CHAPTER 1

REVIEW QUESTIONS
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Chapter 1: Introduction to Business Valuation

1. Primary opportunities for the valuation analyst can be found in working with:
   a. Business owners, investors, attorneys, and individuals performing valuations for a variety of reasons, including estate planning and taxation, litigation support, mergers and acquisitions, and financial statement reporting
   b. Business owners as only the owner of a business can engage a valuation analyst for a valuation engagement of a business
   c. Other CPA firms as every privately held company is required to estimate the value of its intangible assets for financial statement reporting purposes
   d. Business owners in order to estimate the value of a group of assets as allocated on Form 8594

2. What is the basic difference between an appraisal and a valuation?
   a. The act or process of determining the value of a business, business ownership interest, security, or intangible asset is an appraisal whereas a valuation is the process of determining the value of gems, equipment, furnishings, and other tangible assets to be used in determining the value of a business
   b. Nothing; they are the same thing
   c. Appraisal is usually for a tangible asset and a valuation is usually for stock or interest in stock of a company or other intangible asset
   d. Valuation is usually for stock or bond or other public security and an appraisal is usually for a non-public asset, stock or bond

3. Risk management in the valuation niche demands solid training and staying current through continuing education.
   a. True
   b. False

4. A buy/sell agreement:
   a. Avoids litigation
   b. Notes that an independent valuation is to be performed, when, and why
   c. Identifies when or what events trigger a buyout, identifies how any buyout will be funded and identifies the timing of any buyout
   d. Always identifies the interest rate, if any, applicable

5. The most commonly quoted regulatory and professional bodies for business valuation are:
   a. NACVA, AICPA
   b. IRS, DOL, FASB
   c. ASA, IBA
   d. IACVA, ABV
6. Three theoretical standards of value are:
   a. Investment value, going concern value, and fair market value
   b. Fair market value, investment value, and fair value
   c. Going concern value, asset value, and fair value
   d. Book value, fair market value, and liquidation value

7. Fair Market Value is based upon:
   a. In business valuation, a legally created standard of value that applies to specific statutory transactions
   b. The market value, the standard of value applicable in cases of dissenting stockholders’ valuation rights. Fair market value, with respect to a dissenter’s shares, means the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable
   c. The value described by an arms length transaction between a knowledgeable willing buyer and a knowledgeable willing seller
   d. The value described by an arms length transaction involving a willing buyer or a willing seller—and depends upon the reason you have been retained to perform a business valuation

8. A valuation analyst must match the appropriate standard of value to the purpose for which the valuation engagement is performed.
   a. If the context in which the valuation is to be used is not critical and no lawsuit is in process, then the valuation analyst will always select fair value.
   b. A valuation for buying a business will be the same as for selling that business. It is the nature of the business that defines the standard of value.
   c. A valuation for securing a new loan should be done the same as a valuation in a divorce.
   d. The valuation is to be used only for the purpose for which it was done and will likely be inappropriate for another use even by the same company or client.

9. A valuator relies on quantifiable objective data in performing a valuation, attempting to remove as much subjectivity as possible. An advocate:
   a. Does essentially the same thing for a specific client
   b. Introduces subjective factors and attempts to rely more heavily on qualitative factors
   c. Is a valuator who works only for attorneys
   d. Is an attorney who works for a valuation firm to edit valuation reports to prevent ambiguous terms and advocate the use of proper legal terms so the firm won’t be sued

10. What are the three main reasons for tax related valuations?
    a. Estate tax, gift tax, and allocation of purchase price
    b. Estate tax, buy/sell agreements, and litigation
    c. ASC 805 (formerly FASB 141), ASC 350 (formerly FASB 142), and estate tax
    d. ASC 350 (formerly FASB 142), litigation, and gift tax

11. The American Medical Association refers to going concern value as an “in-place value.”
    a. True
    b. False
12. The major point(s) of Internal Revenue Code §2703 is/are:

a. For estate, gift and other tax purposes, the value of any property is determined without regard to any right or restriction relating to the property
b. An exception to restrictions on property exists for any option, agreement, right, or restriction, which (1) is a bona fide business arrangement, (2) is not a device to transfer property for less than its fair market value, (3) is comparable to similar arm’s length arrangements; and (4) these safe harbors must be independently satisfied. The mere showing that a right or restriction to property is a bona fide business arrangement is not sufficient to establish the absence of a device
c. Each right or restriction must be tested separately. A right or restriction is considered to meet the three ‘safe harbor’ requirements if more than 50% of the applicable property is owned by individuals who are not members of the transferor’s family. Property owned by non-family members must be subject to the same rights or restrictions
d. Both a and b, but not c
e. a, b, and c

13. The Internal Revenue Service first introduced the concept of goodwill and excess earnings when they issued:

a. ARM 34
b. Revenue Ruling 59-60
c. Revenue Ruling 68-609
d. APB Opinion 16

14. Which of the following factors should be considered when valuing a closely held business under Revenue Ruling 59-60?

   i. Nature and history of the business
   ii. Economic outlook and industry condition
   iii. Methods to calculate preferred stock
   iv. The earnings capacity of the company

a. i, ii, and iv
b. ii, iii, and iv
c. i, ii, and iii
d. All of the above

15. If a valuator is retained to value a company for estate tax purposes, it is acceptable for the valuator to value the business as a/an:

a. Advocate
b. Independent expert
c. Related party
d. Employee of the company
16. IRC Section 401(a)(28)(C) requires the use of an “independent appraiser” for ESOP valuations to be independent the following conditions must be met:

   a. The valuator is qualified, performs appraisals on a regular basis, and is not a related party
   b. The valuator is qualified, may be a related party, and performs appraisals on a regular basis
   c. The valuator is qualified, does not perform appraisals on a regular basis, and is not a related party
   d. The valuator does not need to be qualified, but must perform appraisals regularly and is not a related party

17. Under Sarbanes-Oxley, an independent auditor is explicitly forbidden to provide “appraisal valuation services, fairness opinions or contribution-in-kind reports” for any of its audit clients.

   a. True
   b. False

18. Before the valuation analyst can proceed in valuing a business, the first step an analyst must determine is:

   a. The purpose of the valuation
   b. The best method to apply
   c. The standard of value
   d. The appropriate marketability discount

19. Which of the following cases provides guidance as to the admissibility of expert testimony in appraising a business:

   a. Daubert v. Merrill Dow
   b. Estate of Walter Gross v. Commissioner
   c. Estate of Davis v. Commissioner
   d. Estate of Roark v. Commissioner

20. The United States Department of Labor issues regulations specifically pertaining to business valuations for:

   a. Employee Stock Ownership Plans
   b. Gift and estate tax returns
   c. Merger and acquisitions
   d. Partner disputes

21. Value equals the benefit stream divided by a required rate of return is an example of what principle:

   a. Alternative principle
   b. Principle of substitution
   c. Investment value principal
22. A fundamental relationship exists between rate of return from an investment and the amount of risk in the investment. Therefore:

   a. An investor would expect a higher rate of return from a treasury note compared to large company stock
   b. An investor would expect a higher rate of return from a six month CD compared to a 5-year treasury bond
   c. An investor would expect a higher rate of return from a publicly traded company compared to a privately held company
   d. An investor would expect a higher rate of return from a publicly traded stock compared to a 5-year treasury bond

23. Strategic/Investment value is defined as:

   a. The amount at which property would change hands between a hypothetical willing buyer and a willing seller
   b. An amount determined under statutory standard of value
   c. The value to a particular investor based on individual investment requirements and expectations
   d. The value as if the business is going to continue operating as it presently is operating

24. Revenue Ruling 93-12 was a significant benefit to taxpayers as it allowed that:

   a. Valuation of a minority (i.e., non-controlling) interest in an entity will not have to consider either the transferor or the transferee as they relate to control of the entity
   b. Valuation of an ownership interest in a business for gift tax purposes would always allow rates of return on tangible assets between 8% and 10%
   c. Contributions of non-cash property for federal income tax purposes shall always be valued based on the historical cost of the property
   d. Adopted the “family attribution” rule, which states that no minority interest discount is available for blocks of stock transferred to family members when the family holds a controlling interest in the entity