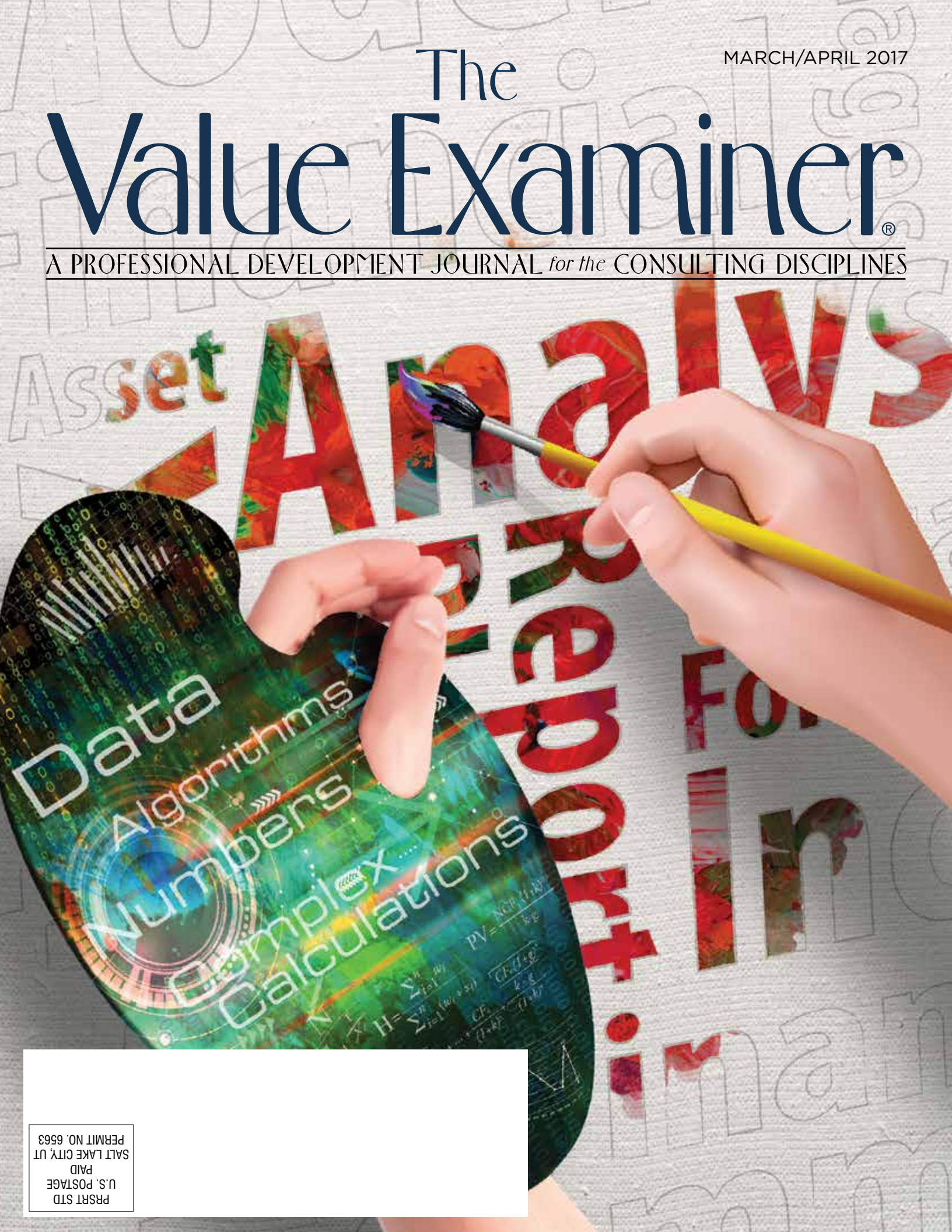
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Theil-Sen Estimation for the Market Approach

By Phillipp D. Schaberl, CPA, PhD; and Keith Sellers, CPA, ABV, PhD

Ordinary Least Squares (OLS) regression is the most common multivariate method for the Market Approach of business appraisals. However, when using OLS regressions for financial and valuation related variables, the analyst is likely to face problems due to outliers and or heteroscedasticity of the regression residuals. This article introduces and explains the Theil-Sen Method (TSM), which can offer significant advantages over OLS.

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To meet these challenges and to offer insights and solutions, NACVA and the CTI's Annual Consultants' Conference—June 7–10, 2017, at the Swissôtel in downtown Chicago—will feature sessions that will shed light on and add commentary to the most critical issues facing the profession. In this Conference Preview, *The Value Examiner* gives an overview of what to expect during the Conference, previews some of the hottest discussion topics, discusses trends with two of the presenters, and provides an interview with John Borrowman reagarding the prospects of hiring qualified value analysts in the future.



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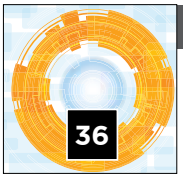
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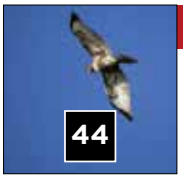


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By Rod P. Burkert, CPA, ABV, CVA

The author interviews sole practitioner Daniel Gilbert, CPA, ABV, CVA, CFF, from Portland, Oregon

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VALUATION

THEIL-SEN ESTIMATION FOR THE MARKET APPROACH

By Phillipp D. Schaberl, CPA, PhD; and Keith Sellers, CPA, ABV, PhD

Ordinary Least Squares (OLS) regression is the most common multivariate method for the Market Approach of business appraisals.[1] However, when using OLS regressions for financial and valuation related variables, the analyst is likely to face problems due to outliers and or heteroscedasticity of the residuals or errors, defined as the difference between the actual and the predicted Y values, where Y is the variable of interest that we want to predict. Fortunately, the Theil-Sen Method (TS/TSM) for regression analysis provides a robust and intuitive alternative to OLS.

The objective of this article is to introduce and explain the TSM, which can offer significant advantages over OLS. First, we discuss the advantages of OLS over ratio analysis while documenting common problems with data sets used in valuation and their implications for OLS. Next, we introduce the TSM as an alternative to estimate regression parameters in the context of business appraisals. We also discuss the advantages and disadvantages of TS relative to OLS. Finally, we run a "horse race" between OLS and TS using a sample of bank acquisitions from the years 2008 to 2016.

There are a few things to keep in mind while reading this article. First, while OLS is widely used, it has some inherent limitations when using common valuation data. Second, although the TSM has recently been used in academic research on the relationship between business value and accounting numbers, the authors are not aware that TS has been used in the valuation of closely held businesses. Third, given the computer intensive nature of the TSM, its implementation might generally require some programming in Python, R, SAS, or Visual Basic. Fourth, the authors have extensive training in OLS and have first-hand experience with the problems associated with data sets commonly used in business valuation and capital market accounting research. As a result, we have started using TS in our valuation engagements and academic work. Based on recent academic research, TS dominates OLS, yielding more accurate value estimates.

OLS VS. VALUATION RATIOS

The most common application of OLS for the Market Approach uses an observed dependent variable such as market price (for publicly traded comparable companies) or price paid (for completed transaction data) on the left-hand side of the regression and several firm-specific financial variables as independent variables on the right-hand side of the regression. One of the major advantages of OLS over using valuation ratios, such as the price-to-earnings ratio, is that OLS will simultaneously find the best fit when using more than one independent variable, avoiding the issue of picking a single valuation ratio or subjectively weighting the results of multiple valuation ratios.

Another key advantage of OLS is the ability to include non-financial, firm-specific independent variables as well as temporal variables that cannot easily be captured in pricing ratios, including indicator or dummy variables. When using

1 For an excellent discussion on the use of OLS, especially multiple regression for the Market Approach, please see Jay Abrams, "Regression Analysis in the Market Approach: Using the Gordon Model as a Guide to Selecting Independent Variables," *The Value Examiner* March/April 2012.

valuation ratios, the analyst will often face the dilemma of removing otherwise comparable firms that do not fit well with one or more of the selected criteria. A well-designed OLS model will often allow the analyst to retain these observations in the analysis by including an additional variable that captures value-relevant information.

For example, assume a dataset shows a systematic difference in price if an otherwise comparable entity is in a large metropolitan statistical area (MSA) or a smaller city. If valuing a company located in a smaller city, the analyst may choose to exclude the otherwise comparable companies located in an MSA when using pricing ratios. With OLS, one could control for the variation in city size with a continuous variable measured as the population of the community or as a dummy variable coded as 1 (0) if the location is (is not) an MSA. Including these observations in the sample yields the following benefits. First, the analyst avoids a potentially critical subjective decision. Second, the sample contains more observations, more information, and more value drivers that potentially help explain the variation in price across firms. In summary, OLS can provide important benefits over pricing ratios when the assumptions underlying OLS are met. In practice, however, violations of these assumptions can result in misleading estimates of value when using OLS.

COMMON PROBLEMS WITH OLS

Two problems that are common when using OLS to estimate the relationships between observed values and accounting and financial data are heteroscedasticity and outliers. According to Ohlson and Kim (2015), "both issues are more or less inescapable in case of dollar value variables."[2] In settings where firm price is regressed on firm-specific accounting variables, the presence of outliers can have a meaningful impact on the parameter estimates in OLS regression which in turn can dramatically change the appraisal value of a business. As we discuss in the next section, academics and practitioners have adopted commonly used methods to reduce the impact of heteroscedasticity and outliers. Unfortunately, these solutions require the analyst to make a subjective selection, thereby reducing the objectivity and defensibility of the resulting valuation.

2 See Ohlson and Kim, "Linear valuation without OLS: the Theil-Sen estimation approach," *Review of Accounting Studies* (2015).

HETEROSCEDASTICITY

Heteroscedasticity is present in a sample where the variability of Y (e.g., firm value) is unequal across the range of values of one or more of the independent variables. To detect heteroscedasticity one usually plots the residuals (on the Y-axis) against the predicted values (on the X-axis). Most applications of OLS for data sets used for valuation purposes (dollar sales, total assets, revenues, net income, etc.) will suffer from heteroscedasticity. As pointed out by Ohlson and Kim (2015), "heteroscedastic error terms raise the specter of inefficient estimation and the need to scale variables." Hence, analysts frequently scale the dependent and independent variables of a regression to mitigate the influence of size. Abrams (2012) explains that a "scaled dependent variable… has the advantage of eliminating or at least reducing the statistical problem of heteroscedasticity." However, he goes on to point out problems created by scaling such as low and unreliable adjusted R squares and, potentially, the lack of a viable denominator (or missing data) for scaling when using some transaction databases.

OUTLIERS

Outliers can lead to several issues. First, they can skew data so that alternative measures of central tendency such as means and medians differ substantially. Second, they can increase the standard deviation and the coefficient of variation, leading to the incorrect rejection of a valuation ratio. Third, they can substantially increase or decrease the arithmetic mean of a metric, resulting in a biased and possibly poor estimate of value. Unfortunately, the adverse effects of outliers are typically magnified, not reduced, by OLS regression.

When estimating the regression coefficients, OLS minimizes the sum of the squared errors (hence the name ordinary least squares). A consequence of this methodology is that an influential outlier can have a disproportionately large impact on OLS coefficient estimates. Thus "outliers", which, in the context of this paper, are defined as observations that have large errors but otherwise appear to be valid observations, tend to have an undue influence on the OLS parameter estimates which can potentially yield misleading results.

To deal with outliers, analysts typically truncate or winsorize the data or subjectively identify and remove individual observations from the sample. Note that these steps require a subjective decision to modify or remove potentially valid and informative observations. In other words, the common

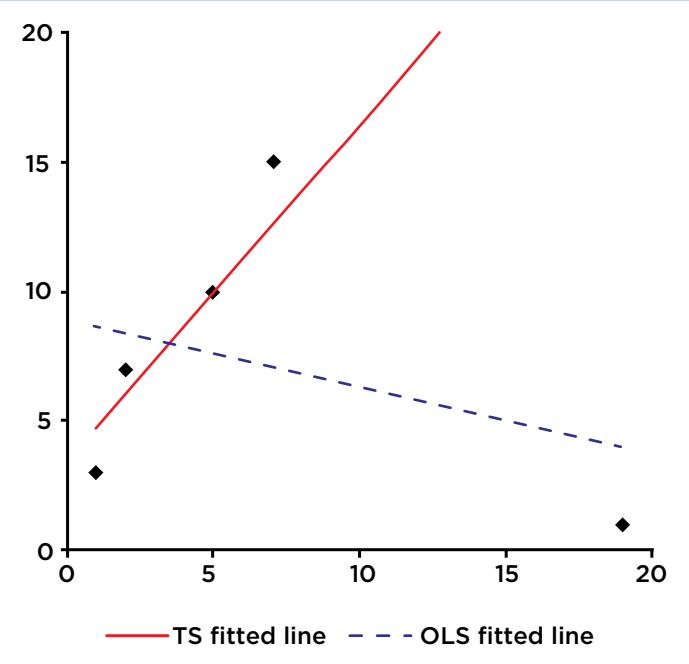
THE THEIL-SEN (TS) ESTIMATION METHOD

TS was first proposed by Theil in 1950 and extended by Sen in 1968.[1] It has been acknowledged in several popular textbooks on nonparametric and robust statistics[2] as a robust alternative to OLS in the presence of heteroscedasticity or outliers and is widely recognized in the field of statistics.[3]

The methodology underlying TS is straightforward. Rather than running a single OLS regression using all available observations in the sample, repeated OLS regressions are run using thousands of small sub-samples of n randomly selected observations, where n equals the number of estimated parameters (i.e., intercept and coefficients). Hence, each sub-sample yields a set of n parameters, some of which may be heavily influenced by outliers. The final TS parameter estimates are calculated as the medians across the thousands of parameter estimates generated from the small sub-samples. Using medians across thousands of sub-samples removes the undue influence of outliers.

Here we show a simple example from Ohlson and Kim (2015, p. 434) that nicely illustrates the difference between TS and OLS. The following data points (X, Y) are plotted in Figure 1: (5, 10), (2, 7), (1, 3), (7, 15), and the outlier, (19, 1). Based on any combination of the first four data points, one can readily infer a positive slope. Only the outlier suggests a negative slope. By minimizing the sum of squared residuals, OLS estimates a slope of -0.26. It is hard to argue that the OLS line shown in Figure 1 is a good representation of the "typical" relationship between X and Y. In contrast, a TS Approach that estimates a slope for each of the ten possible pairs of data points estimates a slope of 1.3.

FIGURE 1



Note that for our approach, it is possible that any given observation may or may not be included in any of the random samples. Hence, some observations are likely to be included in more than one sub-sample regression, especially if the number of regressions is large.[4] One key aspect of TS is the very large number of samples which are typically run. This aspect can make the implementation of TS challenging for users without programming skills. For example, for our study we used the results from 50,000 randomly drawn sub-samples per year, totaling 450,000 individual OLS regressions.[5]

1 See "A rank-invariant method of linear and polynomial regression analysis, *Nederlandse Akademie Wetenchappen*, Series A, 53, 386–392 and "Estimates of the regression coefficient based on Kendall's tau," *Journal of the American Statistical Association*, 63(324), 1379–1389.

2 See Ricardo A. Maronna, Douglas R. Martin, and Victor J. Yohai, Robust Statistics: Theory and Methods, John Wiley & Sons, 2006, for a broad discussion.

3 See for example "Theil-Sen Estimators in a Multiple Linear Regression Model," by Dang, Peng, Wang, and Zhang, available at http://home.olemiss.edu/~xdang/papers/MTSE.pdf.

4 Studies indicate that the TS is robust with or without replacement of the selected observations and we performed our tests allowing replacement.

5 The large number of repeated regressions may appear to be overkill. However, the number of possible combinations for even a relatively small set of data can be staggering. For example, avid poker players are probably aware that there are 2,598,960 distinct five-card poker hands. There would be an identical number of potential discreet samples from fifty-two comparable firms when using five independent variables (calculate as N!/{K!(N–K)! where N is the number of comparable firms and K-1 is the number of independent variables). In the second article on this topic, we discuss the actual number of samples generally required to estimate stable coefficients.

occurrence of outliers in market data leaves the analyst with two poor choices—leave the apparent outlier(s) in the dataset and rely on the potentially biased results, or remove/modify influential outliers and acknowledge that these subjective adjustments to the data have materially altered the outcome of the valuation process.

In summary, OLS offers a very attractive methodology for the Market Approach to valuation when critical underlying assumptions are met.[3] But in cases when the OLS assumptions are violated, as is often the case for data used in business valuation, OLS can generate misleading results due to its sensitivity to influential observations and heteroscedasticity.[4] To address these problems with OLS, we introduce the TSM, an alternative method of robust regression. Results from TS (see sidebar) are unaffected by either heteroscedasticity or outliers. In other words, it gives the analyst a third and much better alternative to the "two poor choices" outlined above when using OLS. Leone et al., (2015) concludes that robust regression "provides a statistical compromise by including all of the original (raw) data points, but down-weighting unusual and influential observations, versus excluding or altering, perhaps arbitrarily, the original data." It is for this reason that we propose the use of TS for the Market Approach.[5]

BENEFITS OF THE TSM

To summarize, we want to point out three key benefits of TS. First, the TS estimates are not affected by heteroscedasticity. Second, there is no need to scale variables. Third, there are no distortions from outliers and extreme observations.

An additional and possibly very important benefit for valuation analysts is potentially greater stability of coefficients across time. When using completed transaction data, the analyst must use judgment as to how far to "look back" when selecting transactions. From a statistical perspective, what one is really doing is determining whether older transactions represent a separate population, distinct from more recent transactions. Widely varying OLS coefficients over time suggest that older data should not be used. However, this instability may be nothing more than the influence of outliers within annual data and rejection of this older data as being "too stale" may inappropriately alter one's valuation conclusion. Research suggests greater accuracy and stability for coefficients over time when using TS. For instance, based on S&P 500 firms for the years 2001 to 2010, Ohlson and Kim (2015) find that the TS coefficients are more stable across time than the corresponding OLS coefficients.

DISADVANTAGES OF THE TSM

Aside from the computational challenges, we have identified only one limitation of TS that might impact a typical valuation analysis. Since the TS estimates are calculated as the median parameters across the different sub-samples, using dummy variables appears to be problematic since the median would, by definition, be either zero or one. Thus, if one wants to capture the effects of, for example, relative size of the local population on the value of a business, one could use a continuous measure such as actual population rather than a dummy variable to capture population size.[6]

Additionally, some widely used and understood statistical measures such as adjusted R squared are not readily available with TS. However, as will be discussed in our follow up article, alternative summary measures of model fit are available. Thus, we do not consider this to be a significant impediment to the use of TS.

TS AND OUTLIERS

The data sets used in capital market research in accounting (CMAR) often contain outlier observations that can have undue influence on the estimated parameters of the models and can therefore influence statistical inferences. Winsorization and truncation of the data are very common univariate approaches used in academic studies. As we mentioned previously, these subjective modifications of the data can potentially alter valid observations.

3 Guthrie et al., shows how two outliers in a sample of 865 firms can result in different inferences when relying on OLS. See Guthrie, K., Sokolowsky, J., & Wan, K.-M. (2012). CEO Compensation and Board Structure Revisited. *The Journal of Finance*, 67(3), 1149–1168.

4 Since a discussion of the critical assumptions underlying OLS regression are beyond the scope of this article, we would like to refer the reader to an introductory statistics text or online sources.

5 According to UCLA's Institute for Digital Research and Education, robust regression can be used in any situation in which you would normally use least squares regression but you have outliers or high leverage data points. Unless the analyst can conclude that these data points are not data entry errors or from a different population (not a comparable company), there is no compelling reason to exclude them from the analysis. "Robust regression represents a compromise between excluding these observations entirely from the analysis and including all the data points."

6 We generally would consider one or more dummy variables for this sort of measure to avoid potential non-linearity but TS appears to negate this concern.

Leone et al., (2015) compared the efficacy of OLS with robust regressions using simulations and accounting data.[7] They did not find any empirical evidence that winsorization or truncation is effective at dealing with the effect of influential observations. They go on to say:

> *Our simulations demonstrate that winsorizing does little to mitigate the effect of observations that are actually influential and truncation imparts a downward bias to OLS coefficients. Thus, researchers should use caution when relying on these approaches. We find that robust regression outperforms truncation and winsorization, especially in the presence of observations that are driven by unusual economic events that are correlated with the dependent and independent variables.*
>
> *The findings lead us to recommend that future CMAR studies consider using robust regression, or at least report sensitivity/robustness tests using robust regression, especially because robust regression focuses on overall model fit to deal with influential observations, in addition to being relatively straight-forward to implement in typical CMAR settings (page 6).*

Similarly, Ohlson and Kim (2015) performed extensive tests using data drawn from S&P 500 firms. While a description of those tests is beyond the scope of this paper, they concluded that TS dominates OLS in terms of goodness-of-fit and stability of parameter estimates across time.

A HORSE RACE BETWEEN OLS AND TS?

Under ideal circumstances OLS will perform as well as TS. However, with real-world data, TS tends to dominate OLS (e.g., Ohlson and Kim, 2015). This has even been demonstrated using information on prices and accounting variables drawn from publicly traded companies. To extend this research to the business valuation profession, we use a large set of completed transaction data to estimate and evaluate regression coefficients using traditional OLS as well as TS.

Our dataset consists of information pertaining to 632 commercial bank acquisitions completed over the period starting on January 1, 2008, and ending on December 31, 2016. We selected this data set for several reasons. First, bank M&A data is extremely "clean" in that all financial information on the banks is publicly available from the FDIC. Second, the large number of transactions across a considerable period and over varying economic conditions provides an opportunity to investigate the stability of coefficients across time. Third, one of the authors has extensive experience in valuing commercial banks, providing key insights into the selection of appropriate independent variables (value drivers) as well as the reasonableness of resulting regression coefficients and model outputs. Thus, the data captures a wide range of observations in terms of size, profitability, etc., over a nine-year period encompassing widely varying market conditions.

We used the following variables in our analysis. The dependent variable, VALUE, refers to the observed price paid to acquire one-hundred percent of the bank. The independent variables where total assets (TA), total equity (EQ), the last twelve-months net income (NI), and total non-performing assets (NPA) measured as the carrying value of past due loans and repossessed real estate.

Table I shows the descriptive statistics for our sample. It is important to note that these descriptive statistics are based on raw data, i.e., the variables are neither winsorized nor scaled. A comparison of the means and the medians reveals that the means are influenced by observations representing larger transactions. This holds true across all variables. P1, P25, P75, and P99 refer to the 1st, 25th, 75th, and 99th percentile, respectively.

7 Leone, Andrew J. and Minutti-Meza, Miguel and Wasley, Charles E., Influential Observations and Inference in Accounting Research (December 1, 2015). Simon Business School Working Paper No. FR 14-06. Available at SSRN: https://ssrn.com/abstract=2407967 or http://dx.doi.org/10.2139/ssrn.2407967

TABLE I: DESCRIPTIVE STATISTICS MAIN SAMPLE

Variable	Mean	Std Dev	P1	P25	Median	P75	P99
VALUE	45,340	61,359	1,653	10,000	21,505	52,013	269,000
TA	316,774	373,563	22,441	85,852	166,844	373,804	1,712,483
EQ	32,262	38,274	2,302	9,337	18,039	39,040	187,107
NPA	6,078	10,927	0	579	2,141	6,590	52,743
NI	2,394	3,383	32	474	1,124	2,688	16,644

We annually estimate models (1) and (2) to compare the relative accuracy of TS and OLS.

$$VALUE_i = \beta_0 + \beta_1\ TA_i\ + \beta_2\ EQ_i + \beta_3\ NPA_i + \beta_4\ NI_i + \varepsilon \qquad (1)$$

$$VALUE_{i} = \beta_0 + \beta_1\ TA_i\ + \beta_2\ \frac{EQ_i}{TA_i} + \beta_3\ \frac{NPA_i}{TA_i} + \beta_4\ \frac{NI_i}{TA_i} + \varepsilon \qquad (2)$$

For OLS, we use model (2) to estimate the β coefficients annually. We scaled EQ_i, NPA_i, and NI_i by TA_i so that only TA_i captures size while EQ_i/TA_i, NPA_i/TA_i and NI_i/TA_i measure level of capitalization, asset quality and profitability, respectively. Prior research has shown that these are important value drivers for valuing commercial banks. This annual OLS estimation yields nine sets of OLS coefficients.

For TS, we apply the following steps for each year. First, we randomly select 50,000 sub-samples with n=5 observations. This random selection was made with replacement, meaning that a selected observation could be randomly selected again. Next, we use OLS to estimate the β coefficients for each sub-sample of n=5. This step yields 50,000 sets of β coefficients per year. Next, we calculate the median across each β coefficient for each year. This process yields nine sets of annually estimated TS coefficients.

Next, we calculate the estimated VALUE using the annually estimated OLS and TSM parameters for each observation, where ε_{OLS} (ε_{TS}) is defined as the absolute difference between the OLS (TS) estimate of VALUE and the actual VALUE. Based on these residuals, we calculate a relative accuracy score (RAS), which is defined as the percentage of times that $\varepsilon_{TS} < \varepsilon_{OLS}$. Consequently, a RAS above fifty percent means that TS outperforms OLS in terms of generating more accurate estimates of VALUE.

Table II presents the relative accuracy scores for each year. As shown in Table II, TS outperforms OLS in all years. On average, TS outperforms OLS 69.9% of the time, a significant improvement.[8]

8 The authors also ran OLS using the unscaled variables. Consistent with the results reported in Table II, the TSM greatly outperformed OLS using our RAS measure.

TABLE II: RELATIVE ACCURACY SCORES

Year	Number of Bank Sales	Relative Accuracy Scores
2013	75	72.00%
2014	101	64.36%
2015	123	56.91%
2016	91	65.93%
Sum	632	

CONCLUSIONS

In this article, we introduce the benefits of OLS regression over ratio analysis while highlighting the common problems one encounters using OLS with business valuation data. We next explain the benefits of an alternative, robust regression procedure known as Theil-Sen. Academic research, as well as our own empirical analysis, demonstrate that TS is superior to OLS in the presence of outliers and heteroscedasticity, producing value estimates with significantly less error and bias.

In a future article, we will provide a more detailed evaluation of TS vs. OLS with different sets of Market Approach data, including large and small sets of completed transaction and guideline public company data. We will also provide a TS model written in VBA which readers can use with their Excel spreadsheets. We demonstrate the use of this model and the interpretation and use of its output, providing readers with a readily available, robust, and defensible alternative when using regression analysis in their valuations. VE



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VALUATION

Noncompete Agreements—What is the Value?

By Brian P Cockerill, MAM, CPA, CFE, CVA

Business appraisers may need to value a noncompete agreement (aka covenant not to compete) when negotiating the terms of a transaction, a purchase, price allocation, asset impairment testing, and for other reasons. In this article, conducting asset impairment testing, I will define the noncompete agreement, discuss how it works, and provide steps in valuing the noncompete agreement using the discounted cash flow method.

STATUTORY LIMITATIONS

One should first consider whether valuing a noncompete agreement is necessary as the law varies among the states. For example, as described below, case law in California does not follow the general rule that covenants to not compete are valid.

> *California Business and Professions Code section 16600 provides that, "...every contract by which anyone is restrained from engaging in a lawful profession, trade or business of any kind is to that extent void." California courts have rigorously applied this provision in the employment context and have routinely invalidated agreements purporting to preclude employees (either expressly or implicitly through penalties) from working for competitors upon completion of their employment.[1] Furthermore, employee noncompete covenants are void in California even if they are reasonably limited in time and geographic scope[2].*

1 See, e.g., *Application Group, Inc. v. Hunter Group, Inc.,* 61 Cal. App. 4th 881, 895 (Cal. Ct. App. 1998); *Metro. Traffic Control, Inc. v. Shadow Traffic Network*, 22 Cal. App. 4th 853, 859-60 (Cal. Ct. App. 1994); *Scott v. Snelling & Snelling, Inc.*, 732 F. Supp. 1034, 1042-43 (N.D. Cal. 1990).

2 Scott, 732 F. Supp. at 1042-43.

WHAT IS A NONCOMPETE AGREEMENT AND HOW DOES IT WORK?

A noncompete agreement is an intangible asset found in many purchased businesses and professional practices. The agreement typically occurs as a condition of purchase of an owner-managed business or professional practice (e.g., dental or tax preparation service) and stipulates that for a specific timeframe (e.g., three years), beginning on the date of the purchase transaction, the seller will not perform activities in a designated geographic area that compete with the acquired practice.

A noncompete agreement is important to the buyer because it is designed to protect the business' ability to grow and prosper, and, because it defines restrictions on the seller's future personal efforts. The value of a covenant is not in addition to the value of the business, but part of it.

STEPS IN VALUING THE NONCOMPETE AGREEMENT USING THE DISCOUNTED CASH FLOW METHOD

To value the covenant, the analyst must first value the entire business assuming a covenant not to compete. Next, the valuator must forecast the value of the lost profits in the event the seller competes. This requires measuring and present-valuing profits that will be lost by the business assuming seller competition for each year of the agreement. Further, the valuator must estimate the probability of competition in each year and apply that probability to the profits that are forecasted to be earned by the buyer assuming seller competition.

LENGTH OF THE COVENANT

The length of the covenant is a key item in determining its value. The covenant should cover a sufficient period of time such that at its expiration, the buyer will have firmly established their hold on the business/practice. Alternatively, business lost due to seller competition could be assumed to be lost into perpetuity depending on facts and circumstances.

ESTIMATING THE PROBABILITY OF SELLER COMPETITION IN EACH YEAR OF FORECAST

A noncompete agreement may prohibit the seller from soliciting the services of the entity's clients and employees for a different business.[3] Specific factors to consider when estimating the probability of seller competition include:

1. Age and health of the seller
2. Seller's plans post-sale to relocate
3. Difficulty in establishing a competing practice
4. Other business interests pursued by the seller, locally or elsewhere
5. Prior evidence of sale and competition
6. Adequacy of sale proceeds to enable seller to retire
7. Other assets of the seller

ILLUSTRATION

For the following illustration, the subject interest will be a sole proprietor tax practice, where the owner generates most of the revenue, while part-time bookkeepers and seasonal tax preparers generate a substantially smaller portion of the overall annual revenue.

It is not possible to value a covenant without knowing the underlying value of the business in order to estimate the profits attributable to the seller. For the case study, we will make the following assumptions:

- Utilization of discounted cash flow method
- Normalized average earnings for years one through four: $89,305; $91,627; $94,009; $96,453
- Combined federal and state income tax rate: thirty-four percent
- Discount rate: 19.88 percent
- Long-term growth rate: 2.6 percent

3 Other provisions typical of purchase and sale agreements include prohibitions against: (1) defamatory statements, (2) disclosure of trade secrets, and (3) use of intellectual property of the entity.

TABLE 1

	Year 1	Year 2	Year 3	Year 4	Average	Growth Rate	Capitalization Rate	Terminal Value
Normalized Average Earnings	$9,305	$91,627	$94,009	$96,453	$92,849			
Federal and State Income Tax Rate	30,364	31,153	31,963	32,794	31,568			
Normalized Earnings (post tax)	58,941	60,474	62,046	63,659	61,280	2.60%	17.28%	363,850
Present Value (Mid-Year Convention)	0.91333	0.76187	0.63553	0.53013				0.53013
Present Value of Benefit Stream	$53,833	$46,073	$39,432	$33,748				$192,890
PV of Benefit Stream	$365,975							

In a small tax practice, it is safe to assume that a certain portion of the revenues and profits are attributable to the seller. In such a case, if the seller opened a competing practice the day after the sale, the buyer would likely obtain less than one hundred percent of what was bargained for. As a practical matter; in the absence of misrepresentation, the seller is unlikely to compete the very next day. Even if the seller decided the day after the sale to open a competing practice, a site would have to be identified and acquired, equipment and furnishings would have to be purchased, a billing system acquired and made operational, old employees rehired or new ones hired and a host of other tasks accomplished.

Normally, some amount of time is likely to transpire between the sale and the commencement of seller competition. The longer this period, the greater the probability that the buyer will retain the profits it purchased from the seller. The buyer is also unlikely to sit idly by if the seller opens a competing practice and will take actions to attempt to preserve the investment that has been made. Taking this into consideration the valuator should consider both the elapsed time before competition commences as well as the buyer's response, when attributing profits to the seller in the forecast period.

EXAMPLE A—ESTIMATED LOST PROFITS

In the following example, the percentage of lost profits attributable to the seller, John Smith, Enrolled Agent (E.A.), is forming a new practice and competing with the buyer must be estimated. It is assumed that the practice has procedures and an established workforce in place. We have attributed seventy-five percent of the profits to the direct efforts of the owner, John Smith, E.A. and twenty-five percent of the profits from part-time seasonal tax practitioners.

It is assumed that seventy-five percent of all purchased profits would be lost by the buyer (a) absent a noncompete agreement, and (b) John Smith, E.A. competes with the buyer starting in year one. The risk of lost profits to the seller's competition would decline from seventy-five percent over time and therefore we use seventy-five percent as the baseline loss in year one. In the second year, the buyer is estimated to recover twenty-five percent of the seventy-five percent leaving 56.25 percent unrecovered. In the final third year, fifty percent of the seventy-five percent is recovered, leaving 37.5 percent unrecovered. A three-year noncompete agreement is assumed. Table 2 summarizes the net profit retained/lost by the buyer assuming seller competition,

The next step is to determine the amount of entity profits under different hypothetical date of competition scenarios. Here follows Tables 3, 4, and 5, presenting the amount of entity profits assuming competition from the seller in years one, two, and three, respectively.

The present value of lost profits per Tables 3, 4, and 5 assuming seller competition in years one, two, and three, needs to be probability weighted (assuming a probability of seller competition of twenty-five percent, fifteen percent, and five percent in years one, two, and three). Table 6 summarizes the weighted present value of profits lost in the event of seller competition. This amount, $99,946, is the value of the noncompete agreement.

TABLE 2

Profits Retained by Buyer in Year Competition Begins				
Year	% Lost	% Recovered	Net Lost	Net Retained
1	75%	0%	75.00%	25.00%
2	75%	25%	56.25%	43.75%
3	75%	50%	37.50%	62.50%
4	75%	100%	0.00%	100.00%

TABLE 3

Profit Lost by Buyer Due to Seller Compensation Assuming Year 1 Competition						
	Total	Year 1	Year 2	Year 3	Year 4	Terminal Value
Present Value of Benefit Stream (Table 1)		$53,833	$46,073	$39,432	$33,748	$192,890
Lost Profits Percentage (Table 2)		75.00%	75.00%	75.00%	75.00%	75.00%
Present Value of Lost Profits	$274,481	$40,375	$34,555	$29,574	$25,311	$144,667

TABLE 4

Profit Lost by Buyer Due to Seller Compensation Assuming Year 2 Competition						
	Total	Year 1	Year 2	Year 3	Year 4	Terminal Value
Present Value of		$53,833	$46,073	$39,432	$33,748	
Benefit Stream (Table 1)						$192,890
Lost Profits Percentage (Table 2)		0.00%	56.25%	56.25%	56.25%	56.25%
Present Value of Lost Profits	$175,580	$-	$25,916	$22,180	$18,983	$108,500

TABLE 5

Profit Lost by Buyer Due to Seller Compensation Assuming Year 3 Competition						
	Total	Year 1	Year 2	Year 3	Year 4	Terminal Value
Present Value of		$53,833	$46,073	$39,432	$33,748	
Benefit Stream (Table 1)						$192,890
Lost Profits Percentage (Table 2)		0.00%	0.00%	37.50%	37.50%	37.50%
Present Value of Lost Profits	$99,776	$–	$–	$14,787	$12,655	$72,334

TABLE 6

Calculation of Probability-Adjusted Profits Lost by Buyer assuming No Non-Compete Agreement			
Year of Competition	PV of Lost Profits	Probability of Competition	Probability Weighted Lost Profits
1 (Table 3)	$274,481	25%	$68,620
2 (Table 4)	175,580	15%	26,337
3 (Table 5)	99,776	5%	4,989
		45%	$99,946

SUMMARY

This article describes the noncompete agreement, how it works, and the steps required to value the noncompete agreement. The article also provides an illustration for performing the valuation of the noncompete agreement using the discounted cash flow method. The author also recommends that the analyst should consider whether applicable state law follows the general rule that covenants to not compete are valid. VE



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"Valuation is a branch of financial economics, and it can be short-sighted and dangerous to develop an appraisal that does not reflect the economic foundations of the transactional elements to which statutes, regulations, and case law apply."

David W. Grauer, Esq., Jones Day, nationally-known healthcare attorney

About the Program

The Institute for Healthcare Valuation (IHV) and Consultants' Training Institute (CTI) are pleased to announce premier healthcare valuation training through a distance education program: the Certificate of Educational Achievement (CEA) for Advanced Education in Healthcare Valuation. The program will launch in the summer of 2017 and will bridge the interdisciplinary nature of healthcare valuation to include: the Four Pillars of Healthcare (regulatory, reimbursement, competition, and technology); the market forces shaping the U.S. healthcare industry; and the valuation of healthcare enterprises, assets, and services.

The program is developed and is being presented by industry thought leaders Robert James Cimasi, MHA, ASA, MCBA, FRICS, CVA, CM&AA, Chief Executive Officer of Health Capital Consultants (HCC), and Todd A. Zigrang, MBA, MHA, FACHE, ASA, President of HCC, alongside a blockbuster faculty comprised of healthcare subject matter experts from the legal, regulatory, and valuation professions.

Why This Training is Critical

"In the current volatile regulatory environment, with the consolidation of hospitals, physicians, and other providers, the determination that the arrangements do not exceed Fair Market Value and are commercially reasonable are essential safeguards for the parties entering into these vertical integration transactions. It is critical that experienced, well-trained valuation professionals consult and collaborate with regulators and legal professionals before establishing and promoting so-called accepted methodologies and approaches," states nationally-known healthcare attorney, David W. Grauer, Esq., of Jones Day.

The training consists of ten four-hour course modules (including eight core courses and two electives) covering basic valuation tenets, competitive forces in healthcare, an overview of the regulatory environment, technological advancements in the industry, changes in reimbursement, development of a commercial reasonableness opinion, inpatient and outpatient enterprises, valuing intangible assets and tangible personal property, and the classification and valuation of healthcare services.

Who Should Attend

Legal professionals and healthcare providers, as well as those valuation professionals wishing to expand their scope of activities in healthcare valuation engagements and those seeking to enhance their current healthcare valuation service lines, will gain comprehensive knowledge through the expansive program. Attendees who successfully complete the course requirements, assessment quizzes, and interactive case study will earn a CEA.

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VALUATION

Conference Preview—What Lies Ahead?

By Nancy McCarthy, Senior Editor, The Value Examiner

Last year, the NACVA and the CTI's Annual Consultants' Conference in San Diego celebrated the milestones achieved by the business valuation profession over the past twenty-five years. Both the pioneers and the new innovators were honored by NACVA/CTI. The Conference was an opportunity to reflect on how far the profession has come, and to also focus on the topics and issues practitioners will be sure to face in the coming years.

This year's Conference takes the last part of that theme and runs with it. The NACVA and the CTI's 2017 Annual Consultants' Conference in Chicago will feature sessions that will shed light on and add commentary to the most critical and hottest trending topics facing the profession. Says Brien Jones, NACVA's Chief Operations Officer and Executive Vice President of Business Development, "It has always been important to NACVA to find the best ways to help guide its members to achieve success professionally and personally. Our goal this year is to look at our lives and our work and find strategies that will create sustainable success going forward."

The tone will be set at the Conference by the first keynote speaker, Peter Leyden, founder and CEO of the new media startup, Reinventors (http://reinventors.net). Leyden is an author, and speaker on new technologies and future trends. He was managing editor of the original *Wired* magazine, director of The New Politics Institute, and worked at Global Business Network.[1] According to Leyden, "We are entering a period of fundamental reinvention on a scale seen only a handful of times in history." Everything, from the way we educate our children, to the way we utilize energy, to the ways in which we govern, and do business are about to change. Leyden's keynote will highlight the changes we should look for as many of the systems that were useful in the past century give way to the emerging all-digital, fully global, more sustainable twenty-first century world.

"Peter Leyden's analysis fits well with our theme," says Jones. "Our message this year is to discover how to translate our past successes into continued success; we are also asking how do we deal with the digital age in the context of our profession."

Least members fear the Conference will only focus on the future, the keynote themes for the Friday sessions will focus on the official role of the valuation or financial litigation expert. The panel is moderated by Michael G. Kaplan, CPA, ABV, CFF, CVA, MAFF, of Kaplan Forensics. In this session, Honorable Judge Elizabeth Gonzalez District Court of Clark County of 8th Judicial District, Honorable Judge Steven I. Platt (Ret.) The Platt Group, Inc., and Honorable Judge Christopher P. Yates Circuit Court the 17th Judicial Circuit of Kent County, Michigan will be on hand to share the challenges that they have encountered with financial professionals and offer guidelines and approaches to solidify valuators opinions and persuasiveness in the legal environment.

The Conference chairs this year are:

- Janae Castell, CVA, MAFF, Woodrum, Tate & Associates, PLLC
- Sarah von Helfenstein, MBA, CVA, Value Analytics & Design, LLC
- Dimitri Yimga, MBA, CPA, CVA, CFE, CGMA, TruVim, LLC
- Mark Hanson, CPA, ABV, CVA, Schenck, SC

1 For more information see http://www.peterleyden.com

Says Sarah von Helfenstein, "We are excited about this Conference. The sessions will feature both established experts and fresh innovators from within the profession. We will also see some interesting sessions given by specialists outside the profession who have something important to contribute."

"We want people to come away from this Conference experience excited and energized to take the pioneering spirit of the profession to the next level," says Brien Jones. "We are hoping to inspire the younger folks in the profession—the Millennials, as it where—to build on the foundation that has been laid by previous generations." In very practical terms, the Conference is an opportunity for NACVA members to redefine who they are within the profession and the practice. Says Jones, "It is becoming clearer that business valuation and financial litigation experts are not seasonal, and provide year-round expertise and advise to their clients." Through panel discussions, workshops, and other sessions it is hoped that attendees will take some of what they learned back to their colleagues in the workplace. "There are new areas of practice and standards emerging in the marketplace," says Jones. "To really succeed in this new world, it is important that we all understand what they are, what is needed to participate fully in this environment, and to master the technology it will require. What better place to explore some of these ideas than the NACVA Conference?"

Having spent the past quarter century pioneering the business valuation and financial litigation profession, NACVA and the CTI are now keenly focused on the future—concentrating the Association's efforts and initiatives to ensure continued success and growth for the profession. The NACVA and the CTI's 2017 Annual Consultants' Conference is June 7–10, 2017, at the Swissôtel in downtown Chicago. VE



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VALUATION

Conference Preview—The Winds of Change Blowing Through Chicago: Highlights of the NACVA/CTI Sessions

By Nancy McCarthy, Senior Editor, The Value Examiner

With apologies to Bob Dylan, the 2016 Nobel Prize awardee in Literature, the times, they are *always* a' changin'. It is the way of the world and without change, people, governments, and businesses would all stagnate. We can debate whether a change is a good one (cell phones) or questionable (selfies), but the one thing that is immutable is that change is necessary for growth.

Change offers us opportunities to examine where we have been and assess where we want to go. This is true in all aspects of life. In the worlds of business valuation and financial litigation, we are poised for a sea change in how we conduct our business and the impact of our actions.

Many sessions at the NACVA and the CTI's 2017 Annual Consultants' Conference in Chicago reflect how the profession is keeping pace with the way clients do business. The panoply of topics reflects how the profession is moving from a specialized field to a major vocation.

THE UNSEEN

Neil Beaton, CPA, CFA, ASA, ABV, CFF, is a managing director with Alvarez & Marsal Valuation Services, LLC. His presentation, **Valuing Things You Cannot See,** is a good example of how the world has changed, particularly the world of valuation. According to Beaton, today's world is a service-oriented business environment; intangible assets continue to comprise much of a company's value irrespective of the intangible nature of these assets. "Information," he explains, "is a unique asset. For example, Airbnb, a company that did not exist six or seven years ago, valued at $3.1 billion, is worth more than a 100 plus year company such as Ford Motors." Companies such as Google and Uber are driven by the Internet. "Qualified information is the new standard," according to Beaton. "Entrepreneurs are bringing ideas to market, not goods," he says. What this does is cause a perfect storm between the establishment as represented by old rules and regulations that guided older ways of doing business, and the new thought on how to do business.

"Changing times cause us to think differently about how we have done things in the past. Some of the old approaches may no longer produce accurate data; some regulations bump up against the purpose and effectiveness of a new technology, or system," says Beaton. The challenge is to use this disruption in the market to refine and improve how we value intangible assets. "There is a new way of thinking about value. There is no such thing as a cookie cutter; we need to learn how to utilize tools that are available to us. Openness and creativity are very important in our world," says Beaton.

George Sandmann, sales and marketing strategist with CoreValue, could not agree more with Neil Beaton. Sandmann has over twenty years of experience in senior management and executive roles across a variety of industries, including

technology, telecommunications, and boutique manufacturing. Currently, he oversees sales, marketing, and business developement for CoreValue, a software technology firm.

WHO'S AFRAID OF TECHNOLOGY?

Sandman is presenting a workshop at the Conference**, Build a Thriving Business Consulting Practice—The CoreValue® Bootcamp.** "This is a session that really gets the participants thinking about who they want to be to their clients. The practice of valuation is changing, dramatically. Practitioners should have the ability to do the kind of work that is not restricted to a particular season (like tax season) or that they are only called in when a business is being sold. Business valuation happens at all stages of the business," he says.

Sandmann believes practioners—both neophytes and seasoned pros—should be asking themselves certain questions, such as how do I:

- Standardize my consulting practice to make it more efficient and profitable?
- Use the best methodology to generate the best client results?
- Teach my team my approach?
- Market my practice?

According to Sandmann, "Obviously, there are many tools available to help practitioners answer these questions. It is up to business valuators to choose the ones that work best for them and their business. However, the days of the green eye shade and pencil are gone. To be competitive, and to not compromise on service, valuation professionals need to embrace technology and not fear uniformed data." He goes on to explain that utilizing practice enhancing tools can seem intimidating at first, the result is a better product for the client. "There is a fear among some professionals that by utilizing algorithms, or other tools, that the human factor in valuation will be lost. Actually, that is far from the truth," says Sandmann. He goes on to explain that technology works best when a human brain employs it and puts it to work. "These are tools," he says, "designed to make the practitioner able to work faster, more efficiently, and, eventually, more profitably."

It is important for all practitioners to remember, according to Sandmann, the largest business consulting practices use a standardized process which allows them to do two things:

- Ensure their professionals are delivering consistent quality and client experience
- Leverage the work from one client, or from one solution set, and deploy across all applicable clients, giving them scale. This maximizes available billable hours and work product profitability

Detailed analysis uncovers maximum service opportunities, ensures that your practice has not missed critical issues, and leverages best practices from assessment through execution—maximizing results.

OVERVIEW OF KEY PRESENTATIONS

Neil Beaton and George Sandmann are two of the many presenters chosen to bring their insights, experience, and skills to the forefront of the NACVA membership. The 2017 Annual Consultants' Conference features several opportunities for you to build your skills, gain confidence, and expand your networks. Time and space does not permit *The Value Examiner* to highlight all the insightful, pertinent, and even somewhat controversial topics that will be presented. However, some of the major trends and issues featured at the Conference include:

GETTING PAID WHAT YOUR SERVICES ARE WORTH

Presenter: Stephen Kirkland, CPA, CMC, CFC, CFF

Many valuators have trouble getting paid rates that reflect the true value of their specialized knowledge and skills. Presenter Stephen Kirkland, Atlantic Executive Consulting, will give specific tips on how valuators can ask for and receive higher rates for their services. His pointers cover all aspects of the engagement including: the initial conversation with a prospect, the engagement letter, on-going discussions with the client, and drafting of invoices.

INTERNET AND REPUTATION MARKETING FOR FINANCIAL ADVISORS

Presenter: Colin Brown, AS Accounting, BS Marketing

Colin Brown, Syncnet, has been marketing online since 1995 and has hosted hundreds of CPA websites. One of his websites, cpawebsite.org, is for the CPA that wants to manage and market his own website at a low cost. His online marketing systems have generated over $300 million in online sales for his customers. He is an expert in all methods of traffic generation on the web. His presentation will discuss:

- Top twelve ways to generate traffic
- What is local marketing
- Managing your reputation online

- How to get on the first page of Google today
- Five things you need to do to your website today

PREPARING THE YOUNGER GENERATION

Presenter: Professor Sanjay Deshmukh, CFA, MSF, MBA, PhD

In this session, Dr. Deshmukh, an associate professor of finance in the Driehaus College of Business at DePaul University, will address and discuss some of the common myths of working with younger generations and the new ideas they are bringing to the workforce. Using his experience as a professor at DePaul University, Dr. Deshmukh will also describe how academia is preparing the next generation of professionals.

VALUE ENHANCEMENT IN RELATION TO AN EXIT PLAN

Presenter: Linda Nayder, CPA, CFE, CEPA

The first step of an exit plan is to ascertain a value for the business. The second step is to look at the current value and devise a plan to increase the value and sell it when it has achieved that higher value. Linda Nayder, L A Nayder Enterprises, Inc. goes through value enhancer items, how they work, and provides case studies showing their application. A goals and objective worksheet, including a project timeline for each of the components, goals, and objectives will be provided for review.

COST OF CAPITAL—CURRENT CONTROVERSIES AND NEW RESEARCH

Presenter: Roger Grabowski, Accredited Senior Appraiser and Fellow (FASA) of the American Society of Appraisers (ASA)

As Shannon Pratt and Roger Grabowski begin work on the upcoming *Cost of Capital: Applications and Examples 6th edition*, they have identified several controversies. In this session Roger Grabowski, a managing director with Duff & Phelps, LLC, will address these issues along with some interesting research both Pratt and Grabowski feel readers of the book will find thought-provoking. This session is a prelude to the upcoming edition, highlighting some of the more important issues and research that will appear in the book.

"DOUBLE DIP" AGAIN…AND AGAIN… AND AGAIN—BRINGING CLARITY TO THIS COMPLEX ISSUE

Presenters: Marc Bello, Robert Grossman, Garth Tebay, Courtney Sparks White

This panel of experts will lead a discussion that will move from a basic description of the issue to a detailed case study of the double dip. They will discuss key cases and publications. Attendees will leave with examples of how to spot a double dip, how this issue works, and how to explain the concept to attorneys and clients. While there is no definitive conclusion and the issue remains state specific, the basic underlying concepts are consistent.

FASB UPDATE ON ISSUES AFFECTING BUSINESS VALUATION

Presenter: Michael Cheng, Bachelor of Science, Accounting

Michael Cheng of the Financial Accounting Standards Board (FASB) will discuss upcoming accounting standards that may affect business valuations. The presenter will cover the Private Company Council and the Board's latest efforts related to business combinations.

Mr. Cheng serves as the Private Company Council (PCC) coordinator where he is responsible for all PCC related matters. He also leads the board's private company decision making framework project focused on determining whether and in what circumstances it is appropriate to adjust financial reporting requirements for private companies following Generally Accepted Accounting Principles (GAAP). Currently, he is leading a project to help the board decide its future agenda.

THE IMPACT OF ADVERSE REGULATORY ACTION ON VALUATION

Presenter: Chris Hamilton, CPA, CFE, CVA

The authority of governmental enforcement agencies is growing, along with the move towards "transparency" requiring public disclosure of, and easy access to, adverse administrative actions. Chris Hamilton, Arxis Financial, Inc., will discuss the nature of the regulatory environment, the effect on the valuation of a business, and the effect of such an

action in valuing damages. He will provide details from real-world cases. A public announcement by the FDA, for example, can severely damage the prospects of the subject food or pharmaceutical company. Hamilton will also lead a discussion on effective research techniques to establish the facts and to find effective means of communicating the impact.

FORENSIC ACCOUNTING TECHNIQUES IN BUSINESS APPRAISALS

Presenter: Karen Kaseno, CPA

The big issue in business litigation—the one the huge verdicts turn on—is whether the plaintiff's lost profits have been proven with reasonable certainty. Every U.S. jurisdiction has adopted the rule that lost profits must be proven with reasonable certainty. What factors do the courts consider when they decide whether the plaintiff has proven its lost profits with reasonable certainty? Karen Kaseno, The Kaseno CPA Firm, APC, discusses these factors in connection with an actual case study.

CONCLUSION

Brien Jones, Chief Operations Officer and Executive Vice President for NACVA, says it best, "These are exciting times to be in this profession." The topics, the speakers, the guests are all geared to make the time in Chicago interesting and, hopefully will light a spark with the attendees. As the saying goes, the future is now. VE



Nancy McCarthy, Senior Editor, Value Examiner, is a writer, editor, and former teacher. She has over twenty-five years as a marketing professional with several financial services institutions including Merrill Lynch, Prudential Securities, and Rydex Investments. E-mail: NancyM1@nacva.com

VALUATION

Conference Preview—The BV Talent Shortage: Here's What You Need to Know

By Rod Burkert, CPA, ABV, CVA

If you have not seen it yet, there is a new BVFLS "taking-the-pulse-of-the-industry" survey you might want to check out. Here is the quick backstory.

After IBISWorld issued a report downgrading the outlook of our very own BVFLS industry (yes, you read that correctly…downgrading), Ron Everett, CBA, CVA, of Business Valuation Center, LLC, was motivated to put together his own fifteen-page research paper to find out why he sees things differently than IBISWorld.

To get Ron's paper, all you need to do is complete a short six-question survey. (You can access the survey at https://www.surveymonkey.com/r/valuation-2017.) To date, there are over 250 responses, which is pretty ginormous for participation by us accounting types.

Of the six questions Ron asked, two in particular caught my attention:

> 1. From your experience, which of the following five factors is your biggest barrier to growth?
>
> *Lack of adequate trained staffing at reasonable cost, was the number two answer.*
>
> 2. What are the biggest impediments, challenges, or frustrations you're facing in building your practice?
>
> *Qualified staffing is the third most cited response.*

That a staffing issue was mentioned prominently, twice, piqued my curiosity. So, I reached out to a few colleagues who have valuation firms, and they concur—staffing issues are a major concern. Even though I am an army of one, I wanted to find out more

Whenever it comes to matters like these, I know who to turn to in order to get the skinny. And that person is John Borrowman, President of Borrowman Baker, LLC. John has provided proven counsel to BVFLS practices and professionals since 1995. He is the only recruiter I know who specializes in our industry.

I got on the phone with John and got his thoughts on the qualified staffing conundrum.

Rod: So, John, let's go for the jugular. Is it really that hard to find trained staff at a reasonable cost these days?

John: Even if you allow for a difference of opinion on "reasonable cost," the answer is, yes.

Rod: Why do you think that is the case?

John: Fundamentally, valuation—in or out of the courtroom—is a business of judgment. The deliverable is an opinion or conclusion of value to a reasonable degree of certainty. If your practice is growing and you feel like it's time to hire, you'll naturally want staff with experience in exercising that kind of required judgment.

Rod: Does the problem get more difficult the greater the experience level?

John: Counter-intuitively, perhaps, it's not a problem until it is. And then it's a big problem. Let me see if I can explain.

Picture the organizational pyramid of the typical BVFLS practice. Draw a horizontal line about one-fourth to one-third of the way up from the base. If you're hiring someone who functions below that line, you can hire from a broad universe. Related analytical experience is usually sufficient. If you're

hiring someone to function above that line, however, your only option is someone already in the profession. The size of your universe plummets.

In twenty years, the recession is the only time I've seen demand and supply come to a rough equilibrium.

Rod: Is the talent shortage more acute in business valuation or litigation support?

John: The pendulum may swing slightly. But, I can't see much difference between the two practice areas.

Rod: What are firms looking for?

John: Everyone would like to hire talent with at least enough experience to grasp the process, to carry out research and modeling, and to write at least a part of the final report. Surprisingly good talent is available at the entry level, but not every practice is equipped to absorb and train them.

At the other end of the experience spectrum, practices are challenged by the same succession issues as their clients. Practices in multiple markets need an heir apparent to champion a new service line or a geographic expansion…not to mention the practice itself.

Rod: What are the staff hoping to find?

John: Candidates not already in the profession are attracted because BVFLS looks fun and challenging. Thanks to a strengthening of collegiate finance curricula, more and more grads are coming in with realistic expectations about a career. Candidates within the profession move from one practice to another in search of better leadership, different work, and, sometimes, money.

Rod: Who is disappointed with what the most?

John: Hard to say. Disappointment usually starts with unrealistic expectations. Neither side is innocent on that score.

Rod: Are there areas of the country where the talent crunch is particularly evident?

John: Not really. Overall, geographic demand correlates closely with market size.

Rod: Are there areas of the country where it's easier to fill your bench?

John: Again, market size is probably the key variable.

Rod: What about those Millennials…are they as bad as some say, or just different?

John: Just different. There is a growing body of managerial guidance you can take advantage of. They're here. They're going to be the major cohort of the workforce. Get over it.

Rod: Why do you think it's getting so much attention now?

John: That's a good question, given that the shortage has been around as long as it has. I know that it gets talked about over coffee and cocktails at BVFLS conferences. And Ron Everett's survey has shone a brighter light on the issue, that's for sure.

Rod: What is the solution at the industry level?

John: The staffing shortage isn't going away, so a "solution" is a pretty tall metric. As a start, I can think of a couple broad strokes at the industrial, or as some would prefer, the professional level. One prong would be to focus more of the BVFLS conference sessions on developing and delivering staff training…a best practices kind of a thing.

A second prong would be to increase the number of entry-level hires who come into the profession with exposure to the research, modeling, and writing that practices need. Nationally, credentialing organizations should continue to support collegiate-level engagement with the profession.

Rod: What is the solution at the firm level?

John: Collegiate level engagement can also happen at the firm level. The smart practice leader has a network that includes a finance professor from at least one local college or university. A presentation to a class could connect you with your next new hire.

In my experience, practices that are successful in the long term are those that take a "grow your own" approach to staffing. And the smaller the market, the more important that becomes. Training less experienced hires will require an investment of time (which means money). The cost of doing that now, though, is small compared to the pain of not being able to find or afford the more experienced staff when you really need them.

That's a wrap…straight from the person who knows the most about this issue. If you think John would be a great person to huddle with about your staffing issues, you can reach him at JohnB@BorrowmanBaker.com. I cannot recommend John more highly. VE



Rod Burkert, CPA, ABV, CVA, is a practice development coach who helps overwhelmed BVFLS professional create more time and income margin in their practices and their lives so they can execute with more purpose have more freedom to do the things that matter most to them.



ACADEMIC REVIEW

Special Topic: A Look into Business Valuation in the Future

By Peter L. Lohrey, PhD, CVA, CDBV

The purpose of this column is to provide the readers of *The Value Examiner*, summaries of contemporary research in valuation and forensic accounting. The manuscripts covered are selected from numerous academic research outlets that include relevant topical coverage of valuation and related forensic accounting issues. The objective is to illustrate the core of this novel research while increasing awareness among the community of the subject matter.

As this column evolves, I encourage the readership to forward relevant manuscripts or working papers for consideration. Please send links and/or files to: jim@dmcpa.com or digabrielej@montclair.edu with ***Academic Research Briefs*** in the subject line.

I was asked by the editor of *The Value Examiner* to provide you with an article speculating on what business valuation may look like in the future. The comments and thoughts that follow are based solely upon the literature that is currently available. I take sole responsibility for the views presented herein, and I do not represent, in any way, that they are authoritative or guaranteed.

So, you wonder what business valuation analysts will be doing ten years from now? Well, to start, it is hard to say. Believe me, if I had the power to predict where our profession is heading, I would not be writing this article. Instead, I would be spending my time earning a fortune, and then heading to somewhere warm and sunny…and where you don't have to pay income taxes.

Having said that, it appears a recurring theme is artificial intelligence and big data will be front and center in bigger and more critical ways in the future. According to the literature, it is where the action is even as you read this article. So, consequently, the future holds several changes in how one prepares for a career as a business valuation expert by 2025—if not sooner. What follows are some highlights of the recent literature containing various opinions on this subject.

THE ROBO-ACCOUNTANTS ARE COMING—HOW TO PREPARE FOR THE ROBO REVOLUTION

Author: Brian Peccarelli, President, Thomson Reuters Tax & Accounting

Source: *CFO.com,* May 9, 2016. http://ww2.cfo.com/accounting/2016/05/robo-accountants-coming

Summary

This article begins by referring a New York Times story with the headline, "The Robots are Coming for Wall Street." This piece predicts that half of Wall Street's analysts will lose their jobs to automation software. On a broader level, The Boston Consulting Group predicts that up to one fourth of professional service sector jobs will be replaced by either smart software or robots.

Peccarelli follows these comments by asking: "Does that mean we'll all be getting our tax advice—or for that matter, financial and legal advice—from robots while we look for new jobs?" In fact, that scenario is already happening. I can tell from personal experience the automated tax apps are alive and well. For example, I have used TurboTax to file my personal tax returns since 2013 and it now sends me e-mail notices at least four times a year.

Finally, Peccarelli provides some hard numbers to support his view. As he points out, in 2015 approximately 4.4 million IT jobs were created to support big data and data science

projects that influence artificial intelligence development. Of these new IT jobs, 1.9 million, or forty-three percent, were spawned in the U.S. alone. He believes the leveraging of this technology by accounting (including business valuation) professionals will help to provide better insights into information filtering and analysis, which in turn will allow accounting/business valuation professionals to become more proactive and less reactive in managing client relationships.

THE END OF THE ACCOUNTING PROFESSION AS WE KNOW IT? AN INTERVIEW WITH DANIEL SUSSKIND

Author: Andrew Harbison, *CA Today*—A Publication by The Institute of Chartered Accountants of Scotland
Source: ICAS.com, July 5, 2016. https://www.icas.com/ca-today-news/the-end-of-the-accounting-profession-as-we-know-it

Summary

Daniel Susskind begins by describing, in broad terms, the two different futures for accounting (business valuation) professionals—both of which will depend on technology. The first future he describes will be quite similar to the present day, where professionals will increasingly rely on sophisticated technologies to improve their usual ways of working. The second future, however, will be quite different from the first. He states, "Here the technology doesn't simply streamline and optimize that traditional approach, it actively displaces the work of traditional professionals."

Susskind believes "increasingly capable systems and machines" will assume more of the tasks currently performed by today's professionals. Further, he forecasts these systems will be able to perform chores completely unsupervised—yet this will not be the most significant change. The people who will operate these systems will be very different from traditional professionals. The types of things that they will be doing will be quite different from what has been done traditionally. This in turn will serve to undo tasks currently performed by outmoded professionals.

The good news is, Susskind asserts that while some professionals have provided a great deal of resistance to the predictions that are made in his book, the most open minded organizations of people he has spoken to are accounting associations. He states that the accounting profession understands the "need to help educate and prepare professionals for this new future." Furthermore, Susskind sees today as "one of the most remarkable periods of technological change."

VOICES: THE FUTURE OF AUTOMATION AND ACCOUNTING

Author: Blake Oliver

Source: *accountingTODAY*, December 15, 2016. https://www.accountingtoday.com/opinion/the-future-of-automation-and-accounting

Summary

This article begins by claiming we are swiftly moving toward a time of "no-code accounting"—or, virtually no data entry. Oliver tells about how he has gone from being a low-paid bookkeeper who was paid by the hour, to a highly valued virtual controller who bills fixed fees. He states, in the future, artificial intelligence will be working while we sleep to prioritize our next day's work and provide us with critical insight into our clients' needs. This, in turn, will make us more valuable to our clients and allow us to do more work per hour. The end result, in Oliver's mind, is that automation will lead those who are willing to adapt into a sunnier and more affluent future.

Oliver points out that historical recordkeeping has been largely eliminated through automation and cloud computing. In years gone by, the amount of money one could earn was limited by the number of clients an accountant could see in a day or per week. That all changed in 2011 when cloud accounting apps provided gigantic efficiencies that immediately reduced the amount of time needed on client work by fifty percent. This then made it necessary for Oliver to move his clients from hourly billing to fixed monthly fees—if he did not do this, he alleges, he would never get all his invoices out to his clients. It was thanks in large part to cloud accounting software automating eighty to ninety percent of transactions for many of his clients (after a great deal of setup work).

The author contends both accountants and business owners are expecting accounting software and services that use automation to provide more efficient results with less human effort/time. Artificial intelligence, which is used to recognize patterns, allows us to predict future outcomes with greater precision. Currently, very little machine learning is applied to accounting software. However, that will rapidly change over the next few years. Oliver does not believe this new technology will replace people; judgments will still need to

be made by human beings when operating new technology. The end result, according to Oliver, will be more decisions made more quickly.

MY TAKE ON BUSINESS VALUATION IN THE FUTURE

I was not able to find specific articles written about the future of business valuation. As a result, I selected articles written about the future outlook/vision for service professionals who provide mostly accounting and legal services. While I know that there are some very distinct differences between business valuation and the other services, I believe the overriding theme regarding the effect of technology on the delivery of our services will affect us in many of the same ways. Specifically, I believe that as artificial intelligence continues its never-ending march forward, it will serve to allow business valuation professionals to provide more efficient and effective services to our clients going forward.

The consensus seems to be: we will be able to provide better service to more clients, and hence, the value of our services will be improving constantly. Given this prediction, I wonder how we, as a profession, will adapt to the changing environment in which we all compete. Will we become a profession of "haves" and "have nots"? By that I mean, will those of us who are better able to adapt our thought processes on how to use artificial intelligence when providing business valuation services be the winners? While those of us who are not able to adapt become the losers? This may end up as the outcome as the concentration of the firms who provide business valuation services intensifies—just as it appears may happen in the fields of law and accounting.

Who knows? Only time will tell. VE



Peter L. Lohrey, PhD, CVA, CDBV, is an assistant accounting professor at Montclair State University. He is also the Director of the Forensic and Valuation Services Department for Paritz & Company, PA, an accounting firm located in Hackensack, NJ. He has over twenty-years' experience in litigation services, valuation, mergers and acquisitions, loan workouts, and expert witness matters. He performed dozens of Fair Value reports for several different clients as the Northeast regional director of a national valuation firm. Dr. Lohrey specializes in commercial damage calculations and business valuation for tax, litigation, and forensic purposes. E-mail: lohreyp@mail.montclair.edu

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LITIGATION CONSULTING

Court Corner

By Peter Agrapides, MBA, CVA

DIVORCE

Banker v. Banker

2017 Tex. App. LEXIS 1799; March 2, 2017
Court of Appeals of Texas, Judge Rodriguez

In the original divorce decree of Kay and John Banker, the court split the marital estate fifty-five percent for Kay, while allowing John to retain ownership of his livestock business (ECL), multiple vehicles and trailers titled in his name, and goods in his possession. The court also entered a judgment of $455,000 against John to offset the assets he kept.

Kay Banker appealed the divorce decree on several grounds. She declared:

1. The trial court incorrectly assessed the value of certain assets. Her argument was the overall division of property was manifestly unfair because it relied on the cumulative value of all assets, including those the court found properly valued.
2. She should be granted a new trial due to the two-year delay between the start of trial in April 2013 and the entry of final judgment in 2015.
3. The trial court failed to account for John's sale of six horses, finding that evidence of a "secret sale" was not credible because the divorce decree accounted for the horses as part of the division of "goods."

The appeals court held that: 1) The division of property under Tex. Fam. Code Ann. § 7.001 (2015 R.S.) was not manifestly unjust and unfair because the court's valuation of the business was supported by the husband's testimony as the business-owner, and the court did not abuse its discretion in declining to value and divide the business's goodwill as a community asset; however, remittitur was required under Tex. R. App. P. Rule 46.5 because none of the evidence supported the court's valuation of the bank accounts as $44,133; 2) Kay Banker was not entitled to a new trial because her evidence of post-trial events was cumulative of her well-developed projections at trial; 3) The court did not abuse its discretion in declining to grant the motion to amend under Tex. R. Civ. P. 63, 66 to include a claim for pre-judgment interest because Kay Banker first attempted to amend two months after final judgment was rendered. The lower court's ruling was affirmed in part, reversed in part, and remanded.

Ning-Yen Yao v. Karen Kao-Yao

2017 N.Y. App. Div. LEXIS 1420; February 23, 2017
Supreme Court of New York, Judge Friedman

At stake in this divorce appeal was the distribution of the husband's (plaintiff—Ning-Yen Yao) equitable share of his enhanced earning capacity, due to his attainment of a medical license during the marriage. The plaintiff argued that the award was faulty because the wife's (defendant—Karen Kao-Yao) expert witness was unreliable, and even if reliable, the plaintiff's enhanced earnings were solely due to his own efforts without any contribution whatsoever, whether economic or noneconomic, by the defendant.

The testimony of an expert in forensic accounting was called as the defendant's expert witness to value that part of plaintiff's enhanced earning capacity attained during the parties' marriage. Plaintiff did not call any expert on this valuation issue.

In preparing his report, the expert witness relied on various documents, including the plaintiff's W-2 forms, information about plaintiff's license to practice medicine, and his employment agreement with the hospital at which he worked, Lenox Hill Anesthesiology (LHA). Much of this information is not in dispute. The plaintiff obtained his New York State medical license on May 5, 2003, and he had income of $122,516 in 2003; $258,210 in 2004; $454,492 in 2005; $715,313 in 2006; and in 2007 his income was $837,253. The plaintiff was on a partnership track at

LHA and was compensated the first year at an amount equal to fifty percent of what a representative full member of that partnership would receive; the second year, his compensation was seventy percent; the third year at ninety percent; and the fourth year and final year of the contract, which was 2007 (also his earning year as of the date of trial) he received compensation equal to one-hundred percent of what a representative partner of LHA was paid.

In valuing plaintiff's enhanced earnings, the expert witness stated in his report and testified at trial, that he was not provided with information regarding how the plaintiff was paid or a breakdown between his basic compensation and any bonuses. He could only state that plaintiff's compensation was determined by the accumulation of "points."

He used a methodology commonly employed in determining the value of a medical license earned during a marriage (*Grunfeld v. Grunfeld*, 94 NY2d 696, 702 [2000]). He first determined that the plaintiff would have earned $173,000 per annum as a typical family practitioner, without the enhancement (baseline earnings). He then determined what plaintiff's earnings were with the license (topline earnings). Although the expert witness proposed two different possibilities for topline earnings, the court accepted the lower value of $733,000, based upon a three-year weighted average of plaintiff's earnings from 2005 to 2007. The expert witness deducted baseline earnings from topline earnings, detailed how tax impacted the amount, and made other adjustments, including a calculation of earnings over a work life expectancy, which was then reduced to reflect present value. He also applied a coverture fraction to reflect the fact that the enhancement was attained partly during the marriage and partly before. Based upon his mathematical calculations, the plaintiff's enhanced earning capacity was valued at $3,740,000.

At trial, plaintiff challenged some of the assumptions and the expert witness made some further adjustments to his calculations. He reduced the coverture fraction from seventy-five percent to sixty-nine percent, to account for the incomplete fellowship and a seven month leave of absence that plaintiff took from his residency (July 2000–February 2001) when he decided to explore a nonmedical career path. The expert witness acknowledged that he had not known about the leave of absence, or realized plaintiff had not completed his fellowship. These adjustments resulted in a lower valuation of $3,440,000, which was ultimately accepted by the court.

The plaintiff's employer was called to testify about the plaintiff's work habits and compensation. Explaining that LHA doctors are compensated according to a formula using "units" and "compensation points," rather than straight hours worked, the plaintiff's boss explained how the plaintiff took unpopular shifts, such as holidays, nights, and weekends, which were worth more, and earned him higher compensation, than more conventional days and hours. Dr. Richter also testified that he could not continue to employ the plaintiff if he does not become board certified, and that plaintiff is the only doctor on staff at LHA who is not board certified. Plaintiff remains employed with LHA on the same employment terms and conditions, notwithstanding that his employment contract expired in 2007. Since 2007, which was his highest grossing year, plaintiff has earned less, but also worked fewer units. In 2008, he earned $554,848.85; in 2009, he earned $565,259.00; and in 2010, he earned $611,829.11.

At trial, issues of equitable distribution, maintenance, and counsel fees were referred to a Special Referee to hear and report. The Referee found the expert witness's valuation flawed, and recommended that his report, testimony, and valuation be rejected in its entirety, resulting in no award of enhanced earnings to defendant (*Halaby v. Halaby*, 289 AD2d 657, 660 [3d Dept 2001]). Alternatively, the Referee recommended that if the valuation of plaintiff's enhanced earnings was accepted by the court, then defendant's award should be no more than ten percent of the enhanced earning capacity, because her contribution to this attainment was "de minimis." The Referee also recommended that plaintiff pay defendant taxable maintenance of $10,000 per month for four years after entry of the divorce judgment.

The appeals court held: 1) The trial court did not abuse its discretion in awarding defendant ten percent of plaintiff's medical license earned during the marriage for her noneconomic contributions because the court properly relied upon defendant's expert in determining the value of plaintiff's enhanced earnings, considered the statutory factors under Domestic Relations Law § 236, as well as defendant spouse's direct and/or indirect contributions to the marriage; 2) The court also vacated various portions of the judgment of divorce, set forth the corrections, and remanded the case to the trial court to effectuate such corrections. The lower court's judgment was vacated, in part, and the case was remanded to the trial court for further proceedings.

EXPERT WITNESS

Estate of Kollsman v. Commissioner

T.C. Memo 2017-40; February 22, 2017
United States Tax Court, Judge Gale

This case revolved around works of art inherited by an heir, the need to quantify different valuation adjustments, and the fair market value of any asset, including:

- "Reasonable knowledge of relevant facts" under the definition of fair market value
- Use of market comparable sale prices when available
- Treatment of post-valuation date events

At the time of her death on August 31, 2005, Eva Franzen Kollsman owned two 17th-century Old Master paintings:

> (1) Village Kermesse, Dance Around the Maypole (Maypole) by Pieter Brueghel the Younger (Pieter Brueghel), measuring approximately 21-1/2 by 29-7/8 inches
>
> (2) Orpheus Charming the Animals (Orpheus) by Jan Brueghel the Elder or Jan Brueghel the Younger or a Brueghel studio, measuring approximately 19 by 27 inches

The fair market values of the two paintings varied wildly, with the IRS expert giving the higher value and the expert hired by the Estate coming in significantly lower:

Expert	Value of Maypole	Value of Orpheus
Hired by Estate	$500,000	$100,000
IRS	$2,100,000	$500,000

As of the valuation date, both paintings were covered with a heavy layer of surface dirt. The expert retained by the Estate placed significant weight on the "dirty" condition of both paintings as of the valuation date and the risks involved in cleaning the paintings. However, less than a month after decedent's death, the Estate's executor and residual beneficiary consulted with a leading fine art restoration and framing company and was later informed that the paintings should be cleaned and the process was "reasonably safe." The paintings were successfully cleaned in December 2005.

Maypole was sold in January 2009, less than three and one-half years after the valuation date, for approximately $2,400,000. The sale took place after it was consigned to the company that employed the Estate expert, and sold for a price that was almost five times higher than the value opined by the Estate expert. The second painting, Orpheus, was considerably bowed at the top and bottom. There was also a question concerning artist attribution, specifically whether the painting should be attributed to Jan Brueghel the Elder or the lesser-regarded Jan Brueghel the Younger. The IRS expert concluded to the former and the Estate expert concluded to the latter (for more information on this case see: value-of-artwork-before-the-dirt-clears/#sthash.Hr55HI2v.dpuf).

In its review, the court held: 1) The petitioner estate under-reported, for purposes of I.R.C. § 2031, the value of two paintings held by decedent at her death. The opinion state the petitioner's expert's valuations were unpersuasive because he had a significant conflict of interest, it appeared that he exaggerated the dirtiness of the paintings on the valuation date and the risks involved in cleaning them, his analysis and conclusions regarding cleaning the paintings were contrary to the well-established principle that the hypothetical willing buyer and seller would be presumed to have reasonable knowledge of relevant facts affecting the value of property at issue, and he provided no comparable information to support his valuations; 2) The respondent's expert's valuations were credible and supported, although slight downward adjustments were required.

NDA Farms v. City of Ames

2017 Iowa App. LEXIS 224; March 8, 2017
Court of Appeals of Iowa, Judge Doyle

The City of Ames, Iowa sought a permanent thirty-three-foot-wide easement running across property owned by NDA farms and another party, Carol Veasman.

The City initiated a condemnation action using the process of eminent domain.

NDA Farms and Veasman appealed the condemnation award to the district court. A jury awarded them damages, attorney fees, and costs. The City of Ames appealed the jury verdict, seeking the ruling overturned.

The appellate court reviewed several of the City's challenges of the trial court's evidentiary rulings including:

- The district court's decision to allow the City's expert witness to be questioned during cross-examination regarding a prior valuation obtained by the City of Ames.

- The trial court's decision to refuse to submit to the jury an instruction drafted by the City that was duplicative of model instructions already provided.
- The district court's refusal to order a new trial on the basis the jury's verdict was not so excessive as to shock the conscience and/or to have been the result of passion or prejudice.

The court held: 1) The district court was within its discretion in denying a city's motion for new trial, Iowa R. Civ. P. 1.1004, based on an allegedly excessive damage award, as both parties' experts were qualified to give an opinion as to the property's value before and after a taking, and the jury chose to accept the evidence and opinion presented by plaintiffs' expert; 2) The property's tax-assessed value was not relevant to the determination of the property's fair market value as a residential development land, and the trial court was within its discretion to exclude the evidence; 3) The trial court was within its discretion to exclude evidence relating to a 1997 disciplinary action against plaintiffs' expert witness, as the expert never admitted any wrongdoing in a consent order. The lower court's ruling was affirmed. VE



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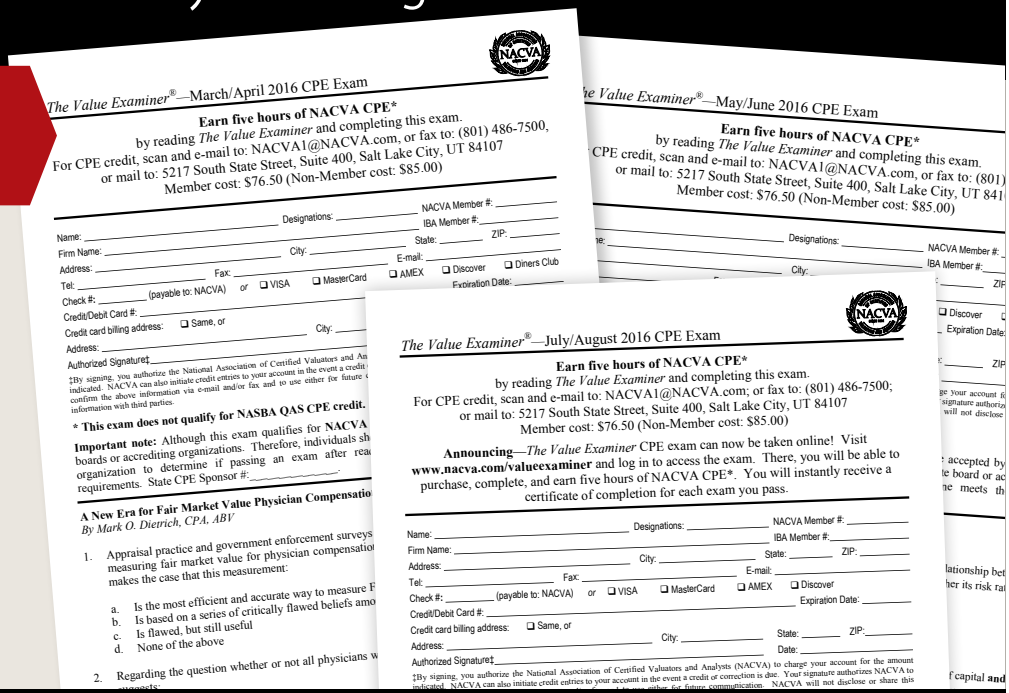
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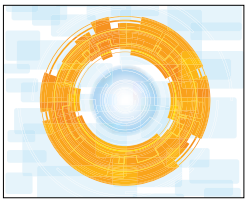
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TECHNOLOGY REVIEW

STOCK OPTIONS IN TECH COMPANIES: DETERMINING WORTH

By Raphael Meyara, MBA

Determining an exercise price for a new grant of stock options, understanding at which company value your stock options are at the money, or valuating stock options at fair market value for secondary deals or an immediate M&A event. These questions apply to CFOs and key employees who were granted stock options. Therefore, it is crucial to derive the most accurate and consistent answers to these questions in a timely fashion. Utilizing software dedicated to helping you get to the right answer is becoming more and more critical.

The right software can tap into the databases you need to answer these questions. The questions you need to ask yourself are all closely related to companies' current cap tables, and in most cases, companies' cap table lifecycles can be summarized in three main steps:

a) **From Creation to Seed stage:** Cap tables are simple, including mostly common shares of founders with a few stock options that have been granted to key employees (i.e., the CTO, CMO, etc.). This is often done in order to motivate them and link their performance to the future success of the company.

b) **From Seed to Series A round**: Cap tables are still relatively simple at this stage. Founders raise additional capital from private investors, mostly through Simple Agreements for Future Equity (SAFE). SAFE's primary benefit for private investors is to automatically convert their investment into equity at a next financing round. This round is defined in SAFE—with similar rights and a discount on the issue price paid by the new investor.

c) **From Series A round and later stages:** Cap tables are complex, and can include different classes of preferred shares and liquidation preferences, warrants, and pools of authorized stock options where a portion is granted at later financing rounds.

EXAMPLE

Let's assume a startup raised four million dollars through a Series A round, based on a fifteen million dollar post money valuation ($4 million/26.67%). In addition, the investor and the company granted an Employee Stock Ownership Plan (ESOP). The company's 409A valuation analysis results in an exercise price of $0.5.[1] The table below describes the post Series A cap table and liquidation preferences of the company.

Step 1: Suppose the company is currently raising five million dollars in a Series B round from new investors. The new cap

1 IRC 409A valuation provides a common share fair value, which is the minimum exercise price for a new grant of stock options. In addition, most pre-Series A companies do not have auditors and do not need a signed 409A valuation report.

Securities	Number of Shares	Fully Diluted Basis (%)	Issue Price/Strike PRice	Liquidation Preferences
Series A	4,000,000	26.67%	1	Non Participating
Common stock (Founders)	10,000,000	66.67%		
ESOP Pool 1-Granted	1,000,000	6.67%	0.5	
Total	15,000,000	100%		

table is created based on the following: five million dollars divided by a twenty percent equity stake in the company on a fully-diluted basis, resulting in a post-money valuation of twenty-five million dollars ($5 million/20%).

Step 2: A few months after the Series B round, the company's management decides to grant additional stock options. The company 409A valuation analysis results in an exercise price of $0.58.

The table below describes the post Series B cap table and liquidation preferences of the company.

Securities	Number of Shares	Fulle Diluted Basis (%)	Issue Price/Strike Price	Liquidation Preferences
Series B	3,759,500	19.03%	1.33	Non participating
Series A	4,000,000	20.24%	1	Non participating
Common stock (Founders)	10,000,000,	50.61%		
ESOP Pool 1-Granted	1,000,000,	5.06%	0.5	
ESOP Pool 2-Granted	1.000.000	5.06%	0.58	
Total	19,759,500	100%		

a) Stock option holders received an exercise price of $0.5 and $0.58. At which company value will they be at the money, or in other words, at which company value will they start to earn money?

Let's use an automated analyzer to answer this question. In this example, stock option holders of ESOP1 and ESOP2 with a strike price of $0.5 and $0.58 will be at the money, and will exercise their stock options only if the company value is at least $14 million and $14.88 million, respectively. If a willing buyer wants to purchase their stock options based on a lower company value, stock option holders will be out of the money (OTM) and will have no interest in exercising and selling their options.

On the next page (ESOP 1) is a table representing waterfall graphs generated by a valuation software company, illustrating the company value at which stock option holders start to be at the money.

b) What then is the true amount of cash received by the stock option holders, if there will be a secondary deal or M&A event based on a company value of fifty million dollars?

Below are tables representing an allocation of the company value and waterfall graphs generated from the software, illustrating the fair market value of these stock options.

VALUATION OF SHARE CLASS (EQUITY OPTIONS PLAN): ESOP 1

Common Share component - 2.085 $M

Total Share Class value - 2.085 $M



VALUATION OF SHARE CLASS (EQUITY OPTIONS PLAN): ESOP 2

Common Share component - 2.005 $M

Total Share Class value - 2.005 $M



So if there is a secondary deal or M&A event based on a fifty million dollar company value, ESOP1 and ESOP2 stock option holders can sell their stock options at a fair market value of $2.085 and $2.005 per stock option, respectively.

CONCLUSIONS

- Using a comprehensive analytical tool to help your clients understand the value of their stock options will give them a stronger basis for future negotiations on fair market value. You can save time by utilizing software that can produce an accurate figure for your clients.
- You can avoid costly mistakes that can occur if you rely on spreadsheets and programs that may contain errors.
- There are many programs available to practitioners. It is important that you review your needs and options to find the ones that best suit your needs. VE



Raphael Meyara is the co-founder and CEO of AlgoValue. Before starting AlgoValue, he was a valuation expert at PricewaterhouseCoopers. He spent several years both modeling and valuating private and traded companies, as well as financial instruments in Excel. He has advised many CFOs and CEOs of early stage and mature companies, as well as sophisticated investors. Raphael Meyara holds an MBA in finance and strategic management from Paris-Dauphine University and a Post-MBA degree. E-mail: raphael@algovalue.com

Securities	% of the Company Value	Payoff ($Million)	Value of one Equity Security ($)
Series B	19.03%	9.719	2.585
Series A	20.24%	10.340	2.585
Common stock (Founders)	50.61%	25.851	2.585
ESOP Pool 1-Granted	5.06%	2.085	2.085
ESOP Pool 2-Granted	5.06%	2.005	2.005
Company Value	100%	50.00	



HEALTHCARE VALUATION INSIGHTS

VALUATION OF COMPENSATION FOR PHYSICIAN SERVICES: CLINICAL SERVICES

By Robert James Cimasi, MHA, ASA, FRICS, MCBA, CVA, CM&AA; and Todd A. Zigrang, MBA, MHA, FACHE, ASA

This column will provide a brief overview of the classification and valuation of compensation for the common types of services rendered in the healthcare delivery industry: I) compensation for physician clinical services; II) compensation for physician executive services; III) compensation for call coverage services; and IV) compensation for medical director services. This first installment in the series of columns will focus on the classification and valuation of compensation for physician clinical services.

Physician services may be divided into two general categories, i.e., clinical related and nonclinical related, with nonclinical-related activities further divided into three generalized subcategories: administrative, management, and/or executive. These categories may be defined by the specific tasks, duties, responsibilities, and accountabilities (TDRAs) involved in each.[1] The challenge for valuation professionals is identifying and separating the various TDRAs for clinical services from those to be provided for administrative, management, and/or executive functions, in order to ensure that compensation for each service complies with the legal requirements of the Stark Law, the Anti-Kickback Statute, and, for non-profit entities, excess benefit/inurement of benefit regulations promulgated by the Internal Revenue Service (IRS).[2]

Before beginning a valuation analysis of compensation for physician services, it is important to understand the economic principles that support the entire valuation endeavor. The dynamics of how economic value is created may be understood within the context of four basic principles related to the economic benefits to be derived from the right to control the subject services to be performed under the contractual arrangement.[3] First, the Principle of Scarcity "influences market participants to assign relative value to goods and services in order to choose between the limited amounts available."[4] Scarcity of goods and services leads to the concept that economic value derives from economic usefulness, also termed utility, which arises from the benefits and/or satisfaction to be derived from the use or ownership of goods and services.[5] Second, the Principle of Substitution asserts, "what normally sets the limit of what would be paid for property is the cost of an equally desirable substitute or one of equal utility."[6] This principle is the basis for the decision as to whether to "buy or build" a product or service.[7] Third, the Principle of Diminishing Marginal Utility asserts, "…the additional benefit which a person derives from a given

1 "Healthcare Valuation: Financial Appraisal of Enterprise, Assets, and Services" By Robert James Cimasi, MHA, ASA, FRICS, MCBA, CVA, CM&AA, Volume 2, Hoboken, NJ: John Wiley and Sons, 2014, p. 863.
2 *Ibid,* p. 866.
3 *Ibid,* p. 894.
4 *Ibid,* p. 893; "Economics" 8th ed. By Michael Parkin, Boston: Pearson Addison Wesley, 2008, p. 2.
5 "Appraisal and Valuation: An Interdisciplinary Approach" By Richard Rickert, American Society of Appraisers Washington, DC: International Valuation Sciences Institute, 1987, p. 6.
6 Cimasi, 2014, p. 894.
7 *Ibid.*

increase of his stock of a thing, diminishes with every increase in the stock that he already has."[8] Fourth, and perhaps most important, the Principle of Anticipation asserts,:

> "The economic benefits of ownership of, or the contractual rights to control, the subject services to be performed under the contractual agreement are created from the expectation of those benefits or rights to be derived in the future; *therefore, all economic value is forward looking*."[9] [Emphasis Added]

Consequently, the economic value analysis for determining fair market value (FMV) should be focused on the economic benefits reasonably expected to be derived from the use or utility of the services in the future, bounded by the cost of an equally desirable substitute, or one of equal utility, for each of the elements of economic benefit (or utility) to be derived from the right to control the services to be performed.[10]

To develop the valuation analysis of physician clinical services, the valuation analyst must obtain the requisite documents related to the proposed compensation arrangement(s), including:

1) The proposed agreement(s) for physician clinical services (including a full description of all TDRAs related to the services to be performed)
2) The time requirements, e.g., the number of hours per week anticipated under the agreement
3) The curriculum vitae for the provider performing the clinical services
4) Documentation as to the board certification, qualifications, and tenure of the providers
5) The medical staff bylaws and roster
6) Agreements for other similar positions at the employer entity, including the scope of services to be performed under each of those agreements
7) Documentation of historical clinical productivity, measured in work relative value units (RVUs), gross charges, net revenue, or count by Current Procedural Terminology (CPT) code for an applicable time-frame to establish a relevant trend for forecasting purposes.[11]

The development of a valuation opinion related to a compensation arrangement makes use of this data to identify and classify the types and the amounts of tasks and duties, along with the level of responsibility and accountability, associated with the subject agreement for services.[12]

The various types of compensation plans for clinical-related services may include, but are not limited to, combinations of the following elements:[13]

1) Base salary (i.e., equal compensation paid to each physician)
2) Productivity-based compensation (e.g., cap compensation and a given productivity percentile by specialty)
3) Compensation based on a per wRVU method
4) Incentive bonus based on productivity[14]
5) An annual stipend for the performance of administrative services, e.g., medical directorships, departmental management, and oversight (which services will be discussed in parts II and IV of this series)
6) Incentive payments based on achieving quality of patient and beneficial outcomes gauged by agreed-upon measures and benchmarks
7) Incentive payments based on specified legally permissible gainsharing arrangements (e.g., achieving certain cost savings and efficiencies)
8) Incentive payments based on the contributions and economic input of the employed physician(s) to achieve specified enhancement of the performance of the enterprise (e.g., the development of a "Center of Excellence."[15]

It should be noted that when considering elements of a compensation arrangement that are productivity-

8 "Principles of Economics" By Alfred Marshall, Eighth Edition, New York, NY: Cosimo, Inc., 2009 (originally published in 1890), p. 79.
9 Cimasi, 2014, p. 894; Rickert, 1987, p. 47.
10 Cimasi, 2014, p. 895.
11 *Ibid,* p. 895–896.
12 *Ibid,* p. 896.
13 *Ibid.*
14 It should be noted, compensation based on productivity (wRVUs), even if not directly tied to an "incentive bonus," may be viewed by the IRS as an "incentive compensation arrangement" as it can vary based on performance.
15 "Fair Market Value: Analysis and Tools to Comply with Stark and Anti-Kickback Rule" By Robert A. Wade, Esq., and Marcie Rose Levine, Esq., Audio Conference, HC Pro, Inc. (March 19, 2008), p. 33; Cimasi, 2014, p. 896–897.

based, careful attention should be paid as to whether the compensation is based on a: 1) percentage of collections; 2) percentage of gross charges; or 3) per wRVU basis. In those compensation structures where compensation is based on a per wRVU basis, such arrangements have the benefit of being based on the physician's actual productivity, i.e., their work effort, regardless of the employer's payor mix or collection rate, which is beyond the control of the physician. Also, if compensation is on a per wRVU basis, special attention should be given to the analysis to ensure that the amount of compensation per wRVU reflects only those amounts that are solely related to the production of wRVUs, and not any amounts related to activities separate and distinct from their clinical productivity, such as a physician owner's profit arising from the provision of ancillary service and technical component (ASTC) by the practice.[16]

Similarly, when a compensation plan proposes paying more than the indicated, industry benchmark survey data (even after the homogenous badges of economic contribution composing the subject services have been identified and separated from one another), an appropriate justification for the excess payment should be documented, supported, and explained.[17] "Special circumstances" that could warrant paying more than the industry indicated benchmark data for a service may include:

1) the unique and, accordingly, scarce skill set of the provider

2) additional TDRAs required of the subject provider, above those of the typical providers in comparable positions, reported in the benchmark survey data

3) the quality of the wRVU generated by a provider is higher in relation to the wRVUs generated by the providers included in the benchmark survey data

4) the production of a similar quality wRVU but at a lower cost per unit

5) other special circumstances regarding the wRVUs produced by a provider[18]

In developing a FMV analysis regarding physician clinical services, the value of services rendered should consider the four provider-specific drivers of clinical productivity: 1) time; 2) efficiency; 3) volume; and 4) quality performance, either in comparison to internal sources or outside industry normative data. [19] First, the amount of time a provider dedicates to clinical activity will work to establish the bounds of that provider's volume of clinical productivity.[20] In accordance with the Principle of Substitution, the provider has a finite limitation on both the number of hours and the volume of clinical-related services per hour that they can provide.[21] Second, variances in the level of provider efficiency typically account for differences in total volume once adjustments for the incongruity introduced by nonclinical time worked, as well as for the variability introduced by fewer hours worked by part-time providers, have been accounted for.[22] Third, volume, i.e., the amount of clinical productivity possible, may be limited by the time spent on nonclinical activities, in a manner similar to that of time and efficiency.[23] Therefore, the extent to which the potential volume of clinical production is limited should be taken into consideration when calculating productivity.[24] Fourth, quality metrics are playing an increasingly important role in measuring a provider's performance for purposes of determining FMV compensation.[25] The rise in the importance of the quality metric as a value driver of clinical productivity is manifested in the movement toward value-based reimbursement (VBR) set forth in the provisions of the Patient Protection and Affordable Care Act (ACA).[26] This new paradigm of healthcare value metrics, i.e., value equals cost plus quality, is a foundation of current healthcare reform efforts.[27]

Another component of a compensation plan that should be considered by a valuation analyst when assessing the FMV of the total compensation to be paid for a particular set of physician services is the amount of fringe benefits included

16 *Ibid*, p. 897.
17 *Ibid.*
18 *Ibid,* p. 897–898.
19 "Measuring Physician Work and Effort" By Bruce A. Johnson and Deborah Keegan, in *Physician Compensation Plans: State-of-the-Art Strategies*, Medical Group Management Association, 2006, p. 114.
20 Cimasi, 2014, p. 908–909.
21 *Ibid.*
22 *Ibid,* p. 910.
23 *Ibid,* p. 910–911.
24 *Ibid,* p. 911.
25 "Pay for Performance: Quality- and Value-Based Reimbursement" By Norman (Chip) Harbaugh Jr., *Pediatric Clinics of North America* 56, No. 4 (2009): p. 997–998; Johnson Keegan, 2006, p. 114.
26 Cimasi, 2014, p. 911.
27 *Ibid.*

within the total compensation arrangement.[28] As set forth in the definitions of the Stark Law, any remuneration, whether in cash or in kind, is considered to be compensation for the purpose of determining FMV and commercial reasonableness.[29] The types of benefits that are often part of a compensation arrangement include:

1) contributions to retirement plans
2) payment of automobile expenses
3) compensation for continuing medical education
4) reimbursement for business-related travel and entertainment
5) payment of malpractice insurance coverage[30]

The valuation analyst should compare the level of benefits in the compensation package to those of applicable, normative benchmark industry survey data, and if the amount of benefits to be provided is significantly above those reported by the benchmark surveys, an adjustment should be made to add the excess benefit amount to the cash compensation being paid to the provider.[31]

One often overlooked type of benefit that should be considered in the determination of FMV and commercial reasonableness is not only the payment of malpractice insurance coverage by the purchaser of the subject services, but also an agreement that would require the employer to be liable for prior claims from services rendered during the malpractice insurance premium period from previous employment, referred to as "prior acts coverage."[32]

After an assessment of the four value drivers of clinical productivity, the proposed compensation arrangement should be compared to applicable, normative benchmark industry sources reflecting similar TDRAs, to determine whether the compensation arrangement meets the regulatory thresholds of FMV and commercial reasonableness.[33] This "benchmarking analysis" should include the following steps to ensure that the most relevant external benchmarking data is used for comparison purposes:

1) Determination of the specific characteristics of the arrangement, including:
    a. Specialty/subspecialty of the provider
    b. Applicable job training and education level of the provider, relevant to the position
    c. Amount of experience of the provider
    d. Site of service (e.g., hospital-based practice, office-based practice); geographic location where the subject services are to be provided
    e. Nature of the revenue stream that produces the income available for clinical-related services compensation
2) Establish the homogenous units of economic contribution to be used as the metric(s) of comparability, which may include:
    a. Productivity components, (e.g., charges, collections, RVU)
    b. Time components (e.g., annual, monthly, hourly, full-time equivalent)
3) Development of the range of applicable, normative benchmark industry data, which should include measures within the range, (e.g., tenth percentile, twenty-fifth percentile, seventy-fifth percentile, ninetieth percentile), as well as measures of central tendency (e.g., mean, median) and measures of dispersion (e.g., standard deviation). The range of normative benchmark industry data is typically compiled by taking a weighted average of the selected external benchmark data sources. The weights assigned to each data source used to compile the range of normative benchmark industry data should include contemplation of the following statistical and descriptive survey characteristics:[34]
    a. Size of the data population sample included in the external benchmark survey
    b. Dispersion of the data; it should be noted that a useful metric for comparing the relative dispersion between data sets is the coefficient of variation

28 *Ibid.*
29 "Definitions" 42 C.F.R. § 411.351 (October 1, 2014).
30 Cimasi, 2014, p. 912.
31 *Ibid.*
32 *Ibid.*
33 *Ibid,* p. 913–914.
34 Wade and Levine, March 19, 2008, p. 35, 80; Cimasi, 2014, p. 914–915.

c. Geographic proximity in relation to the area in which the subject services will be provided

d. Other elements of comparability between the external benchmark data sources and the subject services (e.g., whether the external benchmark data source includes information specific to the specialty/subspecialty of the provider, the date the external benchmark data was compiled in relation to the valuation as of date).

While industry normative benchmark industry survey data can be used to establish FMV compensation rates, further analysis should be performed to meet the related threshold of commercial reasonableness.[35]

The second article in this four-part series on the valuation of compensation for physician services will discuss the valuation of executive compensation agreements in the healthcare industry. VE

35 *Ibid,* p. 915.



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PRACTICE MANAGEMENT

Practicing Solo

"Practicing Solo" features interviews with our industry's seasoned sole practitioners. If you are itching to join the solo ranks, or striving to be more efficient and effective in your established one-person firm, this column offers you practical advice, steeped in experience from the trenches, that can move you forward.

By Rod P. Burkert, CPA, ABV, CVA

INTERVIEW: DANIEL GILBERT

I hope you enjoyed last issue's interview with Margaret McDonnell. Our interview series continues, with this issue featuring Daniel Gilbert, CPA, ABV, CVA, CFF. Daniel hails from Portland, Oregon, and a few months ago, I was lucky enough to spend some time with him when the RV was passing through.

Daniel has been on his own since August 2007… so nice to see that round ten-year anniversary coming up. You can find him at Gilbert Valuations, LLC (gilbertval.com).

Daniel's sweet spots are business valuation, complex commercial litigation, intellectual property valuation, and forensic accounting—primarily for companies with under twenty million dollars in revenue.



Daniel Gilbert

Rod: What was your first year like, and what would have made it better?

Dan: My first full year, 2008, was nerve wracking. I left the safety and comfort of a larger practice where I had been for six years. However, I had no equity interest and no control over my schedule or compensation in that firm. Fortunately, I had been aggressively bringing new clients to the firm and felt comfortable that I could expand this base on my own.

While I was not under a non-compete with my employer, I respected the owner enormously, and he was a friend who gave me a start in this industry. So, we made a gentlemen's agreement that I would only approach the clients that I had brought into his firm or the referral sources that I had personally cultivated. In return, he allowed me to port my direct phone line to my new office so clients could reach me easily.

This arrangement turned out great. When I contacted my relatively small referral base to tell them I was on my own, they not only continued to call me with new work, but also referred me to other attorneys that had previously not used my services. And in my first year out, the profits achieved were similar to my compensation with my previous employer!

Rod: Did you have a formal (or even semi-formal) business plan?

Dan: My business plan was simple. Keep overhead as low as possible and work like crazy to increase my client base.

Rod: How did you first attract clients, and how did that strategy evolve over time?

Dan: As I mentioned previously, I brought with me a handful of clients. I asked these clients to introduce me to others. When they did, I would have coffee or lunch with the prospect. I also joined a local business group that had about sixteen business professionals from different walks of life, including three attorneys, where I could pitch my services on a regular basis. This group was responsible for a significant number of referrals.

Rod: What kinds of engagements did you start with?

Dan: Primarily divorce and estate work.

Rod: Do you practice in a specialized niche today?

Dan: My practice is well balanced between litigation, transactional work, and estate work. I purposely don't specialize for two reasons. First, I really like the varied demands of each of these niches, and it keeps me from getting bored. I have noted that my job satisfaction drops if I get too concentrated in any one area. Second, I don't want to get pigeon holed into a niche and then have that niche change (or disappear). The best example is in the estate area where the increase in the lifetime exemption has really decimated the quantity of work.

Rod: What has been your best marketing tactic?

Dan: Relationships with referral sources, which are primarily attorneys. I have found that if I do good work, then I become the path of least resistance for these folks. Further, they then recommend me to their colleagues and my circle widens. For the first four or five years, I advertised in various publications, primarily the local bar publications to get my name out there. I rarely received a call directly from these ads, but felt the exposure gave me some name recognition. I stopped these ads about four years ago, when I felt I was fully established and my backlog continued to remain full.

Rod: How do you price work?

Dan: I spend a decent amount of time looking at the entity and their financials prior to quoting work. I then primarily base my fees upon my experience with similar entities/situations. I don't do fixed fee work, instead charging hourly. I quote my work as an estimated range, unless it's litigation and it is impossible to estimate. I do have a policy of not exceeding the top end of my range unless something is far different than I was led to believe initially. If that happens, I inform the client and change my estimate. Occasionally, this not-to-exceed policy results in write-offs, but not often.

Rod: How do you differentiate yourself from larger firms?

Dan: I explain that if I take your job, it's me doing the work, not a lower-level employee. I also explain that my fees are always far less than my larger competitors since I don't have the massive overhead to support.

Rod: Do you work from a home office or an "office" office?

Dan: I have an "office" office I go to each day. I tried working at home initially, but found the distractions to be too much. Also, if my office is in my home, I am tempted to work more than I should. For me, having a separate place "to go to work" keeps me sane, and my life a bit more balanced. I do have a computer at home that I utilize when needed, but I try to not work there for extended periods.

Rod: What is your current mobile device?

Dan: I use an iPhone, which I find to be adequate. And I have my Vonage VOIP office line set up to simultaneously ring through to my cell phone. That way, clients can reach me if I am remote, assuming I am available.

Rod: Describe your current computer workstation set up.

Dan: Two large external monitors attached to my laptop. When I need to bring a laptop to a job, to court, or on vacation, I just unhook it and go.

Rod: Besides your phone and computer, any office hardware or software that you just couldn't live without?

Dan: Dropbox has been a godsend. It allows me to have all my materials available, no matter where I am. It also allows my one assistant/employee and I to collaborate on projects.

Rod: What do you listen to while you work?

Dan: Nothing. I can't focus unless it's quiet. Classical music gets the nod when I am doing research reading.

Rod: What tool(s) do you use to manage your to-do list?

Dan: I am a paper guy. I keep a legal pad on my desk with the various projects in process. This list is manually updated frequently. I find the process of moving projects from the old list to the new list motivates me to get things wrapped up. I have tried lots of electronic versions, including Evernote and Excel spreadsheets, where I meticulously figure out time to completion. But I have found that these systems did not work for me.

Rod: What are your best-cost saving ideas?

Dan: Multi-year contracts for the various valuation and research databases. I can usually get a ten to twenty percent discount over a single year subscription. I also have slowed down buying reference books for my library. That is, when I started my practice I bought everything that looked interesting, but with the wealth of information that can be found online, I now mostly purchase reference sources that are specific to an industry I am appraising, but have limited experience in. Recent examples are cannabis and wineries.

Rod: Early bird or night owl—what's your sleep routine?

Dan: I am definitely a night owl. My brain does not engage until at least 10:00 a.m., so I rarely make it into the office before then. I really hit my stride in the late afternoon and early evening.

Rod: Do you have liability insurance?

Dan: Yes. I am insured by the AICPA Professional Liability Insurance Program.

Rod: Do you have any office/admin staff?

Dan: I have one full-time employee, who happens to be my daughter, and she has been with me for the last three years. She handles the bulk of the office administrative tasks and starts each project, inputting data into our models and laying out the reports. Over time, she has become much more proficient and is now working through the process to become an ASA. Business valuation is a great career, and I am thrilled that I could give her the opportunity to head down this path.

Prior to my daughter joining me, I hired people, only to let them go after several months. I initially tried a recent accounting graduate. But, that did not work out at all as I determined he just did not have the aptitude for the work. I then went the academic route, hiring a PhD in Economics. But he had difficulty moving from the theoretical to the practical. Finally, I hired a six-year valuation professional from a large firm. He flamed out—badly. Of course, not everyone will have this experience…but you asked the question.

Rod: Do you have a support group to call on?

Dan: I have an informal network of four colleagues that call each other frequently when we get stuck.

Rod: Who reviews your work?

Dan: My one employee and I are generally the only ones reviewing our work. Frankly, our budgets are too tight to have an external review. It's worked out fine, though, as I have had numerous experts testify opposite me over the last nine years, and they have not located any glaring problems.

Rod: How do you stay technically current with changes in the profession?

Dan: My primary source these days are the BVR webcasts. I also religiously read BVR's *Business Valuation Update*, NACVA's *The Value Examiner,* and Hitchner's *Financial Valuation and Litigation Expert.* Finally, I am an avid reader of Aswath Damodaran's blog (http://aswathdamodaran.blogspot.com/).

Rod: What non-BV business books have you read most recently or want to get to, and why?

Dan: I have been reading quite a bit from Richard Rohr, a Franciscan Priest. I have been meaning to read his book, *Breathing Under Water,* for some time now.

Rod: What's your work-life balance like?

Dan: This is certainly my biggest challenge. I chronically accept more work than I should. I have a bit of a "Robin Hood" syndrome where I fall prey to my client's dilemmas and feel compelled to help them out.

Rod: What practice areas do you think offer the most promise to someone going solo now?

Dan: There is no doubt that divorce work is the easiest to break into, particularly very small companies. And few people, including me, want to touch these cases. They tend to be very time consuming because small company books are notoriously poorly kept.

Rod: Finish this sentence: If I knew then what I know now, I would…

Dan: …not have stressed as much when I went out on my own. It's all turned out fine. VE

That's a wrap! Do you have a Practicing Solo issue you would like me to address? E-mail me at rod@rodburkert.com.



Rod Burkert, CPA, ABV, CVA, is a practice development coach who helps overwhelmed BVFLS practitioners create more margin in their practices and their lives so they have the freedom to do the things that matter most to them. Rod works with entrepreneurially-oriented professionals who have one thing in common: they want to move the needle on their practices further, faster.

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