VALUE MANAGEMENT INC.

Investment Banking + Valuation Services

ISSUES + UPDATES 3RD QUARTER 2022

Holy Cow! New York Yankees Hit $6 Billion in Value

That's what the legendary announcer Phil Rizzuto would be yelling over this news. The New York Yankees have held their ground as Major League Baseball's (MLB) most valuable team, according to *Forbes'* latest rankings. What's more, the Bronx Bombers have become the first MLB team to hit a $6 billion valuation, says *Forbes*, and it is the second most valuable franchise in U.S. sports, eclipsed only by the National Football League's Dallas Cowboys ($6.5 billion). While the Yankees lead MLB in overall value, *Forbes* says that the second-ranked Los Angeles Dodgers ($4.08 billion) received the highest local-TV rights revenue, with $189 million as compared to the Yankees reportedly bringing in $135 million in local broadcast rights fees.

More Business Owners Deciding to Sell, Most Retiring

The long anticipated "Silver Tsunami" wave of retiring baby boomers appears to be arriving and is expected to supply the market with a steady stream of available businesses throughout the year, according to a recent industry report. An increasing number of small business owners, many aging and no longer willing to wait on the sidelines, believe now is the time to exit. Of surveyed owners, over 63% say they are over 50 years old and 30% say they are over age 60. More than a third (37%) say they plan to sell within two years. Of owners recently surveyed, the majority (55%) cite retirement as their motivation for selling, while a substantial 31% say their business is doing well and feel they can currently receive a good price. Active for-sale inventory has climbed 10% over the past year, the report says.

In This Issue:

Holy Cow! New York Yankees Hit $6 Billion in Value ..... p. 1
More Business Owners Deciding to Sell, Most Retiring ..... p. 1
Purchase Price Allocation Study ..... p. 2
New Lease Accounting Rules ..... p. 2
Delaware Chancery Court Allows Breach of Fiduciary Suit to Move Forward on a SPAC ..... p. 3
Delaware Chancery Court Rejects Partnership Valuation in a Freeze-Out as Unfair to Minority Partners ..... p. 3
U.S. District Court Dismisses Valuation Firm's Plea to Require Insurance Company to Defend a Lawsuit Against It ..... p. 4
Goodwill Impairments in U.S. Doubled in 2020 ..... p. 5
Typical Components of M&A Fees ..... p. 5
Strong M&A Outlook in the Food and Beverage Sector ..... p. 6

VMI Highlights:

Please help us in welcoming Max Lesoine to our VMI family! Max recently transitioned from intern to full time employee. We are happy to have him on board.

VMI is the Platinum Sponsor of the ESOP Association's Multi State conference which takes place in Hershey, PA in mid-September. Both Ed Wilusz and Greg Kniesel are leading sessions during the 2-day conference.

VMI is sponsoring Liguori Academy's Boundless celebration featuring the Blues Brothers. Liguori Academy is a private, non-profit high school that provides a free education primarily to students in the Kensington section of Philadelphia.

If your firm is interested in having a VMI expert give an in-house or virtual presentation on business valuations and/or merger & acquisitions, please contact Susan Wilusz at smw@valuemanagementinc.com.

Purchase Price Allocation Study

Houlihan Lokey released its 2019 and 2020 Purchase Price Allocation Study, which examines key data points of purchase price allocations (PPAs) recorded by U.S. public registrants. Among the findings:

- The median allocation of purchase consideration (PC) to intangible assets in 2020 was 34% (unchanged from 2019);
- The median allocation of PC to goodwill in 2020 was 47% (also unchanged from 2019); and
- Healthcare was the only industry with intangible assets and goodwill percentages above the mean and median in 2019 and 2020.

The study reviewed public filings, of which 560 transactions formed the basis of the 2019 study and 475 transactions formed the basis of the 2020 study. The study also provides statistics, other annual data, and a comparison to certain results from its 2018 study.

New Lease Accounting Rules

Lately, there have been discussions about the impact of ASC 840 and 842 (rules on accounting for leases) on valuations of businesses. ASC 840 was the original lease accounting under generally accepted accounting principles (GAAP). It required the "booking" of capital leases on the income statement and balance sheet. ASC 842 replaces ASC 840. The biggest change from ASC 840 to ASC 842 is the requirement to record an asset and liability associated with all leases greater than 12 months in term.

Previously, only capital leases were recorded on the balance sheet as an asset and liability. Now, operating leases will also be recorded on the balance sheet as well as in the footnotes. One of the main potential issues is the fact that financial statements post-implementation of ASC 842[1] might not be comparable to financial statements prior to that date. One of the reasons for the implementation of ASC 842 is to comport with the treatment in international circles and to reflect the economic effect of both capital and operating leases on the income statement and balance sheet. But is that really necessary or even material to many of the small businesses? Expect to see more discussion in the future as the implementation of ASC 842 matures and ages.

[1]Effective for FYE post-Dec. 15, 2021.

Delaware Chancery Court Allows Breach of Fiduciary Suit to Move Forward on a SPAC

***In re Multiplan Corp. Stockholders Litig.*, 2022 Del. Ch. LEXIS 1; 2022 WL 24060 (Jan. 3, 2022)**

Churchill Capital Corp. III (Churchill), a special purpose acquisition company (SPAC), was formed in December 2019. Its purpose was to seek out and acquire a private operating company. Churchill closed its IPO of $1.1 billion in February 2020.

The SPAC's sponsor, led by Michael Klein, was compensated in "founder shares" representing 20% of the SPAC's equity purchased at a nominal price. The SPAC's initial public shareholders paid $10 for one share and a fractional warrant. If a transaction were completed within two years, the founder shares would convert into common shares. If no transaction were completed, the SPAC would be liquidated and the IPO shareholders would receive their $10 per share back with interest while the founder shares would be worthless. The SPAC was structured around giving public stockholders the choice of redeeming their $10 investment from the trust or investing in the post-combination entity after an acquisition target was identified.

The SPAC selected to acquire MultiPlan, a provider of data analytics and technology-enabled end-to-end cost management solutions to the U.S. healthcare industry. After the closing, the SPAC shares declined several dollars to $6.27 per share, below the $10 plus interest that shareholders who declined to participate in the transaction would receive. "By contrast, the founder shares, which converted into shares of the post-merger entity, were pure upside to the SPAC's insiders."

The plaintiffs' claims centered around a misalignment of interests during a prior step in the de-SPAC transaction process. The private placement warrants and founder shares were worth approximately $356 million on an investment of $25,000 and would have

dropped to zero absent a merger. Additionally, Klein engaged a related company, Klein Group, that earned a fee of $30.5 million on the transaction. The result was a special benefit to Klein. Because it was a value-decreasing deal, Klein was, in effect, competing with the Class A public stockholders for the trust funds.

The plaintiffs alleged that SPAC fiduciaries withheld material information that MultiPlan's largest client was building an in-house platform to compete with MultiPlan, thus impairing the public shareholders' right to divest their shares prior to the consummation of the transaction.

The defendants moved to dismiss the plaintiffs' claims "primarily, that the plaintiffs have alleged derivative claims but failed to plead demand futility and that the business judgment rule applies."

Delaware had not yet had an opportunity to consider the application of Delaware law to SPACs. Normal fiduciary principles were applied to the plaintiffs' claims despite the novel issues presented. Here, the entire fairness standard applied in the context of a value reducing transaction. The Court of Chancery of Delaware maintained that there were mismatched incentives (i.e., the upside to founder shares versus downside to public stockholders). "But those stockholders were allegedly robbed of their right to make a fully informed decision about whether to redeem their shares. Accordingly, the defendants' motions to dismiss are denied except as to two named defendants."

Delaware Chancery Court Rejects Partnership Valuation in a Freeze-Out as Unfair to Minority Partners

***In Re Cellular Tel. P'ship Litig.*, 2022 Del. Ch. LEXIS 56 (March 9, 2022)**

This was a coordinated action involving 13 partnerships having similar transactions. The opinion here is part of the coordinated trial. The partnership held a license to provide wireless telephone services in the Salem, Ore., area. AT&T, through a holding company, was the owner of 98.119% of the partner interest in the partnership. AT&T directed the day-to-day operations of the partnership and controlled the partnership.

In 2010, AT&T caused the partnership to transfer all of its assets and liabilities to a newly formed LLC (New Salem) in exchange for $219 million in cash and distributed the pro rata share, $4.1 million, of that cash to the minority partners. AT&T continued the operations of the partnership in the New Salem LLC. Thus, the transactions functioned as a "freeze-out" of the minority partners. "The plaintiffs assert that AT&T breached its fiduciary duties by effectuating the Freeze-Out through an unfair process and by paying an unfair price."

Discovery lasted over the better part of eight years. "As the court noted on several occasions, AT&T was the most obstructive litigant that this judge has ever seen, whether in private practice or on the bench." In December 2020, the case proceeded to a coordinated trial.

The entire fairness of review applies, and thus AT&T had the burden of proving that the freeze-out was entirely fair to the minority partners. AT&T failed to prove that. AT&T correctly anticipated large growth in the next decade and sought to capture that increased value for itself. AT&T did not employ any procedural protections for the minority shareholders. AT&T simply hired an outside valuation firm, claiming it was independent when the record showed that the lead partner of that firm had a long-standing relationship with AT&T and allowed internal AT&T personnel to influence the outcome of the valuation.

AT&T also did not prove that it paid a fair price. At trial, it did not rely on the work of the valuation firm it chose but instead brought in a litigation expert who did her own analysis. Neither expert provided persuasive valuation methodologies. "AT&T therefore breached its duty of loyalty by engaging in an unfair and self-interested transaction at the minority partners' expense. As a remedy, this decision awards the plaintiffs damages equal to the difference between the consideration they received, and a pro rata share of the fair value of the Partnership as determined by the court."

The court determined that fair value to be $714 million and the minority partner's shares to be $13.4 million.

U.S. District Court Dismisses Valuation Firm's Plea to Require Insurance Company to Defend a Lawsuit Against It

***Stout Risius Ross, LLC v. Aspen Specialty Ins. Co.*, 2022 U.S. Dist. LEXIS 48760 (March 18, 2022)**

Stout Risius Ross LLC alleged breach of contract and sought a declaratory judgment that Aspen Specialty Insurance Co. was obligated to defend and indemnify Stout Risius Ross in a separate action brought by Stout Risius Ross' former client, Wilmington Trust. Before the court were Aspen's motion to dismiss and Stout Risius Ross' cross-motion for partial summary judgment. "For the reasons set forth below, Aspen's motion to dismiss is GRANTED and Stout's cross-motion for partial summary judgment is DENIED.

Background.

The Brundle action. In October 2013 Wilmington Trust, as trustee of an ESOP plan for Constellis Group Inc., engaged Stout Risius Ross to provide valuation and financial advisory services related to an ESOP transaction. Tim Brundle, on behalf of the ESOP, sued Wilmington Trust in 2015, alleging violations of ERISA. Stout Risius Ross was not a party to the *Brundle* action. "After a bench trial, the district court held on March 13, 2017, that Wilmington had engaged in a prohibited transaction in violation of its fiduciary duties to the ESOP and entered an award of approximately $29.8 million in damages against Wilmington." The court found that Wilmington Trust rushed its valuation and failed to vet Stout Risius Ross' assumptions. Wilmington Trust's reliance on Stout Risius Ross' report was not reasonably justified.

The 4th Circuit affirmed the district court's opinion in March 2019. The 4th Circuit pointed out "four major failures" in Wilmington Trust's reliance on the Stout Risius Ross report. Even after the affirmation, Wilmington Trust continued to engage Stout Risius Ross for other valuation services. By Aug. 23, 2019, Wilmington Trust had satisfied all of the judgement.

The Aspen policy. On Sept. 25, 2019, Aspen and Stout Risius Ross executed a professional liability insurance policy, covering the period from Sept. 1, 2019, through Sept. 30, 2020. The policy was subject to a "prior knowledge" provision, in part as follows: "Prior to any Knowledge Date identified in the Declarations of this Policy, no Insured knew or could have reasonably foreseen that such Wrongful Act or Interrelated Wrongful Acts might give rise to a Claim."

Wilmington Trust sues Stout Risius Ross. On Nov. 12, 2019, Wilmington Trust filed a summons with notice and an unfiled complaint to Stout Risius Ross. Stout Risius Ross notified Aspen. Stout Risius Ross removed the action from a New York court to this court. Stout Risius Ross moved to dismiss. The court dismissed all Wilmington Trust claims except the claim for contribution. Aspen wrote to Stout Risius Ross on Feb. 4, 2020, denying coverage and citing the "knowledge" provision.

Aspen's Motion to Dismiss.

The *Brundle* opinions. Despite Stout Risius Ross' objection to the contrary, the court agreed with Aspen that it may consider the *Brundle* opinions not for the truth of their assertions regarding the Stout Risius Ross valuation, "but rather for their existence and for the fact that Stout's former client Wilmington was subject to a $29.8 million judgment at the end of the *Brundle* Action."

Prior knowledge provision. Aspen argued that any professional with knowledge of the outcomes of the *Brundle* decisions, both of which occurred prior to Sept. 1, 2019, would understand that a claim might be asserted against Stout Risius Ross. Stout Risius Ross argued that the notion that a party could be sued did not meet Aspen's "high bar" of proving that the exclusion applied. The parties agreed that the language was unambiguous, and they agreed that the subjective-objective two-pronged test applies. "Under this test, courts 'must first … consider the subjective knowledge of the insured and then the objective understanding of a reasonable [professional] with that knowledge.'" Aspen has shown that Stout Risius Ross had both subjective and objective knowledge prior to the Sept. 1, 2019, knowledge date. Stout Risius Ross made a number of arguments to support its position that it could not have known that a claim would be made. The court, however, agreed with Aspen that all of these arguments were unavailing or irrelevant.

The court decided that, under the plain terms of the policy, Stout Risius Ross could have reasonably foreseen that its valuation of the Constellis ESOP for Wilmington Trust might give rise to a claim by Wilmington Trust. Accordingly, Stout Risius Ross had failed to state a claim and Aspen's motion to dismiss was granted.

Stout Risius Ross' motion for partial summary

(Continued on page 5)

(Continued from page 4)

judgment. Stout Risius Ross' motion was based on Aspen's duty to defend. In New York, that duty was "broad" with a low burden to show that there was a possibility of coverage triggering. However, the court noted that the "prior knowledge" provision applied and, thus, there was no coverage. Additionally, Stout Risius Ross will not be allowed to amend, and dismissal was with prejudice.

Goodwill Impairments in U.S. Doubled in 2020

Total goodwill impairment in U.S. public companies was $142.5 billion in 2020, more than double the $71 billion recorded in 2019, according to the "2021 U.S. Goodwill Impairment Study" by Kroll. Even so, the level of impairments still fell short of the amount recorded at the onset of the 2008 financial crisis, which was $188.4 billion, the study says.

The study examines general and industry goodwill impairment (GWI) trends of more than 8,900 U.S. publicly traded companies through December 2020. The top three industries with the largest increase in GWI in 2020 were energy, financials and real estate, and industrials. This edition also gives a preview of the 2021 recovery from the COVID-19 pandemic on goodwill impairments taken by U.S.-based public companies. "At the time of writing, the disclosed top 10 GWI events for 2021 reached a combined $5 billion, which pales in comparison to the top 10 in 2020 of $61.9 billion," the study says.

Typical Components of M&A Fees

Presented below are the typical components of M&A fees, per a survey of investment bankers, brokers, and other advisors (per the "Firmex M&A Fee Guide 21/22").

- Retainer/Work Fee
  - 90% of advisors charge a work fee payable regardless of closing a deal.
  - Monthly retainers of $5,000 - $10,000+ are common.
- Success Fee
  - The main fee payable for M&A services is based on a percentage of the value of a successfully consummated deal.
  - The size of the deal is the main determinant of the amount of the success fee percentage charged – the larger the deal, the lower the percentage – with fees generally ranging from 1% (for transactions over $150 million) to 8% (for transactions under $5 million).
  - Success fees are structured as a scaled percentage or a flat percentage.
- Minimum Success Fee
  - A pre-determined, minimum success fee is common on larger deals.
- Breakup Fee
  - More than a third of providers charge a breakup fee if a client does not proceed with a predetermined bona fide offer.
- Reduce Success Fee by Retainer/Work Fee
  - Most providers will deduct work fees from success fees payable.
- Timing of Success Fee Payments
  - Most providers expect full payment at closing, regardless of when purchase price components are payable.
- Expense Reimbursement
  - Most providers expect reimbursement of out-of-pocket expenses; common reimbursable expenses are for travel and virtual data rooms.

The success fee is usually the largest component of an M&A fee payable. While the size of a contemplated transaction is the main determinant of the amount of the success fee charged, other factors are also considered, including: the complexity of the assignment, the risk associated with closing the deal, the overall activity in the market or of the provider, whether there is an existing relationship between

the provider and the client, and whether there are multiple providers making proposals.

VMI provides exceptional M&A services, uniquely tailored to each client's needs with a custom fit plan focused on achieving the client's agreed-upon goals. VMI offers an M&A fee structure that is competitive. As buyers will only proceed if they feel that it's the right fit, we only make proposals for M&A services when we feel that it's the right fit - we are a fit for the client and the client is a fit for us. If we do proceed, we often propose a true success fee, with no retainer/work fee. Thus, the client does not pay unless we close a deal that they want. Feel free to contact Andrew Wilusz to confidentially discuss a contemplated transaction (amw@ValueManagementInc.com).

Strong M&A Outlook in the Food and Beverage Sector

"With an abundance of capital in private equity markets and large corporate players realigning their strategic vision, we believe 2022 is trending toward another strong year of M&A activity in the food and beverage space," reports "Food and Beverage M&A Landscape" (Spring 2022) from Kroll. As for public-company trading multiples in this sector, the median EV/TTM EBITDA multiple is 14.8x (as of March 31, 2022) overall with subsectors ranging from 26.7x (for alcoholic beverages) to 6.5x (for protein producers).

VALUE MANAGEMENT INC.
Investment Banking + Valuation Services

2370 York Road, E2 | Jamison, PA 18929

Address Service Requested

PRSRT FIRST CLASS
U.S. POSTAGE
PAID
HAVERTOWN, PA
PERMIT NO. 45