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Silver lining

Changes in stock option rules mean new business for valuation firms.

The News

Change in stock option rules spells work for valuation firms

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When Armanino McKenna LLP acquired ValueNomics Research Inc., a Cupertino firm specializing in business valuation, in April, the move appeared to be counter-intuitive. The business valuation practice, which in the past heavily relied on companies going public, was still suffering from the post dotcom doldrums.

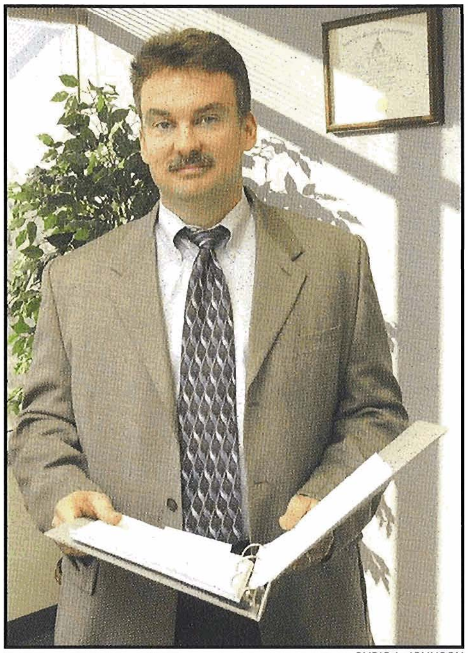
A few months later, the IPO market is still slow but not the valuation business. A new tax law and revised rules designed to promote more transparent reporting and accounting of stock options are encouraging public and private firms to hire valuation professionals to help them set their stock-option policies.

The rules include requiring most U.S. companies to deduct option costs from earnings, which means moving compensation expenses from the footnotes of financial statements to a more prominent spot on the income statement.

Also, a law added to the tax code as part of the American Jobs Creation Act of 2004, will soon require individuals who receive stock options to include that deferred compensation in their annual taxable income the year they received them. That means companies must get a fair-market value of those equities.

As a result, ValueNomics, which specialized in valuations related to litigation and mergers and acquisition, is inundated with tax and accounting work.

"Just in the last few weeks, we've gotten a number of calls involving tax issues," said Dirk Van Dyke, ValueNomics valuation director.



CHRIS A. JOHNSON

NEW RULES IN 2006: Dirk Van Dyke, ValueNomics Research Inc. valuation director, says it is a little tough for privately held companies right now as they review company value in the face of a changing tax law.

Before the law changes, private companies would have required valuations as they prepared for a public offering. Now they need professional help just to get a fair-market value assessment of their stocks.

"It's been a little tough for privately held companies. But I think, right now, they have no choice but to do it because their employees could end up owing personal income taxes and tax penalties," Mr. Van Dyke said.

The demand for valuations is likely to stay high, said Andy Ross, a San Francisco valuation specialist and head of Grant Thornton LLP's economic adviser services practice.

ARMANINO MCKENNA

Business: Accounting and consulting
Headquarters: San Ramon with office in San Jose
Managing Partner: Andrew Armanino
Founded: 1953
Employees: 200
Web: www.amllp.com

Aside from the new accounting rule on employee stock-options reporting, the Financial Accounting Standards Board has issued several other rules that relate to fair valuation. For example, the so-called rule 141R will require companies to present an opinion of fair value, commonly referred to as goodwill, when entering a recent acquisition in its books.

"Valuation professionals are being pulled more and more into the accounting process," Mr. Ross said.

The valuation market is fiercely competitive right now, but as valuation becomes more enmeshed with accounting procedures, Mr. Ross said, regional accounting firms with valuation units will benefit.

Opportunities abound for boutique valuation firms such as Financial Strategies Consulting in Lafayette. The firm specializes in high-tech and biotech business valuation. Greg Ansel, the firm's founder, believes that if the economy stays strong, business will be brisk for his firm as well.

"Companies are now thinking of conducting stock valuations on an ongoing basis, doing semi-annual and annual updates, and they're turning to us for help," he said.

XENIA P. KOBYLARZ writes for the East Bay Business Times, an affiliated publication. Reach her at 925-598-1414.