

American Bar Association

Business Valuation Standards What Do They Mean to You?

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Why should a matrimonial attorney pay attention to business valuation standards? Quite simply, because your knowledge can yield big judgment dividends by supporting your valuation expert or by impeaching the credibility of the opposing expert.

Observance of professional standards distinguishes an expert opinion from fact testimony. Not all standards are applicable to every appraiser, yet quite often two or more sets are applicable to an individual expert who is multi-credentialed or touts membership (even candidacy for a designation) in several organizations. Adherence to standards implies an expert analysis that is diligent, reliable, and verifiable with accepted professional procedures: experts who follow recognized standards are far less likely to fall victim to Daubert challenges. Conversely, experts who fail to perform work in accordance with recognized standards are subject to criticism and may have their credibility impugned by sharp opposing counsel.

Professional Organizations

In 2005, business valuation experts in the United States are likely to be members of -- or received education from -- one of four professional organizations: The American Society of Appraisers (ASA), the Institute of Business Appraisers (IBA), the National Association of Certified Valuation Analysts (NACVA), or the American Institute of Certified Public Accountants (AICPA). All of these organizations either have professional standards or are in the process of adopting standards that address ethics, competency, objectivity, accepted procedures to develop the business valuation opinion, and how to report the opinion. These standards are dynamic; periodic updates, revisions and exposure drafts of new language are being regularly promulgated.

Beyond pronouncements of ethics and due professional care, each of the standards above fundamentally addresses how an appraisal of equity assets is to be performed, and the various forms of reporting. "Development Standards" generally describe identification of the subject, consideration of approaches and methods of analysis, application of premiums and discounts, support for the opinion, and requirements to maintain proper files and work papers substantiating the opinion. "Reporting Standards" generally outline the different varieties of written or oral communication that are acceptable. Several of the standards indicate that in litigation settings, reporting formats may be specified by legal counsel, thereby permitting a departure from noted standards. Any loosening of the reporting standards for litigation purposes, however, does not loosen the developmental standards for doing the analysis or keeping records to support the analysis. Standards promulgated by the AICPA have been in various drafts over the past 3 years, but should be formally released for final "exposure" in the coming months with formal adoption of the requirements anticipated later this year or in 2006. All of the organizations

seem to be moving toward common definition of certain terms. The current International Glossary of Business Valuation Terms can be found at www.bvappraisers.org/glossary/glossary.pdf.

Other Professional Standards

In addition to the four organizations above, attorneys may also see reference to four other sets of professional standards that address business valuation analysis directly or indirectly.

Uniform Standards of Professional Appraisal Practice (USPAP)

These are standards originally developed in 1987 by the Appraisal Foundation (and continually updated; see www.appraisalfoundation.org) as a response to real estate valuation needs from the Savings & Loan debacles in the 1980s. USPAP Standard 9 addresses how to do business valuation work. Standard 10 addresses how to report business valuation work. There are also two trailing sections in USPAP -- "Statements" have the same impact and requirements for practice; "Advisory Opinions" are simply illustrations of specific situations without the weight of Standards. Members of the ASA must conform to USPAP; however, members of IBA, NACVA and the AICPA are not required to conform to USPAP. As the first released standards for business appraisers, USPAP has set the tone that others generally follow.

Chartered Financial Analyst Institute

This Institute (see www.cfainstitute.org) has a code of ethics and standards of professional conduct. CFAs normally opine on investment strategies and are commonly employed by banks and financial management firms, but do serve as experts in business valuation.

The Internal Revenue Service (IRS)

For a copy of the IRS guidelines, see www.bvresources.com/FreeDownloads/irs-guidelines.pdf. The IRS has recently published appraisal standards for internal use and work by their outside appraisers. Conceivably, reference to these standards would only surface in matrimonial issues with extreme tax consequences.

International Business Valuation Standards

These come from the International Valuation Standards Committee (see www.ivsc.org/pubs), and are the least likely to arise in matrimonial settings unless equity assets are being appraised with extensive international connotations with business valuation opinions from foreign appraisal professionals.

What Should a Matrimonial Attorney Do?

When presented with an equity asset issue, the response of most attorneys is to hire an expert, who is an accountant or an otherwise credentialed analyst, to quickly form an opinion. Opposing parties usually do the same, with too often the result of a wide gap in opined value between two dueling experts. Your understanding of the experts' professional standards early in the process can help to avoid this problem, with more efficient use of the clients' resources and a higher quality division of assets.

In hiring your own business valuation expert, first determine if the expert is a member of one or more of the professional organizations. Go the appropriate organization's Web site; check your expert's claimed credentials, and download the current version of standards.

- Inquire as to the "level of service" to be provided.

- Based on preliminary information you have shared with the expert, ask if there are any anticipated qualifications to the opinion.
- Clarify the reporting desired -- oral advisory, some form of written correspondence, and/or formal testimony.
- Ascertain if the expert has any hesitation of competence to undertake the assignment, and how he or she plans to overcome those issues if you are presented with an opposing expert who appears to have presented less than competent work.
- Establish the professional standards under which the work was performed. If the expert is a member of multiple organizations, multiple standards may apply. In this case, the expert may be bound by the highest, or most acute, level of work or reporting, not the lowest.
- Research both the level of analysis undertaken and the reporting of the opinion. Caveats such as calculation, consulting, preliminary findings, or limited opinion are tip-offs that you do not have a full appraisal or unambiguous opinion of value. Ask why!
- Clarify any difference between the standards and the opposing expert's analysis with your own (or separately engaged) business valuation expert. Interpretations of minimum standards given materiality, financial comparison, and common valuation practice are necessary. Remember that the glass of water may be half full or half empty depending on perspective.
- Position the most egregious differences in deposition.
- Have fun in mediation or cross-examination.

Concluding Thoughts

Business valuation professionals are continuing to grope with the development of ethical and work standards through a variety of organizations. These are dynamic, with periodic updates to the wording. Whether a given expert analysis meets or fails to meet the threshold of professional and competent work is a finding of an additional expert opinion rather than a finding of fact. Work with your own expert to provide you with an education of the current progress of standards. In high dollar equity asset matters, your knowledge of what to expect in terms of good expert work and poor expert work should yield the benefits of a compelling presentation.

Organization	Web Site	Written Standards?	Required Adherence?
ASA	www.appraisers.org	Yes	Yes
IBA	www.go-iba.org	Yes	Yes
NACVA	www.nacva.com	Yes	Yes
AICPA	www.aicpa.org	Yes (in draft)	Pending (late 2005/early 2006)

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