

Globalview Advisors

Financial Valuation and Advisory Services

AICPA Private Equity/Venture Capital Accounting and Valuation Guide – Update

BDO LLP – San Francisco

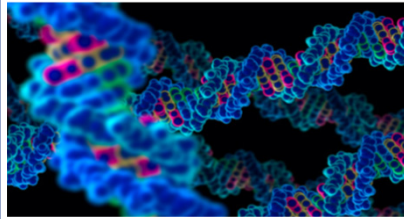
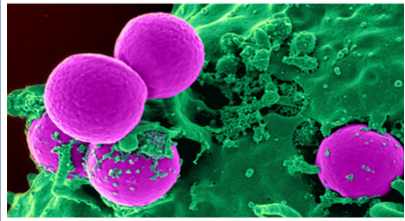
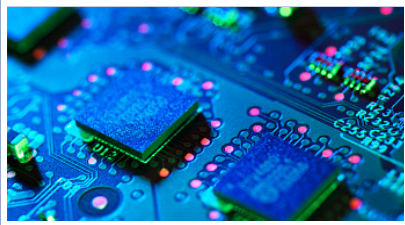
May 15, 2017

Disclaimer

- The views expressed are my own and do not necessarily reflect those of the PE/VC Task Force or any other individuals or organizations.

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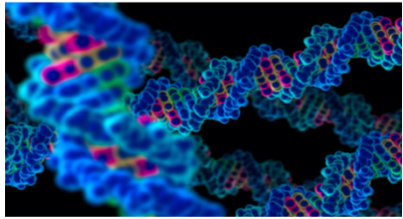
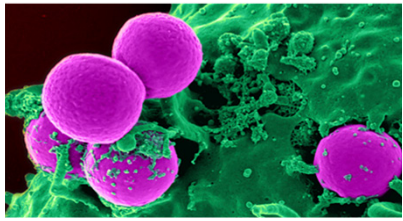
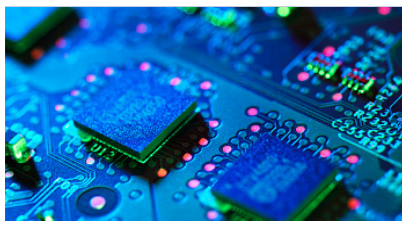
History and Purpose of the Task Force

History and Purpose of the Task Force

- Task Force formed in early 2013
- Concerns of numerous parties on PE/VC portfolio investment valuations
- Purpose—Reduce diversity in practice and inconsistent FV measurements
 - Changes on year to year basis
 - Differences between different preparers for same / similar investments
 - Investors frequently use transaction-specific assumptions, which are not always transparent; however, GAAP focuses on market participant

History and Purpose of the Task Force

- Provide guidance on important issues facing PE/VC
 - Cheap Stock Guide (June 2013)—focus on equity securities issued as compensation
 - IPEV Valuation Guidelines (December 2012), focused on later stage controlling investments; deferred discussion of enterprise-value allocations
 - AICPA Audit and Accounting Guide: Investment Companies - focused primarily on accounting
 - PEIGG—U.S. Private Equity Valuation Guidelines Industry Assumptions vs. U.S. GAAP/IFRS Fair Value Guidance



Task Force Members and Observers

Task Force Members and Observers

Co-Chairs

- Amanda Miller, Ernst & Young
- Sean McKee, KPMG

Valuation Specialists

- Chad Arcinue (Ernst & Young) (Observer)
- Travis Chamberlain (Clifton Larsen)
- Dave Dufendach, (Alvarez & Marsal)
- Shaan Elbaum (PwC) (Observer)
- John Ferro, (Grant Thornton)
- Ray Rath (Globalview Advisors)

Industry Participants

- Timothy Curt (Warburg Pincus)
- Quintin Kevin (Adams Street)
- David Larsen (IPEV, Duff & Phelps)

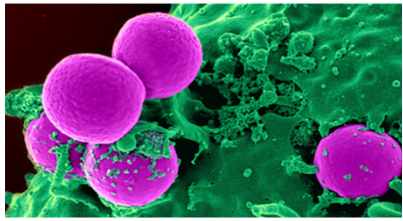
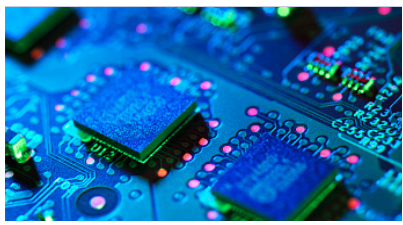
Auditors

- Belanne Ungarelli (PwC)
- Scott Burger (KPMG) (Observer)*
- Adrian Mills (Deloitte)

AICPA

- Yelena Mishkevich
- Mark Smith

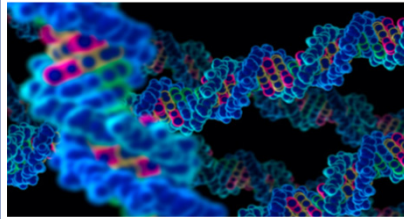
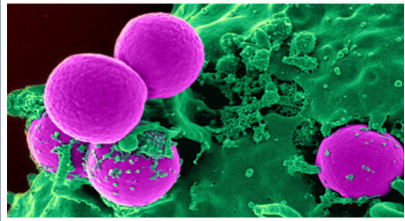
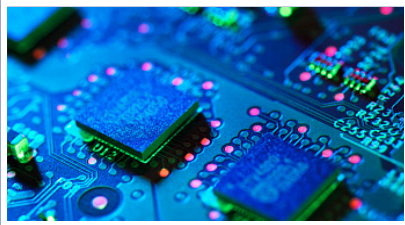
* Formerly an industry participant as the Chief Accounting Officer of Kleiner Perkins but has moved to KPMG via Rothstein Kass.



How the Task Force Was Selected and Functions

How the Task Force Was Selected and Functions

- Selected to bring a mix of views and perspectives
 - Preparers
 - Accountants
 - Valuation specialists
- Task Force objectives include:
 - Harmonize the diverse views of industry participants, auditors and valuation specialists
 - Produce a user friendly guide with examples that can be used to reason through real situations faced by valuation specialists and auditors
- Working title:
 - Valuation of Portfolio Company Investments of Venture Capital and Private Equity Funds and Other Investment Companies



Current Status and Possible Guide Contents

Current Status and Possible Guide Contents

- Introduction
- Chapter 1, Overview of the Private Equity and Venture Capital Industry and Its Investment Strategies
- Chapter 2, Fair Value and Related Concepts
- Chapter 3, Market Participant Assumptions
- Chapter 4, Determining the Unit of Account and the Assumed Transaction for Measuring the Fair Value of Investments
- Chapter 5, Overview of Valuation Approaches
- Chapter 6, Valuation of Debt Securities
- Chapter 7, Valuation of Equity Securities in Simple Capital Structures
- Chapter 8, Valuation of Equity Securities in Complex Capital Structures
- Chapter 9, Control and Marketability

Current Status and Possible Guide Contents

- Chapter 10, Calibration
- Chapter 11, Backtesting
- Chapter 12, Factors to Consider At or Near a Transaction Date
- Chapter 13, Special Topics
 - Enterprise has traded securities
 - P*Q rule
 - Underwriter lockups and SEC Rule 144A
 - Similar vs. identical securities
 - Significant decrease in volume or activity or distressed transactions
 - Pricing services / broker quotes / investment banker quotes
 - Indicative Offers
 - No recent round of financing and no revenue
 - Rights and Privileges not enforced
 - Commitments to portfolio companies (debt, equity)
 - Guarantees

Current Status and Possible Guide Contents

- Dilution
 - Existing capital structure—preferred and common units
 - Future rounds
 - Management securities
 - Investor warrants
- Options and Warrants, Convertible Notes
- Contractual Rights (“contingent consideration”)
- LP Interests—TIS 2220
- Other
- Chapter 14, Frequently Asked Questions

Current Status and Possible Guide Contents

■ Appendices

- Appendix A, Valuation process and documentation considerations
- Appendix B, Valuation Toolkit
- Appendix C, Example Investment Summaries
 - Leveraged Buy-Out (LBO)—value of debt for valuing equity
 - Benefits of Adding Leverage—day 2 gain vs. day 360 gain
 - Downside of Leverage—roll-up, backtesting at exit
 - Real estate development project—value accretion as project progresses
 - Oil & gas development project—value accretion given new information
 - Oil & gas bond—significant decrease in volume or activity
 - Joint venture—agency effect when control rests with junior securities

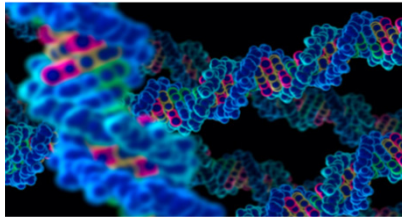
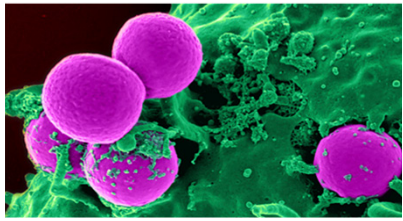
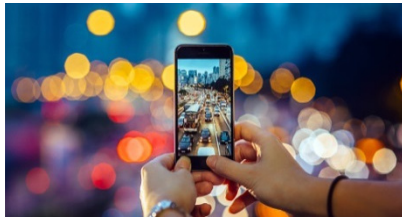
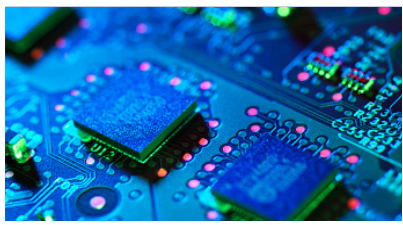
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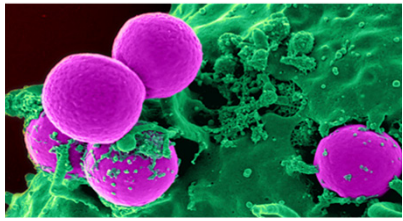
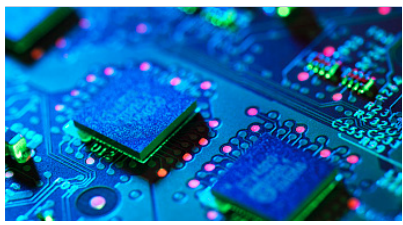
- Emerging market investment—reliability of financial statements
- Start-up with a strategic exit—“last man standing”
- Biotech startup—down-round to strategic sale with earn out
- Software as a service startup—quick ramp but lots of competition
- Clean-tech startup—changes in value due to changes in regulations and government support
- Emerging market startup—opportunities and risks in China
- BDC debt—straight debt, debt with prepayment penalties, convertible debt, warrants
- Restricted stock investment (PIPE)—direct investment in traded public company stock
- Investments in related securities when the enterprise has traded stock



**What are Some of the
Biggest Challenges?**

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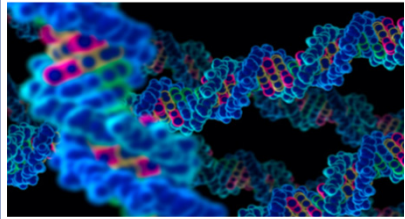
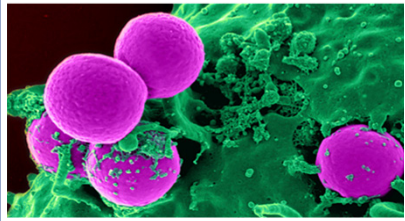
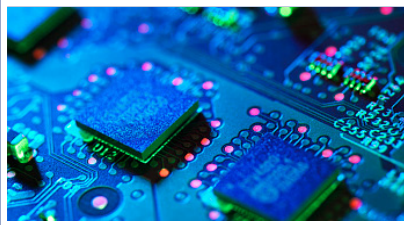
- Delicate balance of reasonable effort vs. undue cost and burden
- Helping prospective users reflect a market participant perspective
- Provide meaningful examples that illustrate a wide variety of situations
- Investor alignment
- Appropriate consistency across time
- Transaction costs



Timeline

Timeline

- Numerous Task Force meetings and conference calls scheduled
- AICPA Financial Reporting Executive Committee (“FinREC”) Meetings
 - Fatal flaw reviews—Fall 2017
 - Target FinREC approval of working draft—Winter 2017
- First public release of working draft—May 2018
- Process comments on working draft, FinREC follow-up—August 2018
- Target publication of final guide—May 2019
- Financial Reporting Executive Committee (FinREC) Mission - determine the AICPA's technical policies regarding financial reporting standards and to be the Institute's spokes person on those matters, with the ultimate purpose of serving the public interest by improving financial reporting.
- Sixteen members from accounting firms, preparers of financial statements and other professionals including a valuation observer from the FVS Executive Committee.



Questions

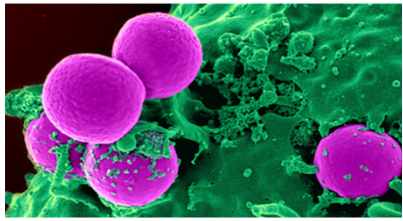
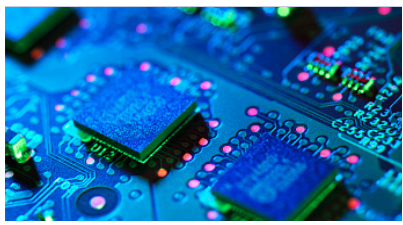
Contact Information

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Raymond Rath, ASA, CFA Globalview Advisors



- Ray is a Managing Director in the Irvine, California office of Globalview Advisors. He has over 30 years of financial valuation expertise in the valuation of businesses, securities interests, and intangible assets.
- Ray has performed valuation projects for financial (both US GAAP and IFRS) and tax reporting, transactions, and litigation projects. In addition to performing valuations, Ray has extensive experience in the review of third-party and management prepared valuations.
- Ray has a wealth of experience in a wide range of industries. In recent years, much of his work has focused on technology and Internet firms. Other industries where he has significant project expertise include consumer products, entertainment and media, food services, health care, and manufacturing, in addition to early stage, rapid growth firms.
- Prior to joining Globalview Advisors in 2012, Ray was a Director in the Valuation Services Practice at PricewaterhouseCoopers LLP. He was also a Senior Manager in the Valuation Services Practice at KPMG LLP and KPMG Consulting, Inc., as well as a Manager at Arthur Andersen & Company.
- Ray received his MBA from the University of Southern California and his BS in Business Administration, cum laude, from the University of Kansas. He is an accredited senior Member of the *American Society of Appraisers (ASA)* in the business and intangible assets valuation disciplines as well as Appraisal Review and Management, and is also a Chartered Financial Analyst (CFA).



End