



ESOP Valuation Issues Q&A

Presented by:

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OVERVIEW

Test your valuation knowledge or learn new facts about valuation concepts and the report process in this fun and interactive session!

AND

PLEASE SILENCE YOUR CELL PHONES

VALUATION PROCESS

Who does what and how

Timeline and expectations

- Documentation gathering
- Due diligence
- Onsite visits and management interviews
- Draft valuation report
- Final valuation report
- Presentation of conclusion to Trustee

ESOP trustee sets price of stock

KEY COMPONENTS OF THE REPORT

1. Entity to be valued (name, type)
2. Valuation date (ex. December 31, 2016)
3. Standard of value (ex. FMV)
4. Ownership interest & value basis (control or minority)
5. Premise of value (going concern)
6. Rights or restrictions (buy-sell agreements)
7. Report date (date final report issued/published)
8. Intended user of the report(ex. ESOP Trustee)
9. Intended use/purpose of the report (ex. ESOP Administration)
10. Examine and notate extraordinary and limiting conditions

FINANCIAL ANALYSIS

Historical:

- Liquidity
 - Profitability
 - Leverage/capitalization
 - Turnover ratio analysis
 - Common-sized financial analysis
 - Comparative financial analysis
- ROA
 - ROE
 - EBIT margin
 - EBITDA
 - Ratio of capex to sales
 - Revenue growth rates
 - Free CF to sales

COMPANY OVERVIEW: NON-FINANCIAL FACTORS

- History
- Type/date of corporation
- Products or services
- Markets and customers
- Seasonal or cyclical factors
- Competition
- Suppliers
- Key personnel
- Management
- Employees
- SWOT
- Business plan for operation, strategic initiatives, and growth
- Goodwill factors

VALUATION APPROACHES

Income Approach

- Discounted Cash Flow Method
- Capitalization of Earnings Method

Asset (Cost) Approach

- Adjusted Book Value Method
- Dual Capitalization of Earnings Method (hybrid)

Market Approach

- Guideline Public Company Method
- Guideline Transaction Method

FINANCIAL ANALYSIS – NORMALIZATIONS

- Level of earnings: Control or minority
- Discretionary expenses
- Non-business related assets
- Real estate (rent)
- Bad debt
- Officers compensation
- Working capital (excess or deficit)
- Inventory (obsolescence)
- Shareholder, related party notes

OTHER ESOP CONSIDERATIONS

- ESOP Internal Loan Amortization
- Repurchase obligation
 - Planning and funding
- Executive compensation
 - Synthetic equity, SARs, warrants, options
- Treatment of contingent purchase consideration
 - Earnout or clawback

ESOP TRANSACTION CONSIDERATIONS

Fairness opinion report

Executive compensation

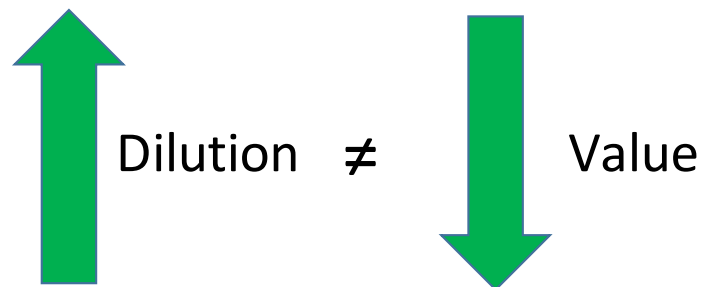
Loan or financing

COMPENSATION & THE IMPACT ON VALUE

All shares of stock owned by the ESOP, whether held as unallocated suspense shares or as allocated shares, must be netted against the total equity value.

An analysis of the impact of exercising options should be conducted to compare the economic dilution vs. the projected increase in company value.

In theory, any dilution should not negatively impact the sponsoring company's total value, and therefore an increase in dilution does not have to mean a decrease in value.



VALUATION EXPERT

Credentialed

- American Society of Appraisers “ASA”
- Association of Certified Public Accountants “ABV”

Experienced

- ESOP technical, case law, regulatory
- Specific industry

Unbiased

- Unrelated party, not conflicted
- No financial interest in outcome

RED FLAGS

Unfamiliar with recognized valuation methodology and concepts

- Application of appropriate methodology is essential

Substantial change in valuation methodology from one year to the next

- Change in methodology is not substantiated or warranted

Does not conduct best practices

- Breach of duty

Errors in previous report

- Math, conceptual, or grammatical

Unfamiliar with current or evolving regulatory issues

- Does not stay current

Does not perform specific service

- Fairness Opinions

Does not request to see the repurchase obligation study

- Circumstances depending

RED FLAGS

Loss of credentialing status

- Ethical violations

Poor service

- Lack of timeliness for responses or missed deadlines

Gross negligence vs. ordinary negligence

- Ethical or theoretical

Conflicts of interest

- “Two Hats”

Unsubstantiated increase in cost or fees

- Change of fee not warranted

COMMON VALUATION ERRORS

- Check the Math!
- Incorrect standard of value applied
- Inappropriate normalizations – double counting discounts or premia (control v minority)
- Inappropriate application of methodology
- Forecasts are not reasonable, defensible, or unaffected by conflicts
- Economic and industry overviews do not tie with financial analysis of subject entity
- Ignores synthetic equity or deferred compensation liability or dilution
- ESOP Adjustments

Don't Forget!

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ERIN D. HOLLIS, ASA, CDBV

Erin D. Hollis, ASA, CDBV, is a Director at Marshall & Stevens Incorporated. She works within the Chicago financial practice group conducting opinions and analyses for closely-held and publicly-traded entities for litigation, taxation and transactional purposes, and with ESOP clients on financial analysis and consulting services needs.

Experience – Since 2000, Ms. Hollis has worked with advisors and closely-held business owners for ESOP valuation needs, and has experience providing valuation advisory and economic analysis services in the areas of litigation, taxation, transactional, and planning purposes. Erin has provided valuation services in industries, such as manufacturing, construction, transportation, agricultural, distribution, retail, wholesale, and a wide range of service industries, including architecture and engineering.

She is a qualified expert witness, and has testified for various marital and corporate litigation matters. She is a prolific author on the subject of business valuation, and has written for several industry trade publications and as a contributing author for professional organizations. Erin sits on the Business Valuation Committee of the American Society of Appraisers (ASA) and the Valuation Advisory Committee (VAC) of the ESOP Association, and is a member of the NCEO.

Education – Erin received a B.A. and B.S. from Michigan State University. She is an Accredited Senior Appraiser (ASA) with the American Society of Appraisers, and Certified in Distressed Business Valuation (CDBV) with the Association of Insolvency & Restructuring Advisors (AIRA).



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DAWN GOESTENKORS

Dawn Goestenkors, MBA, Executive Vice President, Employee Benefits Group

BS Finance, Quincy University, MBA Southern Illinois University - Edwardsville.

Dawn brings vast experience and knowledge gained from more than 10 years in trustee services for employee stock ownership and qualified retirement plans. Dawn's past work experience includes commercial credit underwriting and lending. She has a concentration in plan administration and DOL regulatory issues, as well as deep ESOP transactional experience. Dawn is a member of The ESOP Association, Employee Owned S-Corporation of America (ESCA), National Center for Employee Ownership (NCEO) and frequently speaks on trustee and fiduciary topics. Dawn joined First Bankers in 2007.

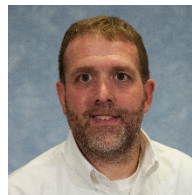


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MATTHEW LININGER

Matthew Lininger is a Product Development Engineer with more than 15 years of experience at Restek Corporation in Bellefonte, PA. For the past 5 years, he has also served the company as an elected Internal ESOP Trustee. During his tenure, he has developed expertise in many ESOP areas and has been heavily involved in the valuation process. He is a member of the Employee Ownership Communications Team at Restek, a group which is responsible for ensuring that employees understand both the valuation process and its results. Matt has attended numerous chapter conferences where he has presented talks on ESOP topics.

Education – Matt earned an A.S. in Plastic and Polymer, an A.S. in Toolmaking, and an A.S. in Automated Manufacturing from the Pennsylvania College of Technology. He is a Certified SolidWorks Professional (CSWP) with Dassault Systèmes SolidWorks Corporation.



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Questions ?



Thank You for Attending!