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APPRAISAL REVIEW REPORT

CONCERNING
BUSINESS APPRAISAL REPORT PREPARED BY
PABLO & ASSOCIATES, P.A.
CERTIFIED PUBLIC ACCOUNTANTS
JOHN PAUL, CPA

AS OF AUGUST 29, 20XX

OF

THE FAIR MARKET VALUE OF A
10% NON-CONTROLLING, NON-MARKETABLE
COMMON EQUITY INTEREST IN

WASHINGTON PRINT ENTERPRISES, INC.

PREPARED BY:

Appraiser One, CBA, ASA, CMEA, ABAR
AMERICAN BUSINESS APPRAISERS, LLC

REVIEW DATE - APRIL 30, 20XX

**APPRAISAL REVIEW REPORT OF
WASHINGTON PRINT ENTERPRISES, INC.
REVIEW DATE - APRIL 30, 20XX**

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1. INTRODUCTION

John Paul, CPA or Pablo & Associates, PA was retained by Margarita Gonzalez, the Executrix of the Estate of her husband, Julio Agosto Gonzalez, to estimate the fair market value of a 10% minority, non-marketable, common equity interest in Washington Print Enterprises, Inc.¹ It was Mr. Paul's understanding that the opinion of value would be used to closed the estate of Julio Agosto Gonzalez.² The opinion was rendered on February 4, 20XX, and was made as of August 29, 20XX.

Washington Print Enterprises, Inc. ("the Subject") is a commercial printer and lithographer incorporated in the State of Arizona, as a Sub Chapter S corporation and had three shareholders as of the valuation date. Washington Print Enterprises has 11,700 shares of common stock issued and outstanding, of which 1,170 shares representing 10% were owned by the decedent at the date of his death.

The appraisal report prepared by John Paul of Pablo & Associates is included as Appendix A to this Business Appraisal Review.

2. REVIEWER'S OPINION OFFERED

I was retained by Attorney John Smith of ABC Law Firm, acting in his role as representative for Margarita Gonzalez, to review the accompanying Appraisal Report (see Appendix A) prepared by John Paul of Pablo & Associates, as of the August 29, 20XX.

This Business Appraisal Review was conducted for the purpose of determining that the approaches and methodologies utilized by John Paul of Pablo & Associates were relevant to the objectives and purpose, as stated in the Appraisal Report prepared by the Appraiser and applied on a reliable basis consistent with generally accepted appraisal practices in the United States of America as of August 29, 20XX. A Business Appraisal Review does not entail the performance of an appraisal of a subject interest. Therefore, this Business Appraisal Review should not be construed to be an opinion of value.

In my opinion, subject to the assumptions and limiting conditions discussed in the Business Appraisal Review Report, the opinion presented by John Paul of Pablo & Associates is not credible and is not in conformity with generally accepted appraisal practices normally relied upon by business appraisers in the United States of America, as promulgated by the *Business Appraisal Standards* of the Institute of Business Appraisers and the *Uniform Standards of Professional Appraisal Practice* (USPAP).

Appraiser One, CBA, ASA, CMEA, ABAR
American Business Appraisers, LLC
April 30, 20XX

¹ Source: Valuation report to Margarita Gonzalez

² Ibid

3. OBJECTIVES AND SCOPE OF APPRAISAL REVIEW

3.1 Adequacy of the Statement of Purpose

The Appraisal and transmittal letter both define the purpose of the work to: “Determine the fair market value of a 10% minority, non-marketable, non-voting common equity interest in Washington Print Enterprises, Inc., as of August 29, 20XX.” The use of the finding was to be for closing of the estate of Julio Agosto Gonzalez.

In my opinion, the statement of purpose is adequate for the assignment.

3.2 Appropriateness of the Definition of Value

The Appraisal uses the definition of fair market value as defined in the *International Glossary of Business Valuation*. In my opinion, the definition used is appropriate for the stated purpose and use of the Appraisal.

3.3 Acceptability of the Appraisal Methods Utilized

The Appraisal depends on two methods in reaching the opinion of value: the asset approach, based on an adjusted asset method; and the income approach, based on a discounted future earnings method.

- The income approach, the appraiser used is acceptable when properly applied.
- The asset-based approach is more problematic as it is a very difficult approach to accurately apply to a business the size and complexity of Washington Print Enterprises.

3.4 Reliability of the Selected Methodologies

The Appraisal depends on two methods in reaching the final opinion of value for the 10% minority equity interest in Washington Print Enterprises.

As noted above, the asset-based approach used is very difficult to use for a business the size and scale of Washington Print Enterprises. The effort to analyze and adjust the value of the assets of such a large and complex business is beyond the scope of most appraisal assignments. Thus without a very large and extensive budget and a great deal of experience, the asset-based approach is likely to be unreliable in determining the value of Washington Print Enterprises.

The income approach used by the appraiser provided basic analysis and understanding of Washington Print Enterprises’ financial condition and when this approach is correctly applied can often be a reliable methodology. However, in this case, the methodology as applied is unreliable.

3.5 Comprehensiveness of the Financial Analysis

The financial analysis completed in the Appraisal is inadequate. The appraiser fails to provide the reader with critical information on Washington Print Enterprises, its historic performance and its likely future performance. The reader is unable to understand the basic components of value as a result of this lack of analysis.

3.6 Assessment of the Company Performance Presented versus Industry Peers

The Appraisal has a weak and incomplete assessment of Washington Print Enterprises' performance versus its industry peers and is not probative enough for the appraiser or the reader to make reliable conclusions as to how Washington Print Enterprises compares to its industry peers. The comparisons, as stated, are contradictory and lead the reader to believe Washington Print Enterprises is above the industry averages, when in fact their performance suggests an increase in business risk.

3.7 Relevance and Credibility of Value Conclusion

In my opinion, the findings in the Appraisal lack relevance and credibility. As discussed in the following section, there are multiple flaws in the Appraisal prepared by John Paul of Pablo & Associates.

3.8 Conformance with Appraisal Standards

John Paul states he followed the Institute of Business Appraisers' Business Appraisal Standards which the reviewer deemed are appropriate for the assignment. However, Mr. Paul departs from the relevant professional standards undermine the credibility of his opinion of value.

4. BASIS AND REASONS FOR OPINION OFFERED

There are numerous errors and omissions contained within the Appraisal which support the reasoning for the opinion provided in this review. Below is a list of some of the more egregious errors and problems which have been made.

4.1 Appropriateness of Normalizing Adjustments

Section 3.3 of the Appraisal Report briefly discusses Mr. Paul's adjustments to the financial statements. These adjustments later become a critical component in the Appraiser's application of the Adjusted Net Asset Value Method. The Appraiser adjusts the carrying balance of "large production equipment"³ to an appraisal conducted by a third-party equipment appraisal company. However, the Appraiser fails to otherwise provide an adequate discussion of his analysis and thought process in reaching his conclusion about the adjusted carrying value of assets. The following are examples:

³ Ibid., Section 3.3.2 at p. 14.

- a. Leasehold improvements were adjusted to “50% of their book value due to the fact that no long-term lease existed between the Company and the landlord.”⁴ There is no analysis supporting the Appraiser’s thought process and conclusion, leaving a reader to believe that the Appraiser made a “leap of faith” in reaching his conclusion.
- b. Furthermore, while certain assets (large production equipment, leasehold improvements, and autos) were adjusted, there is no overall reconciliation of book value-to-adjusted-book-value of all property and equipment. As a result, a reader of the Report does not have a clear understanding of how the overall adjusted carrying amount of property and equipment was derived.
- c. The Appraiser provides no discussion or analysis of the carrying value of other non-current assets, buildings, or the existence and value of work-in-process.
- d. The Appraiser failed to investigate the existence and value of intangible assets.

4.2 Failure to Properly Apply the Income Approach to Value

Many facets of the income approach were developed and applied in a manner not consistent with current business appraisal methodology. The application of an after-tax rate of return (discount rate) to a pre-tax earnings stream significantly produces an over valuation of Washington Print Enterprises.

- a. The development of the earnings stream used weights for each year and provided no support as to why one year was given more weight over another year. The major critical issue is the unsupported decrease in pre-tax cash flows for working capital and capital expenditures. In the Reviewer’s opinion, the development of the pre-tax earnings stream is not supported by the information provided in the Appraisal report.
- b. The development of the rate of return (discount rate) from information obtained in a publication by Ibbotson Associates, *Stocks, Bonds, Bills and Inflation: Valuation Edition 20XX Yearbook* is generally applied in its unadjusted form to a net cash flow earnings stream, which is an after-tax earnings stream rate of return. In the case of Washington Print Enterprise, the application of the net cash flow rate of return as applied to the developed pre-tax earnings stream produced an inflated indication of value.

4.3 Errors in the Reconciliation of Indicated Values

The Appraiser’s reconciliation of indicated values considered values derived from the Asset and Income Approaches. Notwithstanding the Appraiser’s reconciliation contains two material errors that render the opinion of value neither reliable nor relevant:

- a. The Appraiser failed to carryover to Exhibit 6F the correct “Value Indicated by Method” for both the Adjusted Net Asset Value and Discounted Cash Flow Methods. The Appraiser originally computed an indicated value under the Adjusted Net Asset Value Method of \$3,409,000, but recorded \$1,991,000 on the reconciliation. The Appraiser originally

⁴ Appraisal Report, Section 3.3.2 at p. 14.

computed an indicated value under the Discounted Cash Flow Method of \$3,560,000, but recorded \$2,599,000 on the reconciliation.

- b. The Appraiser applied an ownership percentage of 11.54% for the subject interest in completing the reconciliation. The correct ownership percentage is 10%.

4.4 Lack of care in producing report

Throughout the appraisal report and in the transmittal letter, there are careless clerical and typographical errors. Most of these are relatively minor; however, some are major and destroy the credibility and reliability of the Appraisal.

For example, Section 3.3 of the valuation report discusses adjustments to the financial statements. These adjustments later become a critical component in John Paul's application of the adjusted net asset method. Mr. Paul adjusted for leasehold improvements under the fixed asset category by 50% (or \$703,000) of the book value with no analysis or support other than to state this is due to no long-term lease agreement.

Arbitrarily adjusting the income statement and balance sheet without providing detailed support leaves the impression that the Appraiser may be misleading the reader and/or his lack of understanding of Washington Print Enterprise.

5. STATEMENT OF RELEVANT ASSUMPTIONS AND LIMITING CONDITIONS

My opinion is subject to the following assumptions and limiting conditions:

1. Information, estimates, and opinions contained in this appraisal review report were obtained from sources represented to be reliable. However, I assume no liability for the accuracy of such information.
2. Possession of this report, or a copy thereof, does not carry with it the right of publication of all or part of it, nor may it be used for any purpose other than that previously described without the previous written consent of American Business Appraisers, LLC, and then only with proper attribution.
3. This appraisal review engagement is limited to the production of this report, and the conclusions and opinions contained herein. The Reviewer has no obligation to provide future appraisal review services. The Reviewer is not required to give testimony in court, or to attend any hearings or depositions.
4. This appraisal review report may be used only by Margarita Gonzalez as Executrix of the Estate of Julio Agosto Gonzalez, and the Estate's financial, legal, and tax advisors, and is valid only for the specified purpose set forth therein.
5. The Reviewer has assumed that there is full compliance with all applicable federal, state, and local regulations and laws unless otherwise specified in this report.
6. This report was prepared under the sole direction of Reviewer. Neither the professional who worked on this engagement nor any employees of Reviewer, have any present or contemplated future interest in the Estate or the Appraiser, or any personal interest with respect to the parties involved, or any other interest that might prevent Reviewer from performing an unbiased business appraisal review.
7. The Reviewer's compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in, or the use of, this report.

8. We are neither tax nor legal advisors to Margarita Gonzalez, Executrix, or the Estate of Julio Agosto Gonzalez. Our assignment and this report are not intended to, and do not constitute advisory services concerning the preparation and filing of one or more estate tax returns, or any other financial, legal or tax matters related thereto. Margarita Gonzalez, Executrix, and the Estate of Julio Agosto Gonzalez must rely solely upon the advice and counsel of their tax and legal advisors related to these matters.
9. No federal tax information or analysis contained in this document is intended to be used, nor can it be used, for the purpose of avoiding federal tax or penalties under the Internal Revenue Code or promoting, marketing, or recommending any transaction or matter addressed in this communication.
10. All documents provided to the Reviewer are known to be originals or true copies of the originals.
11. The Appraiser's Report dated February 4, 20XX was relied upon by Reviewer to represent Appraiser's opinion of value of Fair Market Value of the Estate's minority, non-marketable, common equity interest in Washington Print Enterprises, Inc., and it is incorporated herein as an integral part of this business appraisal review report.

6. SOURCES OF INFORMATION RELIED UPON BY REVIEWER

The sources of information relied upon by this reviewer included:

- The Appraisal Report, including the transmittal letter.
- Institute of Business Appraisers - *Business Appraisal Standards*.
- Internal Revenue Service Revenue Ruling 59-60.

7. REVIEWER'S CERTIFICATION

I certify that, to the best of my knowledge and belief:

- The facts and data reported by the reviewer and used in the review process are true and correct.
- The analyses, opinions and conclusions in the review report are limited only by the assumption and limiting conditions stated in this review report and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.
- I have no present or prospective interest in the property that is the subject of the work under review and no personal interest with respect to the parties involved.
- I have no bias with respect to the property that is the subject of the work under review or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation is not contingent on an action or event resulting from the analyses, opinions or conclusions in this review or from its use.

- My analyses, opinions, and conclusions were developed and this review report was prepared in conformity with the Institute of Business Appraisers' *Business Appraisal Standards* and The Appraisal Foundation's *Uniform Standards of Professional Appraisal Practice*.
- I have not made a personal inspection of the subject property of the work under review.
- No one provided significant appraisal, appraisal review, or appraisal consulting assistance to the person signing this certification.

Appraiser One, CBA, ASA, CMEA, ABAR
American Business Appraisers, LLC

SAMPLE

8. Appendix A

APPRAISAL REPORT OF WASHINGTON PRINT ENTERPRISES, INC.

**NOTE – FOR PURPOSES OF THIS SAMPLE REPORT, THE
REVIEWER HAS INTENTIONALLY NOT
REPRODUCED A COPY OF THE APPRAISAL REPORT.**

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9. Appendix B - Reviewer's Curriculum Vitae

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