



## Semantic difference: “opinion” of value versus “indication” of value and other distinctions

I believe that we business appraisers should all get on the same page as to what we are calling the conclusion we reach in a valuation assignment—what we are doing is developing our *opinion* of value for the subject property.

### USPAP defines “appraisal” as an opinion

The *Uniform Standards of Professional Appraisal Practice (USPAP)* defines “appraisal” as “the act or process of developing an opinion of value.”

### FRE 703 and 704 use “opinion”

**Rule 703. Bases of Opinion Testimony by Experts** reads in part:

The facts or data in the particular case upon which an expert bases an opinion or inference may be those perceived by or made known to the expert at or before the hearing. If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence in order for the opinion or inference to be admitted.

**Rule 704. Opinion on Ultimate Issue** reads in part:

...testimony in the form of an opinion or inference otherwise admissible is not objectionable because it embraces an ultimate issue to be decided by the trier of fact.

### “Indications” are steps along the way

“Indications” of value are interim numbers that we develop along the way to reaching our final conclusion as to our opinion of value. They may be indications of value from each of two or more approaches, and/or indications from each of two or more methods or procedures within an approach.

In the fourth edition of *Valuing a Business*, we said the following about indications of value:

When all the relevant valuation factors have been individually

## Court denies lack of marketability discount in fair value case

**Jahn v. Kinderman**, 2004 Ill. App. LEXIS 628 (June 7, 2004).  
*Judge McNulty*.

The issue in this minority oppression case concerning **Chicago Metallic Corporation** was the application of a marketability discount in determining fair value. In addition, the court discussed prejudgment and post judgment interest. At trial, the minority shareholders were awarded \$55,485,000 for the fair value of their shares.

analyzed and assessed, they should be brought together to arrive at a final estimate that represents the valuation conclusion. Sometimes it may be obvious that the analyst should rely on the indications of a single valuation approach. This could be due to (1) the nature of the company or (2) the nature of the business interest subject to valuation. In other cases, two or more valuation approaches may produce such similar value indications that it is not mathematically significant how much weight each approach receives. However, in many cases, business valuation approaches and methods generate apparently inconsistent value indications. When the different valuations approaches result in materially different value indications, and the objective of the subject analysis is a point value estimate, the indications should be reconciled into a single value estimate.<sup>1</sup>

Note that we used the term “estimate.” This comports much more closely to “opinion” than to “determination.” Unfortunately, the *International Glossary of Business Valuation Terms* defines “appraisal” as “The act, or process of determining the value of a business, business ownership interest, security, or intangible asset.”

### “Determination” too strong a word

I think that “determination” is a bit strong to describe the conclusion that we reach in a business appraisal. I would like to see us adhere more uniformly to authorities such as *USPAP* and the *Federal Rules of Evidence*, which use the term “opinion” to characterize our estimate of value.

I will recommend to the committee that is now in the process of revising the *International Glossary* that they change the definition of appraisal to developing an “opinion” rather than a “determination.” The chair of the committee is **Jeff Jones**, AASA, CBI, of **Certified Appraisers, Inc.**, 10301 Northwest Freeway, Suite 200, Houston, Texas 77092; (713) 680-1200; [www.certifiedappraisers.com](http://www.certifiedappraisers.com).

In the meantime, I recommend that business appraisers refer to the final conclusion in their report as an “opinion.”

Defendants appealed, arguing that although the valuation may have otherwise been correct, a marketability discount was required. The court of appeals dismissed that claim stating, “These citations ignore the more prevalent current trend toward rejection of such discounts because they fail to fully credit the minority owner’s percentage stake in the value of the enterprise in its entirety.”

The court of appeals reversed the trial court’s ruling denying the minority shareholders of post judgment interest but upheld the court’s denial of prejudgment interest.

# Goodwill at issue in appellate court's reluctant affirmation

**Hoebelheinrich v. Hoebelheinrich, 2004 Va. App. LEXIS 376 (August 3, 2004).** *Judge Annunziata.*

One issue in this marital dissolution was the value of husband's medical practice. Prior to trial, the court requested that both parties submit a list of two experts and that, from the lists, the court would select an expert to value the practice. Wife submitted two names, whereas husband submitted none. The court determined that **Dr. Ward Zimmerman** would be a qualified expert and requested that he value the practice. After the valuation report was submitted to the court, husband complained that the valuation was inaccurate and that he intended to call his own expert, **Janet Shrader, CPA**, during the trial.

## Valuation evidence

Zimmerman's report contained four valuations based on two methods applied to two scenarios to value the medical practice. The scenarios differed on how the husband's salary was treated. Zimmerman first valued the practice using the capitalization of earnings method and treated husband's salary as a business expense. This resulted in a value of \$654,776. Excluding husband's salary resulted in a value of \$1,824,434. Zimmerman then valued the practice using the discounted future earnings method and treated husband's salary as a business expense. This resulted in a value of \$743,608. Excluding husband's salary resulted in a value of \$1,994,921.

Shrader's report concluded the value of the practice to be \$140,000. Shrader used the capitalization of earnings method and arrived at a value of \$515,000. She then used the excess earnings method and arrived at a value of \$460,000. Shrader also concluded that the value of the practice included an intangible that was worth \$300,000. The intangible reflected the goodwill of the practice. She assigned 85% of the intangible to professional and personal goodwill. The balance, 15%, was

assigned to the goodwill as a business entity. The personal goodwill was then subtracted from the equally weighted valuation methods, arriving at a value of \$220,000. Shrader then applied a 35% discount for lack of marketability, resulting in a final value of \$140,000 for the medical practice.

## Holding and rationale

The trial court concluded the proper valuation method was the capitalization of earnings method. The court adopted Zimmerman's lowest value of \$654,776. The court noted that the salary deduction was reasonable but that no marketability discount should be applied because, "[T]here is no evidence that a sale of the practice is necessary or foreseeable."

The court of appeals affirmed the trial court's valuation of the medical practice but noted that in Virginia the courts look at intrinsic value for distribution purposes and that, "The intrinsic value of an asset may include goodwill." The court also noted that, "[A]s a matter of law, goodwill attributable to personal characteristics is considered separate property and goodwill attributable to the business entity is considered marital property." However, "[Shrader] did not testify that [Zimmerman's] method of valuation, which excluded husband's salary, failed to deduct husband's personal goodwill from the value of the medical practice." Thus the court held that, "the present record does not allow us to conclude that Zimmerman's valuation method was insufficient as a matter of law."

### ZIMMERMAN'S VALUATION

	Husband's salary included	Husband's salary excluded
Capitalization of earnings method	\$654,776	\$1,824,434
Discounted future earnings method	\$743,608	\$1,994,921

## Goodwill 'implicit' in capitalization of excess earnings method

**Walker v. Walker, 2004 N.C. App. LEXIS 1319 (July 20, 2004).** *Judge Martin.*

The issue in this marital dissolution was the value of husband's insurance agency. The trial court held that the insurance agency was worth \$300,000 as of the date of separation. The trial court arrived at this amount using wife's expert's capitalization of excess earnings method.



Wife argued on appeal that the trial court erred in not including goodwill in its

valuation. The court of appeals dismissed that argument stating, "This Court has stated that the capitalization of excess earnings method is a valid approach to valuing the goodwill of a business."

The court of appeals further defined the method:

[T]he capitalization of excess earnings method determines fair market value by calculating a company's excess earnings (also known as goodwill) and adding that value to the total value of the company's tangible assets. In this case, the value of the agency's tangible assets was not available and thus, the fair market value of the agency was based solely on the value of the agency's excess earnings (also known as goodwill).

Affirming the trial court as to the valuation issue, the court noted that the capitalization of excess earnings method "implicitly" includes the value of a business' goodwill.

## Economic realities of stock purchase agreement determinative of value

*Gibbons v. Gibbons*, 2004 Ore. App. LEXIS 874 (July 21, 2004). Judge Armstrong.

One issue in this marital dissolution was the value of husband's minority interest in a logging company. Husband acquired 102.23 shares of **Allen & Gibbons Logging, Inc.**, a closely held logging company, during the marriage. The shares were subject to a stock transfer agreement that allowed the company to repurchase the stock, at a value which was adjusted every year, if the shareholder attempted to sell. The agreement allowed the company to purchase the stock with one percent down, with the balance payable over 25 years at an indexed interest rate set at the time of purchase. In addition, the agreement stripped all voting rights from the shares effectively depriving husband of any control.

### Valuation evidence

Both parties submitted expert testimony. Both parties agreed that the shares had a value of \$3,100 per share assuming a controlling interest with voting power. Wife's expert, **Brock Parthemer**, used a minority discount and arrived at \$2,404 per share. Husband's expert, **Charles Chappel**, did not conduct a separate valuation but did criticize Parthemer's use of the asset valuation method. Chappel testified that because husband owned a minority interest and had no voting control—giving him no access to the assets—it was inappropriate to use the asset approach. Chappel further opined that the proper valuation would have been predicated on the actual economic rights that a willing buyer would acquire. He indicated that the preferred method would be to value the cash flow resulting from the application of the stock transfer agreement and combine it with the value of a possible future liquidation.

**Sam Barker** testified that the cash flow resulting from the stock purchase agreement had a fair market value of between \$39,000 and \$52,000 less costs and fees. Using Barker's valuation, Chappel valued the economic rights that a willing buyer would receive at between \$60,000 and \$75,000.

### Holding and rationale

The trial court found that Chappel's analysis was more appropriate because it took into account economic realities. The court valued the interest at \$70,000 or \$684.73 a share. The court of appeals affirmed the trial court as to the valuation issue.

## No value equals no appreciation of stock

*Hirt v. Hirt*, 2004 Ohio App. LEXIS 3937 (August 18, 2004). Judge Carr.

The value of **Hirt's Greenhouse Inc.** stock was at issue in this case. An expert who was agreed upon by both husband and wife concluded that the value of the business, based on an ongoing business analysis on the open market, was zero. The trial court adopted the expert's conclusion and stated that there had been no appreciation of the business or its stock during the marriage. The court of appeals affirmed the ruling.

## Later sale not controlling as to value

*Stephens v. Tanning*, 2004 Minn. App. LEXIS 1081 (September 21, 2004). Judge Lansing.

The issue in this marital dissolution case was the value of **The Geek Squad, Inc.**, a company that provided technical assistance house calls for personal computer users.

The company had distinctive vehicles used to perform these services and all were marked with the signature "Geek Squad" logo.

Husband began the company in 1994. The couple were married in 1998 and separated in 2001. The parties disagreed as to the amount of appreciation that had occurred. The couple jointly selected a neutral appraiser to value husband's 80% share.

Prior to the contested hearing and a final resolution, **Best Buy Inc.** purchased The Geek Squad for 2.4 million dollars and hired husband as a vice president with a yearly salary of \$150,000.

As part of the sale, Best Buy agreed to a presale spin-off of the business-to-business aspect of The Geek Squad. Husband then invested \$252,000 into this new venture.

### Valuation evidence

The neutral valuation expert, **Patrick K. Schmidt, ASA, MBA**, was the only expert to present a valuation report and testify at trial. Schmidt testified that the business was only marginally profitable.

He concluded that the purchase price paid by Best Buy, Inc. was based on husband's contractual commitment of future services and the value of the concept and trademarked logo whose value had been determined before the marriage.

The court noted that, "The evaluator further explained that the business's market value did not reflect the intangible and independent value of the trademark."

### Holding and rationale

The trial court agreed with the appraiser and valued the three years of appreciation of the company at \$128,000.

The court of appeals affirmed the trial court noting that their decision was not clearly erroneous given the facts on record. In its affirmation the court of appeals noted that, "[T]he only empirically assessable factor that changed is the operating revenues generated by the business between October 1998 and September 2001." and that those changes supported the valuation of the neutral appraiser.

The court of appeals also pointed to the lack of contradicting evidence, "In the absence of a contrary theory, the court, in its valuation, relied on the only available expert evidence, the testimony of the neutral evaluator. The only other evidence of value came from [husband's] testimony, which did not contradict the opinion of the neutral evaluator."

# Great resources for compensation information

America's Career Infonet, a component of CareerOneStop, [www.acinet.org](http://www.acinet.org).

Finding detailed information about wages and employment trends is only a click away. America's Career Infonet provides this free information organized by occupation, industry, and state.

The Web site is the portal to CareerOneStop, a set of free integrated Internet resources initiated by the U.S. Department of Labor. Career information is broken into General Information, Wages & Trends, What It Takes, State Information, and Customized Reports. The Wages & Trends link on the home page contains some of the most instrumental information for appraisers. This information includes: occupation reports, detailed wages, metro wages, detailed trends, industry trends, and customized reports.

A search is based on "job family," specific job (title), and state of job location. On entering this information, detailed tables are created for each report mentioned above. The only exception is metro wages, which requires the user to enter the metro location of the job. The Customized Reports section enables the user to choose more than one report and adds the features of What It Takes and State Information reports from the home page. This Web site can be a great asset in determining appropriate compensation.

## Other compensation Web sites

Following is a listing of several other compensation Web sites:

■ [www.bls.gov](http://www.bls.gov)

This free government site provides detailed wage and benefit information from a national level to a regional level.

■ [www.careerjournal.com](http://www.careerjournal.com)

This site is a cohort of *The Wall Street Journal*. It provides wage and salary information primarily as a tool for career development.

■ [www.eri.com](http://www.eri.com)

Economic Research Institute provides salary survey analysis through their Web site. They have a variety of products ranging from salary and geographic assessors to an executive compensation assessor.

■ [www.compgeo.net](http://www.compgeo.net)

This fee-based online resource contains detailed compensation information that covers ten regions within the United States and the Caribbean.

■ [www.worldatwork.org](http://www.worldatwork.org)

Wageweb provides national data on salary and benefit information for free, and has a yearly subscription price for metropolitan salary and benefit information.

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