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VALUATION ISSUES™

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BUSINESS VALUATION STANDARDS: ARE THEY IMPORTANT?

Written by: Gary L. Schroeder, ASA, Managing Director, St. Louis Office



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Business Valuation Standards (BVS) are basically codes of practice that are used in business valuation. In the United States they

have been around since the late 1980's starting with the Uniform Standards of Professional Practice (USPAP) issued by the Appraisal Foundation in 1987. In 1992 the American Society of Appraisers (ASA) issued business valuation standards which was followed by standards published by the Institute of Business Appraisers (IBA) in 1993,

the National Association of Certified Valuation Analysts (NACVA) in 1998, the Internal Revenue Service (IRS) in 2006, and the American Institute of Certified Public Accountants (AICPA) in 2007.

“In today’s world business appraisers must not only adhere to the business valuation standards, but I believe they must exceed these standards.”

All of the standards can be downloaded free online. One of the most convenient sites to accomplish this is www.valuationresources.com/publications/BusinessValuationStandards.htm.

The standards are very similar in terms of content and terminology, including a dependence on the eight factors to consider in business valuation which are listed and discussed in IRS Revenue Ruling 59-60. A detailed discussion of the contents of the various standards, including similarities and differences, is beyond the scope

of this article. Instead I want to ask the question, are business valuation standards important? And if so, why are they important?

To determine if standards are important I go back to the business valuation world prior to standards. When I started out in 1981 I was lucky to be part of a company that had already developed standardized approaches and reports for business valuations. Early on I witnessed numerous reports from others that I would now call “very suspect.” It seemed that almost anything could pass as a business valuation in those days. The users of business valuations had no way of knowing whether a report was good or not, due to many times having nothing to compare it to. Having standards at least gives the users of the reports some idea as to what should be considered in a business valuation and how the valuation should be reported.

Therefore, I believe business valuation standards have been very important in turning the business valuation field into a profession. Did this happen overnight once standards were

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LA Office

Business Valuation Standards: Are They Important?

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issued? No, it has been a gradual trend as more users, including the courts, became aware of the existence of standards and as business valuation appraisers were more and more expected to become accredited by one of the reputable organizations and, therefore, required to adhere to at least one or more of the business valuation standards.

As evidence of this, the courts are becoming very aware of the existence of business valuation standards. In *Kohler et al v. Commissioner* (TC Memo 2006-152; July 25, 2006) the judge disregarded the report of the expert that was not “prepared in

accordance with all USPAP standards” and did not contain “the customary USPAP certification” which states that the report complies with the USPAP standards.

Although following at least one set of business valuation standards is becoming a must for business valuation professionals, I must also point out that strict adherence to any or all of the business valuation standards does not guarantee a quality appraisal and report. In the General Preamble to the ASA Business Valuation Standards, No. IV, it is stated that “These Standards provide minimum criteria to be followed by business appraisers in developing and reporting the valuation of businesses, business

ownership interests, securities and intangible assets.” This seems to imply that quality appraisals and reports should exceed the requirements of the standards.

In today’s world business appraisers must not only adhere to the business valuation standards, but I believe they must exceed these standards. In addition, the users of business valuations should demand this.

In summary, I believe business valuation standards have been very important in professionalizing the business valuation field over the past several decades and they continue to be important as a barometer as to the minimum requirements of a business valuation. □

Effective Written Communication and the “Gobbledygook” story

Written by: Anita Thomson, LA Office



*Anita Thomson (daughter) and
John A. Thomson, ASA, MAI
Managing Director – LA Office*

Assisting my father (Mr. John A. Thomson, ASA, MAI and Managing Director of the LA office) over the last five years prepare for business valuation seminars nationwide has provided me with some wonderful insight into

the world of appraisal. One really important yet basic thought that my father reiterates throughout his seminars and which continually sticks with me is, *effective written communication*.

At the conclusion of many of my father’s seminars, he would quote what I like to title the “gobbledygook” story and preface the story with an article titled, *Effective Written Communication*, which cites excerpts from Jefferson D. Bates. With this

very basic yet funny ending, the audience would leave our seminars satisfied and with a bit of humor.

It begins like this:

Effective Written Communication must be clear!

Clarity. Many of us have taken photographs that we were sure would be prize winners only to discover that the prints came out blurred and out of focus. Writing can also be out of

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Effective Written Communication

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focus, and a good analogy can be made between the rules of picture taking and good writing.

In *Writing with Precision*¹, Jefferson D. Bates develops this analogy as follows:

1. Aim directly, with a specific purpose, at a central subject.
2. Omit all extraneous material.
3. Emphasize the important attributes of the subject. If necessary, give examples.
4. Play down the less important material. If you keep the really important items in sharp focus, you can permit the lesser ones to get a bit “softer.” Just be sure they don’t get “fuzzy” instead.

Mr. Bates makes the point that writing is improved if the writer takes the time to think before writing, just as a photographer should consider the composition of a photograph before tripping the shutter. The enemy of clarity is the use of obscure words and awkward sentence structure, which leave room for multiple interpretations by the reader.

Here’s where my dad begins the “gobbledygook” story:

The worst form of obscurity is what is sometimes called “gobbledygook,” defined as language of circumlocution, jargon, and pomposity.

Some of the worst examples of gobbledygook come from Washington,

D.C. There is an anecdote about a plumber who wrote to a federal bureau to report that he had been using hydrochloric acid to clean out pipes and to ask if it was safe. The first reply he received was: “The efficiency of hydrochloric acid is indisputable, but the chlorine residue is incompatible with metallic permanence.”

“Appraising involves some complex material that can be conveyed only in technical terms. However, much of the obscurity in appraisal reports can be eliminated.”

The plumber was delighted and wrote back that he was glad that they agreed that hydrochloric acid was an effective way to clean pipes. This prompted a second response from Washington, which read: “We cannot assume responsibility for the production of toxic and noxious residue from hydrochloric acid, and we suggest, therefore, that some alternative procedure be used.”

To this, the plumber replied that he was getting excellent results so far and suggested that the officials in Washington might want to recommend hydrochloric acid to other people. Finally, someone who would

rather communicate than sound pompous took over and drafted the third reply to the plumber. **“DON’T USE HYDROCHLORIC ACID; IT EATS THE HELL OUT OF THE PIPES!”** With this statement, the plumber understood.

Appraising involves some complex material that can be conveyed only in technical terms. However, much of the obscurity in appraisal reports can be eliminated. With a little effort, a clearer, more easily understood explanation or description can be written.

In conclusion, my father also tells me that based on his 30 years of appraisal experience, litigation support, and testimony, most folks, judges, juries and attorneys believe that when writing reports, specifically appraisal reports, one should write to an 8th grade level so that most people can understand your meaning. After receiving my Masters and under graduate degrees in Business, I’ve made the decision to fulfill my requirements of the State of California to become a General Certified Appraiser. While fulfilling these requirements I plan to never forget the importance of *“effective written communication”* by following the most basic rules, *BE CLEAR and Say What you Mean and Mean What You Say!* ☐

¹Jefferson D. Bates, *Writing with Precision* (Washington, D.C: Acropolis Bookd, Ltd.).

KTS CALENDAR

Recent And Upcoming Seminars And Speaking Engagements

8/27/09 - Presentation - "Value of Orthodontic Practices",
St. Louis University, St. Louis, MO.

9/16/09 - Business Valuation Roundtable, St. Louis, MO.,
"Valuations for Estate Planning Purposes"

11/09/09 - Presentation - National Business Institute,
"Business Valuation", St. Louis, MO.



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For more information or a free valuation seminar for your firm or professional group, please call Anita Thomson at (877) 587-7008, or e-mail your request to ktsinc@verizon.net.

*"The work goes on, the cause
endures, the hope still lives and the
dreams shall never die"*
— Ted Kennedy

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