1999

Comment letters on Proposed Statement on Standards for Accounting And Review Services Financial Statements included in Written Business Valuations

American Institute of Certified Public Accountants. Accounting and Review Services Committee

Exposure Draft
Proposed Statement on Standards for Accounting
And Review Services
Financial Statements included in Written Business Valuations
Comment Letters

COMMENT LETTER #1

I have just read the exposure draft for financial Statements Included in Written Business Valuation Reports.

Three cheers for SAARS for realizing that financial statements in Valuation reports should be exempt from SAARS 1.

Thank you.

http://www.aicpa.org/ Best Regards,

Larry

Lawrence V. Valente
ValueNomics San Diego, LLC
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Have you purchased your copy of Gary and Dirk's book, "The Business of Business Valuation"?

COMMENT LETTER #2

DON M. PALLAIS, CPA

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February 15, 2000

Sherry Boothe
Audit and Attest Standards File 2000
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Re: Exposure Draft, *Financial Statements Included in Written Business Valuations*

To the Accounting and Review Services Committee

While it might be a good idea to exempt financial statements in formal business valuations from the requirements in SSARS No. 1, I think the ED is conceptually flawed. I recommend the committee reexamine the draft to eliminate these problems.

The conceptual flaws fall into two categories:

- The notion of normalized financial statements
- The use of the business valuation.

Normalized Financial Statements

The ED defines a concept new to AICPA Professional Standards: normalized financial statements. These statements appear to be historical financial statements adjusted to take into consideration some factor that needs to be treated differently for the purposes of the valuation. They are not financial statements as defined by SSARS because they do not constitute "a presentation derived from accounting records that is intended to communicate the entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with GAAP or OCBOA" (AR 100.04). Accordingly, they are not covered by SSARS No. 1 and it is unnecessary for the ED to exempt them from the standard. In this regard they are much like pro forma financial statements, which are also based on historical statements but adjusted to present something not included in the statements. SSARS No. 1 doesn't apply to pro formas either.

The concept might be a harmless exercise—superfluous but educational—except that paragraph 1 says, "this Statement does not preclude an accountant from complying with SSARS 1 in such engagements." Thus it allows the accountant to compile normalized financial statements in accordance with SSARS. This raises a number of unanswered questions. How does one, for example, read the statements for material mistakes in the application of accounting principles or inadequate disclosures when the statements are not measured based on GAAP or any other established criteria? Can pro forma financial statements also be compiled in accordance with SSARS? Can normalized or pro forma statements be reviewed in accordance with SSARS? If so, would the review be different from that described in AT 300, *Reporting on Pro Forma Financial Information*?

The original standard wisely, in my opinion, limited itself to GAAP and OCBOA financial statements. I think the ED would be improved if it merely stated that normalized financial statements are not financial statements as defined by SSARS No. 1, paragraph 4, and that SSARS don't apply to them. The ED could then focus solely on the GAAP or OCBOA financial statements included in the business valuation.

Use of the Business Valuation

Paragraph 4b does not allow the exemption if anything comes to the accountant's attention during the engagement that would cause the accountant to believe that the financial statements included in the written business valuation will be used to obtain credit or for any purpose other than developing and presenting a business valuation of the entity.

This suggests to me that the exemption is available if the valuation (which is based on and includes the financial statements) will be used to obtain credit as long as the financial statements themselves are not to be used for that purpose. It is impossible for me to conceive of a situation in which the valuation is put to a use but the financial statements that underlie it and are included its presentation are not put to the same use.

While superficially similar to the exemption for financial statements contained in personal financial plans, there are two important distinctions between SSARS No. 6 and this ED:

- The exemption in SSARS No. 6 is based largely on the notion that the use of the statements is primarily internal and no outsider is likely to be misled. Personal financial plans are presumed to be used by advisors and others whose interests are consistent with the client's. Business valuations, on the other hand, are customarily used in connection with mediation or negotiation by persons with adversarial interests—for example, partners splitting up a business, a potential buyer of a business, or a venture capitalist financing a takeover. This raises a much different public-protection issue.
- SSARS No. 6 requires a specified form of report that puts the financial statements in context and essentially warns users not to rely on them. Such a requirement seems a reasonable policy choice that's fair to users. No report is required at all in the ED even though it seems more important here than in SSARS No. 6.

Accordingly, if the exemption is to be extended to business valuations, I suggest that the SSARS require language similar to that in SSARS No. 6 to let users know the character of the accountant's service and the extent of responsibility taken for the financial statements.

Thank you for the opportunity to comment on the standard. Please let me know if you'd like to discuss any of these comments further.

Sincerely,
Don M. Pallais

COMMENT LETTER #3

Greene & Wallace, Inc.
Attn: Greg Grunewald
1241 Dublin Road
Columbus, Ohio 43215

Hi Sherry,

Just downloaded and read the draft re financial statements included in business valuation reports. I am glad the committee has addressed this and created the waiver. We have wrestled with this issue many times for financials that we are associated with. What was difficult, was when the'numbers' came from another accountant or from tax returns prepared by some individual who was trying to sell their business. Our assumptions,limiting conditions and report portions that addressed the financials tended to be longer that the valuation itself.

In addition to 'normalized financials' it is common to include 'common sized' financials, which is stated in percentages for comparison with other public information. This might be an additional item for the committee. While on the subject, some valuation methods include prospective financial information as well as historical. We spend as much language on the prospective information attempting to comply with the standards as we do with the historical. Does this area belong with this exposure draft.........

Hope this helps

Greg Grunewald CPA, CVA

COMMENT LETTER #4

I have reviewed the exposure draft and agree with the draft as written. I think that this is a much needed exclusion from the reporting requirements of SSARS 1. The "business" of business valuation is much different than the "business" of preparing financial statements. The needless requirement for CPA business valuators having to comply with SSARS 1 in business valuation work puts us at a competitive disadvantage with non CPA business valuators and creates added cost and complexity without any increase in value to our clients. In today's competitive environment, CPAs and their rule making organizations must be constantly aware of the need to create value for our clients by not needlessly complicating our service to clients. The cost of applying standards must be weighed against value to clients and the appropriateness of the standards to the task at hand.

Sincerely,

David Melton, CPA, CVA

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February 18, 2000

Sherry Boothe
Audit and Attest Standards, File 2000
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Re: Exposure Draft
Proposed Statement
Financial Statements Included in Written Business Valuations

The proposed statement on financial statements included in business valuations has come to my attention. The subject is worthy of consideration and the establishment of guidelines. Unfortunately, I think this very abbreviated statement fails to adequately consider certain apparent issues.

1. As to historical financial statements, a CPA presenting such statements in a valuation report should not be summarily exempted from other usual reporting requirements. I customarily follow certain procedures that should be required.

   The source of the historical statements should be identified. Is it the valuator's own firm? or another firm? What was the level of responsibility expressed in the opinion on those financial statements, audit, review or compilation? How much responsibility is the valuator taking? For example, if the valuator relies upon and takes no responsibility for the historical statements his/her report should so state.

2. The definition of normalized statements is wholly inadequate. Adjustments to historical statements to derive a normalized statement are made to assist in forming an opinion on valuation of the business. These adjustments are often discretionary and used for purposes other than comparison with a comparable entity. For example, adjustments may be directed to developing a pro forma income or cash flow under certain assumptions for capitalization.

3. The valuator's report should identify that the presented statements are normalized. The report should also explain the adjustments as well as

Robert C. Flackman, CPA (Ret.)
Jerome Goodman, MBA, CPA, CVA
Albert L. Potter, CPA, CFP
James P. Madormo, MBA, CPA, CFP
Christopher R. Plunkett, MBA, CPA
Michael Roemer, CPA, CVA
Linda J. Murphy, CPA
Patricia D. Duarte, CPA
Domenick Saglimbeni, CPA/PFS, CFP
Paul M. Caliento, CPA
Joan Krieger, CPA
Patricia B. Ciardullo, CPA

explain that the normalized statements may differ from GAAP or OCBOA.

4. Finally, expressing all this only in the engagement letter is inadequate. Although the engagement letter may include those items in proposed paragraph 4, the disclosures that I have suggested above should be required disclosures in a valuator's report.

Sincerely,

J. Goodman, MBA, CPA, CVA

COMMENT LETTER #6

This statement codifies the general practice of writing around SSARS 1 in business valuation reports in the CPA business valuation community. The proposed statement as written is necessary to maintain a level competitive field between CPA valuators and those without the CPA credential, and our firm strongly supports its adoption.

Joseph T. Gardemal III, CPA, CVA, CGFM
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RA&Co

REMINICK, AARONS & COMPANY, LLP

CERTIFIED PUBLIC ACCOUNTANTS

March 16, 2000

Ms. Sherry Boothe
Audit and Attest Standards
File 2000
American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Boothe:

We are pleased to comment on the exposure draft of the proposed Statement on Standards for Accounting and Review Services (SSARS) entitled *Financial Statements Included in Written Business Valuations.*

In our view, this proposed amendment to SSARS 1 exempting historical and normalized financial statements included in written business valuations from the applicability of SSARS 1 should be modified as follows:

1. The term "Written Business Valuation" should be defined to minimize confusion over the applicability of the pronouncement. Although the words "written business valuation" may be perceived as being sufficiently explicit, there still could be instances where a document is in substance a written business valuation but is not called a business valuation. Moreover, while many people would maintain that the term "Financial Statement" is sufficiently explicit in and of itself, it is a defined term in the Standards for Accounting and Review Services. Therefore, we suggest that the term "Written Business Valuation" be defined as *a document that provides an estimation of the fair value of a business as a whole.* Where the term "fair value" has a general meaning consistent with its meaning within the context of generally accepted accounting principles (GAAP). In a GAAP context, "fair value" is an estimated market exit price[1]. That is, it is an estimate of the amount that would be realized if the entity had sold the asset (which could be a business) or settled the liability on the reporting date.

[1] The term "fair value" is used in various GAAP pronouncements, including: Accounting Principles Board Opinion No. 16 *(Business Combinations),* Statement of Financial Accounting Standards No. 107 *(Disclosures about Fair Value of Financial Instruments),* Statement of Financial Accounting Standards No. 115 *(Accounting for Certain Investments in Debt and Equity Securities),* Statement of Financial Accounting Standards No. 133 *(Accounting for Derivative Instruments and Hedging Activities),* and Statement of Financial Accounting Concepts No. 7 *(Using Cash Flow Information and Present Value in Accounting Measurements).* However, the term "fair market value" is widely used in tax-related valuations. These two terms are generally synonymous, meaning "The amount at which the item could be bought or sold in a current transaction between willing parties."

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2. We believe that there is a similarity between an engagement to submit a written business valuation containing financial statements to a client and an engagement to submit unaudited financial statements that are not expected to be used by third parties. In each case the financial statements are prepared for use only by parties having a familiarity with the entity and/or purpose for which the financial statements are prepared. Therefore, we suggest that the requirements of this proposed Statement be made consistent with the proposed SSARS entitled *Amendment to Statement on Standards for Accounting and Review Services 1, Compilation and Review of Financial Statements*. This could be accomplished by:

    a. Modifying paragraph 4.a. of the Exposure Draft to require: i) a written engagement letter[2], and ii) issuance of a letter to management documenting an understanding with the entity regarding the services to be performed and the limitations on the use of those financial statements,

    b. Requiring that a reference be included on each page of the financial statements included in the business valuation such as "Restricted to Business Valuation Purposes" or "For use only by the management of [*name of entity*] and [*other parties named by client*]."

We otherwise support the issuance of this proposed SSARS and believe that it would provide the profession with much needed additional flexibility to provide services needed by many nonpublic entities.

Respectfully submitted,

Robert J. Sonnelitter, Jr.

Robert J. Sonnelitter, Jr., CPA
Director of Accounting and Auditing
Reminick, Aarons & Company, LLP

[2] The documentation, contained in the engagement letter, of the understanding with the entity regarding the services to be performed should include matters similar to those specified in paragraph 22 of the proposed SSARS entitled *Amendment to Statement on Standards for Accounting and Review Services 1, Compilation and Review of Financial Statements.*

COMMENT LETTER #8

I work for Good Swartz & Berns a local firm with 50 staff and professionals. We are members of the PCPS. This exposure draft is of interest to me as I am a CVA (certified valuation analyst-NACVA) and a CPA. This proposed statement will be very helpful in clarifying this gray area and is most timely.

Performing a compilation in this case puts undue burden on the CPA and also makes the fee ucompetetive. However an important question does not seem to be addressed in this draft. Does the CPA have to report on forward looking statements either prepared by the client or "prepared" by the CPA in a non GAAP format as an incomplete presentation as defined in GAAP? These cash flow or income "forecasts" are only used for the purpose of the valuation and are not stand alone presentations.

Raj Mehra CPA
Good Swartz & Berns, Inc.
11755 Wilshire Blvd Ste 1700
Los Angeles, CA 90025 – 1523

COMMENT LETTER #9

I am very much in favor of the Proposed Statement on Standard for Accounting and Review Services - titled: "Financial Statements Included In Written Business Valuations." Certified Public Accountants are at a distinct disadvantage when competing with non-CPA's when preparing valuations as a result of the current standards. This statement is well conceived and well written.

Edwin J. Bull, Jr. AICPA # 5299675

COMMENT LETTER #10

Business Valuation

Dear Ms. Boothe:

In reference to section 2:

Normalized financial statements are financial statements that contain necessary and appropriate adjustments in order to make an entity's financial information more meaningful when presenting and comparing on a consistent basis the financial results of that entity to those of a comparable entity as part of a business valuation engagement.

This section fails to address the second type of normalization adjustment and maybe the most common type "adjustments to control income levels from minority income levels".

Although the draft goes a long way toward meeting our needs, we also need to address the second type of adjustment.

Thank you for your consideration of this issue.

James S. Rigby Jr.
The Financial Valuation Group 900 Wilshire Blvd.
Suite 514
Los Angeles, California 90017
Tel: 213-362-9991
Fax: 213-623-4809
Website: www.fvgi.com

COMMENT LETTER #11

This draft is essential in Business Valuations - please keep me posted .

Mary Eike, CVA
pondside@earthlink.net

COMMENT LETTER #12

March 23, 2000

Ms. Sherry Boothe
Audit and Attest Standards
File 2000
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Re: Proposed statement on financial statements included in written business valuations

Dear Ms. Boothe:

This letter is to support the proposed statement on financial statements included in business valuation reports.

We acknowledge the additions to the general assumptions and limiting conditions.

Sincerely,

LEMASTER & DANIELS PLLC

Donald A. Reddington, CPA, MBA, ABV
Director, Management Consulting Services

Sean C. Black, CPA
Manager, Management Consulting Services

Brad Haines
Senior Consultant, Management Consulting Services

COMMENT LETTER #13

Dear Ms. Boothe,

Thank you and all those who contributed for preparing this exposure draft. It is wonderful that to have this departure documented.

I have one comment that I believe will improve the definition of normalized financial statements.

I recommend the language in the definition of normalized financial statements that I have left out be deleted. It is shown below for your > convenience.

Normalized financial statements are statements that contain necessary and appropriate adjustments in order to make an entity's financial information more meaningful to the business valuation engagement.

Language deleted: ..."when presenting and comparing on a consistent basis the financial results of that entity to those of a comparable entity as part of a..."

This language scars me. I hope the following explanation conveys why I believe the language might me used against the appraiser inappropriately. I don't want someone judging my adjustments based on guideline companies. I want my adjustments judged based on what is driving the value of the subject company. How do I know if other companies have a condo in a resort location. When valuing the subject company, I treat it as a non-operating asset, because that's the way I believe a willing buyer would treat it. I want that justification to be enough. Comparison to a comparable entity is not the only reason we normalize. We make adjustments based on our judgment of the value of the Company. Maybe we separate out a non-profitable division. Are we doing that for consistency? No Are we doing that for comparability? I think we are doing it to identify the underlying value of the Company. When we adjust owners' compensation are we thinking about comparability to another company or are we valuing services provided to this company? I hope the above conveys my concern. Once again, thank you for the exposure draft and Statement that will follow.

Terry M. Hargrave
310-576-1090

Attached is the exposure draft for the proposed Statement on Standards for Accounting and Review Services entitled "Financial Statements Included in Written Business Valuations".

This proposed Statement exempts from the applicability of SSARS 1, Compilation and Review of Financial Statements, historical financial statements and normalized financial statements that are included in written business valuations. The proposed Statement also defines normalized financial statements.

Comment and responses should be e-mailed to Sherry Boothe at > sboothe@aicpa.org.

If you are unable to open the attached file, the full text of the proposed Statement is provided below.
Sincerely,

Colleen C. Risner for Mark Luttrell
CBIZ - CKS Business Services, Inc.
phone: (661)325-7500
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SUMMARY

WHY ISSUED

Financial statements included in written business valuations frequently contain departures from generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA) because the purpose of such financial statements is solely to assist in developing and presenting the business valuation of an entity. This Statement is being issued to exempt financial statements included in written business valuations from the applicability of Statement on Standards for Accounting and Review Services (SSARS) 1, *Compilation and Review of Financial Statements* (AICPA, *Professional Standards*, vol. 2, AR sec. 100), because users of these statements do not require that the statements be in conformity with GAAP or an OCBOA.

WHAT IT DOES

This proposed Statement -

- Exempts historical financial statements and normalized financial statements included in written business valuations from the applicability of SSARS 1.

- Defines *normalized financial statements* as financials statements that contain necessary and appropriate adjustments in order to make an entity's financial information more meaningful when presenting and comparing on a consistent basis the financial results of that entity to those of a comparable entity as part of a business valuation engagement.

1. This Statement provides an exemption from Statement on Standards for Accounting and Review Services (SSARS) 1, *Compilation and Review of Financial Statements* (AICPA, *Professional Standards*, vol. 2, AR sec. 100), for historical financial statements and normalized financial statements that are included in written business valuations. However, this Statement does not preclude an accountant from complying with SSARS 1 in such engagements.

2. Normalized financial statements are financial statements that contain necessary and appropriate adjustments in order to make an entity's financial information more meaningful when presenting and comparing on a consistent basis the financial results of that entity to those of a comparable entity as part of a business valuation engagement.

3. Financial statements included in written business valuations frequently contain departures from generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA) because the purpose of such financial statements is solely to assist in developing and presenting the business valuation of an entity.

4. An accountant may submit a written business valuation containing financial statements to a client without complying with the requirements of SSARS 1, when all the following conditions exist:

    a. The accountant establishes an understanding with the client, preferably in writing, that the historical or normalized financial statements included in the written business valuation-

        (1) Will be used solely in developing and presenting the valuation of the entity.

        (2) May be incomplete or contain other departures from GAAP or OCBOA and should not be used for any purpose other than developing and presenting a business valuation of the entity.

    b. Nothing comes to the accountant's attention during the engagement that would cause the accountant to believe that the financial statements included in the written business valuation will be used to obtain credit or for any purpose other than developing and presenting a business valuation of the entity.

EFFECTIVE DATE

5. This Statement is effective upon issuance.

COMMENT LETTER #14

Overall, I think the proposal looks good. Two things occurred to me that might also warrant consideration.

1. It may also be appropriate to address the subject of prospective financial statements, as projections are frequently included in written business valuation reports. Sometimes the appraiser helps prepare the projections, and sometimes they have been prepared by the client or another CPA. Clarification of this would be helpful.

2. It may be helpful for the standards to be clear as to any difference due to whether the CPA doing the valuation also compiled, reviewed or examined the financial statements, as opposed to those reported on by other CPA's or internally prepared, etc.

As my practice is limited to business valuation and litigation support work, the statements I use are always prepared by others. This, however, is not the case for many practitioners.

I hope these comments are of some value.

Sincerely,
Edward M. Fidelman, CPA.ABV

#15

KATCH, TYSON & COMPANY
Certified Public Accountants

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May 11, 2000

Ms. Sheery Boothe
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1211 Avenue of the Americas
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Financial Statements Included in
Written Business Valuations

The proposed Statement exempts financial statements included in written business valuations from being in compliance with SSARS 1.

If such exemption is considered to be advisable, then the accountant's name should not be associated, in any way, with the financial statement. If such association was present, the reader would assume that the financial statements met professional standards. The accountant's name should not be mentioned or referenced within the written business valuation document.

Very truly yours,

KATCH, TYSON & COMPANY

Ronald S. Katch

RSK:ar

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ARTHUR ANDERSEN

Arthur Andersen LLP
33 West Monroe Street
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Ms. Sherry Boothe
Audit and Attest Standards
File 2000
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May 25, 2000

Dear Ms. Boothe,

We appreciate this opportunity to comment on the proposed Statement on Standards for Accounting and Review Services (SSARS), *Financial Statements Included in Written Business Valuations.*

We support the efforts of the Accounting and Review Services Committee (ARSC) to clarify the applicability of SSARS No. 1, *Compilation and Review of Financial Statements*, to financial statements in a consulting service report. We believe that the ARSC addressed matters related to the applicability of SSARS No. 1 clearly and succinctly in Compilation and Review Risk Alert – 1999/2000. Paragraph 28 of the risk alert states, "The SSARS contain no provision to exempt historical financial statements included in consulting reports." Accordingly, we ask the ARSC to reconsider promulgation of proposed Statement on Standards for Accounting and Review Services (SSARS), *Financial Statements Included in Written Business Valuations.*

We believe that the Compilation and Review Risk Alert – 1999/2000 is entirely consistent with AU Section 504, *Association with Financial Statements*, paragraph 1, which states:

> "The fourth standard of reporting is:
>
> The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therefor should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor's work, if any, and the degree of responsibility the auditor is taking."

We believe that neither AU Section 504, nor Compilation and Review Risk Alert – 1999/2000, provide a conceptual basis for the proposal to exempt historical and normalized financial statements included in written business valuations from SSARS. The absence of a sound conceptual basis for the promulgation of this proposal creates the risk that there would be no basis for objections to other exceptions to the reporting requirements of SSARS. We are concerned that exceptions to SSARS will erode confidence in those standards and eventually lead to a presumption that the conceptual basis for SSARS is questionable.

We also ask the ARSC to consider the last sentence of AU Section 504, paragraph 1, in its deliberations on the matter of exempting financial statements included in consulting reports from SSARS.

> "The objective of the fourth reporting standard is to prevent misinterpretation of the degree of responsibility the accountant assumes when his name is associated with financial statements."

If practitioners issue a report in accordance with SSARS indicating their level of responsibility for financial statements included in consulting reports, then the likelihood for misunderstandings about the degree of responsibility an accountant is taking would be reduced. Any reduction in the likelihood for a misunderstanding about the degree of responsibility an accountant is taking for financial statements may have a positive effect on the efforts of practitioners to mitigate litigation risk. In addition, a better alignment of the requirements of SSARS and Statements on Auditing Standards regarding association with financial statements would eliminate one possible source of confusion about the applicability of reporting standards, potentially reducing the numbers of reporting errors in practice.

We would be pleased to discuss our comments with you or your staff at your convenience. If you have any questions, please contact Dorsey Baskin at 312-931-2238.

Very truly yours,

Arthur Andersen LLP

Arthur Andersen LLP

LRW

COMMENT LETTER #16

Ms. Sherry Boothe
Arthur Anderson LLP
Audit and Attest Standards
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File 2000
American Institute of
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New York, New York 10036-8775

May 25, 2000

Dear Ms. Boothe,

We appreciate this opportunity to comment on the proposed Statement on Standards for Accounting and Review Services (SSARS), Financial Statements Included in Written Business Valuations.
We support the efforts of the Accounting and Review Services Committee (ARSC) to clarify the applicability of SSARS No. 1, Compilation and Review of financial Statements, to financial statements in a consulting service report. We believe that the ARSC addressed matters related to the applicability of SSARS No. I clearly and succinctly in Compilation and Review Risk Alert - 1999/2000. Paragraph 28of the risk alert states, "The SSARS contain no provision to exempt historical financial statements included in consulting reports." Accordingly, we ask the ARSC to reconsider promulgation of proposed Statement on Standards for Accounting and Review Services (SSARS), Financial Statements Included in Written Business Valuations.

We believe that the Compilation and Review Risk Alert - 1999/2000 is entirely consistent with AU Section 504, Association with Financial Statements, paragraph 1, which states:

"The fourth standard of reporting is:

The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therefor should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor's work, if any, and the degree of responsibility the auditor is taking."

We believe that neither AU Section 504, nor Compilation and Review Risk Alert - 1999/2000, provide a conceptual basis for the proposal to exempt historical and normalized financial statements included in written business valuations from SSARS. The absence of a sound conceptual basis for the promulgation of this proposal creates the risk that there would be no basis for objections to other exceptions to the reporting requirements of SSARS. We are concerned that exceptions to SSARS will erode confidence in those standards and eventually lead to a presumption that the conceptual basis for SSARS is questionable.

We also ask the ARSC to consider the last sentence of AU Section 504, paragraph 1, in its deliberations on the matter of exempting financial statements included in consulting reports from SSARS.

"The objective of the fourth reporting standard is to prevent misinterpretation of the degree of responsibility the accountant assumes when his name is associated with financial statements." If practitioners issue a report in accordance with SSARS indicating their level of responsibility for financial statements included in consulting reports, then the likelihood for misunderstandings about the degree of responsibility an accountant is taking would be reduced. Any reduction in the likelihood for a misunderstanding about the degree of responsibility an accountant is taking for financial statements may have a positive effect on the efforts of practitioners to mitigate litigation risk. In addition, a better alignment of the requirements of SSARS and Statements on Auditing Standards regarding association with financial statements would eliminate one possible source of confusion about the applicability of reporting standards, potentially reducing the numbers of reporting errors in practice.

We would be pleased to discuss our comments with you or your staff at your convenience. If you have any questions, please contact Dorsey Baskin at 312-931-2238.

Very truly yours,

Arthur Andersen LLP

LRW

COMMENT LETTER #17

Comments on "Proposed Statement on Standards for Accounting and Review Services: Financial Statements Included in Written Business Valuations":

1. Paragraph 2 on page 6, starting with "Normalized financial statements...
" makes reference to a comparable entity as part of a business valuation engagement. This point is not clear.

A. The purpose of normalizing financial statements is to create "economic-based" financial statements to assist the valuator in doing a valuation. This may be done in connection with comparing the subject company to "comparable entities", but most often is done to facilitate an "economic-based" assessment of the business' future earnings capacity, regardless of whether or not it is to be compared to a "comparable entity".

I suggest the following rewording:

2. Normalized financial statements are financial statements that contain necessary and appropriate adjustments to restate the reported financial statements to a more meaningful manner to facilitate an analysis for purposes of valuing the business entity. They be also used in connection with and for comparison to comparable entities.

As for Paragraph 4(b), I don't understand the logic of this paragraph. Many valuations are done for possible purchase and/or sale of a company. As such, financing is almost always considered, whether it be credit from a financial institution or from the seller. Therefore, this paragraph would create a problem for many appraisers since:

A. the appraiser may not know to what extent the valuation will be used to help justify a loan, or credit, or to be used in connection with financing a transaction.

B. the appraiser doing a fairness opinion, would not be able to render such an opinion.

C. even in transactions where credit is not being granted to the business directly, such as to an ESOP, the appraiser would not be able to do a proper valuation.

I suggest that the Exposure Draft plainly say that financial statements that are presented in business valuations recognize that GAAP does not reflect the financial results in an "economically correct" manner. That is they are historical in nature, and do not reflect the value of assets and liabilities in a manner that are considered normal when trying to assess the fair market value of an entity.

I also think that the Exposure Draft should refer to the new ABV designation and/or the other professional organizations that provide specialized training to assist a CPA in being qualified to do business valuations. This would help establish a stronger link that the training to become a CPA does not generally provide an individual with the requisite knowledge to make the normalizing adjustments necessary to produce reasonable valuations.

Another statement that should be included is that appraisers should not refer that their work is done in accordance with GAAP, since that is clearly misleading and unfounded. I have seen a number of reports and had appraisers testify to that effect.

These are my quick thoughts. If you have any questions, please feel free to contact me.

Mauricio Kohn, CFA, CMA, CFM
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COMMENT LETTER #18

May 31, 2000

Sherry Boothe
Audit and Attest Standards, File 2000
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Boothe:

The Audit and Assurance Services Committee of the Illinois CPA Society ("Committee") is pleased to have the opportunity to comment on the "Proposed Statement on Standards for Accounting and Review Services, Financial Statements Included in Written Business Valuations" The following comments and considerations represent the collective views of the members of the Committee. The organization and operating procedures of the Committee are reflected in the Appendix to this letter.

SUMMARY

We are concerned about the less stringent requirements of this proposed exemption compared to the similar exemption provided by AR Section 600 for personal financial statements included in written personal financial plans.

We perceive a business valuation to be a higher risk document than a personal financial plan because we believe that most business valuations are used in conjunction with transactions that have a financial impact on third parties. For example, business valuations impact lenders, ESOP plan participants, shareholders who are buying in or selling out, and insurers (i.e., external users). Whereas, a personal financial plan exempted by AR Section 600 can, by definition, be used only to make decisions that will have a financial impact on the person who is the subject of the plan (i.e., internal use).

SPECIFIC CONSIDERATIONS

We recommend changes in two areas, as follows:

- AR 600 requires that there be an understanding that the financial statements will not be used to obtain credit or for any other purpose other than developing the client's goals and objectives (i.e., internal use only). Paragraph 4.a. of the Exposure Draft (ED) requires that there be an understanding that the financial statements will be used only for the business valuation, but does not state the allowable uses of the business valuation.

We recommend the ED exemption be at least as restrictive as the AR Section 600 exemption. The ED exemption should apply only to business valuations restricted for internal use and the understanding with the client should state directly the permissible uses of the business valuation. The indirect "don't ask, don't tell" approach taken in Paragraph 4.b. is inadequate.

If you feel that there are few instances in which an internal use only business valuation is useful to clients, then you may conclude this ED has such limited application that it should be withdrawn.

- AR 600 requires the accountant to issue a written report. The ED does not require a written report.

  We recommend that a written report be required and that it contain language similar to that contained in AR 600. In addition, we.recommend that the financial statements be required to include a legend stating that the financial statements are to be used only for the purpose of developing the business valuation and that the financial statements may be incomplete or contain departures from GAAP or an OCBOA.

Further, we recommend requiring written representations from the client that the financial statements will be used solely in developing and presenting the valuation of the entity and that they will be used only for the uses contained in the understanding with the client.

The Committee would be pleased to discuss our comments and recommendations with you at your convenience.

Sincerely,

Debra R. Hopkins, CPA
Chair, Audit and Assurance Services Committee
Illinois CPA Society

APPENDIX A

ILLINOIS CPA SOCIETY
AUDIT AND ASSURANCE SERVICES COMMITTEE
ORGANIZATIONAL AND OPERATING PROCEDURES
1999/2000

The Audit and Assurance Services Committee of the Illinois CPA Society (the Committee) is composed of nineteen technically qualified, experienced members appointed from industry, education and public accounting. These members have Committee service ranging from newly appointed to twenty years. The Committee is an appointed senior technical committee of the Society and has been delegated the authority to issue written positions representing the Society on matters regarding the setting of auditing standards.

The Committee usually operates by assigning a subcommittee of its members to study and discuss fully exposure documents proposing additions to or revisions of professional standards. The subcommittee ordinarily develops a proposed response which is considered, discussed and voted on by the full Committee. Support by the full Committee then results in the issuance of a formal response, which at times includes a minority viewpoint.

BV #19

FLORIDA INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

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May 31, 2000

Ms. Sherry Boothe
Audit and Attest Standards, File 2000
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

RE: Exposure Draft: Proposed Statement on Standards for Accounting and Review Services (SSARS 1), *Compilation and Review of Financial Statements*

Dear Ms. Boothe:

The Accounting Principles and Auditing Standards Committee of the Florida Institute of Certified Public Accountants (the "Committee") has reviewed and discussed the above referenced exposure draft ("ED"). The Committee has the following comments regarding this exposure draft.

The proposed ED codifies that financial statements included in business valuations fall under consulting services and the Committee recognized the need for the exemption of financial statements used in business valuations to be addressed in the ED.

The Committee believes that the proposed ED is appropriate as currently submitted.

As always, the Committee appreciates the opportunity to share our views and concerns and to comment on exposure drafts. Members of the Committee are available to discuss any questions you may have regarding this communication.

Very Truly Yours,

Joy Gibson

Joy Gibson, C.P.A.
Chairperson,
FICPA Committee on Accounting Principles and Auditing Standards

Committee member coordinating this response:
Lizette Lewis, C.P.A.

#20

June 9, 2000

Ms. Sherry Boothe
Audit and Attest Standards
File 2000
1211 Avenue of the Americas
New York, NY 10036-8775

Re: ED – Proposed Statement on Standards for Accounting and Review Services - Financial Statements Included in Written Business Valuations

Dear Ms. Boothe:

One of the objectives that the Council of the American Institute of Certified Public Accountants established for the PCPS Executive Committee is to act as an advocate for all local and regional firms and represent those firms' interests on professional issues, primarily through the Technical Issues Committee ("TIC"). This communication is in accordance with that objective.

TIC has reviewed the above referenced exposure draft ("ED") and is providing the following comments for your consideration.

General Comment

TIC supports providing an exemption from Statement on Standards for Accounting and Review Services 1 for historical financial statements and normalized financial statements that are included in written business valuations.

Specific Comments

TIC members note that the ED essentially mirrors the first part of AR 600.04, *Reporting on Personal Financial Statements Included in Written Personal Financial Plans*, which was issued in September 1986. However, AR 600.04 also requires that a written report accompany the personal financial statements stating that the personal financial statements:

- Are designed solely to help develop the financial plan
- May be incomplete or contain other departures from GAAP and should not be used to obtain credit or for any other purposes
- Have not been audited, reviewed or compiled

The ED does not require that a similar report accompany the historical financial statements and normalized financial statements that are included in written business valuations.

The members of TIC question why the exemption for historical financial statements and normalized financial statements included in written business valuations should differ from the exemption for personal financial statements included in written personal financial plans. TIC members believe that this difference may prove confusing to practitioners and may limit the usefulness of the exemptions. TIC believes that the exemptions should be consistent. Accordingly, the members of TIC believe that a report similar to that described in AR 600.04 should accompany the historical financial statements and normalized financial statements included in written business valuations.

*****

We appreciate the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

Candace Wright

Candace Wright, Chair
PCPS Technical Issues Committee

cc: PCPS Technical Issues Committee

21

Kansas Society of
Certified Public Accountants

400 CROIX / P.O. BOX 5654 / TOPEKA, KANSAS 66605-0654 / 913-267-6460 / FAX 913-267-9278

June 5, 2000

Sherry Boothe
Audit and Attest Standards, File 2000
American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Boothe:

The Kansas Society of Certified Public Accountants' Board of Directors has voted to adopt the position of its Business Valuation and Litigation Support Committee relative the Proposed Statement on Standards for Accounting and Review Services: *Financial Statements Included in Written Business Valuations.*

The Kansas Society Board is in agreement with the Exposure Draft and urges its adoption.

Sincerely,

T.C. Anderson
Executive Director

Deloitte & Touche LLP
Ten Westport Road
P.O. Box 820
Wilton, Connecticut 06897-0820

Tel: (203) 761 3000
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#22

Deloitte & Touche

June 21, 2000

Ms. Kim Gibson
Audit and Attest Standards
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Re: **File 2000**

Dear Ms. Gibson:

We are pleased to comment on the Proposed Statement on Standards for Accounting and Review Services (SSARS), *Financial Statements Included in Written Business Valuations*.

We support amending existing standards to clarify requirements regarding unaudited historical financial statements and normalized financial statements included in written business valuations. However, as set forth in the attachment to this letter, we believe exemption from SSARS 1 is not appropriate without providing guidance to be followed in its place. Simply providing an exemption from the requirements of SSARS 1 would create an environment in which both clients and users could easily misunderstand the accountant's association with the financial statements and the limitations of the services provided under such engagements. As a result, we believe that an exemption from SSARS 1 would not be in the public interest.

Further, we believe that accountants should be guided by the requirements of AT section 200, *Financial Forecasts and Projections*, when compiling normalized financial statements. Therefore, we recommend that the proposed exemption from SSARS 1 not be adopted. However, if the proposed statement moves forward, we recommend that specific guidelines be established concerning the performance of such engagements and the requirements for disclosure of an accountant's association with the financial statements, disclosure of the nature and effect of normalized adjustments, and other footnote disclosures.

Please contact Robert C. Steiner at (203) 761-3438 if you wish to discuss our comments.

Sincerely,

Deloitte & Touche L.L.P.

Attachment

Attachment

GENERAL COMMENTS

For the reasons discussed below, we do not support the Proposed Statement on Standards for Accounting and Review Services (SSARS), *Financial Statements Included in Written Business Valuations.*

The premise underlying the proposed standard appears to be that written business valuations are obtained primarily for internal use by management. We question the validity of such a premise. We believe it is unlikely that written business valuations are used *solely* by the management of the entity. Valuations are frequently obtained for valuing stock options or warrants, or for use in establishing stock values pursuant to buy/sell agreements among owners of closely held businesses. However, the accountant has no control over the use of the valuation report that he or she has prepared. Consequently, in the absence of a report restriction or legend on the financial statements restricting the use of the valuation, we believe that many entities will obtain valuations for use in connection with contemplated transactions with third parties, including lenders, investors, and potential buyers. Further, even if the business valuation was obtained for use solely within the entity, management may subsequently use it in circumstances not contemplated at the time the business valuation was prepared. Implementing a standard that exempts a practitioner from complying with SSARS 1 is, in our judgment, not in the public interest.

The proposed statement provides accountants with an option to compile historical financial statements and normalized financial statements for inclusion in written business valuations without following the requirements of SSARS 1. It is unclear, however, what standards, if any, would apply to such engagements. For example, the proposed statement fails to address the following questions:

- What standards would be followed in place of SSARS No. 1?
- What disclosures concerning the accountant's association with the historical or normalized financial statements would be included in a written business valuation?
- What disclosures would be required concerning the nature and effect of normalized adjustments (i.e., basis of presentation)?
- What other footnote disclosures would be required?

We believe that definitive guidance related to the compilation of historical or normalized financial statements for inclusion in written business valuations is needed. Allowing engagements an exemption from SSARS 1 in the manner proposed in the exposure draft without providing such guidance would likely lead to significant differences in practice in the performance of these engagements to the detriment of users of such information.

We believe that the framework provided under SSARS 1 is appropriate for such engagements for the following reasons:

- Compilation of financial statements, as defined in AR section 100.04, is "the presenting of information that is the representation of management (owners) in the form of financial statements without undertaking to express any assurance on the statements." We believe that the preparation of historical or normalized financial statements for purposes of inclusion in a written business valuation falls under that definition.

- We strongly believe that professional standards should require disclosure regarding the extent of the accountant's association with the historical or normalized financial statements included in a written business valuation. Under SSARS 1 (as it currently exists), an accountant is required to issue a report upon completion of a compilation, thereby disclosing his or her level of involvement to the readers. Providing such a report is an important element in assuring that the client and the users understand the accountant's role in these engagements and any limitations in the services provided by the accountant.

- We strongly believe that professional standards should provide guidance regarding the disclosure of the basis of presentation for the historical or normalized financial statements. SSARS 1 would require the basis of accounting to be disclosed in the notes to the financial statements; if not, the accountant is required to disclose it in the compilation report. In order for users of such information to be able to fully understand the financial statements, the basis of presentation, including an explanation of the normalizing adjustments, should be disclosed in the notes or, if not, the accountant's report should be appropriately modified.

- We believe the professional standards should also contain guidance regarding other footnote disclosures required for historical and normalized financial statements included in written business valuations. Under SSARS 1, the omission of substantially all disclosures under generally accepted accounting principles is required to be clearly indicated in the compilation report. Furthermore, when only selective matters are disclosed in the notes to the financial statements, such disclosures are required to be labeled "Selected Information – Substantially All Disclosures Required by Generally Accepted Accounting Principles Are Not Included." Again, in order for the client and the users to fully understand the financial statements presented, appropriate footnotes or disclosure of the lack thereof should be required.

We believe that SSARS 1 currently provides an appropriate framework for engagements relating to the compilation of historical financial statements for inclusion in written business valuations. In addition, we believe the preparation of normalized financial statements is analogous to the preparation of prospective financial statements; therefore, it would be inconsistent to have drastically different standards for the two types of engagements. Under AT section 200, when prospective financial statements are reasonably expected to be used by third parties, accountants who have assisted in assembling such information are required to either compile, examine, or apply agreed-upon procedures to the prospective financial statements. Normalized financial statements, by definition, are for the purpose of developing the valuation of an entity; such valuations, we believe, can reasonably be expected to be used by third parties. Therefore, providing an exemption under SSARS 1 for the preparation of normalized financial statements to be included in written business valuations is not consistent with the likely use. Additionally, the guidelines under AT section 200 contain minimum disclosure requirements, including required disclosure of significant assumptions. Therefore, to maintain consistency in the professional standards, we believe accountants should look to the compilation requirements and minimum disclosure requirements under SSARS 1 and AT section 200 when preparing historical and normalized financial statements, respectively, for inclusion in written business valuations.

However, if the proposed standard moves forward, we recommend that specific guidelines be established concerning the performance of such engagements and the requirements for disclosure of an accountant's association with the financial statements, disclosure of the nature and effect of normalized adjustments, and other footnote disclosures.

COMMENT LETTER #23

Thank you for taking the time to contribute to this much-needed SSARS. I think it's going to be of great benefit. I apologize for not getting my comments (given below) to you by Friday, but I hope you will still consider them.

Due to time constraints I have not researched the last couple of comments to the level I wanted to, so you may find that there is additional literature that I have not reviewed yet that already addresses them.

Please feel free to contact me if you wish to discuss any of my comments or elicit additional research from our firm.

Sincerely,

Jeff Freeman, CPA/ABV, CFE
Partner, Litigation and Valuation Services

Carpenter, Kuhen & Sprayberry
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SSARS Proposal Comments

Paragraph 2:
The definition for normalized financial statements may be too limiting. I suggest using a simpler definition of normalized financial statements which would allow for more types of normalization adjustments to be considered. For example, reasons for normalizing financial statements other than improving comparability to other companies and control adjustments include:

- adjustments for non-recurring items to improve historical comparability
- adjustments for non-operating items
- pro-forma adjustments (such as the valuation of an entity "but for" the recurring effect of a past event)
- adjustments to exclude an operating line or segment of the business

Alternative wording of the definition for normalized financial statements, paragraph 2 of the proposed SSARS, could be as follows:

"Normalized financial statements are financial statements that contain necessary and appropriate adjustments that the appraiser believes are appropriate in order to make an entity's financial information more meaningful when presenting and comparing on a consistent basis the financial results of that entity to those of a comparable entity as part of a to a business valuation engagement."

Paragraph 4:
I also suggest modifying paragraph 4 of the proposed SSARS to address:

1) Whether the wording "preferably in writing" should be excluded. I believe it should either be excluded, or that language should be added that the full disclosure of 4.a.(1) and 4.a.(2) within the written valuation report represents sufficient communication to the client and potential users of the report.

2) Paragraph 4.b. allows for the SSARS 1 exemption only if "Nothing comes to the accountant's attention during the engagement that would cause the accountant to believe that the financial statements included in the written business valuation will be used to obtain credit..."Since it is not uncommon for a value conclusion to be used in connection with obtaining financing, either through presentation of the valuation report to a potential lender or by inclusion in a personal financial statement, the existing language could be problematic. Is this statement implying that SSARS 1 would apply in cases where some level of reliance would be placed on a valuation by a lending institution? It seems that the purpose of this statement was to avoid the financial statements being either: 1) removed from the business valuation report and used to obtain credit, or 2) presented within a valuation report to obtain credit, where the valuation report was prepared for a purpose other than obtaining credit.

Other concerns:

What is the definition of "financial statements"?Are proforma financial statements, forecasts and projections implicitly included as exemptable items under this SSARS, or are these addressed via another statement? Does AR Section 200, regarding the required references to predecessor's compilation or review reports, apply when including historical financial statements prepared by another CPA? And if so, should this be exempted under the proposed SSARS as well? How is a "written business valuation" defined? For example, under the Business Valuation Standards promulgated by the American Society of Appraisers and the Uniform Standards of Professional Appraisal Practice there are several types of services that can be provided, including: calculations, limited appraisals, complete appraisals and review appraisals. Should the definition of a written business valuation be explained as inclusive of all types of related engagements?

#24

California Society
Certified Public Accountants

June 15, 2000

Ms. Sherry Boothe
Audit and Attestation Standards, File 2000
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Reference: Proposed Statement on Standards for Accounting and Review Services

Dear Ms. Boothe:

The Accounting Principles and Auditing Standards Committee of the California Society of Certified Public Accountants (the Committee) has discussed the above-referenced exposure draft.

The Committee is the senior technical committee of our state society. The Committee is composed of 40 members, of whom 12% are from national CPA firms, 54% are from local or regional firms, 23% are sole practitioner in public practice, 8% are in industry, and 3% are in academia.

The Committee supports the issuing of the proposed Statement of Position as drafted.

Thank you for the opportunity to comment on the proposed Statement of Position.

Sincerely,

John M. Lacey, Chair
Accounting Principles and Auditing Standards Committee

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