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## Association News

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### CEO's Message Expanding Your Opportunities

By Parnell Black, MBA, CPA, CVA, Chief Executive Officer



As many of you know, I am always on the lookout for new opportunities for our membership. For that matter, that is what NACVA is (and has always been) all about—creating opportunities. We have done so by creating training and certifications in fields of emerging opportunity, starting with business valuation leading to our Certified Valuation Analysts (CVA) and Accredited Valuation Analyst (AVA) credentials, and moving through the entire spectrum of financial forensics leading to our Certified Forensic Financial Analyst (CFFA) credential.

Being at the leading edge of training and certification development, we have been able to provide thousands of individuals with the knowledge, to a degree—skill, and the credibility to offer (or expand) services in disciplines that offer potential for growth. As put to me many years ago by a longtime retired member and mentor—NACVA is about “opening doors of new opportunity.”

One area that I believe members can capitalize on is in Mergers and Acquisitions (M&A). M&A is not for the faint of heart, however, and requires a significant and serious commitment to succeed. Though we have offered M&A training for many years, two years ago we decided to take our commitment up a few notches. In doing so, NACVA partnered with the Middle Market Investment Banking Association (MMIBA) who is the sponsor of all of our M&A training and webinars, as well as the Chartered Merger and Acquisition Professional (CMAP) designation. (If you are not familiar with MMIBA, check them out at [www.mmiba.com](http://www.mmiba.com)) For my CEO's Message, I would like to share with you a compelling article written by Dennis Roberts, CPA, CVA, ABV, CMAP, and MMIBA's Chairman of the Board. It is entitled:

#### A Growing New Practice Opportunity for CVAs and AVAs

Driven by an imminent and unprecedented increase in middle market business sales, Baby Boomers' retirements and shorter lifecycles of technology age businesses, M&A, the purchase and sale of business interests, offers new opportunities to provide transaction services beyond traditional advisory and support roles. The global economy's increasing cross border M&A activity combined with a huge injection of private equity capital seeking investment also will continue to drive M&A activity particularly in the middle market, our current economic slowdown notwithstanding. It is estimated that Baby Boomers alone will dispose of some 809,000 of these middle market business as they age and retire. (See Tables One and Two) <sup>1</sup>.

#### Baby Boomers Statistics

Based on population demographics, it is reasonably estimated that Baby Boomers own approximately 67% of middle market businesses and will sell or otherwise dispose of (as opposed to abandoning) approximately 83% of them<sup>2</sup> as they retire or die in the coming years. Assuming that most of these businesses will be disposed of when their owners reach age 65, more than 671,000 middle market businesses worth an estimated \$2.47 trillion will be disposed of between 2011 and 2029 by Baby Boomers alone (or an average 35,000 middle market businesses a year). Exactly when this wave arrives will be determined not simply by Boomers' ages but also by the economy, interest rates and other factors. There is no question, however, that the selling wave should begin shortly and steadily rise over the next 10-12 years, peak during the 2020s and taper off during the following 10-12 years. The other drivers previously mentioned—shortened business life cycles, one-world cross border M&A deals, and private equity capital seeking middle market business investments—likely will continue to influence middle market M&A throughout this period and beyond.

For CVAs/AVAs, this means a new practice development opportunity to assist business owners seeking to sell their businesses. Many of NACVA's CVAs/AVAs have long assisted clients buying and selling businesses by specializing in due diligence, tax planning and compliance, valuation services and accounting records cleanup and are especially suited for this work because of their comprehensive training, inherently ethical attitudes and “trusted advisor” client status. Yet the lucrative and often highly technical aspects of business sales have been given over to boutique middle market investment bankers.

This article discusses the requisite training and licensing requirements needed to help NACVA members establish the specialized practice knowledge for middle market M&A work, either exclusively or as an adjunct to their own practices.

#### Broker vs. Financial Professional

The best CVAs/AVAs have people skills that rival those of any other business professional anywhere. As with business valuation in the past, most CVAs/AVAs seriously entering the M&A intermediary or investment banking world tend to be professionals with a number of years' experience and the resulting wisdom and maturity necessary for this sophisticated work. In fact, few professions depend more heavily on people skills than M&A advisory.

On the professional side, M&A investment banking takes a second seat to no other financial services industry activities. It requires knowledge of, among other things, accounting and finance, contract law, taxation, negotiation techniques, banking and the capital markets, deal structuring and fundamental competitive analysis. In other words, this is highly sophisticated and technical work, and few professions besides valuation provide as comprehensive a preparation for it.

Finally, middle market M&A transactions involve large sums of money and the ethical and objective professional standards maintained by most NACVA's members are ideally suited to guiding clients through what is likely to be the largest transaction of their lives. There have been too many cases where national business brokerage firms were sued for allegedly selling hyperbole, unjustifiable promises and dubious valuations in return for high retainer fees while in fact closing very few client transactions. The competency and high ethical standards of a NACVA certified member provides a welcome counter given past abuses, and in my opinion, will provide a strong competitive advantage.

What does an M&A intermediary do? The intermediary in a typical sales side<sup>3</sup> M&A engagement will spend (including staff time) somewhere between 300 and 600 hours on the following tasks outlined below on a typical single engagement for his client:

- **The initial phase:** Execution of an engagement letter or financial services agreement; preliminary valuation of his clients' businesses in the M&A marketplace, buyer/investor and industry research, and offering memorandum preparation. Typically about 30 to 45 days.
- **The marketing phase:** Buyer and investor contact, securing non-disclosure documents, and securing preliminary expressions buyer/investor interest. Typically about 60 days but can be much longer.
- **The negotiating phase:** Extensive deal structuring and negotiations, typically with several buyers. Typically 30 to 60 days.
- **The preliminary conclusion phase:** Negotiating phase concludes with a fully negotiated letter of intent (LOI) and then proceeds to buyer/investor confirmatory due diligence.
- **The final phase:** The definitive agreement development phase. Normally about 60 to 75 days and typically with some renegotiation of original LOI deal terms.

This additional M&A practice opportunity is lucrative. For example, the \$10 million sale of a middle market business likely would generate \$25,000 to \$75,000 in support fees for the accountant, \$75,000 to \$100,000 in attorneys' fees and \$8,000 to \$12,000 for the valuator (if applicable). These numbers are estimates based on the author's extensive experience as a middle market intermediary and should be fairly accurate. Now consider that the M&A intermediary would collect a fee of between \$450,000 and \$600,000 for his/her work on the same \$10 million transaction.

#### Training Requirements

As noted above, a command of the basic financial sciences is required as a foundation for entering the M&A advisory world; all CVAs/AVAs inherently share this "basic training," and have demonstrated this through certification. The most important distinction between business valuation and M&A valuation is one of perspective and measurement, given the contrast between Fair Market Value—an abstract concept—and Investment Value, the real world of deals.

Before entering the M&A advisory world, one should first consider acquiring training in M&A conventions (standard financial frames of reference regarding how things are done, how they are measured), M&A protocol (a frame of reference regarding the typical order of things, when they are done), and financial negotiations. M&A negotiating requires work well beyond simply "winging it." Typically, very basic formal training will take about 40 hours and is currently offered by the Middle Market Investment Banking Association (MMIBA). Formal training is not an absolute prerequisite in acquiring these additional skills, however. An equally acceptable form is affiliation with an experienced intermediary. He or she can guide the new M&A practitioner through the first few deals and much can be learned through observation. This method is the more time-honored way to enter the middle market M&A profession. Additionally, a one-week coaching course is advisable to be confident of successfully completing Financial Industry Regulatory Authority (FINRA) examinations for securities licenses.

#### Starting and Running an M&A Practice

**Credibility:** These transactions involve large sums of money and while the CVA/AVA credential brings a great deal of credibility, it probably will not be enough. Credibility largely derives from having represented transactions successfully. Investment bankers and intermediaries typically maintain prominently displayed website libraries of "Tombstones" reflecting completed transactions they have represented. Credibility, the largest barrier to entry, presents a chicken-and-egg dilemma to would-be practitioners. But this is not an insurmountable obstacle: the best way to leap the hurdle is to affiliate or partner, at least initially, with a well-regarded boutique investment bank or to hire someone with the requisite skill set and the Tombstones to prove it.

**Staffing and research:** M&A intermediaries' backrooms serve critical functions in support of buyer and industry research necessary to represent a transaction. They also prepare the offering memoranda that provide buyers or investors detailed client overviews and pitch books to land new business. (These also must reflect reasonably deep knowledge of the potential clients' industries.) Unless you choose to affiliate with an existing boutique intermediary, count on having, even in the smallest practice, one support professional and several databases. Expect to pay from \$45,000 to \$85,000 a year for the support professional and at least \$15,000 annually for the minimal databases and research tools.

**Marketing:** To some degree, a CPA or Valuation firm could expect to receive some baseline of M&A engagements from among its own clients, assuming the requisite credibility and its clients' awareness of its M&A practice. Unless M&A activity is offered as a clearly distinct client service, this rarely will generate sufficient business to develop a serious M&A practice so additional marketing is crucial. Much business-to-business marketing attempts to entice businesses to make impulse purchases of attractive products or services, items they didn't know they needed. Because M&A services are only bought when required, an entirely different marketing approach is necessary. The secret: stay in front of the potential market for long periods of time while trusting that when M&A services are needed the client will associate the firm's name with providing them. This typically is achieved by publishing newsletters regularly, holding seminars, networking actively and, if possible, developing M&A specialty industry practices. All of this is most easily achieved by affiliation with an existing M and A firm.

**Licensing:** It is widely agreed that whether or not it was a matter of original intent, US securities laws probably require practitioners who accept contingent fees as M&A intermediaries, at least those based on stock transactions, should be securities licensed. While the American Bar Association (ABA) and other industry groups have sought for years to change these regulations, until recently there appears to be no quick resolution ahead, although FINRA itself recently recommended a simplification process to the SEC. Most quality boutique investment banks and M&A intermediaries simply recognize the current reality and obtain the necessary licensing (administered by FINRA on behalf of the SEC). Similar to the real estate industry, there are two essential requirements: a broker (broker-dealer or BD) license and a license for the individual intermediaries. Obtaining individual licenses (usually Series 7, 62 or 79 and 63) requires testing, a modest amount of study (30 or 40 hours) in preparation, and a sponsoring BD.

Setting up a BD is more complicated and requires that a firm member obtain a securities principal license, but with the aid of a consultant and perhaps \$10,000 in consulting fees and \$5,000 of minimum capital (assuming M&A is the only function of the BD), it is well within the reach of any CVA/AVA who decides to proceed. The BD will require an annual independent audit and the filing of quarterly (FOCUS) reports with FINRA. FINRA takes BDs seriously and subjects them to heavy scrutiny. During the first year, the extent of oversight may seem annoying and will be time consuming but manageable. Many of those who have committed to going the BD route have also considered that it provides a significant competitive advantage not only to their M&A practice but perhaps to their valuation practice as well. As in the cases of training and credibility, the issue of the BD can also be easily dealt with by simply affiliating with an existent BD. At least some boutique investment banks see this as a great way to affiliate with skilled professionals and to promote deal flow for both the professional and the bank. It is simply a matter of obtaining and associating one's license with those banks that will consider this approach and are themselves licensed broker-dealers.

As a final note, CVAs/AVAs considering this kind of work should of course be aware of issues concerning accepting contingent fees from attest and audit clients and also should review their local state regulatory laws and CPAs should also check with their State Board of Accountancy for prohibitions, if any, concerning this kind of work.

TABLE ONE: Census of U.S. Middle Market Businesses 2002						
			Owned by Boomers 67.7% (See Table Two)		Assuming the Sale of 83% of these Businesses	
	Number of businesses 1,000's	Aggregate Revenues (\$1,000's)	Number of businesses (1,000's)	Estimated Revenue of Businesses (\$1,000's)	Number of businesses (1,000's)	Estimated Value of Businesses sold (\$1,000's)
<b>LOWER MIDDLE MARKET</b>						
Businesses with revenues between \$1 million and \$50 million	1,167	97.7% \$5,358,282,278	790	\$3,627,557,102	656	\$1,505,436,197
<b>MID MIDDLE MARKET</b>						
Businesses with revenues between \$50 million and \$250 million	25	2.1% \$2,425,940,193	17	\$1,642,361,511	14	\$1,681,580,027
<b>UPPER MIDDLE MARKET</b>						
Businesses with revenues between \$250 million and \$500 million	3	0.2% \$1,036,886,217	2	\$681,661,969	2	\$282,889,717
<b>TOTAL MIDDLE MARKET</b>	1,195	100% \$8,791,108,688	809	\$5,951,580,582	671	\$3,469,905

TABLE TWO: U.S. Population—Age Data		
Estimated typical age for middle market controlling business ownership	Total Population	Boomers born 1946 to 1964, ages 64 to 46
35 to 69	116,634,708	78,991,776
Percentage	100%	67.70%

*Dennis J. Roberts, CPA, CVA, ABV, CMAP is the Chairman of a very active national M&A investment bank, the McLean Group LLC. He is also the Author (John Wiley) of the widely acclaimed "An Insider's Guide to the Purchase and Sale of Middle Market Business Interests". Having acted as the investment banker advisor on numerous transactions over many years, he is also a formal business valuator having done such business valuations as the "Nixon Watergate Tapes." He has been acclaimed "Instructor of Great and Exceptional Distinction" by NACVA and was on the Illinois CPA Society committee that developed their original business valuation curriculum for CPAs, which was subsequently adopted by the AICPA. Mr. Roberts is a nationally acclaimed lecturer and speaks on investment banking and valuation subjects with humor, insight, and many anecdotes. He can be reached at (703) 827-0200 or [djroberts@mcleanllc.com](mailto:djroberts@mcleanllc.com) for further information on how to go about pursuing this profession.*

<sup>1</sup> See Table Two: Assuming an approximate age range for the controlling owners of middle market businesses to be between 35 and 69, then Boomers, born between 1946 and 1964, based on census data would own approximately 67.7 % of middle market businesses as defined for this article.

<sup>2</sup> This 83% sale of business estimate was taken from a PriceWaterhouse study.

<sup>3</sup> As a practical matter, most boutique middle market M&A intermediaries spend the bulk of their time on the sales side of transactions although most will also do engagements (perhaps 20% of their total) representing buyers. In addition, institutional capital raises, especially from Private Equity Groups seeking to recapitalize the ownership of middle market businesses, is a substantial part of M&A practice for most.

<sup>4</sup> There are ongoing developments on M&A licensing requirements and practitioners should seek the guidance of qualified counsel before proceeding with registration. Additional information can be found in the Securities Act at Section 3 (a)(4)(A) and in the Guide to Broker Dealer Registration. Of particular note is the recent adoption by FINRA of the Series 79 license which is the first such license granted exclusively for M&A professionals and in certain cases valuation professionals.

Sincerely,



—Pamell Black  
Chief Executive Officer

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