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# Valuation Team Helps Management Plan Technology Acquisition

*New accounting rules required valuation of intangibles during acquisition negotiation in order to make timely SEC filings when the deal was announced*

An acquiring company wanted to know the balance sheet and income statement effects of a planned acquisition. The new accounting standard about the valuation of these is complex, so the company utilized professionals from Teknos to review purchase terms in advance and to calculate the value of intangible assets and contingent liabilities at closing.

## CHALLENGE

A publicly traded company was in negotiations to acquire a small company. The public company CFO knew that she would have to report the balance sheet impact of the deal promptly after it was announced and that she would have to provide research analysts with estimates of the income statement effects for the next couple of years at the same time.

## SOLUTION

At the recommendation of the acquiring company's accounting firm, professionals from Teknos were hired. We reviewed the proposed term sheet and the small company's financial projections, and then ran some preliminary calculations. Once terms had been settled, we ran final calculations and provided a valuation report for the acquiring company to use in preparing its 8-K for filing with the SEC and in making its analyst and investor conference call.

### *Analysis of Situation*

The small company was being purchased for a price substantially greater than its book value because it had developed some valuable technology and intellectual property. According to the new accounting rule, Statement of FASB Accounting Standards Codification Topic 805, *Business Combinations* (ASC 805, formerly FAS 141R), these intangible assets had to be "fair valued" and placed on the balance sheet of the acquiring company at the closing. In addition, the purchase price was a combination of cash and earnout – the earnout also had to be "fair valued" as a contingent liability and placed on the balance sheet of the acquiring company at the closing.

The requirement to immediately fair value all intangibles and place them on the balance sheet at closing, is a substantial change from the old accounting rule. In the past, a variable item such as the earnout was not valued and placed on the balanced sheet until it was likely that there would be a payment and the amount of the payment was known.

### *Preliminary and Final Valuations*

Working in tandem with the transaction team of management, investment bankers, and securities lawyers, we were given copies of the proposed terms as they were being negotiated. Among other assistance we provided was a suggestion about the structure of the earnout which would make it easier for the acquiring company to report its value in the future.

Using the small company's financial projections and the acquiring company's assessment of how the small company would be integrated in its operations, we constructed models which estimated the values of the intangible assets (technology, intellectual property, customer relationships, and workforce) and the contingent liability (the earnout). When the deal terms changed slightly just before closing, we were able to swiftly incorporate the effects of the changes in our models.

Once the deal terms were finalized, we prepared a full length valuation report compliant with ASC 805 and delivered it to the acquiring company before the transaction closed. Management of the acquiring company had solid information about the intangible assets, the contingent liability, and goodwill to incorporate in its filing with the SEC and the subsequent call with analysts and investors.

In a year's time, Teknos will be available to help the acquirer with subsequent reporting by "marking to market" the intangible assets and contingent liability and testing the assets for impairment under the requirements of FASB Accounting Standards Codification Topic 350, *Intangibles – Goodwill and Other* (ASC 350, formerly FAS 142).

*Teknos Associates is a valuation firm which serves emerging growth companies and their venture capital backers. We are a team of experienced and credentialed valuation professionals with backgrounds in appraisal, accounting, investment banking, and venture capital.*

*We provide appraisals to facilitate compliance with a variety of tax and accounting requirements, including option issuance and portfolio valuation. We support merger and acquisition activities with independent fairness opinions. And we offer valuations of intangible assets and liabilities after an acquisition.*

*We have produced hundreds of valuation reports quickly and economically, without sacrificing quality. Our reports have stood up to scrutiny by Big Four audit firms, the IRS, and the SEC. Contact us at to see how we can help you.*