



The Value of Standards—SSVS No. 1 Bursts on the Scene
Podcast of July 4, 2007



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AICPA Standards on Valuation Services

The AICPA has released the final version of standards for valuation services—standards that can apply if the CPA performs a valuation service when preparing a tax return or performing a tax planning engagement. This standard is referred to as *Statements on Standards for Valuation Services* (abbreviated SSVS), with the current single standard referred to as SSVS No. 1, entitled “Valuation of a Business, Business Ownership Interest, Security or Intangible Asset.”

The detailed standard is posted online at:

http://bvfls.aicpa.org/NR/rdonlyres/672E1DD4-2304-47CA-8F34-8C5AA64CB008/0/SSVS_Full_Version.pdf

The tiny print is due to the long URL the AICPA decided to use. Since the text is copyrighted by the AICPA, I can’t reproduce the text in this document (which would be

the easier way to handle it) without getting permission, so we'll live with the above link. I do suggest you download that standard even if you are not a CPA, since if you work with CPAs they are going to be impacted by this rule.

These standards are mandatory and not optional for most CPAs, due to the fact that most State Boards of Accountancy consider the *AICPA Code of Professional Conduct* to be, at the least, an example of the type of conduct that constitutes compliance with state accountancy laws and regulations. Under the *Code of Professional Ethics* bodies designated by the AICPA Council to promulgate technical standards set binding guidance under Rule 201. The Consulting Services Executive Committee, under whose authority these standards have been issued, is one such body.

These standards will be effective for engagements entered into after January 1, 2008.¹

Valuations and Tax Work

Tax practice in many cases involves valuations of various items. For instance, the federal estate and gift taxes are, at their heart, based on the value of the property involved in the transfer. Similarly, for both defined benefit and defined contribution employee benefit plans, the value of the assets in the plan needs to be established as a routine part of the annual compliance work or to compute items like the required annual minimum distribution.

SSVS No. 1 does not impact every case where an item must be valued—rather, it is restricted to certain valuations of certain specific type of interests, when the CPA undertakes to perform certain actions. For most CPAs the issue will be to keep from accidentally triggering these standards, as in that case the failure to follow the standard will expose the CPA to both civil liability to the client for malpractice and potential professional sanction.

What Types of Assets the Standard Applies To

The first key limiting item is that the engagement must involve one of the types of assets that SSVS No. 1 creates standards for. Paragraph 1 of SSVS provides the following list of items that the standard applies to:

01. This Statement establishes standards for AICPA members (hereinafter referred to in this Statement as members) who are engaged to, or, as part of another engagement, estimate the value of a business, business ownership interest, security, or intangible asset (hereinafter collectively referred to in this Statement as subject interest). For purposes of this Statement, the definition of a business includes not-for-profit entities or activities.

Note that even though the standard purports to apply only to AICPA members, as noted above, most State Boards have managed to effectively apply these standards to their

¹ SSVS No. 1, ¶79

licensees—so dropping your AICPA membership doesn't solve this matter unless your State Board has indicated they won't consider these standards enforceable. And even then, it's likely that opposing counsel in a malpractice case won't be quite so understanding.

The terms noted above are defined in two appendices to the standard. Appendix B is the International Glossary of Business Valuation Terms (IGBVT) which has been developed by the AICPA, American Society of Appraisers (ASA), Canadian Institute of Chartered Business Valuators, the National Association of Certified Valuation Analysts and the Institute of Business Appraisers. Appendix C contains terms that are not defined in that document, and so are SSVS specific.

The four classes of applicable assets are defined as follows:

- Business – (uses the definition of “business enterprise” from the IGBVT) a commercial, industrial, service, or investment entity (or a combination thereof) pursuing an economic activity.
- Business Ownership Interest – (from Appendix C) A designated share in the ownership of a business (business enterprise).
- Security – (from Appendix C) A certificate evidencing ownership or the rights to ownership in a business enterprise that (1) is represented by an instrument or by a book record or contractual agreement, (2) is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment, and (3) either one of a class or series or, by its terms, is divisible into a class or series of shares, participations, interests, rights, or interest-bearing obligations.
- Intangible Asset – (from the IGBVT) nonphysical assets such as franchises, trademarks, patents, copyrights, goodwill, equities, mineral rights, securities, and contracts (as distinguished from physical assets) that grant rights and privileges and have value for the owner.

The SSVS will refer to these assets as subject interests—so by definition that's an asset that falls into one of these four classes.

So a CPA in a tax engagement that is faced with an issue of the value of an asset must first look to see if the asset in question falls into one of these categories. If it does not, the standard would not apply. If it does, then the CPA must next consider whether or not the actions he/she is engaged to perform with regard to the value of that asset is covered by this standard.

Engagements Covered

If a subject interest is involved, then the question becomes when the activities the CPA is engaged to perform will trigger the application of these standards to the activity. Since

these standards provide performance, documentation and communication requirements, the applicability of these standards will have a significant impact on the work the CPA will be required, at a minimum, to perform.

As was noted in the quotation from the standard above, the standard applies when a CPA is engaged to estimate the value of a subject interest. The standard defines such an engagement as noted below:

As described in this Statement, the term engagement to estimate value refers to an engagement or any part of an engagement (for example, a tax, litigation, or acquisition-related engagement) that involves estimating the value of a subject interest.²

Note that the standard specifically includes tax engagements as potentially falling under its scope. The standard goes on to note the following:

An engagement to estimate value culminates in the expression of either a conclusion of value or a calculated value (see paragraph 21).³

As noted, paragraph 21 contains the description of those two types of engagements, described as “valuation engagements” and “calculation engagements” respectively.

21. There are two types of engagements to estimate value—a valuation engagement and a calculation engagement. The valuation engagement requires more procedures than does the calculation engagement. The valuation engagement results in a conclusion of value. The calculation engagement results in a calculated value.

The standard notes that the understanding with the client determines the type of engagement—obviously leading to standards that define what is required in that understanding and how it must be documented.⁴ CPAs who fail to recognize that they have triggered this standard may find a number of presumptions they won’t like will be applied to the type of engagement they were engaged to perform when the documentation of a specific understanding doesn’t exist. Obviously, it’s strongly preferred that any such understanding be in writing and specifically address the matters discussed in paragraphs 16 and 17.

Valuation Engagement

The valuation engagement, which is the most involved and would likely be the one deemed to have been accepted if there is any ambiguity on the matter, is further defined as noted below:

² SSVS No. 1, ¶2

³ SSVS No. 1, ¶2

⁴ SSVS No. 1, ¶16 and 17

A valuation analyst⁵ performs a valuation engagement when (1) the engagement calls for the valuation analyst to estimate the value of a subject interest and (2) the valuation analyst estimates the value (as outlined in paragraphs 23–45) and is free to apply the valuation approaches and methods he or she deems appropriate in the circumstances. The valuation analyst expresses the results of the valuation as a conclusion of value; the conclusion may be either a single amount or a range.

The key issue here is the CPA’s freedom to apply the approaches and methods he deems appropriate to determine the value. As noted above, if there is not a written understanding, it will be likely the client will claim he left these matters to the judgement of the CPA in question—a position that would cause the CPA to be stuck with a valuation engagement.

Paragraphs 23-45 contain detailed information about the types of methods and approaches the CPA would consider and the type of information the CPA would obtain. The valuation engagement results in either a detailed report or a summary report.⁶ The choice of type of report to issue is based on the level of reporting detail agreed to by the CPA and the client, again suggesting that in the absence of agreement to a summary report the detailed report is likely going to be the presumed report that the CPA should have issued. The use of either of these reports to communicate the results of a calculation engagement is prohibited.⁷

The contents of a detailed report are found at ¶51 that states

The detailed report is structured to provide sufficient information to permit intended users to understand the data, reasoning, and analyses underlying the valuation analyst’s conclusion of value. A detailed report should include, as applicable, the following sections titled using wording similar in content to that shown:

- Letter of transmittal
- Table of contents
- Introduction
- Sources of information
- Analysis of the subject entity and related nonfinancial information
- Financial statement/information analysis
- Valuation approaches and methods considered
- Valuation approaches and methods used

⁵ “Valuation Analyst” is the term used to refer to the CPA covered by this standard.

⁶ A CPA may be exempted from the reporting, *but not the performance*, portion of SSVS No. 1 in certain legal proceedings. See SSVS No. 1, ¶50.

⁷ SSVS No. 1, ¶48

- Valuation adjustments
- Nonoperating assets, nonoperating liabilities, and excess or deficient operating assets (if any)
- Representation of the valuation analyst
- Reconciliation of estimates and conclusion of value
- Qualifications of the valuation analyst
- Appendices and exhibits

The above listed report sections and the detailed information within the sections described in the following paragraphs 52–77 may be positioned in the body of the report or elsewhere in the report at the discretion of the valuation analyst.⁸

Since each of those sections are required in the detailed report “as appropriate” a CPA whose report omits one of those items could expect to be asked, if their work is questioned, why that information was not needed to meet the stated goal of a detailed report to communicate the items noted in the first sentence of ¶51. As noted, the standard goes on to give more information about the items listed to be included in the detailed report.

While theoretically a detailed report can be an oral rather than written report,⁹ a CPA who attempts to rely on the claim that he/she told the client all of that information may find his client’s memory won’t be terribly clear on that fact—nor, reasonably, would we expect to be even if the client was being scrupulously honest in his recollection of any conversations. So a CPA likely shouldn’t expect to rely on the lack of a requirement for a written report to save the day if challenged on whether the CPA complied with the reporting requirement.

The more limited summary report may initially sound attractive—until you take a look at the list of minimum items to be included which is, amusingly, a longer list than the one we find for a detailed report. To be fair, the level of detail provided will be much more restricted—but this report is not going to be covered by a single sentence vague reference. The standard notes:

71. A summary report is structured to provide an abridged version of the information that would be provided in a detailed report, and therefore, need not contain the same level of detail as a detailed report. However, a summary report should, at a minimum, include

the following:

- a. Identity of the client

⁸ SSVS No. 1, ¶51

⁹ SSVS No. 1, ¶47

- b. Purpose and intended use of the valuation
- c. Intended users of the valuation
- d. Identity of the subject entity
- e. Description of the subject interest
- f. The business interest's ownership control characteristics, if any, and its degree of marketability
- g. Valuation date
- h. Valuation report date
- i. Type of report issued (namely, a summary report) (paragraph 48)
- j. Applicable premise of value
- k. Applicable standard of value
- l. Sources of information used in the valuation engagement
- m. Assumptions and limiting conditions of the valuation engagement (paragraph 18)
- n. The scope of work or data available for analysis including any restrictions or limitations (paragraph 19)
- o. Any hypothetical conditions used in the valuation engagement, including the basis for their use (paragraph 22)
- p. If the work of a specialist was used in the valuation (paragraph 20), a description of how the specialist's work was used, and the level of responsibility, if any, the valuation analyst is assuming for the specialist's work
- q. The valuation approaches and methods used
- r. Disclosure of subsequent events in certain circumstances (paragraph 43)
- s. Any application of the jurisdictional exception (paragraph 10)
- t. Representation of the valuation analyst (paragraph 65)
- u. The report is signed in the name of the valuation analyst or the valuation analyst's firm
- v. A section summarizing the reconciliation of the estimates and the conclusion of value as discussed in paragraphs 68 and 69
- w. A statement that the valuation analyst has no obligation to update the report or the calculation of value for information that comes to his or her attention after the date of the valuation report

72. Appendices or exhibits may be used for required information (paragraph 70) or information that supplements the summary report. Often, the assumptions, limiting conditions, and the valuation analyst's representation are provided in appendices to the summary report.

Calculation Engagement

The other type of engagement is a calculation engagement. That is defined as noted below:

A valuation analyst performs a calculation engagement when (1) the valuation analyst and the client agree on the valuation approaches and methods the valuation analyst will use and the extent of procedures the valuation analyst will perform in the process of calculating the value of a subject interest (these procedures will be more limited than those of a valuation engagement) and (2) the valuation analyst calculates the value in compliance with the agreement. The valuation analyst expresses the results of these procedures as a calculated value. The calculated value is expressed as a range or as a single amount. A calculation engagement does not include all of the procedures required for a valuation engagement (paragraph 46).

The key difference is that in a calculation engagement the CPA does not exercise his professional judgment to select the valuation approaches and methods that will be used (presumably using the one he/she decides the most appropriate). Rather, the CPA and client agree on the approaches and methods that will be mechanically applied without regard to whether they are the approaches and methods the CPA would have selected had he provided his own professional judgment to select the appropriate ones.

However, it's important to note that merely avoiding selecting the valuation approaches and methods won't remove an engagement from this standard—it just lowers the requirements somewhat.

Paragraph 73 begins the description of a calculation report. It provides:

As indicated in paragraph 48, a calculation report is the only report that should be used to report the results of a calculation engagement. The report should state that it is a calculation report. The calculation report should include the representation of the valuation analyst similar to that in paragraph 65, but adapted for a calculation engagement.

Note the requirement that a calculation report state that it is a calculation report. Presumably if a report doesn't make that statement, it will be presumed under the standards to be a report on a valuation arrangement, at which point a user would be able to argue that they had reasonably relied on the implied representation that the CPA had decided the approaches and methods were the most appropriate ones to arrive at a value for the purpose of this valuation.

There are also a list of items that need to be in a calculation report if they apply. Again, if they are left out presumably it's because they do not apply.

The calculation report should identify any hypothetical conditions used in the calculation engagement, including the basis for their use (paragraph 22), any application of the jurisdictional exception (paragraph 10), and any assumptions and limiting conditions applicable to the engagement (paragraph 18). If the valuation analyst used the work of a specialist (paragraph 20), the valuation analyst should describe in the calculation report how the specialist's work was used and the level of responsibility, if any, the valuation analyst is assuming for the specialist's work. The calculation report may also include a disclosure of subsequent events in certain circumstances (paragraph 43).¹⁰

Thus, for instance, if no hypothetical conditions are disclosed presumably the CPA is "vouching" for his belief that the conditions presumed are the actual conditions and/or most likely future conditions. Similarly, if no specialist is identified, the CPA is presumed to take full responsibility for all work involved in the valuation.

Finally, there is a list of required items for a calculation report:

The calculation report should include a section summarizing the calculated value. This section should include the following (or similar) statements:

- a. Certain calculation procedures were performed; include the identity of the subject interest and the calculation date.
- b. Describe the calculation procedures and the scope of work performed or reference the section(s) of the calculation report in which the calculation procedures and scope of work are described.
- c. Describe the purpose of the calculation procedures, including that the calculation procedures were performed solely for that purpose and that the resulting calculated value should not be used for any other purpose or by any other party for any purpose.
- d. The calculation engagement was conducted in accordance with the Statement on Standards for Valuation Services of the American Institute of Certified Public Accountants.
- e. A description of the business interest's characteristics, including whether the subject interest exhibits control characteristics, and a statement about the marketability of the subject interest.
- f. The estimate of value resulting from a calculation engagement is expressed as a calculated value.

¹⁰ SSVS No. 1, ¶74

- g. A general description of a calculation engagement is given, including that (1) a calculation engagement does not include all of the procedures required for a valuation engagement and (2) had a valuation engagement been performed, the results may have been different.
- h. The calculated value, either a single amount or a range, is described.
- i. The report is signed in the name of the valuation analyst or the valuation analyst's firm.
- j. The date of the valuation report is given.
- k. The valuation analyst has no obligation to update the report or the calculation of value for information that comes to his or her attention after the date of the report.¹¹

An example report is shown at paragraph 77 of the standard.

Excluded Engagements

A number of engagements are excluded from the application of this standard. These exceptions are documented in paragraphs 5-10 of the standard.

Attest engagements (such as audits, compilations and reviews) are the first group of excluded engagements

This Statement is not applicable to a member who participates in estimating the value of a subject interest as part of performing an attest engagement defined by Rule 101 of the AICPA Code of Professional Conduct (for example, as part of an audit, review, or compilation engagement).¹²

If the value is provided to the CPA by another party (including the client), the standard does not apply:

This Statement is not applicable when the value of a subject interest is provided to the member by the client or a third party, and the member does not apply valuation approaches and methods, as discussed in this Statement.¹³

This particular exception is one that may be often encountered in tax practice, and may be the most useful for those in tax practice to use to assure they do not trigger this standard. It will be important to document that if the CPA is obtaining the value from the client that the client agrees they are the ones to provide the value.

Accountants doing a valuation as employee for an employer's internal use is not required to comply with this standard—but note that the exception would not apply if the

¹¹ SSVS No. 1, ¶76

¹² SSVS No. 1, ¶5

¹³ SSVS No. 1, ¶6

accountant was aware the valuation would be used by outsiders (like a lender) or if the CPA is deemed to be in public practice (such as if a controller did a valuation for some party other than his/her employee, such as helping out a neighbor who needs to value his business for a personal financial statement).

This Statement is not applicable to internal use assignments from employers to employee members not in the *practice of public accounting*, as that term is defined in the AICPA *Code of Professional Conduct* (AICPA, *Professional Standards*, vol. 2, ET sec. 92. 25). (Interpretation No. 1, “Scope of Applicable Services” of *Statement on Standards for Valuation Services*, Illustrations 24 and 25).¹⁴

Economic damage calculations are not covered by this standard unless the determination has an engagement to estimate value.

This Statement is not applicable to engagements that are exclusively for the purpose of determining economic damages (for example, lost profits) unless those determinations include an engagement to estimate value. See also Interpretation No. 1, Illustrations 1, 2, and 3.¹⁵

Illustration 3 of the interpretation outlines a case where the standard may apply, depending on whether the damages being measured related to a startup business are for lost profits (not a problem) or the loss of value of the business (would trigger the standards).

Mechanical computations are another exception that may be useful in tax practice. The mechanical computation exception is defined as follows:

This Statement is not applicable to mechanical computations that do not rise to the level of an engagement to estimate value; that is, when the member does not apply valuation approaches and methods and does not use professional judgment. See Interpretation No. 1, Illustration 8.¹⁶

For example, if a valuation is done by applying straight mathematical factors from a table with no professional judgment involved, then SSVS No. 1 is not triggered. That would include, as well, valuing a small block of publicly traded stock using a market price at a point in time.¹⁷

If it is not practical to obtain relevant information, the standard does not apply.

¹⁴ SSVS No. 1, ¶7

¹⁵ SSVS No. 1, ¶8

¹⁶ SSVS No. 1, ¶9(a)

¹⁷ A “small block” would be an amount of stock that is not enough to, by itself, significantly influence the price of the stock in question if it were sold. For most situations that a tax CPA runs into with public companies and shares held by their clients, this exception will clearly apply—and when it doesn’t the CPA would generally be very aware of that fact (the client has a large block of the stock of the company).

This Statement is not applicable when it is not practical or not reasonable to obtain or use relevant information; as a result, the member is unable to apply valuation approaches and methods that are described in this Statement.¹⁸

However, CPAs need to note the footnote reference at the end of this paragraph—that if the information comes from client estimates that you find to be reasonable, the exception appears to evaporate:

Unless prohibited by statute or by rule, a member may use the client's estimates for compliance reporting to a third party if the member determines that the estimates are reasonable (based on the facts and circumstances known to the member). See Interpretation No. 1, "Scope of Applicable Services" of Statement on *Standards for Valuation Services* and *Statement for Standards on Tax Services* No. 4

In essence, if you state that it was impossible to obtain the information and you still produce a valuation, you would seem to be saying indirectly that you did not believe the client's estimates on those matters were reasonable.

There is also a limited exception for issues where other authorities conflict with some specific provisions in SSVS No. 1. The exception extends only to the item of conflict, and on all other issues compliance with SSVS is required.

If any part of this Statement differs from published governmental, judicial, or accounting authority, or such authority specifies valuation development procedures or valuation reporting procedures, then the valuation analyst should follow the applicable published authority or stated procedures with respect to that part applicable to the valuation in which the member is engaged. The other parts of this Statement continue in full force and effect (Valuation Services Interpretation No. 1).¹⁹

Tax Practice Application

At the same time that SSVS No. 1 was issued, the Consulting Services Executive Committee issued Interpretation No. 1-01. The interpretation gives official standing to what was originally an unofficial explanatory set of questions and answers to explain application of this standard to various engagements. The illustrations deal with a number of issues that tax practitioners might expect to run into.

Illustration 6 outlines the general rules that tax practitioners will need to understand to deal with the SSVS in tax practice:

¹⁸ SSVS No. 1, ¶9(b)

¹⁹ SSVS No. 1, ¶10

16. *Illustration 6.* When does the Statement apply to members who determine values related to tax reporting and planning engagements?

17. *Conclusion.* The Statement applies when the member is engaged to estimate the value of a business, business ownership interest, security, or intangible asset (SSVS paragraph 1). The application of valuation approaches and methods and the use of professional judgment (SSVS paragraph 4) are required, unless an exception applies (SSVS paragraphs 5 through 10).

Despite protests from some in tax practice during the exposure period, no general purpose tax exception was placed in these standards. Note this is fundamentally different from the *Statements on Standards for Accounting and Review Services* where tax returns were simply defined not to be financial statements to which those standards would apply, despite the fact that corporate and partnership tax returns contain much the same information as is contained in documents that do meet the definition of financial statements.²⁰

For SSVS No. 1 the fact that the number is used solely for a tax return engagement has no impact on whether the standard must be applied.

Illustration 7 deals with the required reporting in the case of a tax return engagement.

Illustration 7. If the sole purpose of an engagement is reporting a value in a tax return and the Statement applies to this engagement, are any separate reports (specifically, valuation reports) required to be issued? To whom are those reports required to be provided? Is a report required to be attached to the tax return? Are any specific disclosures required?

19. *Conclusion.* The Statement requires the preparation of a written or oral valuation report (SSVS paragraphs 47–78) that is communicated to the client (SSVS paragraph 47) but does not require that any report be attached to the tax return or mandate any other tax-specific disclosures. In limited circumstances, a taxing authority may require its own report, which would obviate the need for a separate valuation report (SSVS paragraph 10 and *Illustration 18*). There is also a reporting exemption for certain controversy proceedings (SSVS paragraph 50 and *Illustration 4*).

Unlike *SSARS*, there is no issue here of needing to attach the report to the item being reported upon, or to make any notation on that document about the existence of a report. The seeming contradiction may make more sense when you remember that attest is all about giving assurance (or lack of assurance) to third parties, while these standards are about reporting information to the client that engaged the expert for valuation.

²⁰ In fact, if everything on a standard corporate tax return were transcribed to a blank piece of paper, that resulting document would clearly be a financial statement as the *SSARS* define it.

That distinction may also explain why the Accounting and Review Services Committee felt they had to make a tax return exception for compilations and reviews, while the Consulting Services Committee believed no such exception was warranted for valuation reports.

Mechanical computations are covered in Illustration 8.

20. *Illustration 8.* Are mechanical computations of value, for example, computations using actuarial tables, excluded from the Statement?
21. *Conclusion.* Mechanical computations of value are excluded from the Statement if they do not rise to the level of an engagement to estimate value, that is, if the member does not apply valuation approaches and methods, and does not use professional judgment, as described in the Statement (SSVS paragraph 9(a)).
22. Examples of services that do **not** rise to the level of an engagement to estimate value include: (a) computations of a remainder interest under a grantor retained annuity trust (GRAT) using actuarial tables; (b) determining the value of relatively small blocks (relative to the total amount of corporate stock outstanding) of publicly traded stock whose per share price is readily ascertainable; (c) preparing a tax return using the valuation of a business that was provided by a third-party appraiser, or by the client (SSVS paragraph 6); and (d) calculating cash “hold back” requirements for tax contingencies (SSVS paragraphs 1,4, and 9(a)).
23. Examples of services that rise to the level of an engagement to estimate value include: (a) valuing a block of publicly traded stock, if the analysis includes consideration of a discount for blockage, lock- up, or other contractual or market restrictions such that valuation approaches and methods are applied, and professional judgment is used to determine the fair value, fair market value, or other applicable standard of value; (b) valuing stock that is not publicly traded; and (c) computing the fair market value of assets in a charitable remainder trust (CRT), if the engagement requires the application of valuation approaches and methods, and the use of professional judgment to estimate the fair market value.

Note that the valuation of non-publicly traded stock would always, under the interpretation, fail the “mechanical” test.

Illustration 9 deals with the limitations of the jurisdictional exception—it is not a panacea for tax practice, as it only grants a pass on those parts of an engagement where tax rules would conflict with SSVS No. 1—otherwise the CPA must comply with the standard.

24. *Illustration 9.* Does the “jurisdictional exception” (SSVS paragraph 10) provide that an engagement to estimate value is not subject to the Statement if a member determines and reports values using procedures mandated or allowed by the Internal Revenue Code (IRC), Internal Revenue Service (IRS) regulations, court cases, or other published guidance and other sources of federal, state, and

local law solely for purposes of tax return preparation and other tax services using these methods?

25. *Conclusion.* No, the “jurisdictional exception” would not exempt the engagement from this Statement, even if the engagement’s sole purpose was to value a subject interest (SSVS paragraph 1) for tax reporting purposes. Only the portion of the Statement that differs from the published governmental or judicial authority is superseded for purposes of the engagement. The remainder of the Statement applies to the engagement.

In this case, we are looking a similar standard as is applied for tax basis financial statements in the attest arena. If the tax law conflicts with the regular standards, you follow the tax law—but if the tax law is silent on the issue, the CPA follows the regular standards.

Illustrations 10 and 11 will be of interest to CPAs assisting with estate planning—and also should be of interest to attorneys working with the client’s CPA to provide such services who have come to rely on the CPA doing a “rule of thumb” valuation for planning purposes.

Illustration 10 deals with the valuation for a partnership.

26. *Illustration 10.* Is an interest in a publicly traded partnership whose shares are frequently traded considered a “security” under the Statement? Is an interest in a family limited partnership (FLP), or in another nontraded partnership, considered a “security” under the Statement?

27. *Conclusion.* Whether interest constitutes a “security” is a legal determination. However, where the value of a security is readily ascertainable, a valuation analyst does not need to apply valuation approaches and methods and use professional judgment. Accordingly, the valuation of such an interest would not be subject to the Statement (SSVS paragraphs 1 and 9(a)). An interest in a nonpublicly traded partnership, such as an FLP, whether considered a security or not, is a business ownership interest. The valuation of such nonpublicly traded interest requires the application of valuation approaches and methods and the use of professional judgment, and, accordingly, would be subject to the Statement (SSVS paragraphs 1, 4, and *Illustration 6*), unless the exception under SSVS paragraph 9(b) applies (*Illustration 13e*). If the engagement requires the valuation analyst to consider and apply adjustments, for example, valuation discounts or premiums, then the engagement would be subject to the Statement.

The key factor to note here is the partnership interest would be a business interest, so a nonpublicly traded partnership (virtually all FLPs would meet this test) would generally be an entity that would bring an engagement under these rules.

Illustration 11 is a detailed estate planning discussion, and illustrates some of the nuances that have to be considered when attempting to apply this standard to such an engagement.

28. *Illustration 11*. A client engages a member to provide advice for planning purposes (such as estate planning, personal financial planning, or merger and acquisitions planning). The client holds an ownership interest in a family business being operated as a limited liability company, an interest in a private real estate limited partnership, publicly traded stock, a personal residence, and a retirement account (not an IRA). Is this a valuation engagement subject to the Statement?

29. *Conclusion*. It depends. Providing technical advice, without reference to values for the various assets, is not subject to the Statement. However, if a member calculates a value to illustrate various planning options, he or she may fall under the Statement with regard to various assets. If one or more of the assets for which value is to be determined for purposes of the plan illustrations is a business, business ownership interest, security, or intangible asset, and the client or a third party does not provide the values for these assets, or the member does not use assumed or hypothetical values as part of the overall engagement, the member performing the valuation(s) is subject to the Statement with regard to these assets (SSVS paragraph 1 and *Illustration 6*). In this example, if the member applies valuation approaches and methods and uses professional judgment to determine the value of the ownership interest in the family business or the interest in the private real estate limited partnership in order to provide planning advice, the Statement would apply. In contrast, if the client or a third party provides the values for these assets, or the member uses assumed or hypothetical values, the Statement would not apply because the member would not be applying valuation approaches and methods and using professional judgment. In addition, the exception under SSVS paragraph 9(b), where it is not practical or reasonable to obtain or use relevant information, could apply (see *Illustration 13e*). The computation of the “estimated estate tax” or other taxes once the values have been determined, assumed, or provided is not subject to the Statement, as the computation is a tax computation but would be subject to the Statement on Standards for Tax Services (*Illustration 10* at paragraph 27 of this Interpretation).

It is important to note that if the values presented are hypothetical (say, indicating a number we’d use for preliminary purposes prior to getting a formal outside appraisal) or provided by the client, the standard does not apply. Similarly, it may be possible that a “not practical” position could be taken for a preliminary estimate that is going to be used to determine if it is worthwhile to go forward—but that position is on more shaky ground, and could become even more troublesome if the client decides that this “rough estimate” is good enough when faced with the proposed fee for a formal valuation by an outside appraiser.

Illustration 12 is really a whole set of illustrations regarding situations where an estimate of value is a portion of a larger tax engagement. This set of examples is prefaced by the paragraph below:

30. *Illustration 12.* There are many instances where a tax engagement involves the need for a member to estimate value. The estimation of value may not be the primary purpose of the engagement, but rather a necessary task to perform or item to consider, when making a tax determination concerning the reporting of a transaction on a tax return.

The interpretation goes on to deal with each of the following specific situations and gives advice on the applicability of SSVS No. 1.

The first example deals with a determination of whether an entity would be able to service a debt in order to make a determination on the debt's deductibility.

31. *Illustration 12a.* A member has been engaged to determine the deductibility of interest on a nonrecourse loan. Under applicable regulations, interest on a nonrecourse loan cannot be deducted if it is clear that the company will be unable to service the debt. For purposes of tax reporting, a conclusion must be reached concerning the ability of the company to service the debt. Is this considered a valuation engagement subject to the Statement?

32. *Conclusion.* This is not a valuation engagement covered by the Statement because it is not the valuation of a subject interest (SSVS paragraph 1). This example is a debt-service analysis.

The next example deals with a situation that would arise with any tax that is based on value, such as an intangibles tax, in a situation where the taxpayer must report a value on the return.

33. *Illustration 12b.* There are compliance filings that require an estimate of the value of a company. For example, the "market value" of "intangible personal property," as defined by a state's taxing authority may need to be reported annually on an intangible personal property tax return. A client has a subject interest that is considered intangible personal property for purposes of the return. The member has been engaged to prepare the tax return. Is this a valuation engagement subject to the Statement?

34. *Conclusion.* It depends. If the state requires an estimation of the value of a subject interest, and the estimation of value requires the application of valuation approaches and methods and the use of professional judgment (SSVS paragraphs 1 and 4), the Statement applies. If, however, the client or a third-party appraiser provides the value of the subject interest to the member, the Statement does not apply (SSVS paragraphs 1 and 6). In addition, the exception under SSVS paragraph 9(b), where it is not practical or reasonable to obtain or use relevant information, could apply (*Illustration 13e*). Alternatively, if the state follows more informal rules where the application of valuation approaches or valuation methods are not necessary, the Statement does not apply (SSVS paragraph 4).

Again the CPA would have to comply if professional judgment is used unless the client or a third party provided the value, or the CPA came to the conclusion it was impractical to obtain the information. Of course, the conclusion that it was impractical to obtain the information could be problematical if the taxing agency examines the return at issue, since it would seem to be an admission up front that the valuation is potentially less reliable and might suggest it would be worthy to challenge.

The next example deals with a situation that occurs quite often in tax practice when basis must be allocated based on the fair value of the various assets.

35. *Illustration 12c.* There are times when a member must allocate value among various assets. For example, IRC sections 1060 and 338 require the allocation to assets, based on relative values, of consideration paid. In partnership taxation, there may be allocations under IRC sections 754, 743, and 734 and special tax basis adjustments for partnerships (sales or exchanges and transfers at or upon death) may require an allocation of value among various partnership assets. Are these types of allocations engagements to estimate value subject to the Statement?

36. *Conclusion.* It depends. If one or more of the assets to which value is to be allocated is a subject interest (that is, a business, business ownership interest, security, or intangible asset), and the client or a third party did not provide the member with a value for those assets, then the member performing the allocation would be subject to the Statement, and the member is required to apply valuation approaches and methods, and use professional judgment to value those assets (SSVS paragraphs 1, 4, and *Illustration 6*), unless an exception applies (SSVS paragraphs 5–10). For example, in an IRC section 1060 allocation, after the allocation of purchase price to cash, receivables, inventory, and depreciable tangible assets, there is a residual amount of value allocable to goodwill or going concern. The mechanical assignment of the residual amount to goodwill or going concern is not subject to the Statement. However, if the member allocates this residual amount to specific intangible assets (such as to various customer-based and supplier-based intangibles), such allocation is based on the assets' relative values. Because the member applies valuation approaches and methods and uses professional judgment to value those specific intangible assets, the Statement applies.

Note the last half of the answer, and the importance of whether intangibles are valued based on a purely mechanical approach (allocation of the residual) or if there is an allocation among the intangible assets based on the value of the each. The latter triggers the application of the standards.

Family limited partnerships are again dealt with in *Illustration 12d*, emphasizing that the fact that a CPA doesn't apply a discount doesn't take the engagement out of the realm of SSVS No. 1.

37. *Illustration 12d.* If the member does not apply any discount and simply computes the fair market value of an interest in a family limited partnership (FLP) for tax purposes, is this a valuation engagement subject to the Statement?

38. *Conclusion.* Yes, the Statement applies if the member determines the value of the FLP or an interest in an FLP. The application of valuation approaches and methods, and the use of professional judgment are required, unless an exception applies (SSVS paragraphs 5–10). The fact that the member does not apply a discount does not exempt the engagement from the Statement (SSVS paragraphs 1–4 and 9(a)).

Charitable remainder trusts (among other types of entities) require annual valuations—and the interpretation notes that the nature of the underlying assets will determine if SSVS No. 1 is applicable.

39. *Illustration 12e.* Would the Statement apply to the computation of the fair market value of assets in, or the computation of the required distribution of, a charitable remainder trust (CRT)?

40. *Conclusion.* It depends on the underlying assets held by the CRT. The Statement would apply only if the member determines the value of a business, business ownership interest, security, or intangible asset (SSVS paragraph 1). To the extent that the CRT holds assets that, to be valued, require the application of valuation approaches and methods, and the use of professional judgment, such as an interest in a limited liability corporation (LLC), the Statement would apply. However, if the CRT only holds publicly traded stock with a readily ascertainable value, the Statement would not apply because valuation approaches and methods and professional judgment would not be needed in the computation (SSVS paragraphs 1 and 4, and *Illustration 6*).

Generally, a CRT consisting of a diversified portfolio of publicly traded securities won't present any issues—but one that holds nonpublicly traded stock would trigger these rules. Of course, most CPAs were aware that such assets in the CRTs presented issues in any event.

Partnership asset contribution rules can require tracking the fair market value of assets contributed by partners at the time of contribution. Example 12f points out that, depending on the assets contributed, SSVS No. 1 may be triggered.

41. *Illustration 12f.* In circumstances in which the value of assets contributed by partners to a partnership differ from their cost basis, each difference must be tracked for tax purposes under IRC section 704(c) so that amounts of gain or loss can be properly assigned to the contributing partners. Are these types of asset value assignments valuation engagements subject to the Statement?

42. *Conclusion.* It depends. If one or more of the assets for which value is relevant under IRC section 704(c) is a subject interest that is, a business, business

ownership interest, security, or intangible asset, and the client or a third party does not provide the valuation, and the member applies valuation approaches and methods and uses professional judgment to value these assets for IRC section 704(c) tax purposes, then the Statement applies (SSVS paragraphs 1 and 6, and Illustration 6).

Cost segregation studies generally won't present problems under this standard due to none of the assets being subject interests, as is pointed out in Illustration 12g:

43. *Illustration 12g.* A member has been engaged to perform a cost segregation study. The study involves an analysis of the costs of building a structure and the allocation of such costs to the real and personal property components of the structure so that depreciation of those components may be properly computed. Is this a valuation engagement subject to the Statement?

44. *Conclusion.* No, none of the assets constitutes a subject interest (SSVS paragraph 1).

Illustration 12g points out that in determining if a client qualifies for relief under the insolvency option in Section 108 a CPA may end up getting yanked into an engagement subject to SSVS No. 1.

45. *Illustration 12h.* A member has been engaged to provide advice to a company regarding the tax planning for income from discharge of indebtedness under IRC section 108. The company has advised the member that the company will be able to negotiate a settlement in complete satisfaction of an obligation at 30 cents on the dollar. Is this a valuation engagement subject to the Statement?

46. *Conclusion.* It depends. Under IRC section 108(a), gross income of the company excludes income from discharge of indebtedness only under certain circumstances. One of those circumstances is the insolvency of the company. Under IRC section 108(d) (3), insolvency results from an excess of liabilities over the fair market value of assets. If (a) the company must rely on the insolvency provisions of IRC section 108; (b) one or more of the assets for which value is relevant under IRC section 108 is a subject interest (that is, a business, business ownership interest, security, or intangible asset); (c) the company or a third party does not provide the valuation; and (d) the member applies valuation approaches and methods, and uses professional judgment to value the subject interest(s) for purposes of the IRC section 108(d)(3) insolvency determination, the Statement applies.

Illustration 13 is a comprehensive example dealing with issues that arise in preparing an estate return. Since the starting point of an estate tax return is the value of the assets being transferred, clearly there is exposure to SSVS engagements, so this particular illustration looks at a number of assets that might exist in an estate. The basic outline of

the assets in the example estate is found in the introductory paragraph to the set of examples.

47. *Illustration 13.* An executor has engaged a member to prepare an estate tax return, which requires determining values for the following estate assets: (a) shares in a publicly traded company, “TI Corporation,” whose shares are infrequently traded; (b) a large block of stock in “LB Corporation,” a publicly traded company; (c) a brokerage account consisting of shares in various publicly traded companies; (d) “CHB Corporation,” a closely held business owned by the decedent and the decedent’s family; and (e) a 5 percent interest in “RP,” a privately held rental real estate partnership. Does the Statement apply to any of the following assets owned by the estate? (See *Illustration 10* at paragraph 27 of this Interpretation regarding the valuation of a security.)

The first example deals with the publicly traded stock whose shares are infrequently traded, which creates a “maybe” answer, as explained below.

48. *Illustration 13a.* Does the Statement apply to shares in a publicly traded company, “TI Corporation,” whose shares are traded infrequently?

49. *Conclusion.* It depends; although the price of a share of publicly traded stock is ascertainable from published sources, there are no definitive criteria that would indicate when the Statement applies to shares that are infrequently traded. A key consideration is the average daily trading volume of TI Corporation stock on or around the valuation date. The concept of fair market value incorporates the notions that (1) cash could have been received for the stock at the valuation date, and (2) the share price of an infrequently traded stock could decrease if a relatively large block of the stock were to be put on the market on that date. If the subject shares held by the estate do not represent a significant percentage of the daily trading volume of TI stock on or around the valuation date, and the price of a share of the stock is readily ascertainable on the valuation date, then the resulting value (the quoted share price times the number of shares owned) represents a cash price that could have been received at the valuation date for the block, and the Statement does not apply because the calculation of value is mechanical (SSVS paragraph 9(a)). If, however, the subject shares held by the estate represent a large percentage of the average daily trading volume of the stock, the quoted market price for a share may not be adequate for purposes of determining the fair market value of the block of shares on the valuation date. In that case, the Statement applies because valuation approaches and methods need to be applied, and professional judgment needs to be used in determining the value of the block (SSVS paragraphs 1 and 4) (See *Illustration 10* at paragraph 27 of this Interpretation regarding the valuation of a security.)

The fact that the shares are traded infrequently raises the chance that the shares in the estate might be significant enough to render the price from public sources not a reliable

indicator of the value, due to the fact that if the estate's shares were placed on the market the price could change. The next example deals with the same issue, but this time triggered not because the shares trade infrequently, but because the decedent holds a large block of such stock.

50. *Illustration 13b.* Does the Statement apply to a large block of stock in "LB Corporation," a publicly traded company?

51. *Conclusion.* The answer depends on the amount of shares to be valued in relation to the average daily trading volume in LB Corporation on or around the valuation date. There are no definitive criteria that would indicate when the Statement applies to the valuation of a large block of publicly traded stock. The concept of fair market value incorporates the notion that cash could have been received from a sale of the block on the valuation date. A large block could decrease the share price if sold on the valuation date. The Statement would typically not apply to the valuation of a large block (for example, 200,000 shares) of a large and actively-traded public company. Even though the value of the estate's stock may be large in absolute terms, the daily trading volume in such stock on the valuation date may be sufficiently high that a sale of the block on the valuation date would not affect the market price of a company's shares. In such a case, the quoted market price of a share times the number of shares held by the estate may be considered to reflect the fair market value of the subject block of stock, and because it would not be the case that valuation approaches and methods would need to be applied and professional judgment used, the Statement would not apply. If, however, the large block of publicly traded shares represents a significant percentage of the daily trading volume, the Statement would apply because valuation approaches and methods would need to be applied and professional judgment used to determine the value (SSVS paragraphs 1 and 4).

In this case the trading volume generally argues against an issue arising, but if the block is large enough SSVS No. 1 may again become an issue. The next example, however, deals with what most practitioners will run into most often—the brokerage account containing a number of different stocks, no single position of which is a significant portion of the trading volume of any of the stocks on a particular day.

52. *Illustration 13c.* Does the Statement apply to a brokerage account consisting of shares in various publicly traded companies?

53. *Conclusion.* The Statement would not apply to the determination of the value of a brokerage account consisting of publicly traded securities, except as discussed in paragraphs 49 and 51 of this interpretation. Absent certain scenarios involving infrequently traded securities or large blocks of stock, the application of valuation approaches and methods and the use of professional judgment are not necessary in that determination (SSVS paragraphs 1 and 4).

As would be expected, in this case SSVS No. 1 would not be applicable.

A closely held business changes the equation and, as you might expect, SSVS No. 1 will come into play if the CPA is the party that values that interest.

54. *Illustration 13d.* Does the Statement apply to “CHB Corporation,” a closely held business owned by the decedent and the decedent’s family?

55. *Conclusion.* The Statement would apply to the determination of value of CHB Corporation because valuation approaches and methods need to be applied, and professional judgment needs to be used to determine the fair market value of the ownership interest in CHB (SSVS paragraphs 1 and 4).

The next illustration deals with valuing a partnership interest, but also discusses a real world problem that CPAs will run into—an uncooperative entity that refuses to provide the information necessary to fully comply with SSVS No. 1.

56. *Illustration 13e.* Does the Statement apply to a 5 percent interest in a privately held rental real estate partnership (RP)?

57. *Conclusion.* The Statement would apply to the determination of value of the 5 percent interest in rental real estate partnership (RP) because valuation approaches and methods need to be applied and professional judgment needs to be used to determine the fair market value of the ownership of a fractional interest in a privately held partnership (SSVS paragraphs 1 and 4). However, where it is not practical or not reasonable to obtain or use relevant information and, therefore, the member is unable to apply valuation approaches and methods, the Statement would not apply. For example, the member has requested from RP’s general partner financial information the member needs in order to apply valuation approaches and methods. The general partner is not responsive to the member’s requests, and the due date for filing the estate tax return is near. Given the small ownership interest, and given that RP is likely a relatively small percent of the total estate, unless prohibited by statute or by rule, the member may then use the taxpayer’s estimates if the member determines that the estimates are reasonable (based on the facts and circumstances known to the member) (SSVS paragraph 9(b)).

Note that, in this case, the example doesn’t resort to the exceptions to the application of SSVS No. 1, but rather points out that the CPA may still comply with SSVS No. 1 by using these estimates as part of the overall valuation engagement for this asset. CPAs may find that if they are too quick to use the “not practical” exception to SSVS No. 1, they may be second guessed later by a claim that the CPA should have complied with the standards except for the estimates that were provided by the client for the information that it was not practical to obtain.

Similarly, the client doesn’t give an estimate of value, but rather is assisted by the CPA in arriving at that number in some way, the CPA may find that once again the issue will be raised that what we had was not a value provided by a third party, but rather an estimate

for one item in the overall valuation project which the CPA then should have used as part of an overall SSVS No. 1 valuation.

Illustration 14 emphasizes some of the issues that arise when accepting values from the client or a third party in lieu of performing an SSVS No. 1 engagement.

58. *Illustration 14.* Would the answers to *Illustration 13* change if the values were provided by the client or a client-engaged third party?

59. *Conclusion.* The Statement would not apply if the values were provided by the client or by a client-engaged third party because the member is not applying valuation approaches and methods and using professional judgment to determine value (SSVS paragraphs 1 and 4). However, the member would be subject to Statement on Standards for Tax Services No. 3, *Certain Procedural Aspects of Preparing Returns*, in providing appropriate due diligence with respect to the values provided to the member (see AICPA, *Professional Standards*, vol. 2, TS sec. 300). It is also recommended that the understanding between member and client in these circumstances include documentation of the fact that the member is not determining but rather is being provided with the value of the subject interest.

Note the “suggestion” that the understanding with the client clearly indicate that the CPA is not responsible for the valuation, but that the valuation is provided by some other party. As well, the CPA still must consider the application of SSTS No. 3 and, though not stated in the illustration, Circular 230 ¶10.34 and applicable portions of the Internal Revenue Code regarding tax return positions when evaluating the values provided.

The next example deals with the situation where the CPA goes out and obtains the services of a third party appraiser to provide the value for the subject interest.

60. *Illustration 15.* Would the answers to *Illustration 13* change if the values were provided by an outside third-party specialist hired by the member?

61. *Conclusion.* If the member engages an outside third-party specialist to assist with the member’s work, and it is the member expressing a conclusion or calculated value, the member will be applying valuation approaches and methods and using professional judgment; thus, the Statement would apply (SSVS paragraphs 1 and 4; SSVS paragraphs 20, “Using the Work of Specialists in the Valuation Engagement”). If, however, the third-party specialist is determining the value in his or her own name and providing that value to the client, and the member will not be applying valuation approaches and methods or using professional judgment (SSVS paragraphs 1 and 4, and *Illustration 6*), the Statement would not apply, but the member would be subject to Statement on Standards for Tax Services No. 3, *Certain Procedural Aspects of Preparing Returns*, in providing appropriate due diligence with respect to the values provided (AICPA, *Professional Standards*, vol. 2, TS sec. 300).

Note that *someone* needs to provide a report and value *to the client* and if the CPA does that, then the CPA has undertaken an SSVS No. 1 engagement and must integrate the outside expert's work into an engagement the CPA will be responsible for. From a practical standpoint, this most likely means the CPA would not directly engage the specialist, but would rather have the client directly engage the outside specialist to avoid any indication that this is the CPA's use of a specialist. If the latter does occur, the entire engagement would be subject to SSVS No. 1's standards, even if the outside appraiser himself was not a CPA and not subject to the SSVS standards otherwise.

The Interpretation directly deals with the idea of a CPA "getting creative" and trying to engineer his/her way around the standard.

62. *Illustration 16.* The client and the member agree that the member will value a partnership interest and then apply an "average" discount that the member is to determine (based on the results of various studies and case law). Does the Statement apply? If so, is this a valuation engagement or a calculation engagement?

63. *Conclusion.* Yes, the Statement applies because the member determined the value of the partnership interest by applying valuation approaches and valuation methods and using professional judgment. This would be considered a calculation engagement because the member and the client have agreed on the specific valuation approaches or valuation methods the valuation analyst will use and the extent of valuation procedures the valuation analyst will perform (SSVS paragraph 21(b) and Illustration 6).

The illustration also makes clear that the "problem" with the partnership interest is not just limited to the question of valuation discounts—valuations is more than simply picking a discount (though sometimes CPAs and attorneys in the estate planning context seem to act as if that is all the valuation is about, as if the underlying value of the partnership interest prior to discounting is a simple number to arrive at in all cases).

CPAs can have informal discussions with clients about estate or tax planning where values would be an issue without triggering the standard, as noted in the next illustration:

64. *Illustration 17.* Would the Statement apply if a member has an informal conversation or communicates in writing with a client regarding the alternative tax consequences of gifting versus selling a business using a presumption of a specific value of the business?

65. *Conclusion.* No, the Statement would not apply. The member is providing tax advice using an assumed or hypothetical value of a business and is not determining value, applying valuation approaches and methods, and using professional judgment to value a business (SSVS paragraphs 1 and 4, and Illustration 6).

The key factor here is the use of a hypothetical assumption for the value, as opposed to an actually computed value. CPAs may want to assure their communications with the client make it clear that the value in use is hypothetical.

Illustration 18 outlines the issues that arise in a transfer pricing study under IRC §482 to illustrate the application of the jurisdictional exception. In this case, the overall IRS regulations on both the performance and reporting for the valuation of any intangible assets end up, in total, virtually eliminating the applicability of SSVS No. 1. But it's important to remember that in other situations, if the rules of the agency are not this comprehensive that SSVS No. 1 is used to “fill in the blanks” and would be applicable. In fact, even in this case the illustration stops short of saying that no part of SSVS No. 1 would apply—that determination would remain a matter of the professional applying the jurisdictional exception to the exact case in front of him/her.

66. *Illustration 18.* Would the Statement apply to a transfer pricing study (IRC section 482) that involves the use of specific methodologies, data, terminology, and documentation requirements that are provided in the IRS regulations and procedures, and whose methodologies and documentation requirements differ from those contained in the Statement?

67. *Conclusion.* No. To the extent that the transfer pricing study applies, for example, to the valuation of inventory or services, the Statement would not apply (see SSVS paragraph 1 and Illustration 6). To the extent that the transfer pricing study applies to the valuation of intangible assets, the Statement would normally apply. However, because the IRS regulations require that the taxpayer reasonably calculate an arm's-length price according to the best method that is determined using third-party comparable data under explicit IRS rules and documentation procedures, and to the extent these IRS rules and procedures differ from the Statement, the jurisdictional exception (SSVS paragraph 10) would exempt the valuation of the intangible assets from the developmental provisions of the Statement (SSVS paragraphs 25–48). In addition, to the extent that the IRS regulations (such as IRS regulation section 1.6662-6(d) (2) (iii)) and procedures provide specific documentation requirements for avoiding potential penalties, and if a transfer pricing report is provided to a client according to such IRS documentation requirements, the jurisdictional exception would apply to the reporting provisions of the Statement (SSVS paragraphs 50–78) and thus a valuation report would not be necessary.

CPAs have to remember that *all* relevant professional standards must be complied with, as the next illustration makes clear.

68. *Illustration 19.* In a situation where the Statement applies to members who determine value as part of tax engagements, would the member also be required to be in compliance with the Statements on Standards for Tax Services (SSTs)?

69. *Conclusion.* Yes, the Statement would apply only to the valuation determination and reporting aspects of the engagement but the SSTs would apply to all aspects of the engagement. For example, even though the Statement would govern the determination of value of an applicable asset reported on a tax return, the member would also have to be in compliance with SSTs No. 1, *Tax Return Positions*, for that valuation.

This issue cuts both ways—a CPA who is a business valuation specialist is not exempted from SSTs No. 1 or Circular 230 ¶10.35 with regard to his/her report, just as neither CPA is exempted from SSARS No. 1's compilation performance or reporting requirements if they manage to submit (as SSARS No. 1 defines that term) a financial statement to a client. The fact that many CPAs see themselves as specialists does not mean they can ignore the other professional standards out there, or that they are not applicable if the CPA performs work that would be covered by those standards.

The final tax illustration²¹ deals with the applicability of the standard to IRS settlement negotiations, including offers in compromise.

70. *Illustration 21.* Do settlements or negotiations of value in offers-in-compromise or tax disputes fall under the Statement?

71. *Conclusion.* No, settlements or negotiations of value in offers-in-compromise or tax disputes are part of a tax process. However, if a member prepares a valuation in preparation for a settlement or negotiation of value, and the valuation involves the application of valuation approaches and methods and the use of professional judgment, the valuation would fall under the developmental aspects of the Statement. The settlement or negotiation process itself is not a valuation and would not fall under the Statement. In addition, the Statement's reporting exemption for certain controversy proceedings would apply as the valuation was performed specifically for the administrative matter (SSVS paragraph 50).

Note the exception from the reporting portion of the standard, but the potential applicability of the performance standards. However, the actual negotiation process where compromise values are discussed to arrive at a value that will be used for purposes of resolving the underlying tax issue would not be subject to those standards.

²¹ Note that this illustration is improperly numbered in the version of the Interpretation I have from the AICPA website—Illustration 20 comes after Illustration 21. We are not skipping a tax illustration, as Illustration 20 comes in the next section of the Interpretation. I would not be surprised to see the AICPA correct this typo, so you may find the illustrations renumbered at some point and that Illustration 21 that we are discussing will instead be listed as Illustration 20.