The
Valuation Vantage

The McLean Group
Investment Bankers to the Middle Market

INSIGHTS & PERSPECTIVES ON LEADING CORPORATE FINANCE VALUATION ISSUES

Summer 2007

INSIDE THIS ISSUE:

The McLean Group's Valuation Practice

As a core competency and complement to its merger & acquisition practice, The McLean Group provides business valuation services, including intangible asset and financial security valuations for a variety of transaction, financial reporting, and tax purposes.

FINANCIAL VALUATION ISSUES AND IPOs

Valuation practitioners need to be aware of several significant valuation issues prior to a company going public

[An excerpt from the original article published in ***Disclosures****, the magazine of the Virginia Society of Certified Public Accountants, January/February 2007, by Andy Smith, CPA/ABV, ASA, CVA, CMA and John Jacob, AVA]*

The number of initial public offerings (IPOs) in the United States has increased by a compounded annual growth rate (CAGR) of approximately 11 percent since 2003. This growth compares to the five-year low in 2003 for the U.S. IPO market when 178 companies went public versus the approximately 300 that took place in 2006.

Continued on page 2

AICPA ISSUES SSVS NO. 1 – VALUATION OF A BUSINESS, BUSINESS OWNERSHIP INTEREST, SECURITY, OR INTANGIBLE ASSET

In June 2007, the American Institute of Certified Public Accountants ("AICPA") released Statement in Standards for Valuation Services No. 1 ("SSVS No. 1" or the "Statement"). After over six years of discussion and debate, the long awaited standard provides formal guidance to AICPA members with best practices in providing business valuation services. The statement is effective for all engagements that begin after January 1, 2008. SSVS No. 1 does not apply to the estimation of economic damages. The Standard specifies the requirements necessary for engagements that involve a Conclusion of Value opinion or a Calculated Value opinion.

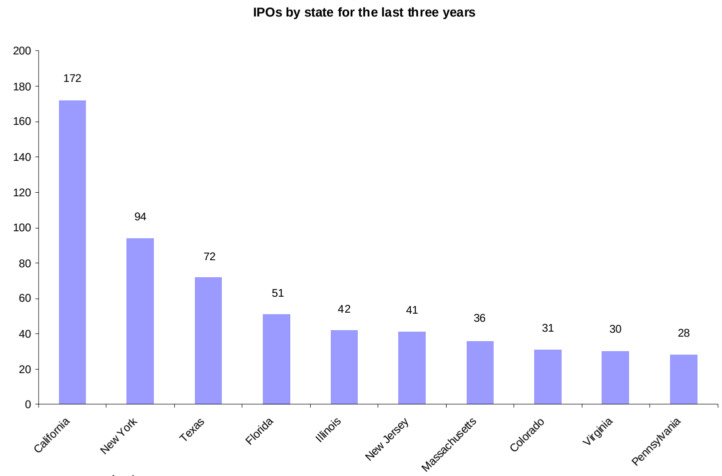
THE MCLEAN GROUP COMPLETES ITS ANNUAL ACCOUNTING ANALYSIS OF PURCHASE PRICE ALLOCATIONS FOR GOVERNMENT CONTRACTING M&A TRANSACTIONS

The firm's study surveys the accounting disclosure of 111 acquisitions of government contractors. Specific details regarding the types of intangible assets that are valued as well as benchmarks for the percentage of the purchase price that are recognized as goodwill versus identified intangible assets. Amortization periods are also summarized. For a copy of the white paper, please e-mail Andy Smith at asmith@mcleanllc.com.

FINANCIAL VALUATION ISSUES AND IPOs (continued)

IPOs in Virginia

Between the high-tech center in Northern Virginia, the growing government contracting market from Norfolk to D.C., and the state's active manufacturing base, Virginia has more than 400 public companies. From November 2003 to November 2006, approximately 30 IPOs took place in Virginia. The Northern Virginia area is first in the state with approximately 20 IPOs, followed by the Richmond area with approximately five IPOs and two IPOs each in the Charlottesville and Roanoke areas. This represented approximately 3 percent of the overall U.S. IPO market. In terms of the number of IPOs by state, Virginia ranks ninth nationally.



Source: Capital IQ

The financials sector has the largest number of IPOs in Virginia in the last three years, with approximately 13.

Cheap stock

One of the fears in an S-1 filing is that the company may have granted stock (or other equity securities such as options, warrants, or restricted shares) at a value that is significantly below fair value. This is commonly referred to as cheap stock. The SEC will typically look back 18 to 24 months to determine if the company's prior equity awards may require adjustment.

Purchase price allocations

Under Statement of Financial Accounting Standards (SFAS) 141 (which is planned to be revised in the fall of 2007, stay tuned), acquisitions are accounted for under the purchase method of accounting. In general, when a business is purchased, the acquired current assets, fixed assets and identifiable intangible assets are recorded at fair value and the remaining difference is allocated to goodwill. The goodwill is not amortized.

The first step in a purchase price allocation is to determine the purchase price, which can be easy if it is a 100 percent cash acquisition. But if non-cash consideration or contingent consideration is involved, it can be much more difficult. Next, intangible assets are recognized as separate, stand-alone assets when they can be separately identified and if they arise from contractual or other legal rights; or if non-contractual, only if they are capable of being transferred, licensed, rented or exchanged. An assembled workforce is not separately recognized, but it is typically analyzed and valued as part of other calculations.

SPOTLIGHT ON COURT CASES

Kohler v. Commissioner (July 25, 2006)

In Kohler v. Commissioner, three issues of interest were discussed. The Court found that the valuation reports written by the IRS experts did not include documentation regarding USPAP standards which are generally accepted in valuation reports. In addition, the Court found that the IRS expert did not have the credentials of a valuation association. The taxpayer's experts, in contrast, did have the necessary valuation credentials and experience and included appropriate USPAP standards in their reports. With regards to the use of projections, the Court ruled that the IRS expert formulated his own assumptions about forecasts and failed to use the forecasts of Kohler's management.

Gesoff v. IIC Industries (May 18, 2006)

The importance of fairness opinions was made clear in the case of Gesoff v. IIC Industries. Minority shareholders of IIC Industries were given a price that was not fair by CP Holdings, the 80% owner of IIC Industries, according to the Court. The Court came to this conclusion based on a series of actions by CP Holdings and related parties. Due to the events of September 11, 2001, the $10.50 tender offer was unsuccessful. The tender offer was made before this date and was based on a fairness opinion by Jesup & Lamont, an investment banking firm. CP Holdings concluded that the price was more than fair due to the general downturn in U.S. public equity markets as a result of the September 11th events. However, the Court noted that the operating subsidiaries of IIC Industries were outside of the U.S. In addition, the Court made the following conclusions:

- The special committee assigned to give a recommendation for the transaction should have had more than one member.
- The special committee should have been given a clearer mandate and the power to reject a transaction.
- The special committee should have been given access to independent legal counsel and independent financial advisors.

SELECTED TRANSACTIONS:

ARROWHEAD Global Solutions, Inc.
has been acquired by
CapRock COMMUNICATIONS
Federal IT and Communications Solutions Provider
As M & A Advisors — The McLean Group

Abraxas
has acquired
Dauntless
IT Government Contracting
As M & A Advisors — The McLean Group

cybertrust
has been acquired by
verizon business
Fairness Opinion
Managed Security Services
As Business Valuators & Financial Advisors — The McLean Group

CONTACT US:

Andy Smith
Managing Director,
Valuation Services
asmith@mcleanllc.com

Dennis Roberts
Chairman
droberts@mcleanllc.com

TMG OFFICES:

- Washington, DC (headquarters)
- Atlanta, GA
- Austin, TX
- Baton Rouge, LA
- Boston, MA
- Bozeman, MT
- Cheyenne, WY
- Chicago, IL
- Cleveland, OH
- Las Vegas, NV
- Miami, FL
- Reno, NV
- Sacramento, CA
- San Diego, CA
- San Francisco, CA
- St. Louis, MO
- Wooster, OH

The McLean Group

1660 International Drive
Suite 450
McLean, VA 22102

(703) 827-0200 *Phone*
(703) 827-0175 *Fax*
www.mcleanllc.com

The McLean Group
Investment Bankers to the Middle Market