

Statutory *Fair Value*?

The Orange County Bar Business Law Section

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“I conceive that great part of the miseries of mankind are brought upon them by false estimates they have made of the value of things.”

- Benjamin Franklin

Valuation Assignment

- What is being valued (Subject Interest)
- Effective date of valuation (Valuation Date)
- Premise of value (going concern, liquidation)
- Level of value (control, minority, marketable)
- Intended use(s) of the valuation
- Intended user(s) of valuation
- **Standard of Value**

Standards (Definitions) of Value

- Fair market value



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Standards (Definitions) of Value

- Investment/strategic/synergistic value

\$ + \$

=



Standards (Definitions) of Value

- Intrinsic value



Standards (Definitions) of Value

- Liquidation value



Standards (Definitions) of Value

- Fair value
 - Accounting fair value

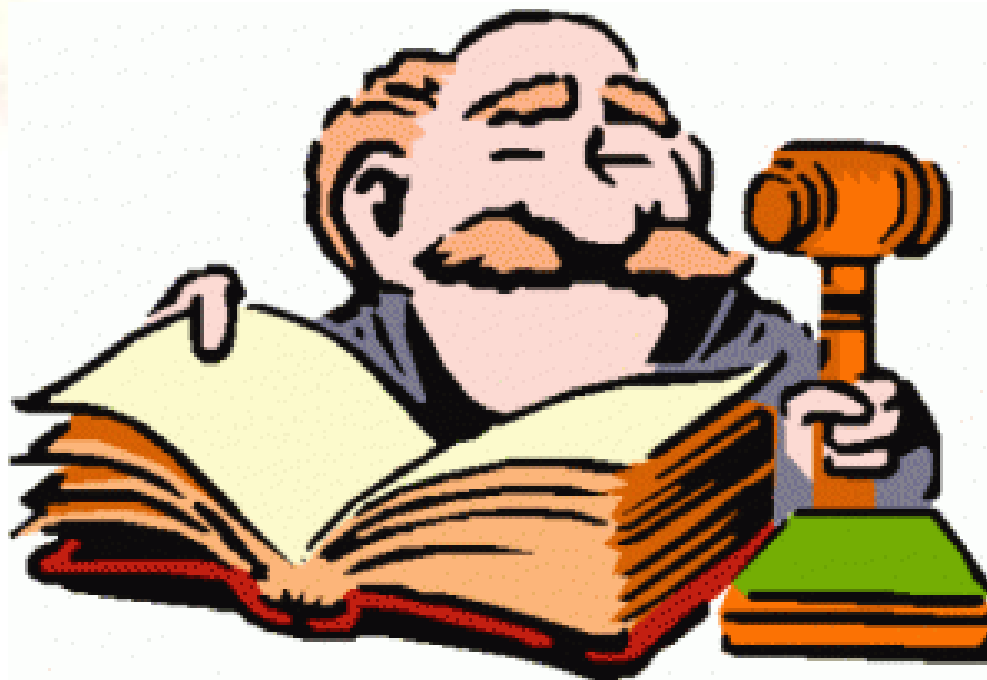
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£	-	£	-
£	-	£	-
£	-	£	-
£	1,229.28	£	1,229.28
£	1,531.06	£	2,760.34
£	1,425.36	£	4,185.70
£	1,276.66	£	5,462.36
£	1,139.12	£	6,601.48
£	1,289.34	£	7,890.82



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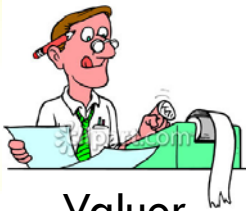
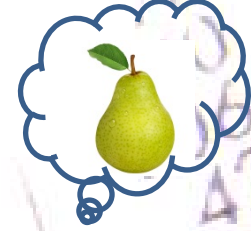
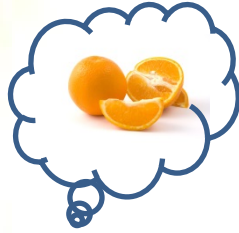
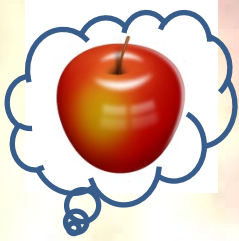
Standards (Definitions) of Value

- Fair value
 - Statutory fair value



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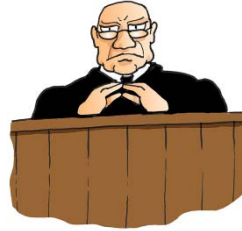
\$ Fair Value \$



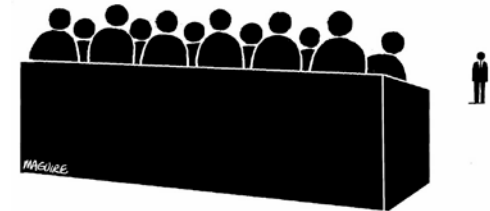
Valuer



Attorney



Judge

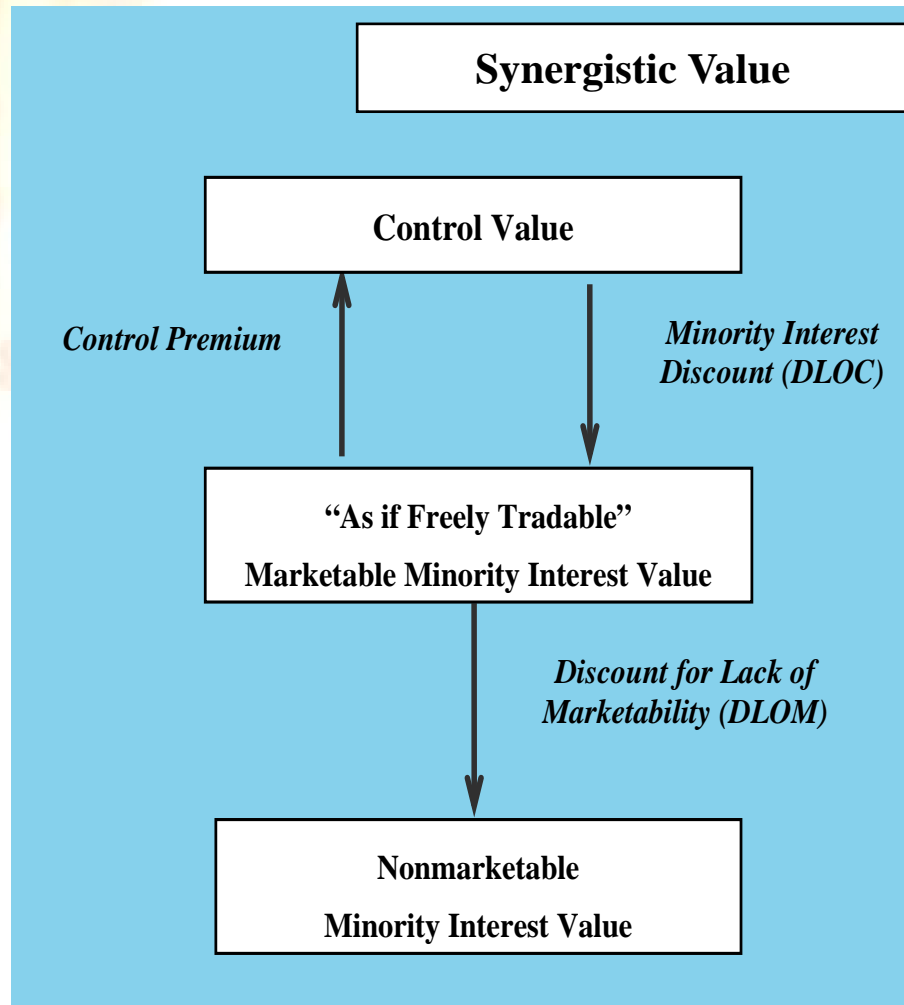


Jury



Client

The Levels of Value



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Prerogatives of Control

- What are the prerogatives of control?
 - Appoint board members
 - Declare distributions
 - Sell assets and/or liquidate company
 - Borrow against corporate assets
 - Hire and fire personnel
 - Deal with related parties
 - Issue new equity

Non-controlling Interest

- Pro-rata control value
 - Enterprise value less debt
 - Times ownership %
- Fair market value
 - Enterprise value less debt
 - Less impact of lack of control
 - Less impact of illiquidity and non-marketability
- Statutory fair value
 - Depends on # of shareholders

Florida Statutes

- No discounts for lack of marketability or minority status if 10 or fewer owners.
 - 10 owners of 10% each?
 - 100 owners including one 51% holder?
 - 100 owners including one 67% owner?

Control or Non Controlling Cash Flows?

- Unadjusted cash flows assumed to be non-controlling
- Control adjustments
 - Officer compensation
 - Owner discretionary expenses
 - Income or expense associated with non-operating assets or liabilities
- **QUESTION**: In a statutory fair value appraisal, should control adjustments be made?

Marketability vs. Liquidity

- Marketability:
 - The capability and ease of transfer or salability of an asset
 - Interests in privately-held businesses are non-marketable – no secondary market
 - Even marketable interests can be illiquid

Marketability vs. Liquidity

- Liquidity:
 - The ability to convert an asset into cash without significant loss of principal
 - About $\frac{1}{4}$ of the smallest public firms do not trade daily
 - Half-life of a 5% block in a large company is 10 months; Half life of a 5% block in a small company is 20 years
- Investor bears **volatility risk** until liquidity event

Thanks to **Jon Swergold, Esq.**, Greenberg Traurig (Miami) for the legal and statutory research presented in this presentation.

The Florida Business Corporation Act - Chapter 607 (“FBCA”)

- The FBCA adopts the Revised Model Business Corporation Act (“RMBCA”) with limited, but significant exceptions.
- The RMBCA, represents the majority view, explicitly stating that “fair value” shall be “computed without discounting for lack of marketability or minority status”
- The FBCA severely and arbitrarily limits this language to apply to a corporation with **ten (10) or fewer shareholders.** Fla. Stat. § 607.1301(4)

The Florida Revised Uniform Limited Partnership Act of 2005 - Chapter 620 ("FRULPA")

- The FRULPA adopts the Revised Model Uniform Limited Partnership Act ("RULPA") with limited, but significant exceptions.
- The RULPA, represents the majority view, and uses "buyout" price rather than "fair value". "Buyout" price is to be calculated as a going concern, without consideration of a minority discount. However, other discounts, such as lack of marketability, may apply.

The Florida Revised Uniform Limited Partnership Act of 2005 - Chapter 620 ("FRULPA")

- The FRULPA rejects the "buyout" concept and uses the term "fair value" without regard to discounts and marketability, but arbitrarily limits this language to apply to a limited partnership with **ten (10) or fewer limited partners.** Fla. Stat. § 607.1301(4)

Definition(?) of “Fair Value” Under Fla. Statute 607.1301

(4) “Fair value” means the value of the corporation’s shares determined:

(a) Immediately before the effectuation of the corporate action to which the shareholder objects.

Definition(?) of “Fair Value” Under Fla. Statute 607.1301

(4) “Fair value” means the value of the corporation’s shares determined:

(b) Using customary and current valuation concepts and techniques generally employed for similar businesses in the context of the transaction requiring appraisal, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable to the corporation and its remaining shareholders.

Definition(?) of “Fair Value” Under Fla. Statute 607.1301

(4) “Fair value” means the value of the corporation’s shares determined:

(c) For a **corporation with 10 or fewer shareholders**, without discounting for lack of marketability or minority status.

Definition(?) of “Fair Value” Under Fla. Statute 620.2113

- (4) “Fair value” means the value of the limited partner’s partnership interests determined:
- (a) Immediately before the effectuation of the appraisal event to which the partner objects.

Definition(?) of “Fair Value” Under Fla. Statute 620.2113

- (4) “Fair value” means the value of the limited partner’s partnership interests determined:
- (b) Using customary and current valuation concepts and techniques generally employed for similar businesses in the context of the transaction requiring appraisal, excluding any appreciation or depreciation in anticipation of the transaction to which the partner objects unless exclusion would be inequitable to the limited partnership and its remaining partners.

Definition(?) of “Fair Value” Under Fla. Statute 620.2113

(4) “Fair value” means the value of the limited partner’s partnership interests determined:

(c) For a limited partnership with **ten or fewer limited partners**, without discounting for lack of marketability or minority status.

Florida's Appraisal Rights Statutes - §§ 607.1302 and 620.2114

- Under Florida Law, the right to an appraisal applies to certain defined conversions or mergers of corporations/limited partnerships, share exchanges, dispositions of assets, or amendments to the corporation's articles of incorporation.
- Corporations/limited partnerships may also delineate a list of transactions for which the entity may voluntarily choose to provide appraisal.

“Fair Value” and Florida’s Dissolution Statute

- Shareholders’ right to dissolution set forth in §607.1430(2) and §607.1430(3) (2006).
- Alternative to dissolution is the “fair value” purchase by corporation/majority shareholder pursuant to §607.1436.
- No statutory definition of “fair value” in a dissolution action.

Relevant Appraisal and Dissolution Case Law

- Munshower v. Kolbenheyer, 732 So. 2d 385 (Fla. 3d DCA 1999)
 - Discount for lack of marketability was properly factored in dissolution action – Court looked to NY Law
 - Rationale for discount – lack of public market
 - Prior to Amendment of Florida Statute
 - Adopts Minority View

Relevant Appraisal and Dissolution Case Law

- Boettcher v. IMC Mortg. Co., 871 So. 2d 1047 (Fla. 2d DCA 2004)
 - In dissenter’s rights action, in calculating fair value, Court required exclusion of appreciation or depreciation in share value, absent extraordinary circumstances, in assessing proposed asset sale
 - In valuing company court “should consider proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court... [such as] net asset values, market price, earnings and the like.”

... Relevant Appraisal and Dissolution Case Law (continued)

- G & G Fashion Design, Inc. v. Garcia, 870 So. 2d 870 (Fla. 3d DCA 2004)
 - In dissolution action, fair value of shares calculated based upon what a willing purchaser in an arms length transaction would offer for an interest in the subject business.
 - Relying on New York Law
 - Actual offer made by a third party – Good faith?

... Relevant Appraisal and Dissolution Case Law (continued)

- Williams v. Stanford, 977 So. 2d 722 (Fla. 1st DCA 2008) and Foreclosure Free Search v. Sullivan, 12 So.3d 771 (Fla. 4th DCA 2009)
 - Minority shareholder may be entitled to equitable remedies beyond an appraisal.

... Relevant Appraisal and Dissolution Case Law (continued)

- Cox Enterprises, Inc. v. News-Journal Corp., 510 F.3d 1350 (11th Cir. 2007)
 - In dissenting shareholder case, comparable sales/fair market value method is appropriate for determining “fair value” of minority shareholder’s stock.
 - Court did not adjust calculation of fair value to account for corporate waste, but did adjust operating margin using identified comparables
 - Entity to be valued as a going concern being managed in a reasonably prudent manner going forward

... Relevant Appraisal and Dissolution Case Law (continued)

- Pueblo Bancorporation v. Lindoe, Inc., 63 P.3d 353 (Colo. 2003)
 - In appraisal rights type action, Court held the meaning of “fair value” is a question of law; fair value means “proportionate or pro rata” interest without discounts.

Other Discounts or Premiums?

- Voting vs. non-voting
- Key person discount
- Trapped-in capital gain discount
- Blockage discount
- Pass Through Entity Premium

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