



## BUSINESS VALUATION ADVISOR

*Commentary on the business of business valuation for estate planning professionals and business owners*

Welcome to the first edition of Tucker & Meltzer's *Business Valuation Advisor*. This newsletter is for the information of attorneys, financial planners and business owners who deal with business valuation issues and are interested in the current thinking in business appraisal. It is not a "how to" publication, but more of an explanation of a complex professional service.



### Commentary

**F**AIR MARKET VALUE (*as a concept*). First of all, let's get something straight about business valuations – Fair Market Value (FMV) is not the price at which an individual business owner *would* sell his business; it is the hypothetical definition of price used in our civil and tax courts to provide an equitable framework for the value of a business.

**Fair Market Value is . . . the amount at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of the relevant facts.** <sup>[i]</sup>



From this seemingly simple definition of FMV, an entire industry has matured in the past 25 years to provide expert business valuation opinions. These opinions of value are tested in the court system everyday. Be it the IRS disputing an expert's findings or in divorce court proceedings or minority shareholder disputes. Whole books and learned theses have been written on FMV concepts. Here at Tucker & Meltzer, we will examine FMV concepts in the context of specific companies in unique situations. But mostly we will inform you of what FMV is not, for when the blind wise men examined the elephant they could only tell you about a small part of the beast they examined. To wit-

FMV is not *fair* to one side or the other, depending on which side of litigation you happen to be on. It also has nothing to do with the *market* (only comparatively and conceptually), since the stock may have never been exposed to an active market. It is also not the *average* of two valuations or the *middle value* of some range. FMV is Revenue Ruling 59-60 applied to a specific set of facts by trained valuation analysts, using all of the information at their disposal, and a set of valuation principles in which both sides have agreed to arrive at an equitable value to suit the particular situation. <sup>[ii]</sup> – *Editor*. □

### The Tucker & Meltzer Difference

Tucker & Meltzer Valuation Advisors are independent business valuation advisors. We provide no other services (accounting, legal, financial planning or investment). Tucker & Meltzer represents an economical alternative to more expensive accounting and large valuation firms. We offer accurate, well documented, up to date, and market based value comparisons and promise an exceptional turn-around time. We have the experience and knowledge to handle the tough jobs and we look forward to having the opportunity to work with you.

**FMV IS NOT FAIR TO ONE SIDE OR THE OTHER.**

### Announcing . . .

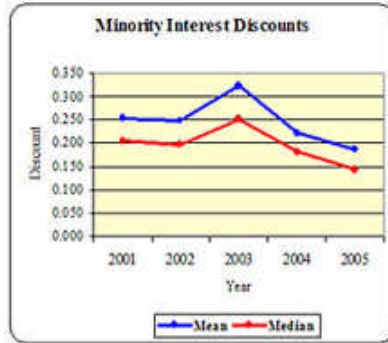
**Brooke Tucker** has been elected President of the Maryland Chapter of the American Society of Appraisers for the 2006-2007 term. He is an Accredited Member of ASA.



## Valuation Perspectives

**MINORITY INTEREST DISCOUNTS.** The minority interest or lack of control discount (DMIN) is better understood and easier to document than other discounts. Discounts are readily available from observations of publicly traded securities. The graph below depicts the "all industry" DMIN (mean and median) for the last five years from Mergerstat/Shannon Pratt's Control Premium Study.

Other observations are available from closed end mutual funds (Net Asset Values) and REITs. Many valuation practitioners use the median value from Mergerstat/Shannon Pratt's Control Premium Study which was 14.3% at the end of 2005. DMINs can also be selected for specific industries and timeframes, i.e. 19.5% for commercial banks (2003-2005). From the median DMIN value, the valuation expert must then determine the degree of discount to apply to the subject. This



is a subjective opinion which requires experience and knowledge. A 2% interest would generally have a greater discount than a 49% interest. A lack of voting rights would also increase the discount. All too frequently, valuers have applied discounts based on "acceptable ranges" or "industry norms" when observable and empirical data is available for analysis. Users of valuation reports should expect market based studies and/or other empirical evidence as of the valuation date to support the selected discount. □

## Cases In Brief

### ESTATE OF KELLY VS. COMMISSIONER, T.C. MEMO, 2005-235 OCTOBER 11, 2005

This case was about the application of discounts for lack of control and lack of marketability to interests in two family owned entities. Kelley-Louden, Ltd. ("KLLP"), held assets totaling \$1,226,421, which consisted of \$807,271 cash and \$419,1580 in certificates of deposit. The second company was Kelley-Louden Business Properties, LLC ("KLBP LLC") whose only asset was a 1% interest in KLLP. The Court allowed a 32% combined discount for lack of control and lack of marketability. See the full case write-up on our web site [\[click here\]](#). □

<sup>[i]</sup> Revenue Ruling 59-60. <sup>[ii]</sup> First printed in July/August 2004.



Tucker & Meltzer - Valuation Advisors is a business valuation firm focused on the needs of family limited partnerships and closely-held companies. The firm's founding partners have extensive experience and credentials in valuing closely-held and asset holding companies. We have performed over 300 valuations for companies in a large number of industries, reflecting our broad experience in accounting, finance, litigation services, valuation theory and capital transactions.

[S.G. Brooke Tucker](#), AM - 410.790.6940  
[Anne R. Meltzer](#), CPA, ABV - 410.998.2085

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## On the Subject of Discounts

### Philadelphia EstatePlanning Council

"Viewpoints on Valuation: the Appraiser, the Attorney, the IRS and the Judge" - May 2, 2006

"There is no automatic discount - it will depend on the facts and the quality of the appraiser."

*Judge David Laro*

"There is no discount, unless you prove it."

*John A. Darazsdi, Esq., IRS*

**ALL TOO FREQUENTLY, VALUERS HAVE APPLIED DISCOUNTS BASED ON "ACCEPTABLE RANGES" OR "INDUSTRY NORMS."**

## Recent Assignments

- FLP-MRKTS - Estate
- FLP-Real Estate - Gift
- Title Company - C Conversion
- Web Hosting - Stock Options
- Printing Company - Sale
- Imaging Manufacturer - Investment

## Privacy Statement

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