation Services* (SSVS) of the American Institute of Certified Public Accountants.
- Our report **[is]** in accordance with American Institute of Certified Public Accountants, ***Statement*** *on Standards for Valuation Services* and …
  - **First paragraph has typos**

New Report Reviews

- The following is a **true copy of the summary conclusion of value report** which I prepared.
- I certify that the foregoing statements made by me are true. **I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment for contempt of court.**
- **Income approaches base valuation on the earnings or benefit stream of a business focusing not on the assets of the business**, but on the ability of the business to produce income. Under income approaches, the purpose of a business is conceptualized as being able to generate income.
- **The discounted cash flow method is also called the discounted forecasted future earnings method.**

 35

35

New Report Reviews

- **In order to incorporate future growth into the estimate, it is often advised that an income forecast for at least three years is used,** although this introduces problems of its own due to the difficulty of forecasting that far into the future. **An additional complication is introduced because income in the present has a higher value than income in the future, and therefore some discount must be applied to future earnings.**
- **Management did not provide detailed future projections and as a result the discounted cash flow method was not used.**
- **In the capitalization of cash flow method, the estimate of the value of the business is derived by starting with the current annual income of the small business being valued** (measured in cash flow), dividing that quantity by the required percentage rate of return on the investment in the business minus the growth rate of the firm. **This is a standard valuation technique that is theoretically sound.**

 36

36

New Report Reviews

- **The market approach to valuing closely held companies is becoming increasingly popular.**
- **There has been praise for its objectivity since this approach consists of reviewing annual sales and other financial variables of comparable businesses for guidance in valuation.**
- A control premium is utilized when valuing a controlling interest. A minority or lack of control discount is applied when valuing a minority interest. **A control premium was not used in this valuation because the valuation methods used usually result in a control value.**
- According to IRS Revenue Ruling 59-60 1959-1 CB 237-IRC Sec. 2031 etc., potential income (earnings) is a major factor in many valuations of closely held stock. **As a result, the Capitalization of Cash Flow method is assigned a higher weight.**

Economic Outlook Sections

- Many National Economic Outlook sections omit most references and have very few cites
  - Grounds for severe cross-examination
  - Can you just cite overall canned economic data, or should all the data be properly referenced and cited?
- Does the economic outlook for industry, national, and regional need to be tied to valuation?
- Do you need a paragraph saying how it was used?

Valuation Approaches/Methods

- What level of reliance on transaction method?
- Is the Rule of Thumb method really a method?
- Should the asset approach be excluded for a profitable operating company?
- Should you use a *Mandelbaum* analysis in DLOMs?

Report Signatures

- Dual signatures – Yes or No?
- May allow both experts to be called to testify, which could be a problem
- May want to pick one as a primary appraiser and one as assisting the primary appraiser

Report Protection and Reliance

- How many Assumptions and Limiting Conditions?
  - How caveat language can hurt you
- Should you rely on R.R. 59-60 in non-tax situations?

 41

41

Glossary Madness

One more damn thing we have to deal with 

Do you have a BV Glossary Problem?

New Glossary is well done though

 42

42

2001 International Glossary of Business Valuation Terms (2001 Glossary)

- **"Adopted"** by:
  - American Institute of Certified Public Accountants (AICPA)
  - American Society of Appraisers (ASA)
  - Canadian Institute of Chartered Business Valuators (CICBV)
  - National Association of Certified Valuation Analysts (NACVA)
  - The Institute of Business Appraisers (IBA)
- All five groups adopted this glossary
- There are 123 terms and definitions
  - Of those 123 terms, 52 have been eliminated from the 2022 Glossary

 43

43

2022 International Valuation Glossary – Business Valuation (2022 Glossary)

- **"Compiled and Directed"** by:
  - American Society of Appraisers (ASA)
  - Chartered Business Valuators Institute (CBV Institute)
  - Royal Institution of Chartered Surveyors (RICS)
  - Saudi Authority for Accredited Valuers (TAQEEM)
- In the U.S., ASA has **"officially adopted"** this glossary
  - No longer part of their BV standards though
- The AICPA has not done so
- There are 148 terms and definitions

 44

44

Glossaries Impact

1. CPA and/or ABV only
   - ➢ Must follow 2001 Glossary
2. ASA only
   - ➢ Must follow 2022 Glossary
3. CPA/ABV, ASA
   - ➢ Must follow 2001 and 2022 Glossaries

 45

45

The IRS, Appraisers, and Penalties – Watch Out!

- MNCPA BV Conference **“Surprise”**
- BV tax work may no longer be low-risk engagements

 46

46

Penalties – Watch Out!

Katherline S. Jordan, Director of tax controversy at GBX Group LLC, "Appraisers as Collateral Damage in the Syndicated Conservation Easement War," Viewpoint, *Tax Notes Federal*, vol. 177, November 7, 2022, pp. 837–842.

- "Desperate for wins in the face of a multiyear war on syndicated conservation easements but with significant appellate and Tax Court losses in cases involving donors, the IRS has trained its sights on ancillary participants, including appraisers and return preparers." [IRS, "IRS Increases Enforcement Action on Syndicated Conservation Easements," IR-2019-182 (Nov. 12, 2019) ("In addition to auditing participants, the IRS is pursuing investigations of promoters, appraisers, tax return preparers and others.").] (p. 837)
- "But just as targeting civilians in war is illegal under international law, the IRS's method of attacking appraisers is patently unlawful." (p. 837)
- "the IRS has weaponized section 6695A against appraisers who have performed appraisals in connection with syndicated conservation easements and is now auditing almost every appraiser who has ever touched an easement appraisal." (p. 837)

Elimination of Multitiered Review Process

- "After section 6695A's enactment in 2006, the IRS published detailed procedures for the consideration of a section 6695A penalty in the Internal Revenue Manual …" (p. 838)
- "Until January 2020, the IRM contained a multitiered review process for section 6695A cases that granted appraisers some semblance of due process. Because the penalty is linked to a taxpayer's underpayment, the IRM recommended that the section 6695A penalty not be proposed until the underlying taxpayer examination was completed." (p. 838)
- "… the IRM implemented a two-step process that required the initial determination of a penalty to be reviewed by a manager, primary review appraiser, and secondary review appraiser. In theory, this multistep process should have ensured that inexperienced IRS personnel wouldn't be charged with assessing penalties against appraisers, particularly given the career-damaging consequences of even the proposal of a penalty." (pp. 838–839)
- "… in January 2020 the IRS eliminated the multitiered review process for section 6695A appraiser penalty cases. This change in process allowed IRS examiners with no appraisal experience to determine the appropriateness of a penalty." (p. 838)

AICPA Response

- "The American Institute of CPAs responded swiftly, warning that the IRS's actions would allow untrained IRS agents to initiate a section 6695A penalty case against an appraiser without any input from independent IRS appraisers." (p. 839)
  - Letter from AICPA to Assistant Secretary for Tax Policy David Kautter, IRS Commissioner Charles Rettig, IRS Chief Counsel Michael J. Desmond, and Holly Porter, IRS associate chief counsel (passthroughs and special industries) (June 16, 2020).
- "That course of action appears to occur regularly; in a deposition for the EcoVest case, a revenue agent tasked with evaluating section 6695A penalties admitted multiple times to not having read 'in depth' the relevant Treasury regulations and case law on how to determine the value of an easement, saying instead that it isn't her job to determine value." (p. 839)
  - See Deposition of Melissa Irons (May 11, 2021) in *United States v. Zak*, No. 1:18-cv-05774 (N.D. Ga. May 11, 2021).

AICPA Response

- "The AICPA cogently noted that **many of its members perform expert testimony on matters of valuation in federal, state, and local venues where professional reputation forms a core component of credibility.**"
- **"the receipt of a Letter 4477, informing a valuation analyst of the possibility of penalty imposition, is discoverable information** [and can be used] against a valuation analyst in any litigation setting as a means to call into question the valuation analyst's reputation and credibility even when the outcome of the section 6695A penalty proceedings resulted in no sanctions or findings against the valuation analyst (i.e. the work was performed in accordance with IRS requirements)." (p. 839)
- "the IRS hasn't retreated. Instead, it has blanketed appraisers with audits under section 6695A, many of which are conducted without even the pretense of due process and with little regard for the very section of the law it ostensibly aims to enforce. **In fact, the campaign against appraisers, and its inextricable link to the IRS's campaign against syndicated conservation easements, may have professional and financial ruination — or the mere specter of those outcomes — as its endpoint.**" (p. 839)

Guess What?

- Expectations are that this has– and will – bleed into other BV tax work
- Again, watch out?

 51

51

VPS Polls – Who's Doing What?

 52

52

Webinar Polls

What cost of equity data do you currently use? (pick all that apply)

	3/1/22	2/2/22	11/17/21	1/26/21	2/25/20	1/21/20	7/16/19	6/18/19	1/8/19
Duff & Phelps Navigator	90%	86%	83%	86%	84%	92%	88%	91%	89%
BVResources COC Pro	22%	19%	19%	23%	24%	21%	21%	32%	20%
Damodaran's data and analyses	16%	14%	20%	12%	13%	12%	14%	17%	12%
Pepperdine survey data	14%	10%	12%	7%	8%	13%	8%	18%	9%
Other or none of the above	6%	5%	7%	6%	13%	7%	9%	11%	5%

	Mean Average	Median Average
Duff & Phelps Navigator	88%	88%
BVResources COC Pro	22%	21%
Damodaran's data and analyses	14%	14%
Pepperdine survey data	11%	10%
Other or none of the above	8%	7%

Hardball with Hitchner, Issue 20, June 2022, www.valuationproducts.com.

Webinar Polls

Do you apply a size premium?

	11/17/2021	9/15/2020	7/16/2019	6/18/2019	1/8/2019	Mean Average	Median Average
Yes	87%	83%	80%	92%	90%	86%	87%
No	8%	13%	17%	8%	9%	11%	9%
Not applicable	4%	3%	3%	1%	1%	2%	3%

What CRSP size premiums do you use for smaller businesses? (pick all that apply)

	11/17/2021	11/15/2018	9/17/2018	4/26/2017	Mean Average	Median Average
Micro-cap	18%	18%	10%	21%	17%	18%
Decile 10	73%	71%	72%	70%	72%	72%
Subdecile 10b	18%	21%	6%	18%	16%	18%
Subdecile 10z	3%	12%	3%	12%	8%	8%
I do not use CRSP data	11%	8%	8%	13%	10%	10%

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Webinar Polls

Have you increased your ERP and/or company-specific risk with COVID known or knowable?

	3/2/2021	1/26/2021	10/29/2020	7/1/2020	6/9/2020	5/14/2020	Mean Average	Median Average
Both	19%	16%	31%	29%	28%	42%	28%	29%
Neither	9%	18%	5%	5%	6%	5%	8%	6%
ERP only	4%	4%	5%	3%	9%	11%	6%	5%
CSR only	54%	51%	38%	52%	43%	23%	44%	47%
Not applicable	13%	11%	21%	11%	14%	20%	15%	14%

When using Duff & Phelps data, which ERPs do you use? (pick all that apply)

	7/30/2020	11/15/2018	Mean Average	Median Average
CRSP historical (1926 forward)	41%	41%	41%	41%
CRSP supply-side (1926 forward)	37%	39%	38%	38%
Risk Premium Study (1963 forward)	35%	21%	28%	28%
D&P recommended ERP	46%	35%	41%	41%
I do not use D&P	6%	5%	6%	6%

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55

55

Webinar Polls

Which income approach methods are you now using most for small businesses with COVID?

	10/29/2020	5/14/2020	Mean Average	Median Average
Build-up Model	58%	66%	62%	62%
MCAPM	6%	7%	7%	7%
Both	24%	15%	20%	20%
Neither or other	2%	2%	2%	2%
Not applicable	10%	9%	10%	10%

Which of the following models do you typically use for smaller businesses? (pick all that apply)

	11/15/2018	3/29/2017	Mean Average	Median Average
BUM	50%	52%	51%	51%
MCAPM	21%	14%	18%	18%
Both	15%	19%	17%	17%
Other	13%	16%	15%	15%

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56

56

Webinar Polls

What do you normally use in terms of a long-term growth rate?

	2/2/2022	1/26/2021	7/30/2020	11/15/2018	9/17/2018	1/31/2018	6/28/2017	3/29/2017
3% or less	47%	43%	46%	38%	42%	41%	41%	38%
3% to 5%	47%	51%	46%	57%	54%	55%	54%	57%
3% to 6%	4%	3%	4%	4%	3%	4%	4%	5%
7% or higher	1%	0%	0%	0%	0%	0%	1%	0%
Not applicable	2%	3%	3%	1%	2%	1%	0%	0%

	Mean Average	Median Average
3% or less	42%	42%
3% to 5%	53%	54%
3% to 6%	4%	4%
7% or higher	0%	0%
Not applicable	2%	2%

 57

57

Webinar Polls

Do you usually tax affect the earnings of PTEs as a starting point in a valuation?

	3/1/2022	9/30/2021	2/25/2020	10/17/2019	5/16/2019	10/11/2018	8/14/2018	1/31/2018	10/26/2017
Yes	66%	74%	75%	78%	71%	73%	71%	76%	84%
No	18%	15%	19%	13%	19%	17%	24%	20%	10%
Not applicable	16%	11%	6%	8%	10%	10%	4%	4%	6%

	Mean Average	Median Average
Yes	74%	74%
No	17%	18%
Not applicable	8%	8%

What S-corp models do you currently use, if any? (pick all that apply)

	9/30/2021	10/17/2019	2/13/2019	10/11/2018	8/14/2018	10/26/2017	Mean Average	Median Average
Delaware MRI	22%	28%	26%	27%	36%	39%	30%	28%
Treharne	6%	14%	13%	14%	19%	13%	13%	14%
Van Vleet SEAM	22%	28%	25%	18%	26%	21%	23%	24%
Fannon	5%	10%	10%	11%	15%	10%	10%	10%
None of the above	55%	41%	51%	48%	39%	50%	47%	49%

 58

58

Webinar Polls

If you only have the usual minimal data concerning a transaction, do you usually rely on transaction databases as:

	3/1/2022	2/2/2022	2/25/2020	2/13/2019	9/17/2018	Mean Average	Median Average
A primary method and value	8%	9%	9%	9%	3%	8%	9%
A secondary or corroborating method and value	71%	69%	65%	72%	59%	67%	69%
Dismiss the method and value as unreliable	20%	18%	26%	18%	33%	23%	20%
Not applicable		4%					

Do you believe you can have an opinion of a calculated value as an expert witness?

	3/1/2022	7/30/2020	2/25/2020	1/8/2019	3/22/2018	1/31/2018	Mean Average	Median Average
Yes	40%	50%	39%	55%	62%	51%	50%	51%
No	49%	45%	53%	43%	33%	41%	44%	44%
Not applicable	11%	5%	8%	3%	6%	8%	7%	7%

 59

59

Webinar Polls

Which economic report(s) do you use? (pick all that apply)

	2/2/2022	11/17/2021	Mean Average	Median Average
Mercer	16%	13%	15%	15%
TagniFi	16%	11%	14%	14%
BVResources	63%	54%	59%	59%
ValuSource	27%	19%	23%	23%
None of the above	18%	25%	22%	22%

What is your policy concerning draft reports in litigation?

	6/15/2021	12/17/2019	8/16/2017	Mean Average	Median Average
Keep all internal drafts and drafts sent to attorney	18%	15%	13%	15%	15%
Do not keep internal drafts but keep drafts sent to attorney	23%	30%	32%	28%	30%
Do not keep any drafts	31%	23%	28%	27%	28%
Policy depends on attorney instructions per engagement	19%	17%	16%	17%	17%
Not applicable	8%	15%	10%	11%	10%

 60

60