

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Introduction and Purpose

As part of the audit engagement team's review of MMN Builders, Inc.'s financial statements you have been asked to review the valuation analysis performed by Appraisal Professionals, LLC for purposes of goodwill impairment testing under SFAS 142. The valuation analysis has been organized as follows with each section requiring individual attention and review:

Subject	Report Section	Exhibit Number
Company and Testing Background	Section 1	
Industry Overview	Section 2	
Engagement Overview	Section 3	
Impairment Executive Summary	Section 4	Exhibits I and II
SFAS 142 Step 1 <ul style="list-style-type: none">▪ Discounted Cash Flow▪ Publicly Traded Company Multiples	Section 5	Exhibits III-VIII
SFAS 142 Step 2 for the Northeast Reporting Unit	Section 6	Exhibits IX-XIV
Assumptions and Limiting Conditions	Appendix 1	
Accounting Guidance	Appendix 2	
Valuation Methodology	Appendix 3	
Certifications and Qualifications	Appendix 4	

The following review program is intended to assist auditing professionals in reviewing goodwill impairment testing and measurement analyses performed in accordance with SFAS 142. It provides a structured approach and contains suggested technical references. This review program is divided into sections which roughly correspond to those listed in the report structure table above. This program organization is meant to facilitate a structured review of each section of the valuation analysis. These sections can be reviewed all at once or in a piecemeal fashion.

The attached program contains a list of questions and comments designed to guide your review. Effort should be made to answer each question in as much detail as possible, noting all means expended to gain comfort with each aspect of the valuation analysis. Simple "Yes" or "No" answers should be avoided when possible. In the event that the information provided within the subject valuation report and calculation schedules is not sufficient to answer a given question within this program, such deficiencies should be noted along with suggested steps to be undertaken to ensure a resolution of the issue. In making such a suggestion, students should consider the materiality of the issue and its importance to the overall impairment testing and measurement exercise. Materiality may be assessed through the use of sensitivity analyses. For example, if an assumption lacks support, an analysis of how different the impairment conclusion

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

would be if that assumption were changed upward or downward could be performed. The methodologies used and conclusions reached through such an analysis should be noted within this program.

Through deliberation of the considerations noted within this review program students should reach an assessment of the 5-8 key value-driving issues for which further clarification, analysis, and diligence is required in order to assess the reasonableness of the impairment conclusions reached. These key issues should be those which will have the largest impact on the impairment conclusion. Students should prepare a presentation including the following items to be discussed for each of the key issues identified:

1. Identification and explanation of the key issue;
2. An explanation of how this matter was determined to be critical to the impairment calculation;
3. A summary of any sensitivity analyses which have been performed to determine the effects of changes to the approach taken by the appraiser to address the subject issue;
4. Suggested methods of verifying the accuracy or inaccuracy of the appraiser's approach or conclusions reached as related to the issue; and
5. Next steps required to further address the issue and reach an ultimate conclusion.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Brief Introduction Goodwill and intangible assets not subject to amortization (i.e. indefinite-lived intangible assets) shall be tested for impairment on an annual basis and between annual tests if an event (i.e. a "triggering event") occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit/intangible asset not subject to amortization below its carrying amount.</p>	
1. Note who performed the valuation analysis (i.e., management, third-party valuation firm, etc).	
2. If a third-party appraiser is used, are the preparers of the analysis qualified to perform a valuation exercise of this nature? Consider and document the expertise and experience of those persons preparing the fair value measurements and review and document their respective qualifications to perform the work. Include a discussion that goes beyond discussing the reputation of the independent valuation firm, e.g., is the preparer a Chartered Financial Analyst (CFA) or a member of the American Society of Appraisers (ASA), and does the specialist have relevant industry experience? Is the preparer familiar with the guidance in the relevant accounting pronouncements?	
3. Does the valuation report conform to the AICPA's <i>Statement on Standards for Valuation Services</i> by including a statement of representation by the appraiser, a listing of the appraiser's qualifications, and a section for assumptions and limiting conditions?	
4. Note what types of assets (e.g. goodwill, indefinite-lived intangible assets, etc.) are being considered for impairment and the order in which these assets are being tested. The order of impairment testing should be as follows and	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>impairment should be recorded before moving to the next category:</p> <ul style="list-style-type: none"> • Indefinite-lived intangible assets (SFAS 142) • Long-lived intangible assets (SFAS 144) • Goodwill (SFAS142) <p>The order of testing is important to ensure the carrying values of the underlying assets are properly adjusted for applicable impairment in the proper order. For example, testing goodwill for impairment before testing long-lived assets could result in a larger write-down in goodwill and a smaller (or no) write down in long-lived assets than had the testing been performed in the prescribed order. This is a result of the fact that by not impairing long-lived assets first, you increase the carrying value against which you test goodwill for impairment. This results in a larger goodwill impairment charge and a lower carrying value against which you then test the long-lived assets for impairment.</p> <p>Has the above order been followed correctly in the calculation of impairment within the analysis?</p>	
<p>5. Note the date of test and whether the analysis has been performed as an annual impairment test or as a result of a “triggering event.” If as a result of triggering event, note the event.</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Goodwill - Step 1 Step 1 is similar to performing a business valuation. The first step of the goodwill impairment test is to compare the Fair Value of the reporting unit to its Carrying Value, including goodwill.</p>	
<p>6. Note how many reporting units ("RUs") the entity has and whether all or some portion thereof are being tested for impairment (not all reporting units are always tested – could be a triggering event in one reporting unit and not others; could be that some reporting units do not have goodwill to test). An annual test may be at any time during the year but must be performed at same time every year. Different reporting units may be tested for impairment at different times.</p>	
<p>7. How were the entities being tested identified to be reporting units? Paragraph 30 of SFAS 142 defines a reporting unit as "an operating segment or one level below an operating segment (referred to as a component). A component of an operating segment is a reporting unit if the component constitutes a business for which discrete financial information is available and segment management regularly reviews the operating results of that component."</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>8. Note basis on which Fair Value ("FV") of RUs are determined (i.e. on an asset, invested capital or equity basis). Accounting guidance refers to the notion of net assets, which presumably implies an equity basis. However, depending on facts and circumstances (e.g. debt at corporate level may not be able to allocated to RUs in a reasonable manner), an invested capital (i.e. business enterprise value) basis may be more appropriate. What is key in this assessment is to ensure that the manner in which the FVs of RUs are determined is consistent with Carrying Value ("CV") determination. In other words, if the FV is based on an invested capital basis, the CV against which the FV is tested should be on an invested capital basis as well. If the FV is based on an equity value, the CV should be book equity.</p>	
<p>Goodwill - Step 1 Valuation of Reporting Units <i>Note: If reviewing a SFAS 142 goodwill impairment test with multiple RUs, please answer the following questions in light of the valuations performed for all RUs.</i></p>	
<p>9. Note methodologies used to determine the FVs of the RUs (e.g.: DCF, market multiples etc).</p>	
<p>10. Were multiple methodologies used? If so, how was the concluded business value arrived at? Is the spread in the various indications of value by methodology significant? If a single methodology was used, note why and whether or not any attempts we made by the appraiser to corroborate conclusions using an alternative methodology.</p>	
<p>11. Were any premiums (e.g. control premium) or discounts applied in valuing the RUs (e.g. lack of control ("LOC"), lack of marketability ("LOM"), etc.)? If so, note their percentage</p>	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<ul style="list-style-type: none"> • How are premiums/discounts determined? • Are premiums/discounts used reasonable given the facts and circumstances? <p>NOTE: Premiums/discounts, in the context of impairment testing are heavily scrutinized by the SEC. Control premiums are often applied in the application of market multiples from publicly-traded comparable companies. Because those multiples are derived through prices of publicly-traded shares and because those shares represent minority interests in the company's equity, a premium for the right to control the reporting unit being tested for impairment is often applied. On the other hand, discounts for lack of marketability are often used to adjust for the fact that publicly-traded shares are liquid while business enterprises are not.</p>	
Market Approach – Guideline Public Company Method (“GPC Method”)	
12. Was the GPC Method applied? If not, note reason.	
13. Selection of Guideline Companies - Does the selection of guideline companies appear reasonable? Factors to consider include: <ul style="list-style-type: none"> • Industry and business description; • Size, profitability, expected growth and geographic location; • Confirm that companies are not subject to unique 	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>factors (lawsuits, pending acquisition, etc) which would skew multiples; and</p> <ul style="list-style-type: none"> • Ensure there is sufficient trading volume to provide a reasonable basis for the stock price. In other words, prices for thinly-traded stocks may not be good representations of market values. 	
<i>Calculation of Multiples</i>	
<p>14. Calculation of Multiples</p> <p>Are multiples calculated appropriately? Factors to consider include:</p> <ul style="list-style-type: none"> • How is enterprise value (most commonly defined as market value of equity plus book value of preferred stock, if any, plus net interest bearing long term and short term debt) defined (e.g. definitions may vary especially with regard to treatment of cash as excess cash held by one or more of the comparable companies may skew their multiples)? • Share prices used to calculate the market value of equity should be consistent with the impairment testing date; • Book value of preferred stock, cash and interest bearing debt should be pulled from closest filing prior to impairment testing date; • Numerator and denominator should be consistent when calculating multiples. For example, if the numerator is enterprise value, the denominator should be an operating metric which does not reflect the impact of capital structure, such as 	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>revenues, EBITDA or EBIT. If the numerator is equity value, the denominator should represent a flow to equity holders only, such as net income.</p> <ul style="list-style-type: none"> • Has the appraiser considered differences between the subject company and the guideline companies for factors such as size, risk, growth, and profitability? <p>If not, please note why.</p> <p>If so, how did they make their adjustments?</p>	
<p>15. If various multiples were used, how was the concluded indication of value arrived at for this approach?</p> <p>Is the spread in the various indications of value significant?</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
Income Approach – DCF Analysis	
16. Was an Income Approach applied? If not, note reason.	
17. Which Income Approach was used: free cash flow to the firm (FCF) discounted at WACC, free cash flow to equity (FCE) discounted at cost of equity, adjusted present value technique, capitalization of earnings, etc.? Note that the FCF using WACC approach is most common in practice. However, depending on what industry the subject company belongs to, other approaches may be more appropriate (e.g. for financial services, a FCE using cost of equity is typically used).	
18. Projections a. Understand and document the basis for projections. How were they derived? b. How do growth rates and margins compare to historic and industry growth rates? In situations in which information is lacking, request that the appraiser provide substantiation. Gain an understanding for large variances relative to historical trends and industry indications.	
19. Taxes a. What is the basis for the tax rate (i.e., combined federal and state rates)? Is it correct for the geography? b. Consistent with the concept of cash flow analysis, cash	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>(i.e., effective) tax rates should be used.</p> <p>c. Are there any Net Operating Losses ("NOLs") which have been or should have been considered within the analysis? NOLs have the effect of lowering taxes as a result of historical losses.</p>	
<p>20. Capex & Depreciation</p> <p>a. Have capital expenditures and depreciation been properly accounted for? Factors to consider, include:</p> <ul style="list-style-type: none"> • Comparison to historic and industry data (fixed asset turnover ratios, percentage of revenue, etc.); • Consistency with the expected growth in the business (i.e. it's difficult to obtain significant growth without significant capex); • Capex and depreciation should be internally consistent (i.e. you cannot depreciate more assets than you have purchased through capex). <p>b. At the end of the discrete projection period, do depreciation and capex offset each other? If not, does the gap appear reasonable given the revenue and other expenses in the terminal value calculation? It is unlikely that capex would exceed depreciation into perpetuity or that depreciation would exceed capex for an extended number of years.</p>	
<p>21. Working capital ("WC")</p> <p>a. Has an adjustment been made for working capital? Is the level of working capital implied reasonable?</p>	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Factors to consider, include:</p> <ul style="list-style-type: none"> • Comparison to historic and industry data (i.e., current ratios, days receivable/payable, inventory turns, working capital as percentage of revenue, etc); • Level of expenses. 	
<i>Terminal Value</i>	
<p>22. What methodology has been used to calculate the terminal value?</p> <ul style="list-style-type: none"> • The Gordon Growth method takes the free cash flow in the last year of the forecast period and grows it one more year at the long term growth rate. This free cash flow is then capitalized at a rate equal to the discount rate minus the perpetual long term growth rate (i.e. $k-g$). • The Exit Multiple method assumes that the business is sold at the end of the explicit forecast period. 	
<i>Gordon Growth Model</i>	
<p>23. Does the terminal value calculated using this method appear unreasonable? Consider the following factors:</p> <ul style="list-style-type: none"> • Has a normalized cost of capital been utilized (for early stage companies, the risk-profile at the terminal period should be much lower than at the valuation date)? • Were sales from the last projection period grown by the assumed long term/residual growth rate? Have the 	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>operating margins been set at long term sustainable levels?</p> <ul style="list-style-type: none"> • Is capex adequate to sustain growth? • Does capex have a sustainable relationship with depreciation? • Does long term sustainable growth rate appear reasonable? Typically, this growth rate will range from 2-5%. • Are working capital requirements adequate to support sales growth? • What is the implied Exit Multiple and does it appear reasonable? One approach to test this would be to compare the implied multiple to comparable company multiples or historical industry multiples. 	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<i>Exit Multiple Approach</i>	
<p>24. Does the terminal value calculated using this method appear reasonable? Consider the following factors:</p> <ul style="list-style-type: none"> • M&A and Public Company multiples. • Multiples for mature players in the industry (focus on longer-term averages for industry versus current multiples which might be distorted). • Guideline company multiples or historical industry multiples. <p>Was a discount applied to the multiple used? Note that usually it is appropriate to take some discount to reflect the fact that all things being equal, the multiple in future years should be less as growth slows over time.</p>	
<i>Discount rate</i>	
<p>25. Have present value ("PV") factors been calculated properly? Was the PV factor adjusted to account for partial year cash flows in the first year, if applicable?</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>26. Note the discount rate and assess reasonableness. Ensure that the discount rate used is consistent with the projected cash flow stream. In other words, when discounting cash flow to all stakeholders, the cost of capital for the entire firm (WACC) should be used. When discounting cash flow to equity holders only, the cost of equity should be used.</p> <p>Factors to consider, include:</p> <ul style="list-style-type: none"> • Company's stage of development and investor's required rate of return; • Capital structure and leverage; • Has the cost of debt been tax-affected? 	
<p>27. Which approach was used to calculate the cost of equity: capital asset pricing model ("CAPM"), build up approach, arbitrage pricing theory, Fama-French three factor model, dividend discount model, other?</p> <p>In practice CAPM is the most commonly used approach.</p>	
<p>28. Risk free rate – Does the risk free rate appear reasonable? Note the source used.</p>	
<p>29. Market risk premium ("MRP") - Is the MRP between 4% and 7%? Note the source used.</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>30. Beta - Consider the following in assessing the utilized beta:</p> <ul style="list-style-type: none"> • Was the beta determined using a reasonable peer group analysis? Does the selection of guideline companies appear reasonable? • Are betas unlevered and relevered appropriately? The capital structure assumption used to relever the subject company's beta should be the same as that used to weight the debt and equity in the calculation of the subject company's WACC. 	
<p>31. Capital structure - Consider the following in assessing the assumed capital structure:</p> <p>What capital structure is assumed in the calculation of the WACC? Is the capital structure based on company-specific parameters or is an industry average used? When assessing fair value for tax or financial reporting purposes, the common practice is to use the industry average capital structure.</p>	
<p>32. If applicable, does the discount rate include a size premium? If so, does the magnitude of the premium appear reasonable? A size premium is typically applied to cost of equity as determined by CAPM.</p> <p>NOTE: Company-specific risk premiums are highly judgmental and subject to scrutiny.</p>	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Goodwill Impairment - Step 2 (i.e. for all RUs where FV < CV) <i>Note: Step 2 analysis should be performed similar to a SFAS 141 exercise and should make reference to all tangible and intangible assets/liabilities. This includes intangibles that may not be recorded on a reporting unit's balance sheet.</i></p>	
33. List all tangible and intangible assets/liabilities included in the Step 2 analysis. Does this list appear to be complete?	
34. Is the appraiser's assumption that CV is equal to FV for any assets or liabilities? Is this a reasonable assumption given the nature of the assets/liabilities?	
35. Has the impairment loss been measured as the difference between book value of goodwill and the implied fair value of goodwill? The implied fair value of goodwill should be calculated as the Step 1 FV of the RU less the FV of all assets/liabilities identified and valued in the Step 2 analysis.	
<p>Goodwill Impairment - Step 2 (i.e. for all RUs where FV < CV)</p> <p>Valuation of Intangible Assets</p> <p>Assets valued using the Income Approach – Excess Earnings Method. The application of the Excess Earnings Method to value intangible assets is discussed in AICPA Practice Aid on In Process Research & Development. The fundamental premise of the Excess Earnings Method is that the value of an intangible asset is equal to the present value of the net cash flows attributable to the subject intangible asset. Intangible assets valued using the excess earnings method are generally the primary intangible assets acquired in a transaction and often include technology (developed and in-process) and customer relationships. On rare occasions, customer relationship assets may not be identifiable in early-stage companies when the Target has no history of revenues.</p>	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
36. Note the assets valued using this approach.	
37. Is the use of this method to value the given asset reasonable in the overall context of the deal and the manner in which the asset can be marketed (e.g., key value-driving assets, such as customer relationships and enabling technology, are often valued using the Excess Earnings Method)?	
38. Do the gross margins or COGS % of revenues differ significantly from the margins used in Step 1 to determine the business enterprise value? If so, is there a reason why?	
39. If valuing customer relationships, note the probability of attrition and retention. What is the basis for the probabilities applied (e.g., historical attrition rates or probabilities of renewal). Ensure proper support is obtained if appraiser relied solely on management indications of renewal. An analysis of detailed historical customer turnover information may be appropriate to assess attrition estimates.	
40. If valuing customer relationships, is some level of growth embedded in the revenues attributable to existing customers before the attrition? Some level of growth may be appropriate to reflect the fact that the company may be selling new products and/or services to existing customers before they leave.	
41. If valuing customer relationships, note maintenance Sales and Marketing expense. Typically, these expenses are lower for existing customers than for new customers and an adjustments needs to be made.	
42. Has a tax amortization benefit been applied?	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Contributory Asset Charges</p> <p>Under the Excess Earnings Method, charges for assets that contribute to the generation of cash flows are deducted from operating profits of the intangible asset being valued in order to arrive at only those cash flows attributable to the subject asset. Contributory assets typically include fixed assets, working capital, workforce, and other intangible assets. Typically, returns on assets are applied as a percentage of revenue. Charges are broken down into returns OF and returns ON which are analogous to the principal and interest concepts of a loan. Returns OF represent the payback of the initial capital employed to purchase or develop the asset (i.e. the principal). Returns ON are the returns one expects to generate on his initial investment in the asset (i.e. the interest). Charges for the returns OF should only be taken for assets whose value depreciates over time. Charges for returns ON should be taken for all assets that contribute to value. At times, returns OF are already embedded in the cash flow projections, such as with depreciation for fixed assets. Under such circumstances, only a return ON needs to be taken.</p>	
43. Have all assets which contribute to the generation of cash flows been identified as contributory assets?	
44. Is return ON working capital reasonable? Working capital rates of return should be similar to short term lending rates. Only a return ON working capital is appropriate. It is incorrect to ever reflect return OF working capital in the form of working capital investments because the hypothetical return OF working capital is conceptually offset by a borrowing of funds. Thus, working capital is not a wasting asset for which a return OF is required.	
45. Is return ON fixed assets reasonable? Fixed assets rates are those implied by operating leases, capital leases, or both. Returns OF are typically included in the depreciation charged to arrived at operating profit. If depreciation is included in this charge, it should be tax-effected.	
46. A charge for use of the RU's work force should be included. Is return OF work force included in the calculation of the charge? Only a return ON work force should be considered because use of and replenishment of the work force is already captured in the cash flow assumptions in the form	

PricewaterhouseCoopers is pleased to provide these materials for use in classroom discussion and individual study. They may be used without further permission from PwC by faculty members and students for non-commercial, academic purposes only. (c) 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP (a Delaware limited liability partnership) or, as the context requires, other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
of employee salary and training expenses.	
Assets valued by the Income Approach	
Relief from Royalty Method	
Intangible assets valued using the Relief from Royalty Method are generally considered secondary to those assets valued using the excess earnings method. Generally trade name and core technology (often in the form of patents) are valued in this way; however, this approach may also serve to validate values of technology derived using the excess earnings method. Consider how the royalty rate was determined and whether the rate itself is reasonable. After-tax royalties greater than 10% are not typical.	
47. Note the assets being valued using this method.	
48. Is the royalty rate based on market data (e.g., Royalty Source)? The market data should reflect licensing transactions involving similar assets.	
49. Is the royalty based on a proportion of operating profit? A general rule of thumb is that 25% to 33% of normalized operating profit is attributable to intangible assets (e.g., trade names or patents).	
50. Is the royalty rate applied to applicable revenue stream? Patent royalties should only be applied to the applicable technology (future and existing revenues). Trade name royalties should only be applied to those products sold under that trade name.	
51. Has a tax amortization benefit been applied?	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Area	Auditor's Comments and Observations
<p>Assets valued using the Cost Approach. This approach captures the costs associated with replicating or replacing the acquired asset in its existing state, and is based on the principle of substitution (i.e., an investor would pay no more for an asset than it would cost to replace its functional utility). These costs may or may not include applicable costs to finance the endeavor. Methods under the Cost Approach include:</p> <ul style="list-style-type: none"> • Reproduction cost new – Cost to exactly replace asset • Replacement cost new – Cost to replace asset’s functionality <p>Both methods adjust for various forms of physical, functional, and economic obsolescence.</p>	
52. Note type of asset valued using this approach.	
53. Has the Cost Approach only been used for those assets that are not deemed to be the primary cash generating assets?	
54. Have the costs to recreate the asset been tax-effected? If not, explain why. If costs are after-tax, has a tax amortization benefit been applied?	
55. Have only soft costs been considered? Investments in capital equipment should not be included.	
56. If any employee salaries have been included, are these indications fully-burdened? Fully-burdened salaries should be used.	

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

Key Issues for Further Investigation

- 1. Projections:** The report does not provide any support for the assumptions used to develop cash flow projections for the RUs. Care must be taken to reconcile these projections to:
 - a. Historical performance
 - b. Industry-wide historical metrics and forecasts
 - c. The company's internal budgets and forecasts

- 2. SFAS 144:** We have only been presented with the SFAS 142 analysis but not the SFAS 144 analysis which preceded it and resulted in a substantial reduction in the carrying value of the company's home inventories. Because these inventories are the largest asset on the Northeast RU's balance sheet, changes to their fair values and carrying values will have a large impact on both the Step 1 and Step 2 analyses. The audit team will need to confirm the accuracy of the SFAS 144 impairment charge before forming an opinion of the SFAS 142 results.

- 3. Trade name royalty rate:** No support (such as data on royalty rates charged for the use of similar assets by third parties) has been given for the 0.75% royalty rate. The following table shows the effects of changes to that rate on the value of the trade name and the amount of goodwill impairment. As you can see, the royalty rate conclusion can have a sizable impact on the level of impairment.

	Royalty Rate	Trade Name Value	Goodwill Impairment
	0.25%	12	(99)
	0.50%	24	(110)
Current Analysis	0.75%	36	(121)
	1.00%	48	(132)
	1.25%	59	(143)
	1.50%	71	(155)
	1.75%	83	(157)
	2.00%	95	(157)

VALUATION FOR MMN BUILDERS INC. AS OF JUNE 30, 2007
SFAS 142 REVIEW PROGRAM

- 4. Probability of customer attrition:** No support has been presented for the 75% annual probability of retention. The following table shows the effects of changes to that probability on the value of the customer relationship and the amount of goodwill impairment. As you can see, the probability conclusion can have a sizable impact on the level of impairment. Historical customer attrition data or other support should be sought to confirm the accuracy of this input.

	Prob. Of Retention	Customer Value	Goodwill Impairment
	60.00%	17	(111)
	65.00%	20	(114)
	70.00%	23	(118)
Current Analysis	75.00%	27	(121)
	80.00%	31	(125)
	85.00%	36	(130)
	90.00%	41	(135)