

VALUATION REPORT

ABC Construction
As of June 30, 2009

Michael F Cannon
MCOM Corporation

June 30, 2000

Mr. John Smith
123ABC Construction Road
Any Town, California 12345

Dear Mr. John Smith,

I have prepared and attached my valuation report of ABC Construction, as of June 30, 2000. The purpose of the valuation is to render an opinion as to the Fair Market Value of 100% of the stock of ABC Construction.

Fair market value under such circumstances is defined as follows in Revenue Ruling 59-60:

The amount at which property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. Court decisions frequently state in addition that the hypothetical buyer and seller are assumed to be able, as well as willing, to trade and to be well informed about the property and concerning the market for such property.

My report is based on historical financial statements provided to us by management. I have not audited or reviewed ABC Construction's financial statements, had I audited or reviewed the underlying data, matters may have come to my attention that could have led me to use different amounts from those provided and led to a different opinion. Accordingly, I accept no responsibility for the underlying data presented in this report. Users of this business valuation should be aware that business valuations are based on future earnings potential that may or may not materialize. Therefore, the actual results achieved during the projection period may and probably will vary from the projections used in this valuation, and the variations may be material.

Based on my study and analytical procedures, I have concluded that a reasonable estimate of the Fair Market Value of the 100% stock interest of ABC Construction, as of June 30, 2000, is \$9,500M or \$172.73 per share.

I have no financial interest or contemplated financial interest in the property that is the subject of this report. My fees for this valuation are based upon my normal hourly billing rates and in no way are contingent upon the results of my findings. I have no responsibility to update this report for events and circumstances occurring subsequent to the date of this report.

This report has been prepared for the specific purpose of valuing ABC Construction stock as of for a Sale of Business and is intended for no other purpose. This report is not to be copied or made available to any persons other than those indicated in this report without the express written consent of MCOM Corporation.

Sincerely,

Michael F Cannon
MCOM Corporation

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INTRODUCTION

I. Purpose

The purpose of this report is to establish the Fair Market Value of the stock of ABC Construction as of June 30, 2000 in conjunction with a Sale of Business.

II. Unique Facts and Circumstances

Every valuation contains unique aspects that have an impact on the valuation approach and methodologies considered and applied. In this valuation the following *unique facts and circumstances* are specifically identified in order to apprise the reader of their application.

- ? It is widely acknowledged that the electrical contracting industry and the construction industry in general is a mature and low growth cyclical market strongly tied to the general US economy. Accordingly, economic factors have been analyzed for both the US and the Southwest generally and the specific market areas of Southern California and Arizona where ABC Construction has sales.
- ? An analysis of the financial statements and the comparative common size ratios to the industry demonstrate that ABC Construction is an extremely profitable operation that significantly exceeds the performance levels of the industry in general and specific comparative companies in particular. Consequently, care has been taken to analyse performance potential into the future based on a variety of methods over and above industry comparisons.
- ? ABC Construction has maintained cash and investment instrument levels (retained earnings) in the the company that are far beyond the levels required to operate the company. This excess asset value has been eliminated from the financial statements to ascertain a Fair Market Value of the performing assets. The owners advise me that, prior to a sale, these assets will be removed from the operation.
- ? The electrical contracting industry in Southern California has heretofore resisted significant consolidation due to a low cost of entry for small operations and a widely accepted attitude on the part of general contractors to work with small sub contractors. This may change in the near future due to downward pressure on margins caused by the arrival of large, nation and state wide GC's and sub contracting companies that operate under high volume low margin principles. ABC Construction's high union wage policies may put it at a disadvantage in this more competitive market.

- ? Southern California has been inundated with a vast supply of cheap labor from illegal aliens coming across the border from Mexico. This factor has also put pressure on ABC Construction to make lower bids to get jobs. While a majority of jobs are assigned to ABC Construction without competitive bidding, this may change in the near future with the potential lower costs offered by cut rate competitors with illegal alien workers.
- ? For the sake of simplicity and ease of reading, the financial statements and number of ownership shares have been input in their (,000) form.

III. Approach

My approach has been to determine an estimate of value that would provide a fair and reasonable return on investment to an investor or owner, in view of the facts available to me at the time. My opinion is based on, among other things, my estimate of the risks facing ABC Construction and the return on investment that would be required on alternative investments with similar levels of risk.

Among other factors, this valuation takes into consideration all elements of valuations listed in Internal Revenue Service Ruling 59-60, which generally outlines the valuation of closely held stocks and includes the following:

- ✍ The nature of the business and the history of the enterprise from its inception.
- ✍ The economic outlook in general and the condition and outlook of the specific industry in particular.
- ✍ The book value of the stock and the financial condition of the business.
- ✍ The earning capacity of the company.
- ✍ The dividend-paying capacity.
- ✍ Whether or not the enterprise has goodwill or other intangible value.
- ✍ Sales of the stock and the size of the block of stock to be valued. There have/have not been any previous transactions involving the Company's stock. The current block of stock represents a control/minority block of stock that does/does not have swing-vote characteristics requiring additional analysis.
- ✍ The market price of stocks of corporations engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over the counter.

My study included, but was not necessarily limited to, the above-mentioned guidelines.

I applied various valuation methods in estimating the value of ABC Construction as of June 30, 2000. The various methods considered were:

- ✍ Book Value Method
- ✍ Adjusted Book Value Method - Going Concern
- ✍ Adjusted Book Value Method - Summary Liquidation
- ✍ Capitalization of Earnings Method
- ✍ Discounted Earnings Method - Summary Projections
- ✍ Capitalization of Excess Earnings Method
- ✍ Guideline Company Method
- ✍ Dividend-Paying Capacity

IV. Contingent and Limiting Conditions

This report has been prepared for the specific purpose of valuing 100% of ABC Construction stock as of June 30, 2000 for a Sale of Business and is intended for no other purpose. This report is not to be copied or made available to any persons other than those indicated in this report without the express written consent of MCOM Corporation.

This report is made subject to the following contingent and limiting conditions:

- ✍ Users of this business valuation report must recognize that business valuations are based on future earnings potential that may or may not materialize. Therefore, the actual results achieved during the projection period will likely vary from the projections utilized in this valuation, and the variations may be material.
- ✍ Some assumptions invariably will not materialize, and unanticipated events and circumstances may occur. Therefore, the actual performance in any areas forecasted/projected will vary from the forecast/projection, and the variations may be material. MCOM Corporation will not express any form of assurance on the likelihood of achieving the forecast/projection or on the reasonableness of the used assumptions. Any such forecast/projection is presented as part of the valuation and is not intended to be used separately.
- ✍ The value premise(s) cited in this report are fundamental to the value opinions rendered herein, and I reserve the right to reconsider such premise(s) should subsequent or additional information be discovered, although no such obligation exists.

- ✍ I have relied upon the representations of the owners, management and other qualified third parties concerning the value and useful condition of all equipment, real estate, investments used in the business, and any other assets or liabilities except as specifically stated to the contrary in this report. I have not attempted to confirm whether or not all assets of the business are free and clear of liens and encumbrances, or that ABC Construction has good title to all assets.
- ✍ The estimate of value included in this report assumes that ABC Construction will maintain the character and integrity of the company through any sale, reorganization or reduction of any owner's/manager's participation in the existing activities of the company.
- ✍ Since neither ABC Construction management nor advisors have advised us otherwise, I assume that there is full compliance with all applicable federal, state, and local laws and regulations unless the lack of compliance is stated, defined, and considered in the valuation report.
- ✍ Public information, purchased private information and industry statistical information are from sources I deem reliable; however, I make no representation as to the accuracy or completeness of such information, and have accepted the information without further verification.
- ✍ This report and its related calculations were prepared using various software applications potentially including Microsoft Word© and Microsoft Excel©, BVM Pro©, Professional Report Writer, and/or various Internet-related software, third-party data (as indicated) and information.
- ✍ I assume no responsibility for the legal description or matters including legal or title considerations. Title to the subject assets, properties, or business interests is assumed to be good and marketable as represented by owners, management and advisors of ABC Construction unless otherwise stated.
- ✍ I assume no hidden or unapparent conditions regarding the subject assets, properties or business interests.
- ✍ Unless otherwise stated in this report, I did not observe, and have no knowledge of, the existence of hazardous materials with regard to the subject assets, properties, or business interests. However, I am not qualified to detect such substances. I assume no responsibility for such conditions or for any expertise required to discover them.
- ✍ No opinion, counsel or interpretation is intended in matters that require legal or other appropriate professional advice. It is assumed that such opinions, counsel or interpretations have been or will be obtained from the appropriate professional sources.
- ✍ The analyses, opinions, and conclusions presented in this report apply to this engagement only and may not be used out of the context presented herein. This report is valid only for the effective date(s) specified and only for the purpose(s) specified herein.

- ✍ Although I have exerted considerable diligence and applied my best efforts in constructing this document, immaterial anomalies, if any, may arise. Even so, I am confident that my overall conclusion would still fall within a materially consistent conclusion.
- ✍ While the client has not informed MCOM Corporation of any intent to do so, any third parties to whom this report is shown may be assured that this report, while performed in the employ of the client, was materially prepared on a non-advocacy basis. Any third persons; however, are cautioned that MCOM Corporation has no duty to you and, therefore, no warranty is expressed or implied. Nothing in this report is intended to replace your independent sole judgment, due diligence, or decision to seek professional legal, accounting, or valuation counsel.
- ✍ This report has been prepared solely for the use of the party or parties named and specifically for the purposes set out therein. In accordance with normal practice, I hereby disclaim liability to any other person. Any other person should not rely upon the information and conclusions reached nor should any statement in this report be used for any other purpose without written consent from MCOM Corporation.
- ✍ The statements and opinions given in this report are given in good faith and in the belief that such statements are not false or misleading. In preparing this report I have relied upon information believed to be reliable and accurate provided by the owners, management and advisors of ABC Construction and other sources. I have no reason to believe that any material facts have been withheld from us, nor do I warrant that my investigation has revealed all of the matters in which an audit or more extensive examination might disclose.
- ✍ This valuation reflects facts and conditions existing at the date of this valuation. Subsequent events have not been considered, and I have no obligation to update my report for such events and conditions.
- ✍ MCOM Corporation does not purport to be a guarantor of value. Valuation of closely held companies is an imprecise science, with value being a question of fact, and reasonable people can differ in their estimates of value. MCOM Corporation; however, performed conceptually sound and commonly accepted methods and procedures of valuation in determining the estimate of value included in this report. MCOM Corporation is not liable for any use, reliance, financial applications, report distribution or other utilization of any kind, by any party not having written authorization from MCOM Corporation.
- ✍ The appraised estimate of fair market value in this report is based on the definition applied throughout such report. An actual transaction in the shares may be completed at a value higher, lower or equal to the value rendered herein. I make no guarantee of any kind with regard to the likely or ultimate amount that may result in any future transaction.
- ✍ The opinion(s) offered in this report do not constitute an offer to buy or sell the shares.

- ✍ The valuation analyst, by reason of performing this valuation and preparing this report, is neither required to give expert testimony nor attend in court or any government, professional or regulatory hearing, including IRS matters with reference to the matters contained herein, unless prior written arrangements have been made with MCOM Corporation regarding such additional engagement as to the timing, fee arrangements, and nature of the services required.
- ✍ None of the partners or employees of MCOM Corporation have any present or contemplated future interest in the property being valued, any personal interest with respect to the parties involved, or any other interest that might prevent us from performing an unbiased valuation. My compensation is not contingent on an action or event resulting from the analysis, opinions, or conclusions in, or the use of, this report.
- ✍ Possession of this report does not carry with it the right of publication. It may not be used for any purpose by any person other than the client to whom it is addressed without my written consent and, in any event, only with proper written qualifications and only in its entirety.
- ✍ Neither all nor any part of the contents of this report shall be disseminated to the public through advertising, public relations, news, sales, or other media without my prior written consent and approval.
- ✍ Liability of MCOM Corporation and its partners and employees for errors and omissions, if any, in this work will be limited to the amount of its compensation for the work performed in this assignment.

This report is further subject to any other contingencies, assumptions, and limiting conditions that may be set out elsewhere within this report.

V. Scope Limitation

The scope of this valuation engagement and report is limited. I was engaged to perform a valuation for ABC Construction with the intent of ascertaining an approximate estimate of value where the scope of the market and comparative data would provide adequate information for analysis. This data was only partially available to me for my review. Had I been able to perform a more detailed analysis, matters might have come to my attention that could have had a material impact on the estimate of value contained in this report.

Accordingly, my level of assurance on the estimate of value is reduced. This report is not intended to serve as a basis for expert testimony in a court of law or other governmental agency without further analysis and resulting documentation.

OVERVIEW OF THE COMPANY

I. History and Ownership

The following information was gleaned from company records and a detailed site visit conducted with the owners and principle employees at the company headquarters in August of 2000. A full copy of the site visit report is included as an exhibit at the end of this report.

A. Form of Organization

Company Name: ABC Construction Company

1. **Company's primary address:** 5529 ABC Construction Blvd, Any town, Cal 91365
2. **Date of Company's inception:** 1985
3. **Type of entity (C-Corp., S-Corp., LLC, LLP, etc.):** C-Corporation
4. **State Company organized:** California
5. **Company's primary SIC code number:** 1731 Electric Work **Secondary SIC code number(s):** 235310 NAICS Electrical Contractors
6. **If corporation, number of shares authorized:** 55 (,000) **Number outstanding:** 0
7. **If corporation, number of shares of treasury stock:** 0
8. **Describe other classes and/or types of stock:** None

B. History

The company was started in 1985 by John Smith' father, Reginald. Reginald was an English merchant marine sailor who disembarked in San Diego shortly after World War II. His tanker ship had been destroyed by a Japanese U-Boat and he was one of a few survivors picked up by an American convoy returning to the west coast after re-supplying US troops in Hawaii. He was only 20 years old and fell in love with California and shortly afterwards with a California girl. They were married and had a son, John, in 1945.

Reginald and his young family moved to the small towns in the mountains inland from San Diego and settled in the town of Any town in 1946, as far away from the sea as he could get. Having worked in electricity in the merchant marine Reginald began to

look for work as an electrician's assistant, and this became his trade for the next 40 years. He worked for electrical contracting companies in the area and when his son graduated from high school, he too joined the trade. Reginald and John worked together as a team for a local electrical contractor for over 20 years while John married and started his own family. Not wanting his grand children to have the same difficulties as he had had in starting out, Reginald decided to start his own electrical construction business. He wanted to leave something tangible for his grand children before he died.

By 1985 Reginald was turning 60 and his son 40. They were both master electricians and, over time, had built up a loyal clientele of construction companies who preferred to work with them as a team on jobs. The move to open their own business was a natural one. Both father and son prospered and enjoyed working together. Having been employees of the same industry for a long time, they deeply understood the problems that workers had to live with. Consequently, they based their business on some sound principles; Develop and maintain strong relationships with customers, develop repeat business, treat employees fairly and pay union wages and benefits, compete based first on quality work, done on time and within budget, and only then on price. This formula was very successful and ABC Construction became known as a quality company that delivered on time and within budget. There was none of the labor strife that plagued some of the other contracting firms in the area and the high quality staff at ABC Construction were happy and generally did not leave for work in other companies. This low turnover and high quality gave ABC Construction a big advantage when bidding for new jobs.

The company was successful and served to provide a good living to Reginald and John and the handful of employees they had. By 1996 Reginald was approaching 71 and he had no desire to expand the business further, but John could see that there were many missed opportunities to profitably increase the size of the business. Just as Reginald was contemplating retirement from the business he and his wife were killed suddenly in a car accident coming home from church on a Sunday morning.

Growth and Expansion

John vowed to continue the business as before but also to find ways to expand it and make it more profitable. Over the next 4 years John worked hard to further develop the business based on the sound principles forged with his father over the previous 10 years, and by 2000 the business had reached very high levels of revenue and profit with a stable clientele and group of employees. This expansion and growth came because of John's insistence in systematizing the operation and focusing on good planning and execution. John standardized all the trucks to the same brand, engine displacement and general features to simplify maintenance. He built and standardized what he called work "kits" that included all the tools and parts crews would need to work on a job. This eliminated the tremendous wasted time most crews face when they start a job and then have to stop to go and get either parts or tools or return to home base before the job was done. John estimated that this alone made his work crews 25% more efficient than his competitors. This made ABC Construction more profitable and gave them margin to bid competitively on jobs.

Customer satisfaction was high when John took over the business. Many of the customers were friends of Reginald and, at first out of pity, they continued to work with ABC Construction. But when they saw that John maintained the high level of quality and service and kept prices reasonable, they passed their allegiance along to him. John's easy and reliable manner helped immensely in this. Surprisingly, a lot of ABC Construction's business came to them without competitive bids or price haggling. Industry research shows that this is not an isolated phenomenon. The "Guide to the Electrical Contracting Market" from 1999 states that fully 44% of all jobs come from no bid jobs from established customers. GC's and construction companies often develop relationships of trust with key suppliers and routinely work with them without the hassle of the bidding process or strong price negotiations. John was always careful to never abuse this relationship of trust, making sure that the prices he charged were always within the reasonable range. This was crucial in communicating to customers that ABC Construction was a trusted partner.

While ABC Construction had done an excellent job in maintaining established business, John reminisced that it had been hard work to expand the business beyond the locally owned general contractors and establish relationships with the state wide construction firms that typically had larger projects with a more consistent flow. John had had to demonstrate ABC Construction's strong record of project completion on time and in budget and back it up with performance guarantees that sometimes kept him awake at night. State wide construction firm contracts were instrumental in doing two things that greatly expanded ABC Construction's business. First, they helped expand their business in Nevada and secondly and most importantly, they gave ABC Construction an opportunity to compete for government construction business. While Nevada contracts added a growing 15% to 25% to the revenue line, the government construction jobs, all of which had no problem paying the union wage and benefit premiums charged, added another 10 to 15% to the growth of the business. All in all, John was satisfied both with the growth and the diversity of the business. No one client represented more than 10% of the overall business. The growing pains they experienced going from a small operation to a medium sized one were mostly overcome and with 12 three man crews ABC Construction had the flexibility to react quickly to the market and solve problems. John was particularly proud of Shirley's contribution to the success of the business in that she helped John develop a forecasting plan and organize work so that ABC Construction had a continuous backlog of booked projects that projected an average of 3 months into the future. This early warning system allowed ABC Construction to carefully plan staffing needs and add crews when the work load was going to be greater and move them out when the load diminished.

John's wife Shirley participated fully in business developments by taking over all the office and administrative work. While neither she nor John were financial experts they felt that the person they had hired shortly after Reginald's death, Joe Wilson, would do a good job.

Current Situation

By 2000 John began to feel some concern for his own health and he and Shirley decided to sell the business. After more than 35 years as a master electrician of which 15 years were in his own business, John felt he could say he had done it all. His grown

children had never shown an aptitude or interest in the business so he felt justified in selling it to a third party. Reginald had moved as far away from the sea as possible but John had always held a desire to retire and cruise the west coast on a boat.

John is a mature businessman who is characterized by his steady and unruffled way of doing business. He has taken a careful and cautious approach to the sale of the family business. He is not in a hurry nor will he make a rash decision to free himself up from his daily responsibilities. John feels that the business is in great shape and he can take the time he needs to sell it in the best way possible for him, for his clients, and for his employees. If John had been able to go to college he would have made an excellent engineer.

John and Shirley spoke frankly to me and revealed that neither of them were knowledgeable about how to sell or price a business for sale. They advised me that the Construction Manager, Lee Williams, had expressed a strong interest in buying the business but that there was no commitment on either side. John determined that he would make his decision to sell based on the best, fair estimate of the business value. If that were to coincide with Don's interest and ability to pay he would be happy to see the business go to someone who knew the company and understood how it was run. John also expressed concern that the loyal clientele that ABC Construction had built up over the years be adequately served after his departure.

C. Ownership (,000)

<u>Name</u>	<u>Percentage</u>	<u>Common</u>	<u>Non Voting</u>	<u>Preferred</u>
John Smith	54.55	30	0	0
Shirley Smith	36.36	20	0	0
Mark Smith	5.45	3	0	0
Mary Smith	3.64	2	0	0

(Mark and Jill are the grown children of John and Shirley. Neither one has demonstrated an interest in the business)

D. Prior Sales Transactions of Company Stock

There have been no prior transactions in the company stock.

E. Subsidiaries and Affiliates

There are no subsidiaries or affiliates.

II. Management

A. Overview

Management team

NAME	TITLE	DUTIES	COMP.
John Smith	CEO/President/Co-Owner	Bidding, marketing, mgmt	120k
Shirley Smith	VP/CO-Owner	Office Management	120k

Key employees

NAME	TITLE	DUTIES	COMP.
Lee Williams	Construction Manager	Supervise 4 foremen Quality control	60k
Jack Schwartz	Estimator	Job Costings & budgets	40k
Steve Gonzalez	Maintenance Foreman	Supervise 2 mechanics Maintenance all equipment	45k
Joe Wilson	Office Manager, Controller	Supervise 2 staff; AP/AR	55k

B. Staffing

Number of Employees:

Full-time 14 **Part-time** None **Temporary** Varies by season **Contracted** 37

Are any employees covered by a collective bargaining agreement? Yes No

No copy of the collective bargaining agreement was available for me to include here, however, Lee Williams was kind enough to outline the key elements of the union contract. ABC Construction is a member of the *National Electrical Contractors Association* (NECA) and the union that ABC Construction employees belong to is the *International Brotherhood of Electrical Workers*. It covers all foremen, and electricians. Lee Williams, who formerly was a member has now moved into a

management position. Both these organizations contribute to a *Joint Apprenticeship Training Committee* that provides ongoing training for entry level employees. The basic terms of the collective bargaining agreement are as follows;

1. Hourly wages ranging from \$14.00 to \$24.00 based on seniority and job title
2. Medical insurance split 50%/50%
3. 401K program with 50% contribution of ABC Construction for every \$1 of employee contribution
4. 2 week paid vacation, increasing to 4 weeks after 10 years of service
5. Paid time off for apprenticeship programs
6. 50% contribution to continuing education programs in general electrical area

ABC Construction has been and continues to be very respectful of the union and willingly meets union demands that are negotiated on a statewide and national basis. Based on this good relationship, there has been labor peace throughout the life of the company. Electricians know ABC Construction to be a top tier company to work at and when a position comes open many apply for it.

C. Employee Benefits

Salaried staff have the same benefits that accrue to the hourly employees. This includes 50/50 medical insurance, 401k contributions of 50% of every employee dollar contributed, 2 weeks paid vacation leading up to 4 weeks with seniority, company contributions to continuing education. There are no unfunded pension liabilities or any need to accrue for this in the future.

D. Family Involvement

This is a family business. John and Shirley Smith have taken the base built by John and his father and developed it into a very strong, mid sized electrical contracting company. Eventhough they are family members their competence is not in question due to the results they are producing. A salary survey however has shown that they are over compensating themselves by 20k in John's case (120k instead of 100k) and 62k in Shirley's case (120 instead of 58k). This fact was taken into consideration in the normalization of the income statement and fully discussed with the owners.

E. Books and Records Quality

The accounting method is accrual. My observations of the financial records of the company, the staffing of the administrative area as managed by Shirley Smith and staffed by Joe Wilson and his two staff is completely adequate to provide sound financial reporting for this size and complexity business.

F. Employee Turnover

Turnover was analyzed as part of the RRCM discount rate. ABC Construction is characterized by labor peace and very low turnover. Most hourly employees recognize ABC Construction as a great place to work, especially in the light of the conditions and benefits available in other companies in the industry in that area. ABC Construction rarely loses an employee, and when one is lost, they have no problem finding a replacement of very high quality.

III. Physical Facilities

Premises

The facility is leased from the Smith Family Limited Partnership. This limited family partnership was set up by Reginald shortly before his death in 1996. It appears that he had two brothers and one sister who still live in England. Reginald did not have the money to start the business in 1985 so he made a deal with his brothers and sister to start and fund a partnership to buy the property and building on ABC Construction Boulevard. He made a long term agreement to rent the property at a competitive rate from the family partnership and his brothers and sister agreed to a long term contract and a transferable right of first refusal if they ever decided to sell the property. As the business prospered Reginald offered on several occasions to buy the property from the family partnership but neither his brothers nor his sister wanted to change the arrangement. Sensing that one day the company might have a problem, Reginald wisely bought the property adjacent to the current property just prior to his death. He reasoned that, if the family partnership ever decided to increase the rent beyond a reasonable amount or sell the land for an amount beyond his means, the company would have the resources to quickly reconstitute an operational base next door.

The current, rented facilities are 5400sq feet of building space on a two floor building that is on three acres with a full acre paved for vehicle parking and equipment storage. Administrative offices are on half of the second floor. The other half of the second floor is used for storage of inventory. The first floor is made up of two mechanics bays for truck and machinery maintenance. Adjacent to this are two workshops. The first is a machine shop with lathe, drill press, shapers and sophisticated pipe bending machines. The second is a metal fabricators shop equipped with a shearing machine, hand bending presses and rivet guns for fabricating the various electrical boxes and custom units that cannot be bought as inventory. Additionally, there are two small cubicles with desks that serve as offices for the construction manager and the estimator. The estimator also serves

as dispatch for job teams and is responsible for replenishment of inventory in the trucks that go to the job sites. At the extreme end of the building on the ground floor are 4 stand up dispatcher podiums. These are used by the four foremen to direct the activities of the work teams that they direct to the job sites.

This site set up provides ABC Construction with a competitive advantage over other firms since they can quickly build custom electrical boxes to solve problems. Teams at the job site call in the dimensions of the custom work and the maintenance foreman and his mechanics build the required units and drive them to the site.

The current premises are adequate for the current work load. John Smith advised that he had resisted the temptation to expand the facilities and invest more money in assets. He had felt that, given the cyclical nature of the industry, it would be better to deal with a bit of discomfort from time to time rather than have additional overhead charges to cover. The current rental contract is valid for an additional 9 years with annual review of rental amount based on a local rental survey done by an independent firm. So far these reviews have been done by Sue Land at Commercial Realty Company. My review of the rental agreement shows that it is a firm contract for the next 9 years. Unless there is mutual consent to eliminate it, both parties are obliged to abide by it. This is to the advantage of ABC Construction since the rental amounts are incidental as relates to overall revenues and represent a very small portion of expenses. This amount, even as it grows over the coming years, will continue to be less than the carrying costs of new construction on the additional land the company owns. This advantage could be negated if the additional land were to be developed so as to produce revenue to ABC Construction.

The adjacent land that ABC Construction purchased is a 5 acre parcel with equal ease of entry and exit. It is undeveloped. On several occasions customers have suggested ABC Construction build a larger building for themselves and rent excess space to construction companies. ABC Construction has considered doing this as it would provide additional revenue to the operation and hedge revenues from operations. But this has not been done so as to respect the agreement made by Reginald with his brothers and sister. John recognized that if the business continues to grow at over 10% in the following year as it did in the past year, his seasonal space pressure would begin to become a permanent space problem. In that case, he would be forced to begin to develop the adjacent property. John said that he frankly hoped to pass that issue on to the new owners. Having the additional land ready for development and owning a long term reasonable contract on existing facilities represented a very stable basis upon which to run and expand the business.

John also felt that in a selling situation he did not want to distract himself from the operations of the business or embark on a new project of that magnitude.

Age and condition of any major pieces of equipment used in the Company's business.

Most of the \$1.35 million in equipment is made up of rolling stock and electrical construction "kits" that accompany each truck when it goes out on a job. There are a total of 18 trucks and 20 electrical construction kits. These kits include ladders, wire cutters, bolt cutters, soldering equipment, portable welding equipment, electrical generators, spare parts and tools of all types.

The kits are standard for each truck and are maintained and tested weekly by the maintenance team. Any tools that fail are reported by the work crews and replaced immediately. Employees who abuse equipment are reprimanded. All kits are in excellent condition and provide lasting service. The life of a kit generally exceeds 5 years. The maintenance group replaces kits and kit equipment as it completes its useful life. The rolling stock is carefully maintained by the maintenance crew. This has been a source of pride for John as it was for his father. Full mechanical review of the rolling stock is done every 30 days or 3000 miles, whichever comes first. Trucks are equipped with bypass oil filters which have virtually eliminated engine wear and breakdown. Average mileage per truck per year is 25,000 miles. In 4 years trucks that reach 100,000 miles are assessed for quality and value. In most cases the maintenance crew overhauls engines, suspensions and transmissions and puts them back in service for another 2 years. As the vehicle approaches 150,000 miles of service it is retired from the fleet and sold at auction. The maintenance team works shifts that do not conflict with the truck's use during the daylight working hours of the work crews. Approximately \$300k of the equipment is made up of the machine and fabrication shop tools and presses. This equipment is robust and requires less maintenance and generally does not need replacement. Lathes and drill presses routinely are in service in companies for 30 to 40 years, with an occasional change of an electric motor; which, in the case of ABC Construction, are rewound by staff and reinstalled. Office equipment and computer equipment is replaced every 5 years. ABC Construction's software is up to date and compatible with the latest advances used in the industry.

IV. Contracts, Regulatory, Environmental, Other

A. Contracts

The electrical contracting industry generally operates under defined contracts on all jobs undertaken. These contracts can be drawn in a variety of ways depending on how the GC has done his contract with the developer. The most common are listed below.

Fixed Cost

Fixed cost is the simplest and represents over three quarters of the jobs held by ABC Construction. This simply means that ABC Construction contracts to complete the work in a specific period of time for a specific amount. Penalties can be charged for either delays beyond the allotted time or work that does not pass inspection. These contracts are generally in the form of firm bids for the work.

Cost Plus

Also used by GC's, cost plus contracts pay a sub contractor a set percentage over the actual direct and indirect costs the sub contractor logs on a job. The plus amount typically fluctuates between 7% and 12%. Additional bonuses can be paid for meeting specific performance levels or time deadlines. ABC Construction has approximately 10% of its contracts in this type.

Contingency

ABC Construction also has a portion of its contracts which include an estimated cost with cost escalations and contingency fees built in. These contracts are often used when the scope of work, in renovations for example, is not completely known at the outset of the job. In other cases the sub contractor's work can be affected by the non-completion of work by other sub contractors who are out of the scope of control of the first. In these cases contingencies are established to compensate the sub contractor for forced down time or lost job time.

Due to ABC Construction's very significant advantage in work efficiency they are able to make outstanding margins in all the contract alternatives mentioned above. Most advantageous to ABC Construction is the closed cost, fixed cost contract. In these cases their efficiency routinely produced margins of over 20% to the company.

B. Covenant Not To Compete

There are no covenants to not compete.

C. Proprietary Content

ABC Construction has 3 work advantages that can qualify as proprietary content in the sense that most electrical contracting companies do not have the discipline or in house expertise to duplicate them. They are; work kits that allow jobs to be done more efficiently and at lower cost, in house machine shop that can quickly make custom parts that other companies have to wait days or weeks to get, and 3 month back log and planning for jobs that includes staff needs, kit needs, and raw materials required. This pre-thinking of the key issues has consistently produced great rewards to ABC Construction.

D. Patents

ABC Construction holds no patents.

E. Copyrights

ABC Construction holds no copyrights.

F. Regulatory Issues

ABC Construction, like all electrical contracting companies comply with all federal, state and local code rules for electrical installation. Work done by ABC Construction is inspected by a myriad of different groups at almost every stage of work completion. GC has staff that are hired specifically to check for code violations. State and county governments also have periodic reviews of work quality as well.

G. Environmental Issues

ABC Construction has no environmental issues.

V. Marketing and Sales

A. Sales and Marketing

ABC Construction employs no direct sales people and marketing efforts are limited in scope. Mr. Jones, along with Lee Williams, are responsible for client contact at the managerial level. The majority of work that comes to ABC Construction comes from referrals and from repeat business from existing clients. The quality of the work the company does is the best calling card the company can have. This has been the management's belief from the beginning and their single minded focus on quality and service have proved them to be right.

B. Products and Services

The best way to describe the products and services provided by ABC Construction is to quote the California Occupational Guide number 121 on electricians.

“Electricians plan, lay out, install, repair, and maintain electrical equipment that provides light, heat, communications, and power. Electricians perform electrical work required in the building and remodeling of structures. They assemble, install, and connect lighting and power systems, thermostats, intercoms, signaling systems, and ventilators. Electricians follow blueprints and specifications to install electrical wires, cables and conduit systems. Electricians must have good mechanical ability, a thorough knowledge of the principles of electricity, circuitry, and power distribution within a building and familiarity with the materials and techniques of construction. For safety, electricians follow local electrical building and safety codes. On small

jobs they may work alone with minimal supervision, and they may supervise an apprentice. On large jobs they may work under the direction of the electrician supervisor or foreman.”

More specifically, ABC Construction provides all these services to both the residential and industrial markets. While ABC Construction revenues come primarily from new construction, remodeling jobs have begun to take a small but growing part of the business. Mark has supported the growth of this business to offset the potential slow down in work that comes when the construction industry takes a cyclical dip.

Common residential jobs can be the electrical installations for a new sub development of homes built by a customer general contractor. The contract is usually done between the general contractor and the electrical company. The residential developer approves the GC overall budget but most often does not intervene in the choices the GC makes for sub contractors. Consequently, the relationship between the GC and the sub contractor is extremely important.

Typically, ABC Construction would receive a call from a GC advising of a housing development going up and a timetable for when structural framing would begin and be ready to receive electrical installation. Shirley and John would chart the size of the development, dates and optimum mix of crews and timing to complete the project and then develop a project budget. John would review this budget with the customer along with the timing schedule. With a signature from the GC, ABC Construction would book the job and prepare staff as well as review inventory, schedule trucks, work crews and “kits” and back up in case something fell through. This process occurs generally with enough lead time for ABC Construction to purchase inventory and have it delivered just in time so that it can be included in the “kits” and used on the job site. Industrial jobs are done through very much the same process with the exception that they can often be larger and require a higher degree of expertise to comply with all the complexity an industrial or office building can demand. These jobs are managed by the most expert crews and often John himself and Don as well as the foremen pitch in and work directly on them.

C. Customer Concentration/Principle Suppliers

<u>Customer Name</u>	<u>Estimated Volume</u>	<u>Comments</u>
Newhaul Homes	650K	Tract home builder, requires fast, Accurate and inexpensive work
Jackson Brothers	700K	Office construction, warehouses, 16 year relationship is excellent
Depot Construction	350K	Referral business installation jobs of retailer merchandise. Possible

Fortune Development	750k	to expand this business into more areas High end apartment buildings and Luxury single family and town-Homes., High margin business With top of the line materials and Systems. Premium price for the Best quality work. Excellent and Growing relationship with Red Bluff
State of California	500k	Various projects from rewiring Existing bldgs to new const.

<u>Customer Name</u>	<u>Estimated Volume</u>	<u>Comments</u>
County of Any towm	500K	1 st year of a 10 year long plan To rehabilitate county schools, Hospitals, and offices
Nevada Gaming Inc	375K	New resort and casino wiring And refurbishments
Reno Development	450K	Single family tract homes and Town home developments
Any town Homes	725K	16 year relationship with this Successful local builder who has Land ownership to continue

		At the present rate for the next 7 years
Sun City Retirement Community	700K	Long term project of mid level and quality assisted living homes And apartments
EEZZ Storage	595K	Air conditioned storage units with 220volt current.
All others	1,000MM	Composed of new construction And re-modeling, residential and Industrial. No one customer Exceeds 200K
Total	<u>7,295MM</u>	

Composition of clients is excellent with no one client exceeding 10% of total revenues. This heralds high stability of revenues for ABC Construction. Furthermore, ABC Construction competes successfully in a broad range of electrical installation markets; new construction, residential, business, remodeling, contract installations, government work, and others. With expertise in all these areas ABC Construction helps itself overcome any downturn in any one of these market segments.

Primary Suppliers

<u>Supplier name</u>	<u>Inventory supplied</u>	<u>Alternate?</u>	<u>Comments</u>
Essex Wire	all types of wiring	Many	Dependable, good price, partial Lots
Johnson Wire	wiring products	Many	Bulk discounts and special orders Not a problem

Conduit experts	Conduit	Many	Bulk and small shipments Friend of Mark Smith
ABC Panels		Two	Standard and custom panels For switches
Jackson Switches	Switches and breakers	3	Standard switches and breakers for Single and multi family

C. Competition

Based on statistics produced by the Guide to the Electrical Contracting Market published in 1999, there are more than 7,500 electrical contracting companies in the State of California. The vast majority of these companies are comprised of 4 or less employees including the owner. They comprise an astonishing 58% of all companies. Another 19% of these companies are comprised of 5 to 9 employees, including the owner. This means that fully 77% of all electrical contracting companies in California are small, almost individual firms. The surprisingly fragmented nature of this market means that ABC Construction faces very stiff competition for work. Since most of these smaller firms will not have the resources to provide the infrastructure, materials, or the experienced personnel that ABC Construction offers, they typically compete on price alone. In many cases they employ illegal aliens at rock bottom wages to compete better. This represents a segment of the market that ABC Construction is consciously avoiding.

ABC Construction estimated that it had approximately 500 direct competitors in his geographical and local market area. As with the national averages, the vast majority of these competitors are the smaller, less capitalized, shoe string type operations that often bid jobs as lowest cost bidder. These small firms stay in business by picking up the smaller jobs and the rock bottom priced jobs that other, more established firms will not take. They are characterized by average to poor work, few or no work quality guarantees, lack of timeliness and an ever changing cast of characters as bottom rung employees. In many cases these firms are not used because they are not able to commit to completion times on larger jobs. They just do not have the size or manpower to handle them. They do not pay union wages or benefits.

From the other end of the spectrum there are the very large, state wide firms that have great economies of scale and employ several hundreds of electricians. These firms are successful on large projects for the speed with which they can complete a job and the generally good quality of work they do. However, in many cases, they truck crews in from other parts of the state and local General Contractors are not always comfortable working with people they don't know.

There is also a small group of direct competitors that are more or less the size of ABC Construction, with more or less the same kind of pedigree; local electricians who have worked hard and built up a steady and consistent work product and clientele and

who hire them consistently. John is friendly with this group of competitors and they often refer work to each other when they are overbooked. This is true but friendly competition. There has always been enough work for these firms to prosper. John estimates that the competitive set looks like this, but he had no statistics or research studies to back it up.

Total California

	Competitive Firms	Description	Number	Estimated % Firms
Total	Entire California Mkt	all firms, all sizes	7500 est	100%
	1-4 employees	smallest firms	4350	58.4%
	5-9 employees	next smallest	1455	19.4%
	10 -19 employees	mid sized	900	12.0%
	20-49 employees	mid sized	532	7.1%
	50-99 employees	large	150	2.0%
	100+ employees	mega	82	1.1%

Source: Guide to Electric Contracting Market, US Census 1999,
 California estimate of establishments
 John Smith estimates

Southern California/Western Nevada Local Area Market

	Competitive Firms	Description	#	Estimated % Firms	Sales Est.
Total	Entire SoCal/Nev	all firms, all sizes	500	100%	460MM
	<i>1-4 employees</i>	<i>smallest firms</i>	292	<i>58.4% both combined</i>	
	<i>5-9 employees</i>	<i>next smallest</i>	97	<i>19.4%</i>	<i><u>30MM</u></i>
	10 -19 employees	small mid sized	60	12.0%	90MM
	20-49 employees	mid sized	36	7.1%	108MM
	50-99 employees	large	10	2.0%	82MM

100+ employees mega 6 1.1% 150MM

Source: Guide to Electric Contracting Market, US Census 1999, California estimate of establishments

John Smith competition estimates

There are no statistics to measure sales by company but ABC Construction management's estimates are that the smaller jobs, the lowest margin jobs are handled by the smallest and next smallest firms. This, he estimates does not represent more than 20% of total market sales volume. The remaining 80% of the market is divided unequally between the rest of the companies in the local area market. As follows most industries, margins increase as sales volume goes up. Thus, companies in the 10 to 19 employee range will have sales revenues averaging about \$1.5MM per company. This makes margins razor thin and these companies are usually not very profitable. The large and mega companies will be working with margins in the 10 to 15% range, depending on the job.

D. Product / Service Differentiation

ABC Construction has pioneered an extremely effective tool to make work crews and job results more efficient and cost effective. John Smith, ABC Construction President and CEO, developed the idea of creating work "kits" for each of his trucks and crews going out on jobs. John's 3 month pipeline planning of jobs allows the company to know what materials and tools will be needed on each job. The maintenance personnel are tasked with making sure that when trucks go out on jobs they have a "work kit" that has all the tools and materials they will need to complete the job. These kits make ABC Construction around 25% more efficient in every aspect; time, staff, quality, quality control, and on spec work. Additionally, having a machine shop on the premises has allowed ABC Construction to make custom junction boxes, repair complicated and costly high voltage breakers, and do complex conduit bending by receiving specs over the phone and delivering the parts to the site within hours. No other electrical contractor of any size has this efficiency level.

Advantages

ABC Construction has some significant advantages over its competitors. The long term commitment to on time, within budget work has paid off. They are well established in the market after 16 successful years of operations. They have a wide variety of customers with none representing more than 10% of the overall sales. The quality of the work is excellent. Happy, well paid employees at union rates are stable and there is low turnover. ABC Construction has a strong reputation in the market, with excellent facilities and equipment. Importantly, they have a high degree of repeat business from existing customers. Over 50%

of the business comes in the door from existing customers that do not require costly new business visits, sales pitches, and low-ball bidding. Finally and most importantly, ABC Construction's system of work trucks with work "kits", the innovative way they plan work and employee quality and permanence give them a competitive advantage over firms of all sizes. This allows them to work faster and more efficiently and produce a better margin than competitors.

Disadvantages

Supervisory staff is overextended with so many work teams and projects to manage. Union wages are automatically approximately 20% higher than non union competitors. This is mostly offset by the higher degree of efficiency that ABC Construction demonstrates on projects. Competitive threats are significant and come from larger firms constantly working to develop relationships with ABC Construction's customers. The pace of innovation is increasing and requires constant vigilance that, in an average size firm like ABC Construction, is more difficult to invest in and manage. Finally, the maquiladora and illegal alien problem has increased dramatically over the past few years. When interest rates rise and construction budgets are squeezed, General Contractors need to cut corners in every area. During these times it is very difficult for GC's to continue paying higher amounts for work that they could get for very much less with illegal workers. In these cases, ABC Construction cannot compete. ABC Construction plans for these situations and so far has been able to avoid them but it is an ongoing issue.

E. Relative Product / Service Quality

As stated in other parts of the business review, ABC Construction is well known for the quality of work they do. Customers routinely return to give work to ABC Construction because of their ability to deliver a superior product on time and within budget. High quality comes from careful job planning, the establishment of work kits that reduce down time and allow teams to be more efficient, an in house machine shop and metals shop that can provide custom junction boxes and conduit bending on demand and have it on the job site within hours. ABC Construction is able to solve problems quickly and efficiently. These attributes are highly regarded by GC's. These product superiorities are accompanied by very good personal relationships among ABC Construction management and the managements of the GC's.

F. Pricing

Pricing is an area where ABC Construction has some potential problems in the future. The fact that ABC Construction pays union wages and benefits puts the company at a disadvantage against low cost illegal aliens who work for wages far inferior to

those ABC Construction pays. Even with much greater efficiencies and higher quality, it will be harder and harder for ABC Construction to compete with companies who are able to charge much less.

G. Size of the Company

At 47 employees ABC Construction is considered a mid sized electrical contracting company. They have developed sufficient sales and gross profit size (\$7.2MM and \$2.2MM respectively) to have the resources to compete successfully with most other competitors. In many ways, ABC Construction has an advantage over larger companies because they are not so large that jobs get lost in a huge infrastructure that operates on volume and low margins. ABC Construction is able to give personal, dedicated and highly effective service to clients. The quick turn around of the machine shop for custom junction boxes and complex conduit bending as well as the effectiveness of the kits in speeding work make ABC Construction a very efficient partner to GC's. ABC Construction also has an advantage over smaller firms in the market due to their revenue and profit size. They are able to maintain a top quality infrastructure to keep the work teams working effectively and there is additional staff that can be called on when needed in a pinch. Mr. Jones himself is known to roll up his sleeves and handle the most difficult jobs himself.

H. Market Size and Share

Based on the estimated size chart reported above, ABC Construction appears to have approximately 6.6% of the market share of the mid sized electrical contracting market (7.2mm/108mm segment volume) or 1.5% of the overall Southern California/Western Nevada market. It can be said that this revenue level is one of critical mass in the sense that the company is able to maintain a top quality shop with well functioning equipment and a good flow of work supplies and not succumb to the low resource problems that plague the smaller companies. At the same time ABC Construction is still small enough to provide personalized service to their clients. ABC Construction clients are, however, increasingly the targets of other larger companies. Since product quality is not an area where the larger companies can compete, they are focused on lower prices and the ability to bring innovative solutions to developer's problems like massive work teams who can finish a whole development in a very short time. In some cases these large firms are successful in bypassing the GC altogether and getting jobs assigned directly by the developer. This is not a trend yet but it is an area where ABC Construction will need to take care. As the industry evolves ABC Construction will need to make sure they continue to be relevant to key customers.

I. Industry Life Cycle

The construction industry life cycle, of which electrical contracting is a part, depends largely on the overall economic indicators for the country and, more specifically, for the geographic region and local area. Home buying, office building construction for

rental, and public sector construction all depend on a healthy economy and optimistic individuals who see a safe future for themselves and are willing to take on a long term financial commitment. The same factors are in play in the decisions of businesses. Occupancy rates, positive outlooks for businesses, growing companies look on investments in real estate as a necessary part of their overhead. When times are tough, these areas are the first to be cut to protect the life's blood of the company.

ABC Construction is in a strong position to capitalize on the good times that are forecast for Southern California but at the same time they have a good hedge against tough times. They have quietly been increasing their involvement in the do it yourself industry and the remodeling/refurbishing industry to gain knowledge and expertise to use if the construction market declines.

ABC Construction has also resisted the temptation to invest in expensive construction of new offices or plant. They operate efficiently out of their current site and do not plan to make changes in the physical plant.

Supervisory staff is stretched thin covering 12 work teams but the company's plan is to elevate a work team boss to a supervisory level once an aptitude has been shown in that area. This is a policy of promoting from within and shows all staff that growth within the company is possible and is fostered.

VI. Summary of Positive and Negative Factors

Positive Factors

1. Excellent profit margins
2. High quality work
3. On time and on budget
4. Excellent work relationships with staff
5. Excellent client relationships
6. Strong repeat business
7. Ability to change quickly, adaptability
8. Balanced client list
9. Strong market reputation
10. Gowing

Negative Factors

1. Risk from larger companies
2. Illegal aliens undercutting price
3. Pace of innovation
4. Selection made at developer level
5. Unknown if RB can manage the growth they will need to remain competitive.
6. Stretched supervisory staff

VII. Principal Sources of Information

Financial data and operational information from ABC Construction Staff
US Department of Commerce/Bureau of the Census
1992-97 Economic Census Construction Industries, Final Reports, California
US Department of Commerce/Bureau of Economic Analysis
Engineering Record
Electrical Contractor
Air Conditioning, Heating & Refrigeration News
CIT Group Industry 2001 Construction Industry Forecast
US Department of Labor/Bureau of Labor Statistics
California Employment Development Department
Federal Reserve Bank, Beige Book
California Department of Finance
FDIC, Regional Economic Conditions
Nevada Department of Employment, Training & Rehabilitation
Construction Financial Management Association
Robert Morris Associates, Samples of company data
BizComps and IRS company transactions

ECONOMIC OUTLOOK AND INDUSTRY ANALYSIS

In conjunction with the preparation of this valuation opinion, I have reviewed and analyzed current economic conditions and how ABC Construction and the industries in which it competes might be impacted.

I. The National Economy

THE NATIONAL ECONOMY Third Quarter 2000 and Outlook for 2001

The following discussion and analysis of the national economy for the third quarter of 2000 is based upon a review of current economic statistics, articles in the financial press and economic reviews from current business periodicals. The purpose of the review is to provide a representative “consensus” on the condition of the national economy and its general outlook through 2001.

ECONOMIC SECTOR ACTIVITY

During the third quarter of 2000, the economy of the United States showed further evidence of a slowdown. **Retail** and **automotive** sales, along with **housing starts**, moderated from the brisk pace set earlier in the year. Government spending slackened and inflation remained becalmed. As validation, the **yield curve** —which had inverted earlier in 2000— began to flatten, as yields on 5-year bonds finally slid below long-term interest rates. The Federal Reserve Bank, in the quarter, continued to hold short-term interest rates steady at its August meeting, but still tilted toward tightening later in the year. The consensus is that we have seen the last of the Fed’s increases for this business cycle, nonetheless. By keeping a tight grip on the money supply, the central bank has been successful in allowing enough to flow into the economy to maintain growth without re-igniting inflation. Recent increases in the price of **crude oil** and prospects for ramping up of gasoline, heating oil and natural gas prices have led many “outsiders” to conclude the consequences of the new energy crisis will be similar to those we experienced in the 1970s; the consensus of “insiders” thinks otherwise. The rapid inflation and spiraling interest rates during that decade were not driven by the oil embargo of 1973 —rather, these phenomena occurred *in response to* the Fed’s actions to deal with that dislocation. This time, the Fed’s mindset is totally different. The Board is allowing liquidity in the system to grow only as fast as the system’s ability to absorb it through the production of goods and services. While relative prices can undulate in this environment, increases in one sector cannot necessarily be passed along to others; case in point, the price of gasoline. Presuming *gasoline prices* rise to \$2.00 or more a gallon for a prolonged period, prices of *sport utility vehicles* would be expected to drop six months later. If consumers drive less often to the mall and buy fewer items when there, the prices of other goods will not necessarily rise. Finally, the Fed’s *Beige Book* of November 1 (reflecting economic activity during the third quarter of 2000) noted higher **petroleum-based manufacturing input costs**, but qualified it by mentioning *strong competition* amongst producers, which prevented the majority of firms from passing on much of the cost increases to their customers.

A. GEOGRAPHICAL DISPERSION OF THE FEDERAL RESERVE BANKING SYSTEM

The twelve Federal Reserve Districts are geographically divided, straddling states and regions of the U.S.:

II.	DISTRICT #	BANKING CENTER	REGIONS SERVICED
	ONE	Boston	New England
	TWO	New York	NYState, Northern New Jersey, Puerto Rico, Virgin Islands
	THREE		Phil, Delaware, Eastern Pennsylvania, Southern New Jersey
	FOUR	Cleveland	Ohio, Western Pennsylvania, Eastern Kentucky

FIVE	Richmond	Maryland, Virginia, W. Virginia, N. Carolina, S. Carolina
SIX	Atlanta	Georgia, Eastern Tennessee, Alabama, Southern Mississippi, Florida, Southern Louisiana
SEVEN	Southern Michigan	Chicago, Illinois, Northern Indiana, Southern Wisconsin, Iowa,
EIGHT	St. Louis	Missouri, Arkansas, Western Kentucky, Southern Indiana, Western Tennessee, Northern Mississippi
NINE	Minneapolis	Northern Wisconsin, Northern Michigan, N. Dakota, S. Dakota, Minnesota, Montana
TEN	Kansas City	Kansas, Nebraska, Oklahoma, Colorado, Northern New Mexico, Wyoming
ELEVEN	Dallas	Texas, Southern New Mexico, Northern Louisiana
TWELVE	San Francisco	California, Oregon, Washington, Idaho, Nevada, Utah, Alaska, Arizona, Hawaii, Guam, Samoa, other U.S. Pacific territories

III. CONSUMER SPENDING

Retail sales have generally slowed from earlier in the year, and merchants described growth as “modest” over the quarter. Retailers in New York and Richmond Districts noted marginal movement in the volume of sales as the quarter closed, and in the Atlanta, Boston, Chicago and Philadelphia Districts, sales levels had met merchants’ expectations. Inventory levels were described as “balanced” in Atlanta, Dallas, New York and Philadelphia, while Chicago and Kansas City identified with somewhat higher than desired accumulation. **Apparel sales** showed mixed responses, but early cool weather contributed to some pickup in sales volume. More broadly, the retail outlook has become increasingly conservative since last quarter, which may have stemmed inventory growth already.

Reports on recent **motor vehicle sales** were mixed, but still at generally high levels. Sales in the Kansas City District were up slightly in September, and dealers were largely successful in **managing inventories** during the model changeover period. Automobile sales were better than a year ago in Chicago, and inventories there were considered under control, but they were reported as slowed in Dallas and Philadelphia, and slightly below last year’s [record] levels in Cleveland.

IV. SERVICES AND TOURISM

While the service sector continued to post solid growth, attracting and retaining employees remained difficult. Boston noted the pace of **restructuring in the insurance industry** has slowed, and little additional retrenchment is planned. Some **information technology and systems** industry contacts reported difficulty in finding and keeping qualified employees. There was some softening in revenue growth for business service firms in the Richmond District. Dallas signalled the demand for **transportation services** remained strong, even with recent *fuel surcharges*; in San Francisco's large and diverse region, there was strong demand for most services over the quarter.

Tourism and hospitality-oriented regions had mixed seasonal results. Atlanta and Richmond cited growing concerns that rising fuel prices have already discouraged tourists. Minneapolis reported fall season tourism in its District was on a par with last year. San Francisco noted healthy growth in tourism to Hawaii was boosting hotel occupancy rates and room prices

V. REAL ESTATE AND CONSTRUCTION

Most reports characterized the level of activity in **single-family housing** markets as "healthy," despite slowing sales and construction volume. There were scattered reports, nonetheless, of rising home inventories in the Atlanta, Boston and St. Louis regions, and some *price concessions* in the Atlanta District. The Kansas City, New York and San Francisco Districts reported some pickups in housing activity. Generally, contacts anticipated the market would remain seasonally strong, although the pace of construction and home sales was expected to decline further through year-end.

Commercial real estate markets, overall, continued to perform well, although there was increasing evidence that construction levels are waning slightly. Contractors in the Atlanta District noted construction backlogs had declined, and construction has slowed in the St. Louis District. Vacancy rates retreated marginally in parts of the Atlanta, Kansas City, New York and San Francisco Districts. Site and utility inquiries have decreased significantly in central Indiana, and contract work has shrunk [seasonally-adjusted] in the Dakotas and Minnesota. In the business district of New York City, despite rapidly escalating office rents, industry authorities plan only a moderate volume of new construction over the next couple of years.

VI. MANUFACTURING

Manufacturing activity was generally steady during the quarter, with only a few areas of continuing weakness. Atlanta, Boston, Dallas and San Francisco reported expanding activity in the **high technology sector**. Manufacturers' **capital spending plans** were strong in Boston and Philadelphia, while Atlanta and St. Louis reported expansions in *light vehicle production facilities*. Although overall manufacturing conditions remain favorable in the New York and San Francisco Districts, weakness in the **Euro** had reduced orders for some manufactured goods. The pace of manufacturing activity increased in Kansas City and Minneapolis Districts, however. Strong demand for household appliances led to factory expansions in the St. Louis District, while large **shipyard contracts** were boosting

activity in the Atlanta District. San Francisco reported strong sales in the **aerospace, semiconductor and pharmaceutical sectors**. Petroleum product **refineries** were operating at near capacity in Dallas and New York. Less favorably, **paper and lumber mill** production was slowing and inventories were accumulating according to Atlanta, Dallas and Minneapolis. Chicago reported an increase in **steel imports** led to slower production and softer pricing in that industry. Heavy-duty truck producers continued to cut back output in Chicago and Cleveland because of a weaker volume of new orders. In the Philadelphia District, working hours have been reduced at many manufacturing plants, and inventories have risen. Atlanta noted that the downsizing of the **apparel industry** continued during the quarter.

VII. BANKING AND FINANCE

Growth of **loan demand** remained strong across the country, but with some softening noted. Overall lending activity was reported as “solid” in Atlanta and Chicago, and “stable” in the New York District. Total loans outstanding were up slightly, according to St. Louis. Kansas City, Philadelphia and Richmond reported growth of lending activity slackened in September. Dallas revealed the pace of financial sector activity continued seasonally slower than a year ago. In New York there was a slight pickup in commercial and industrial sector loan volume, while Cleveland and Philadelphia banks reported marginal increases in business lending activity. **Refinancing** activity continued to decrease in the Kansas City, New York and Philadelphia Districts, but increased in Chicago as the quarter ended. Atlanta and New York reported further *weakening* in demand for both residential and commercial mortgages. Real estate and consumer loan demand remained unchanged in St. Louis, against rising home inventories and slowing construction.

Many Federal Reserve Board contacts continued to express concerns about **credit quality**, although most reported that overall, it was still at “healthy” levels. In New York, credit standards were tightened further on commercial and industrial borrowers, while commercial lenders in Richmond were monitoring *hotel and other commercial real estate loans* closely during the quarter. Chicago reported business lending standards remained tighter than earlier in the year; in Atlanta, there were expectations that third [and fourth] quarter *credit losses* would rise. San Francisco reported credit quality was generally good, but there was some tightening of *credit conditions* for commercial real estate lending. Lending standards were largely unchanged in the Kansas City District, and Philadelphia reported credit quality for both business and personal loan portfolios continued “steady” over the quarter.

VIII. LABOR MARKETS

Demand for labor remained robust during the quarter, overall, to the extent the Federal Reserve Board described markets as “taut.” Some reports cited notable **upward pressure on wages**. In the Philadelphia District, firms were having considerable trouble finding qualified workers, and many companies raised wages in greater magnitudes this year so far than in the latter 1990s. The **skilled labor shortage** also remained a challenge in Boston and Richmond Districts, and employment agencies reported trouble filling job openings in New York. Dallas indicated that while labor markets remained tight, the recent shakeup of Internet companies had released some

high technology workers in the District. In the Kansas City region, employers were increasingly using **flexible work schedules** to attract and retain workers. Minneapolis reported widespread concern over worker availability and retention. In the Cleveland District, contacts noted strong wage increases in fast-growing companies across the “old economy-new economy” spectrum; this scenario also prevailed in San Francisco and St. Louis.

IX. PRICES

While **petroleum-based input product prices** continued to rise over the quarter, strong competition reportedly prevented many firms from passing along much of the cost increases to customers, except in **transportation** and a few local industry areas. Rising costs resulted in increased pressure on **profitability** for firms in the Atlanta, Cleveland, Minneapolis, Philadelphia and San Francisco Districts. Price pressures were characterised as “diminishing somewhat” in New York, and —with the exception of **energy**— most prices were stable in the Cleveland, Dallas and Kansas City Districts. Atlanta’s construction and manufacturing pace were contributing factors in the decline of building materials prices, such as lumber and drywall (which had previously escalated, bolstered by weather-related activity). Strong **import competition** has been depressing prices in the San Francisco District, but, in contrast, Boston noted some manufacturers were passing along more of their increasing costs to customers than in previous reports over the last year. The increasing cost of **health and other insurance** programs continued to be reported as a concern in Atlanta, Chicago and Philadelphia, despite merger and acquisition activity in those industries.

X. AGRICULTURE, ENERGY AND NATURAL RESOURCES

Oil and natural gas exploration were at sustained high levels in the Dallas, Kansas City and Minneapolis Districts during the quarter, spurred by strong demand and price increases nationally. Agricultural production results varied greatly, however, across the country. St. Louis, for instance, reported cotton estimates for District States were below normal as the quarter ended —reflecting a smaller-than-expected increase in **harvested acreage** and a sizeable drop in **yield**— while the Dallas District noted most of the cotton and sorghum crop has been declared a total loss. The weather, again was a contributing factor, as a prolonged dry period hurt harvests. On the other side, record **corn and soybean** harvests were expected from Kansas City, and Chicago projects them to be up 6 and 5 percent, respectively, from last year. Farmers in North Carolina and Virginia made “good progress” harvesting the peanut and cotton crops. Pasture and livestock conditions ranged from fair to excellent nationally; while **low grain prices** have cut feed costs for Kansas City District livestock producers, the *high price of young feeder cattle* has cut into feedlot profits. San Francisco District ranchers reported continuing strong demand for beef, along with firm prices, but the ongoing drought in the Southwest is a persistent constraint on profits in this sector. Rising oil prices and a **shortage of diesel fuel** have increased packaging and shipping costs in most of the agricultural sector nationally during the quarter.

OUTLOOK

Although this economic cycle's expansion appears to be slowing —and there are clearly risks to the outlook— the consensus of economists contributing to our forecast predicts a sharp downturn will be avoided. According to the latest *National Accounts Report* from the U.S. Department of Commerce, the prognosis for a “soft landing” is strong, as Gross Domestic Product growth in the quarter eased to 2.7% (on an annualized basis), following 5.6% and 4.8% paces in the second and first quarters, respectively. The slowdown was influenced primarily by a deceleration in **inventory growth**, a downturn in **government spending** and slower growth in **business investment**; forecasts for the latter two variables have diminished in this quarter's consensus. While business investment has played a significant role in the U.S. economic expansion since 1995 —increasing by over 10% in each of the last four years— we must keep in perspective the third quarter slowdown follows exceptionally strong growth in the first and second quarters.

Furthermore, although it has contributed to downgraded projections for 2000 and 2001, **investment** is still expected to increase by 13.3% this year and 8.5% the next.

It is also significant that two more recent indicators of **demand** —the Conference Board's *Consumer Confidence Index* and the *Redbook Measure of Retail Sales*— have both declined, signalling another slowdown during the fourth quarter. Slower demand typically serves to ease **inflation concerns** that have been [qualifiedly] fuelled by a persistently tight labor market and rising energy prices. Again, the key to sustenance of the economic expansion rests with the end-user **consumer**. The retail outlook has become *increasingly conservative* since last quarter:

- ? Merchants in the Atlanta District expect fourth quarter sales growth to be modest
- ? Dallas retailers lowered their outlook for the next six months
- ? Retailers in Chicagoland and contiguous States anticipate consumers will have less discretionary income, because of higher home heating costs this winter
- ? Inventories are higher than desired in the Kansas City District
- ? Continued volatility in the equities markets has constricted windfalls that drove spending in the 1990s
- ? Political uncertainties at the national level have kept many investors on the “hesitant side” this quarter

While the consensus of [political] economic thought embodied here continues to expect no change in the Fed's monetary policy over the next quarter, debt and equity market oscillations —combined with tensions in the Middle East, and the trans-Atlantic trade wars— also raise the probability of a move to **ease** short-term interest rates, sometime in next year's first half. Given a recovering **earnings** scenario, a “shakeout” in the *virtual* side of the high technology sector, and the potential for lower interest rates, the outlook for the next year is looking more optimistic at this time.

November 2000

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XI. The Regional Economy

The Federal Reserve Bank of San Francisco had these general comments to make about the 2000/01 forecast for California.

“California’s economy continued its robust expansion in recent months. Following strong growth in total non-farm employment during the first quarter of this year, growth picked up further in April and May to a pace over 5 percent on an annual basis. As of May, employment is 3.3% above its year earlier level. Much of the growth so far this year, especially in May, came from the hiring of a large number of temporary Census workers. The pace of private sector job growth this year has been about equal to the 2.7 percent pace recorded in 1999, with the fastest growth evident in the construction transportation, and communications sectors. The unemployment rate was 5% in May, exactly equal to its level at the end of last year.”

“Real Estate sales and construction activity remained at high levels in most District states, although the pace of growth slowed in some areas. Condo and single family home prices continued to increase in California, except for some parts of the Central Valley...The commercial real estate market also is very strong in most areas in California. Contacts in the state noted that rental space and construction labor were in short supply, and rents and construction costs increased.”

The Western Economic Development report published by the Federal Reserve Bank of San Francisco highlights are indicative of economic growth expectations going forward from this report in June of 2000.

“Executive Summary

- The Twelfth District’s robust economic expansion continued in recent months. The employment growth rate of 3.6% so far in 2000 is well above the corresponding national rate, and both were boosted by a surge in federal government hiring of temporary Census workers in recent months.
- In California, private sector jobs have grown at about the same strong pace as last year, and the availability of labor and real estate is remarkably tight in the San Francisco Bay Area.

- Among District states, Oregon, Alaska, and Utah have exhibited the slowest growth this year, with job creation well below the national average.
- Growth in District construction employment has slowed this year, as evidence of slight cooling in residential real estate markets has emerged. The exception is California, where continued strong demand relative to supply has been raising home sales prices at a double-digit yearly pace.
- Prospects for the District manufacturing sector have improved this year, largely due to an increase in domestic and international demand for high-tech products.

Based on the robust growth predictions for continued growth in the housing market in California, we have taken a more modest growth approach. Given the size of ABC Construction and the composition of the market where they operate, we predict that the market will grow in 2001 at a rate of between 5 and 10%. We estimate this growth rate will soften in subsequent years to an average of 1 to 3%.

XII. The Local Economy

Additional indications of strength in the regional market come from the California Department of Finance Economic Indicators for July/August 2000. Here are some highlights;

- Growth in the California economy continues to outpace the robust national performance. Employment growth remains strong. Construction is growing, real estate demand is strong and exports are expanding.
- California's job market is strong, registering large gains in most key measures including the civilian labor force, civilian employment and private non agricultural wage and salary jobs.
- On a year over year basis, non farm employment grew by 3.2 percent in June reflecting the addition of over 450,000 jobs. Construction continues to be the fastest growing industry, expanding 8.7 percent over the year.
- Statewide, total residential construction, measured by permitted units, increased 25% over the year, to a seasonally adjusted annual rate of 188,200 units.
- Multi-family unit permits jumped 146% while single family permits were down 15%.
- Through the first half of 2000 housing permits are up over 7% from comparable year ago levels.

- Following strong performance in May, non residential construction measured by permitted value dipped 3.7% on a June to June comparison but is still up over 8% this year.

The estimates of growth at the state level are supported by the optimistic review of performance for the local market. Having had experience with these forecasts and knowing that they can change drastically with changes in the national economy, we project a modest growth for the local market and estimate average growth for the next 5 years of 1 to 3%.

We believe that this growth rate will be achievable for ABC Construction going into the future, even if economic conditions deteriorate and the industry growth slows or retracts in some years. This is because of several reasons. ABC Construction's strong margin that allows them to reduce profit and remain competitive. The high quality of the product and the good relationships with clients will continue to get them bids even in downturning markets. The flexibility with which ABC Construction approaches the market, having a client base in new construction, residential, office, government, and remodeling, allows them to emphasize different targets depending on where the revenue is.

XIII. Industry Outlook

Local industry outlook factors include a recognition that individual stand alone family home starts may be lower than last year by a small margin but that will more than be made up by an increase in multifamily homes and industrial and office construction. ABC Construction is well positioned to continue to take advantage of this trend in the market, being considered as one of the best quality firms in the market.

A key issue going forward for the industry is the prediction of where interest rates will head in the next year and following year. Currently, most forecasters including, Bob Murray at McGraw-Hill, Bill Toal at Portland Cement Assn. and FMI (source Electrical Contractor Magazine, January 2000) predict that inflation will be kept at bay by an ever vigilant Federal Reserve board which is ready to increase interest rates if the economy appears to show signs of inflation. This hair trigger response to macro economic factors and the risk that interest rates could rise will have a dampening effect on the construction market.

The most important factor affecting the construction industry, along with local employment, are the interest rates levels for new development. Since interest rates are a leading indicator of economic activity and employment rates are a trailing indicator, we can be sure that developers and the overall construction industry will be highly sensitive to interest rate movements and in many cases plan future development based on how interest rates move.

We predict a cautious growth period for the construction industry and an optimistic future for ABC Construction, especially because ABC Construction offers so many of the characteristics that are prized by GC's and developers. When and if the industry slows down, ABC Construction will continue to be called to bid and will be hired because of their reputation of quality and on time within budget results. The greater risk for ABC Construction is from larger firms working at lower margins and low cost immigrant workers who undercut pricing.

When interest rates increase, developers margins are immediately affected. This produces a cascading effect that first impacts GC margins and immediately afterwards the major sub contractors. Loyalty to suppliers has been a trade mark of many GC's but it will not withstand major reductions to their margins. ABC Construction will need to be ready with an ability to work for less money and continue to raise efficiency standards. Given that their margins are very significantly above the norm for the industry, we predict that ABC Construction will weather any storm that arises.

FINANCIAL ANALYSIS

Financial analysis is executed for various purposes including 1) assessing the financial condition of the subject, 2) identifying potential normalizations to be considered, 3) determining the financial risk of the subject, 4) using the results of financial analysis to support derivation of the company-specific risk premium, etc.

Analysis of financial statement ratios can be a useful tool in a business valuation. It can identify and quantify some of the company's strengths and weaknesses, both on an absolute and relative basis to other companies or industry norms. Financial statement analysis should be done early in the engagement to develop an understanding of the business as well as to develop additional inquiries of management. Similarly, financial statement analysis should be done at the conclusion of the engagement as part of a benchmarking analysis. While there are several analytical tools available, the most commonly used are ratio analysis, common size financial statement analysis, horizontal-vertical analysis, etc.

Ratio analysis focuses on (1) liquidity ratios – an indication of the company's ability to meet its current obligations; (2) coverage ratios – designed to measure the margin by which certain of the company's obligations are met; (3) leverage ratios – assesses the long-term solvency of the business; (4) operating ratios – measures how efficiently a company uses its assets; and (5) and other ratios (for example, operating cash resulting from revenues, officers' compensation as a percentage of sales). Each of these ratios may be compared with its peer group through various published databases or with industry specific data. Care must be taken in strict reliance on some of the published databases in that they may not be statistically valid. They do; however, provide a general framework for comparison.

I. Historical Data

A. Balance Sheets

The following represents the historical assets, liabilities and equity of ABC Construction for the respective years shown:

	2000	1999	1998	1997	1996
ASSETS					
Cash	3,553	2,655	1,519	415	259
Accounts Receivable	891	714	689	750	290
Inventory	49	45	39	30	25
Other Current Assets	0	0	0	0	0
Total Current Assets	<u>4,493</u>	<u>3,414</u>	<u>2,247</u>	<u>1,195</u>	<u>574</u>
Fixed Assets	1,825	1,593	1,463	1,390	1,362
Net Intangible	0	0	0	0	0
Other Non-Current	150	150	150	150	150
Non-Operating Assets	0	0	0	0	0
Total Assets	<u><u>6,468</u></u>	<u><u>5,157</u></u>	<u><u>3,860</u></u>	<u><u>2,735</u></u>	<u><u>2,086</u></u>
LIABILITIES & EQUITY					
Accounts Payable	10	12	15	13	11
Short Term Notes Payable	135	119	111	88	73
Current Portion of LT Debt	0	0	0	0	0
Other Current Liabilities	3	4	2	5	3
Total Current Liabilities	<u>148</u>	<u>135</u>	<u>128</u>	<u>106</u>	<u>87</u>
Long Term Debt	1,831	1,517	1,158	830	705
Other Non-Current Liabilities	0	0	0	0	0
Non-Operating Liabilities	0	0	0	0	0
Total Liabilities	<u>1,979</u>	<u>1,652</u>	<u>1,286</u>	<u>936</u>	<u>792</u>
Total Equity	<u>4,489</u>	<u>3,505</u>	<u>2,574</u>	<u>1,799</u>	<u>1,294</u>
Total Liabilities & Equity	<u><u>6,468</u></u>	<u><u>5,157</u></u>	<u><u>3,860</u></u>	<u><u>2,735</u></u>	<u><u>2,086</u></u>

B. Income Statements

The following represents the historical income and expenses of ABC Construction for the respective years shown:

	2000	1999	1998	1997	1996
Revenue	7,295	6,489	5,755	4,156	3,529
Cost of Goods Sold	5,055	4,458	3,956	2,965	2,498
Gross Profit	<u>2,240</u>	<u>2,031</u>	<u>1,799</u>	<u>1,191</u>	<u>1,031</u>
Operating Expenses	401	333	289	224	191
Officers' Compensation	240	192	168	144	120
Depreciation/Amortization	73	84	86	68	57
Interest Expense	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Operating Expenses	<u>714</u>	<u>609</u>	<u>543</u>	<u>436</u>	<u>368</u>
Operating Profit	1,526	1,422	1,256	755	663
Other Income/(Expense)	<u>84</u>	<u>67</u>	<u>53</u>	<u>31</u>	<u>22</u>
Income Before Taxes	1,610	1,489	1,309	786	685
Income Taxes	<u>626</u>	<u>558</u>	<u>491</u>	<u>324</u>	<u>270</u>
Net Income	<u><u>984</u></u>	<u><u>931</u></u>	<u><u>818</u></u>	<u><u>462</u></u>	<u><u>415</u></u>

II. Comparison to Industry

A. Comparison to RMA

In making a comparison of ABC Construction to the industry, I have used information from The Risk Management Association (reprinted here with permission from the source). Risk Management Association (RMA) provides its *Annual Statement Studies (Statement Studies)* based on information provided by member banks and other financial intermediaries. A key value of this popular data source is that the format of the information has been reported in a consistent format for several years.

The ratios and other information provided by RMA can be particularly useful when comparing *Statement Studies* data between different periods. However, RMA recommends that *Statement Studies* data be regarded only as general guidelines and not as absolute industry norms.

The information in the *Statement Studies* is currently provided for over 600 industries in common size format with accompanying ratios. The industries are organized both by Standard Industrial Classification (SIC) and by the North American Industrial Classification System (NAICS).

Both balance sheet and income statement information are presented for each industry in six size categories according to total assets or total sales (or revenues). RMA also provides the comparative historical data for each industry for five years.

RMA defines and illustrates the calculation of the ratios. The ratios are grouped into four categories: liquidity, coverage, leverage, operating, and specific expenses. Each ratio is then presented with three values: the upper quartile, median, and lower quartile.

1. Ratio Analysis

The following table shows a comparison of ABC Construction to the RMA data.

	Median Qrtl RMA Curr Yr	IRS	2000	1999	1998	1997	1996	Median Minimum	Maximum
LIQUIDITY RATIOS:									
Current Ratio	1.6	1.4	9.4	10.5	10.2	8.0	5.9	0.0	0.0
Quick (Acid-Test) Ratio	1.3	1.1	9.1	10.1	9.8	7.7	5.6	0.0	0.0
Revenue/Accounts Receivable	5.7	4.8	8.6	9.6	8.8	5.8	12.8	0.0	0.0
Average Collection Period	64	76	42	38	41	63	29		
Inventory Turnover	126.0	29.7	96.2	92.7	94.8	91.5	94.3	0.0	0.0
Days' Inventory	3	12	4	4	4	4	4		
COGS/Payables	12.4	9.2	505.5	371.5	263.7	228.1	227.1	0.0	0.0
Days' Payables	29	40	1	1	1	2	2		
Revenue/Working Capital	10.1	11.0	5.8	5.1	4.9	5.6	8.3	0.0	0.0
COVERAGE RATIOS:									
Times Interest Earned	6.2	8.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NI+Non-Cash Expenditures / Current L.T. Debt	3.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
LEVERAGE RATIOS:									
Fixed Assets/Tangible Worth	0.3	0.4	1.5	1.1	0.8	0.9	1.2	0.0	0.0
Debt-to-Tangible Net Worth	0.0	2.5	2.1	1.7	1.3	1.2	1.4	0.0	0.0
Debt-to-Equity	1.4	2.5	2.1	1.7	1.3	1.2	1.4	0.0	0.0
OPERATING RATIOS:									
Gross Profit Margin	22.10%	23.83%	30.71%	31.30%	31.26%	28.66%	29.22%	0.00	0.00
EBT/Tangible Worth	21.00%	45.79%	168.82%	156.64%	129.47%	101.09%	124.53%	0.0	0.0
EBT/Total Assets	7.40%	13.11%	54.85%	57.04%	56.91%	46.28%	51.61%	0.0	0.0
Fixed Asset Turnover	30.7	24.4	5.3	6.3	6.8	5.7	5.1	0.0	0.0
Total Asset Turnover	3.2	2.6	2.5	2.5	2.5	2.4	2.6	0.0	0.0
EXPENSE TO REVENUE RATIOS:									
% Deprtn., Deprtn., Amort./Revenue	0.90%	1.24%	1.00%	1.29%	1.49%	1.64%	1.62%	0.0	0.0
% Officer's &/or Owner's Compensation/Revenue	3.50%	3.69%	2.17%	2.03%	2.05%	2.41%	2.41%	0.0	0.0

B. Comparison to IRS

In making a comparison of ABC Construction to the industry, I have used information from *IRS Corporate Ratios*. *IRS Corporate Ratios* is published annually by ValuSource. ValuSource compiled this data from the *IRS Source Book, Statistics of Income and Corporation Tax Returns* based on more than 3.7 million business tax returns. Data is provided for more than 230 industries.

Users can search data by either Standard Industrial Classification (SIC) or by industry type. Results are presented in balance sheet, income statement, and ratio format divided by up to 13 asset sizes. The information can be reported either by "returns with and without net income" or "returns with net income." We have used the information from returns with net income.

While this is a trailing indicator since it is normally two to three years old when it is released, it is still highly valuable to put our target company analysis into good perspective. Since Integra data is not available to us it is worthwhile to have a comparison number for the RMA data which is more recent.

The following table shows a comparison of ABC Construction to the IRS data.

	Median Qtl RMA Cur Yr	IRS	2000	1999	1998	1997	1996	Median Minimum	Maximum
LIQUIDITY RATIOS:									
Current Ratio	1.6	1.4	9.4	10.5	10.2	8.0	5.9	0.0	0.0
Quick (Acid-Test) Ratio	1.3	1.1	9.1	10.1	9.8	7.7	5.6	0.0	0.0
Revenue/Accounts Receivable	5.7	4.8	8.6	9.6	8.8	5.8	12.8	0.0	0.0
Average Collection Period	64	76	42	38	41	63	29		
Inventory Turnover	126.0	29.7	96.2	92.7	94.8	91.5	94.3	0.0	0.0
Days' Inventory	3	12	4	4	4	4	4		
COGS/Payables	12.4	9.2	505.5	371.5	263.7	228.1	227.1	0.0	0.0
Days' Payables	29	40	1	1	1	2	2		
Revenue/Working Capital	10.1	11.0	5.8	5.1	4.9	5.6	8.3	0.0	0.0
COVERAGE RATIOS:									
Times Interest Earned	6.2	8.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NI+Non-Cash Expenditures / Current L.T. Debt	3.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
LEVERAGE RATIOS:									
Fixed Assets/Tangible Worth	0.3	0.4	1.5	1.1	0.8	0.9	1.2	0.0	0.0
Debt-to-Tangible Net Worth	0.0	2.5	2.1	1.7	1.3	1.2	1.4	0.0	0.0
Debt-to-Equity	1.4	2.5	2.1	1.7	1.3	1.2	1.4	0.0	0.0
OPERATING RATIOS:									
Gross Profit Margin	22.10%	23.83%	30.71%	31.30%	31.26%	28.66%	29.22%	0.00	0.00
EBT/Tangible Worth	21.00%	45.79%	168.82%	156.64%	129.47%	101.09%	124.53%	0.0	0.0
EBT/Total Assets	7.40%	13.11%	54.85%	57.04%	56.91%	46.28%	51.61%	0.0	0.0
Fixed Asset Turnover	30.7	24.4	5.3	6.3	6.8	5.7	5.1	0.0	0.0
Total Asset Turnover	3.2	2.6	2.5	2.5	2.5	2.4	2.6	0.0	0.0
EXPENSE TO REVENUE RATIOS:									
% Depn., Depn., Amort./Revenue	0.90%	1.24%	1.00%	1.29%	1.49%	1.64%	1.62%	0.0	0.0
% Officer's &/or Owner's Compensation/Revenue	3.50%	3.69%	2.17%	2.03%	2.05%	2.41%	2.41%	0.0	0.0

C. Comparison to Trade Association Data

No trade association data was available to compare to the RMA and IRS data.

III. Normalizations

Accountants are trained in the cost basis of accounting. That is, assets are usually recorded at their historical cost. Assets are generally not restated from historical cost to their current values, except in certain industries. This is fundamental to generally accepted accounting principles (“GAAP”).

-----A fundamental accounting principle is: The book value of assets minus the book value of liabilities equals the book value of the business owner’s equity. This formula is an accounting identity.

-----A fundamental business valuation principle is: The current value of assets minus the current value of liabilities equals the current value of the business owners’ equity. This formula is an economics identity.

-----In the asset accumulation method, the analyst restates all of the assets and liabilities of the subject enterprise from their historical cost basis to the appropriate standard of value. After this revaluation, the analyst can then apply the “assets minus liabilities” formula to indicate the value of the subject entity.

-----Once this has been done, the asset accumulation method will typically indicate the value of 100% of the subject entity, on a marketable, controlling ownership interest basis. If the ownership interest is subject to some other level of value, then appropriate valuation discounts and/or premiums may be applied.

-----In short, assets and liabilities should be adjusted to their estimated fair market value as of the valuation date. Remember that certain liabilities (such as income tax on built in gains) may not be on the balance sheet provided by the entity. Similarly, certain intangible assets (such as goodwill, patent values, etc.) may not be recorded. Conversely, certain assets may have to be written down, such as impaired goodwill.

Nearly every valuation requires financial statement normalizations (adjustments) that result in an impact on the valuation techniques considered and applied. Such normalizations are typically financial transactions of a non-recurring, non-operating or non-market nature.

Normalizations are adjustments to financial statements for items not representative of the present going-concern status of the business. Normalizing adjustments could include elimination of effects of discontinued operations, elimination of effects of nonrecurring events, or adjustment of abnormal depreciation charges.

Adjustments may also be necessary to place the financial statements in conformity with generally accepted accounting principles (GAAP – Generally Accepted Accounting Principles). Certain expenses, partially deductible (or not deductible at all) for income tax purposes, should be fully deductible under GAAP, for example, meals and entertainment or officer’s life insurance premiums. Whenever possible, financial statements should always be adjusted to be in conformity with GAAP prior to making normalization adjustments.

Prior to preparing valuations of a business enterprise, the valuation analyst must frequently make adjustments to the financial statements of the entity. The ultimate goal of the adjustments is to accurately reflect the entity's financial position as of the valuation date as well as its “normal” results of operations for the periods being analyzed. The goal is not to “correct” the financial statements; rather it is to present them as an outside investor would look at the entity.

In this valuation, the following normalizations were reflected in my analysis and are specifically identified below in order to apprise the reader of their application.

A. Balance Sheet

1. Balance Sheet Adjustments

Cash was adjusted in the amount of \$-3,053M. My adjustment to cash is effective as of June 30 2000(the valuation date). This adjustment is composed of \$903M in cash in excess of operating needs and \$2150M in short term investments in excess of operating needs.

Accounts receivable were adjusted in the amount of \$-45. My adjustment to accounts receivable is effective as of June 30, 2000 (the valuation date). This adjustment represents 5% of accounts receivable which are over 180 days old. We are considering them uncollectible and eliminating them from the balance sheet.

Inventory was adjusted in the amount of \$4. My adjustment to inventory is effective as of June 30, 2000 (the valuation date). This adjustment corresponds to revaluing inventory from LIFO to FIFO and taking off a small amount for breakage and losses in normal operations.

Fixed assets were adjusted in the amount of \$-442. My adjustment to fixed assets is effective as of June 30, 2000 (the valuation date). This amount corresponds to a revaluation of \$458M to FMV in equipment based on a recent certified appraisal. Additionally, we eliminated \$900M in FMV undeveloped land value that is not used in the operation of the company.

2. Adjusted Balance Sheet

	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>
ASSETS					
Cash	500	685	605	100	209
Accounts Receivable	846	678	654	712	275
Inventory	53	48	42	32	27
Other Current	0	(0)	0	0	0
Total Current Assets	<u>1,399</u>	<u>1,411</u>	<u>1,301</u>	<u>844</u>	<u>511</u>
Fixed Assets	1,383	1,037	844	732	692
Net Intangible	0	0	0	0	0
Other Non-Current	150	150	150	150	150
Non-Operating Assets	0	0	0	0	0
Total Assets	<u><u>2,932</u></u>	<u><u>2,598</u></u>	<u><u>2,295</u></u>	<u><u>1,726</u></u>	<u><u>1,353</u></u>
LIABILITIES & EQUITY					
Accounts Payable	10	12	15	13	11
Short Term Notes Payable	135	119	111	88	73
Current Portion of LT Debt	0	0	0	0	0
Other Current Liabilities	3	4	2	5	3
Total Current Liabilities	<u>148</u>	<u>135</u>	<u>128</u>	<u>106</u>	<u>87</u>
Long Term Debt	1,831	1,517	1,158	830	705
Other Non-Current Liabilities	0	0	0	0	0
Non-Operating Liabilities	0	0	0	0	0
Total Liabilities	<u>1,979</u>	<u>1,652</u>	<u>1,286</u>	<u>936</u>	<u>792</u>
Total Equity	953	946	1,009	790	561
Total Liabilities & Equity	<u><u>2,932</u></u>	<u><u>2,598</u></u>	<u><u>2,295</u></u>	<u><u>1,726</u></u>	<u><u>1,353</u></u>

Income Statement Adjustments

Officers Compensation was adjusted by -\$82M to reflect the lowered amounts of salary the owner (President, CEO) and his wife (Administrator) would earn based on a certified salary survey. The specific amounts are President/CEO \$120M to \$100M and Administrator \$120M to \$58M)

Other income of -\$84M was eliminated from the income statement as it represents funds received from a farmers market that takes place on Saturdays in the property. This is income not relevant to the ABC Construction operation, is sporadic and not under any control by the company.

Income Taxes were adjusted by a -\$2M to reflect the lowered income from operations numbers.

3. Adjusted Income Statement

	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>
Revenue	7,295	6,489	5,755	4,156	3,529
Cost of Goods Sold	5,055	4,458	3,956	2,965	2,498
Gross Profit	<u>2,240</u>	<u>2,031</u>	<u>1,799</u>	<u>1,191</u>	<u>1,031</u>
Operating Expenses	401	333	289	224	191
Officers' Compensation	158	132	118	100	85
Depreciation/Amortization	73	84	86	68	57
Interest Expense	0	0	0	0	0
Total Operating Expenses	<u>632</u>	<u>549</u>	<u>493</u>	<u>392</u>	<u>333</u>
Operating Profit	1,608	1,482	1,306	799	698
Other Income/(Expense)	0	0	0	0	0
Income Before Taxes	<u>1,608</u>	<u>1,482</u>	<u>1,306</u>	<u>799</u>	<u>698</u>
Income Taxes	624	554	490	328	272
Adjusted Net Income	<u><u>984</u></u>	<u><u>928</u></u>	<u><u>816</u></u>	<u><u>471</u></u>	<u><u>426</u></u>

METHODS CONSIDERED AND REJECTED

I. Book Value Method

I considered the Book Value Method (Rejected); my review indicates that the value of the enterprise is driven by earnings/cash flows, not by the underlying assets. The value of the enterprise is based upon an assemblage of assets held to generate earnings. The book value of the individual assets is less important than the manner in which management has utilized them. The result of the Book Value Method (Rejected) is \$4,489M.

II. Adjusted Book Value Method, Going Concern

I considered the adjusted book value, going concern method; however, my review indicates that the value of the enterprise is driven by earnings/cash flows, not by the underlying assets. The value of the enterprise is based upon an assemblage of assets held to generate earnings. The values of the individual assets are less important than the manner in which management has utilized them. The result of the adjusted book value method is \$1,000M.

III. Summary Liquidation Value Method

The liquidation value method was considered but rejected because the enterprise is (1) an ongoing enterprise and (2) is more appropriately valued using other method(s). The result of the summary liquidation value method is \$4,000M.

IV. Summary Discounted Cash Flow Method

I considered but rejected the summary discounted cash flow method because I was unable to satisfy myself as to the forecast of future cash flows prepared by management. While I think they are conservative and reasonably accurate, I believe there is an inherent risk in projecting earnings out for ten years. There are many imponderables that transcend the ability of a valuator to predict them that far into the future. The result of the summary discounted cash flow method is \$9,700M.

V. Capitalization of Excess Earnings Method

Based upon the information available to me, I considered but did not use the excess earnings method. As stated in the book “Valuing a Business” by Shannon Pratt, “The excess earnings method was originally created for the purpose of valuing the intangible value of a business, not for the purpose of valuing the company as a whole.” (pg.283) The result of the capitalization of excess earnings method is \$9,200M.

VI. Guideline Company Method

For the market approach to be used, there must be a sufficient number of comparable companies to make comparisons, or, alternatively, the industry composition must be such that meaningful comparisons can be made. My search of the various transaction databases under the enterprises SIC (NAICS) code, 1731/ 235310 did not provide an adequate number of companies with which to compare the enterprise. The companies found showed such a wide variance of the various price multiples that a meaningful comparison with the enterprise could not be made. Similarly, my search of comparable public companies did not provide meaningful data with which to draw a conclusion. The average result of the guideline company methods is \$8,800M.

VII. Dividend-Paying Capacity

Revenue Ruling 59-60 states:

Primary consideration should be given to the dividend-paying capacity of the company rather than to dividends actually paid in the past. Recognition must be given to the necessity of retaining a reasonable portion of profits in a company to meet competition. Dividend-paying capacity is a factor that must be considered in an appraisal, but dividends actually paid in the past may not have any relation to dividend-paying capacity. Specifically, the dividends paid by a closely held family company may be measured by the income needs of the stockholders or by their desire to avoid taxes on dividend receipts, instead of by the ability of the company to pay dividends. Where an actual or effective controlling interest in a corporation is to be valued, the dividend factor is not a material element, since the payment of such dividends is discretionary with the controlling stockholders. The individual or group in control can substitute salaries and bonuses for dividends, thus reducing net income and understating the dividend-paying capacity of the company. It follows, therefore, that dividends are less reliable criteria of fair market value than other applicable factors.

I did not consider the Dividend Paying Capacity method because when the capitalization of dividends method is used as an element in valuation, it usually is by reference to dividend yields on guideline publicly traded companies. In the case of electrical contracting, I did not find a reasonably representative publicly traded company in this clearly defined field.

METHOD APPLIED

Among other factors, this valuation takes into consideration all elements of valuations listed in Internal Revenue Service Ruling 59-60, which generally outlines the valuation of closely held stocks and includes the following:

- ✍ The nature of the business and the history of the enterprise from its inception.
- ✍ The economic outlook in general and the condition and outlook of the specific industry in particular.
- ✍ The book value of the stock and the financial condition of the business.
- ✍ The earning capacity of the company.
- ✍ The dividend paying capacity.
- ✍ Whether or not the enterprise has goodwill or other intangible value.
- ✍ Sales of the stock and the size of the block of stock to be valued.
- ✍ The market price of stocks of corporations engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over the counter.

I. Capitalization of Earnings Method

This income method is often the appropriate method to use when estimating the value of a closely held entity. This is because the approach focuses on the present value of the projected future benefits that would accrue to the owner of the company.

Investors are primarily concerned with realizing a rate of return on their investment, which translates to the investor's required rate of return. Once the future economic benefit stream of a company is determined, applying the investor's required rate of return results in the value of such an investment. This is known as the capitalization of earnings (i.e., the future economic benefit stream) method.

There are two primary methods used to determine the value of an ownership interest when using the income method. If earnings have been and are expected to continue in a more or less stable manner, then the capitalization of earnings method will often apply. On the other hand, if earnings are less stable and less predictable, then a discounted future earnings method may be more appropriate.

When using the capitalization of earnings method, the calculation consists of dividing expected future earnings by the difference between an investor's required rate of return and the investment's estimated long-term growth rate.

Once the risk has been quantified in a discount or capitalization rate, it must be applied to a defined stream of economic benefits.

A. Earnings Base

The income approach can be operating profit, gross profit, income before tax or net income, i.e., (Generally Accepted Accounting Principles) or OCBOA (Other Comprehensive Basis of Accounting) earnings. Cash flow bases are driven by some measure of available cash such as discretionary, comprehensive cash flows. I have selected an income base because;

- ✍ Operating profit represents income before “other income and expense” and before income taxes. Adjustments may be made for items identified each year that may be subtracted, or added, to most closely approximate expected results. This represents a “pre-tax” cash flow and the discount rate may need to be modified to account for this.
- ✍ Gross profit (net sales less costs of sales) may be appropriate in certain industries. Adjustments may be made for each year that may be subtracted or added. This represents a “pre-tax” cash flow and the discount rate may need to be modified to account for this.
- ✍ Income before tax may be appropriate in certain circumstances. Unlike operating income, this measure includes “other income and expense.” Adjustments may be made each year for items that may be subtracted or added. This represents a “pre-tax” cash flow and the discount rate may need to be modified to account for this.
- ✍ As the name implies, this represents net income.

Based upon my analysis of ABC Construction, I have concluded that the appropriate earnings base is Income Before Tax. I selected Income before tax as an earnings base because I believe that the tax circumstances of potential buyers will be varied and complex. A before tax measurement of value allows them to apply their own particular set of circumstances to the valuation to make their purchase decision. If a post tax measure is taken potential buyers will have to recalculate the valuation to generate a measure of value they can use with their own circumstances.

1. Ongoing Capacity

Once the appropriate earnings base has been developed, an estimate of the ongoing earnings capacity is developed. This estimate can be based upon average earnings, weighted average earnings or trend line earnings. The selection of the ongoing capacity is a matter of informed judgment. I have selected weighted average earnings as my method to estimate the ongoing capacity. I chose to weight the earnings of the past 5 years as opposed to project a growth rate out over the next ten years for two key reasons. First, I believe that the most conservative way to measure earnings is to estimate an earnings number that ABC Construction can achieve based on earnings behavior it has exhibited in the past. I feel

confident that, even if circumstances in the future change, ABC Construction will be able to meet the weighted average earnings I project. Secondly, I believe that the projection of an earnings growth rate into the future is fraught with many difficulties that go beyond the predictable factors normally used in making a business valuation. Macro political and economic factors, natural phenomena, wars and terrorism are more felt today than previously. It is safe to say that the future is less predictable than it was before. Based on this, I feel more confident estimating a future revenue flow based on what ABC Construction has already done than a projected increase in sales year over year.

B. Capitalization Rate

There are several methods for developing a capitalization rate. I have selected the Risk Rate Component Model as the most appropriate method for developing a capitalization rate. This method is discussed in more detail below.

1. The Risk Rate Component Model

This model provides an alternative method for those companies that are smaller than those contained in the Ibbotson Associates SBBI reference materials. The smallest size companies contained in those sources are companies with tens of millions in equity.

The two main components are a risk-free rate premium and a composite of premiums that are related to the specific industry and operations of the subject company.

This model falls back on the use of tools familiar to accountants in the performance of other assignments, specifically engagements for audited or reviewed financial statements. Those tools include analytical procedures (ratio analysis) as in-depth research so that the valuation analyst can exercise that aspect of being a professional: *informed judgment*.

The valuation analyst who uses the Risk-Rate Component Model (“RRCM”) method must conduct sufficient research through ratio analysis, review of external performance data, and management interviews.

The theoretical basis for this method is that “investors in ‘risky’ investments require a rate of return above and beyond a risk-free safe investment as compensation for bearing the risks associated with holding the investment.” The RRCM model is a composite of a risk-free-rate, plus the value of risk associated with additional component.

The capitalization rate derived from the RRCM is a pre-tax rate and is applied to earnings-before-income-tax.

The components to be analyzed in the Risk-Rate Component Model method are taken from Section 4, 5, and 6 of Revenue Ruling 59-60. The components are organized into four categories to provide the computed value of risk to the enterprise. The categories are:

- ✍ Competition
- ✍ Financial Strength
- ✍ Management Ability and Depth
- ✍ Profitability and Stability of Earnings

The model allows further adjustment to the final risk rate when the subject company is impacted by national and/or local economic circumstances.

The categories are material and significant aspects of a going concern. The RRCM is designed to be flexible. The valuation analyst is able to add additional relevant components that bear on the risk of the subject company. Similarly, the analyst can delete components that are irrelevant to the subject company being valued.

In this valuation, I have concluded that the value of risk associated with the subject company is 17.53%, calculated as follows:

Risk-free rate of return, based upon the rate paid on
 20 year US Treasury Bonds, as of June 30, 2000 5.90%

The US Treasury Bond rate is a common rate used to calculate the risk free rate of return available to any investor.

Competition 3.89%

A relatively moderate rate of risk was calculated for competitors attacking ABC Construction’s client base and revenue stream. I felt that given ABC Construction’s strong client relationships, excellent margin and high quality work, they would be able to fight off attacks and retain clients in most predictable circumstances.

Financial Strength 1.50%

I chose a low risk rate for the financial strength aspect of this model. ABC Construction has comported itself in a very conservative and careful way financially, with customers, suppliers and with its own management and growth. There is little doubt that the company is structured and organized to continue this conservative practice into the future.

Profitability and Stability of Earnings..... 4.18%

A moderate risk rate of slightly more than 4% has been applied to the profitability and stability of earnings estimates. ABC Construction has been consistently profitable and has produced stable earnings in the past. I have also taken into consideration the risk that larger companies will attack ABC Construction clients and that illegal immigrant labor will undercut pricing.

Management Ability and Depth 2.06%

While the current owners are essential to the success of the company, client relationships are also well managed by the company staff. We have no doubt that the current team, along with new owners will represent a strong management staff and this area will not be the source of significant added risk to the company. The skills required to manage and run a company of this type are readily found in the marketplace.

Capitalization rate derived from Risk Rate Component Model..... 17.53%

2. Non-Operating/Excess Assets

For valuation purposes, the non-operating/excess assets were removed from the balance sheet because they are not part of the ongoing business operations of the Company. I identified the following assets, with associated costs/values, as not necessary for the ongoing operations of the Company:

The liabilities associated with these assets were also adjusted. Certain liabilities were identified as unrelated to the ongoing operations of the Company and were removed.

My adjustment to non-operating/excess assets as of the valuation date \$100M. This amount represents current managements final assessment of excess retained earnings left in the company. During the review of the normalized financial statements management came to the conclusion that this additional amount could be removed from the operation without risk.

C. Discounts and Premiums

1. Discount for Lack of Marketability

Included in my calculation of value is an additional discount for lack of marketability. A discount for lack of marketability is necessary to reflect the lack of liquidity of this equity interest. Based upon the following, I have applied a 3.50%, or \$343 discount for lack of marketability.

Two general types of empirical studies provide evidence for the existence and magnitude of the DLOM. The first type, restricted stock studies, compares the trading prices of a company's publicly held stock sold on the open market with those of unregistered or restricted shares of the same company sold in private transactions. The second type, pre-IPO studies, examines the prices of transactions while the company was still private, compared to the eventual IPO price. The

restricted stock studies have found average DLOMs in the range of 30% to 35%, while the pre-IPO studies have reported average DLOMs generally around 45%. Empirical evidence suggests that the primary factors in determining the size of the DLOM are as follows:

- ? Size of distributions or dividends
- ? Size of revenues
- ? Size of earnings
- ? Revenue growth and stability
- ? Earnings growth and stability
- ? Product risk
- ? Industry risk.

Companies with higher distributions, revenues, earnings, growth, and stability generally exhibited lower discounts. In my estimation, ABC Construction has very little discount in this area because of its excellent financial performance over the last five years and the ready marketability to mid sized companies or to larger “mega” sized companies it has shown. My site visit taught me that some “mega” companies had already begun to make discrete inquiries and some similar sized companies had also made inquiries. I did take a modest 3.5% discount to cover minimal risk and to account for probable additional expenses in the preparation and organization for a sale of company.

D. Valuation Conclusion

I have developed a per share value to initiate a value for the interest being valued. The development of the value of the interest being valued is summarized below.

Value per share as of June 30, 2000.....	\$171.91
Number of shares being valued	55M
Value of 55 shares as of June 30, 2000	\$9,455M
Rounded	\$9,500M

Adjusted Income Before Tax		1,700
Capitalization Rate		<u>17.53%</u>
Sub-Total		<u>9,698</u>
Valuation Adjustment		<u> </u>
Sub-Total		9,698
Excess and Non-Operating Assets		<u>100</u>
Sub-Total		9,798
Marketability (Discount)	-3.50%	<u>(343)</u>
Calculated Value		9,455
Number of Shares Outstanding		<u>55</u>
Calculated Value Per Share		171.91
Number of Shares Being Valued		<u>55</u>
Calculated Value of Shares Being Valued		<u><u>9,455</u></u>
Selected Value of Shares Being Valued		<u><u>9,500</u></u>

JUSTIFICATION OF PURCHASE

To test the reasonableness of my opinion as to the fair market value of the Company, I performed a proof of valuation analysis, titled “Justification of Purchase.” This analysis includes assumptions regarding the cash down payment, the terms of the purchase notes, and the Company's projected cash flows.

The Justification of Purchase technique assesses whether the subject company could “pay for itself” if market debt financing criteria were applied against the opinion of value. The indicators of a successful Justification of Purchase technique include: 1) whether cash flow is sufficient to provide reasonable compensation to the hypothetical purchaser, 2) whether acquisition debt is fully amortized over a reasonable time frame, and 3) whether the hypothetical purchaser earns a reasonable return on the cash down payment.

The assumptions regarding the terms of the hypothetical purchase are presented in the following schedule:

		<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
Projected Growth Rate	350%								
Projected Pre-Tax Income	1,761	1,823	1,886	1,952	2,021	2,092	2,165	2,240	2,319
Interest Expense on Purchase Notes		411	378	343	307	268	228	185	141
Projected Post-Sale Pre-Tax Income		1,412	1,509	1,609	1,714	1,823	1,937	2,055	2,178
Income Taxes	3500%	494	528	563	600	638	678	719	762
Projected Post-Sale Net Income		918	981	1,046	1,114	1,185	1,259	1,336	1,416
Depreciation/Amortization Expense		0	0	0	0	0	0	0	0
Principal Payments on Purchase Notes		645	678	713	750	788	828	871	915
Projected Post-Sale Cash Flow		<u>272</u>	<u>302</u>	<u>333</u>	<u>365</u>	<u>397</u>	<u>431</u>	<u>465</u>	<u>500</u>

CONCLUSION OF VALUE

I. Conclusion and Opinion

Conclusions of Value can be expressed as an Opinion of Value, as a single number, or an Estimate of Value, as a single number or a range of numbers. Where, in the professional judgment of the member, an Opinion of Value cannot be expressed, the member may report an Estimate of Value.

A rationale for a conclusion relies upon a combination of the Income-related and Market-related Methods as described above. The Income-related Methods provide a strong indication of value since a hypothetical (non-strategic, non-synergistic) buyer would seek information on the client's actual financial statements.

The Income-related Methods provide a strong indication of a "floor" value since they are based on actual (albeit normalized) data, and a hypothetical (non-strategic, non-synergistic) buyer would certainly seek information on the client's actual financial results.

Given the strong and sustained financial performance, their exemplary client relationships, strong labor relations, stability of earnings expectations, substantial margins, and overall ability to adapt and compete in almost any future market conditions, I have established an Estimate of Value as the conclusion of this business valuation.

Therefore, based upon the facts and circumstances of the valuation, my estimate of the resultant fair market value of ABC Construction, Inc., on a control, non-marketable basis as of June 30, 2000 is \$9,500M

**"The standard is an objective test using hypothetical buyers and sellers in the marketplace, and is not a personalized one which envisions a particular buyer and seller." LeFrak v. Commissioner, 66 T.C.M. (CCH) 1297 (1993). See also Estate of Bonner v. United States, 84 F.3d 196 (5th Cir. 1996)."

II. Synthesis and Reconciliation

Because valuations cannot be made on the basis of a prescribed formula, there is no means whereby the various applicable factors in a particular case can be assigned mathematical weights in deriving the fair market value. For this reason, no useful purpose is served by taking an average of several factors (for example, book value, capitalized earnings and capitalized dividends) and basing the valuation on the result. Such a process excludes active consideration of other pertinent factors, and the end result cannot be supported by a realistic application of the significant facts in the case except by mere chance.*

* Footnote – assigned mathematical weights in deriving the fair market value – "Revenue Ruling 59-60, Section 7, Averaging of Factors."

The following comparative data summarizes and the various methods that I have accepted or considered and rejected, along with their respective final values. Each method is rated relative to the applicability of the method relative to ABC Construction's facts and circumstances, and strengths/weaknesses are briefly discussed.

A. Asset Approach

Book Value Method\$4,489
 Application Weak

Strengths include providing information on the net assets of the company. This has value when the company is not a going concern or an enterprise that is producing significant revenue on its own. This is a useful measure for holding companies and the like or for companies that are producing losses.

Weaknesses include the inability of this method to take into consideration the earnings capability of the company. For companies that are generating revenue at a reasonable rate of return for the assets employed, this is not an adequate method to measure value.

Adjusted Book Value Method Going Concern\$1,000
 Application Weak

Strengths include establishing the value of the level of assets required to operate the business as a going concern.

Weaknesses here are based on the fact that the assets have been reduced by the amount of adjustments made to the going concern balance sheet. These adjustments will have removed the majority of the retained earnings in the business, leaving enough cash to operate it. This method is inappropriate since it significantly underestimates the assets of the business in a purely asset sale.

Adjusted Book Value Method Summary Liquidation\$4,000
 Application Weak

Strengths include providing the valuator with a quick benchmark number that demonstrates the value of the assets alone in a sale.

Weaknesses of this method for businesses that have a solid income flow include the fact that the business will be significantly undervalued by not taking into consideration the economic benefit and income producing ability of the assets.

In general the asset approach is inappropriate to value ABC Construction because it eliminates from the equation the major strengths of the business, namely its revenue producing capability. ABC Construction has a solid income stream and an asset approach is not appropriate to value a company of this nature.

The mean, median, and standard deviation results for all asset approach methods are \$3,163, \$4,000, and \$1,889, respectively.

B. Income Approach

Capitalization of Earnings Method \$9,500M
Application Strong

Strengths include valuing the business based on its earnings capabilities. Since this is the major characteristic of ABC Construction, we believe this is the most appropriate method to value the business. It is strictly based on applying a reasonable capitalization rate to a very predictable earnings flow number on a yearly basis, observing the past five years of earnings growth. By taking a careful measure of the business results themselves and estimating a reasonable rate of return *from the past five years* based on all the key operational factors, we believe we have applied valuation techniques and methods that will most accurately reflect the value of the business going forward. While we have some reasonable belief that the income growth percentage rates we estimate going forward will be accurate, we prefer this more conservative method of measuring future economic benefits. There are many imponderables in the projections of earnings forward for ten years. Since the value of the business is very similar in these two methods, we opted for the more conservative value.

This method would not be appropriate for businesses that have few or no earnings or that have a very uneven revenue stream. Neither of these is the case of ABC Construction.

Discounted Earnings Method Summary Projections \$9,700M
Application medium

Discounted earnings is effective to measure the business value when the stream of earnings is estimated on a yearly basis going forward. We believe that the estimates of growth going forward do reflect a conservative opinion of ABC Construction's growth potential. However, we also believe that any projection of a growth rate for ten years into the future must be fraught with potential unforeseen circumstances that could change it considerably. And given that this method is very sensitive to the input variables, we have preferred to consider it as an alternative but prefer to take the more conservative estimate of revenue from past results that is presented by the capitalization of earnings method. We are more sure of ABC Construction's ability to continuously produce revenues in the 1,700M range for the foreseeable future than we are of predicting a continuous, albeit small yearly rate of increase. Since both these methods produced a very similar value number, we opted for the one which we believe to be more conservative.

Weaknesses include an extreme sensitivity to changes in the input variables, meaning the projected cash flows and the discount rate. Minor changes in these components make significant changes in valuation. In an environment where interest rates are falling, this may not be an appropriate method.

Capitalization of Excess Earnings Method.....	\$9200M
Application	medium

Strengths include a simplified method that has been in use for many years.

Weaknesses include information quoted from Kalman A. Barson “Is it time to Bury Revenue Ruling 68-609” published in FairShare: The Matrimonial Law Monthly, Jan 1998. “It is my belief that the time has come when othr valuation aapproaches, valid (and sometimes more appropriate), should be used instead of relying on RR68-609. It is important that the judicial and legal communities recognize that a valuation report is not necessarily deficient or suspect simply becaue it uses approaches to valuation other than 68-609, or it doesn't use 68-609 at all. Indeed, RR 68-609 says that, “The formula apaproach should not be used if there is better evidence available from which the value of intangibles can be determined... Accordingly, the formula approach may be used for determining the fair market value of intangible assets of a business only if there is no better basis therefore available.”

In our estimation, the previous two income methods are more accurate in measuring going forward value for ABC Construction.

The Income-related results (Capitalization of Earnings, Discounted Future Earnings (Summary and Capitalization of Excess Earnings), fall within a very narrow range, thus corroborating one another. I am confident that such Income-related Methods provide sound indicators of value since they represent the “residual” economic benefits available to the equity holders after the growth needs of the business have been met. Since the resulting numbers from the first two methods are very similar, we have more confidence in those methods than in this one. Consequently, it was not used as the final measure of value.

The mean, median, and standard deviation results for all income approach methods are \$9,467, \$9,500, and \$252, respectively.

C. Market Approach

Guideline Company Method – Price to Earnings.....	\$8,800M
Application	medium

– A market approach can be indicative of value for our target company if enough similarities can be found in the market based companies we analyze. In general, this can be an effective way for a willing buyer to determine where to make an investment, given that he has complete freedom to deploy those assets.

- In our search for similar companies in this industry we did not find a company that closely resembled ABC Construction in any meaningful way. While these companies can give us a general view of what they are able to do in the industry, they do not reflect ABC Construction. ABC Construction is a company that is significantly more successful in common size terms than any of the companies we reviewed. Consequently, we determined that this valuation method would not be valid for our work here.

In general, the Market-related results are based upon indicators within public and private markets consisting of transactions similar to the company's business and revenue size. When the similarities to the target company are close, this can be a useful valuation method.

As indicated by the preceding results, the various methods accepted as appropriate converge closely overall and within their respective categories. This convergence provides strong assurance of accurate methodology. *The mean, median and standard deviation results are provided for comparative illustration only.* The mean, median, and standard deviation results for all methods are \$6,670, \$8,800, and \$3,468, respectively.

REPORT APPENDICES

I. Appendix A: Qualifications of Appraiser

Michael F Cannon, President, MCOM Corporation

OBJECTIVE

Helping public and private sector companies increase their productivity by providing complete marketing, management and M&A services around the world

QUALIFICATIONS

25 years of international management, marketing, and communications experience, emphasis **overseas**

Skilled facilitator and **link** between private sector and public sector interests

Proven leader of regional operations for multiple subsidiaries and clients

Experienced manager of overseas start up operations

Successful in turning around failing subsidiaries, **divesting and acquiring assets** and **business valuations**

Trusted counselor of clients, consistently honored with new business

Respected strategic thinker for key international brands

Creative designer of practical systems to maximize operational effectiveness overseas

Adaptable team builder in any environment

Resourceful problem solver who makes companies profitable

18 years living overseas in 6 countries and 3 continents with **high level contacts** in all areas

Trilingual in English, Spanish, and French, knowledge of Portuguese and Italian

ACHIEVEMENTS

Created senior management course for business and marketing effectiveness now in use by major marketers

Directed Strategic Merger and Acquisition activity for major worldwide advertising agency in Latin America resulting in significantly improved acquisitions at substantially lower cost.

Developed the strategic work plan for a new corporate initiative for major public sector firm

Created the concept and pilot plan for a new weekly Hispanic TV show on broadcast television.

Wrote the business plan with the council president for the Latin American Multichannel Advertising Council (LAMAC), the equivalent of the Cable Ad Bureau for the United States

Lead consultant for overall contraceptive communications program for TFGI, USAID and Indian government in the 5 key northern states resulting in a much higher product adoption rate.

Restructured and reoriented operations for Fortune International, a real estate development company

Reorganized ad sales activities at Gems Television, a Latin American cable television channel.

Created and established the ad sales concept, strategies, and companies for HBO Latin America

Assumed Presidency of failed FCB Mexican subsidiary and loss ridden Central American companies and took them to highest profit ever in two years

Developed the FCB Professional Skills System and established it throughout Latin America. It became the basis for agency work in 20 countries and 25 subsidiaries.

Invented a complete computerized ad agency operating system and beta tested it in Mexico. Was used as one of the key base models for the FCB integrated system.

Created “virtual” account service teams that kept headquarters staff low, stimulated talent, and increased profit

Spearheaded pan regional headquarters strategic brand planning and in market competitive activities for clients like **Colgate, Nestle, L’Oreal, MasterCard, Texaco,** and others.

Developed the overall strategic plan for Colgate Dental Cream, the leading dentifrice in Latin America and directed all regional advertising development and execution.

EXPERIENCE

MCOM Corporation (Miami, Fla.) 1/98-Present

President 1/98-Present

- Founded company to provide global marketing, management and communications consulting services to clients in the public and private sectors. Specialized in reorganizing sick companies, acquiring and divesting assets, business and asset valuations, rescuing failing brands and setting up new projects from initial market and consumer research through product positioning, development and marketing and advertising plans. Clients served recently in Argentina, Chile, Peru, Ecuador, Mexico, India, Philippines and the United States and include such names as Deloitte Touche Tohmatsu, Gems Television, HBO Latin America, Fortune International, Bates WorldWide Latin America, The Futures Group, Academy for Educational Development, Center for Administrative Justice, American Institutes for Research, Zorro Productions, GCS Alliance, McBride Consulting, Applied Integrated Management Systems (AIMS), and Roche Diagnostics Corporation.

HBO Latin America Advertising Services (Miami, Fla.) 2/96-6/98

President 2/96-12/97

- Started new company for HBO Latin America to position four new pan regional pay TV channels and two Brazilian channels for ad sales; The Warner Channel, Sony Entertainment Television, E! Entertainment Television, Mundo Ole, HBO Brazil and Cinemax Brazil.
- Set up, staffed and supervised operations in Miami, Brazil, and Mexico. From 0 to 3rd highest in pan regional ad revenues in 18 months out of a total of 65 pay TV channels.

FCB Latin America (Miami, Fla.) 7/92-1/96

Sr. Vice President, Regional Client Service/New Business Director 7/94

- Overall supervision FCB pan regional clients

- Development of region wide new business program that produced 20% revenue increase

Sr. Vice President, Area Manager Mexico & US Hispanic 7/92-7/94

- Reorganization of NYC, Dallas offices, establishment of Miami office

FCB Mexico (Mexico City) 3/90-6/92

President, CEO 3/90-6/92

- Revenues doubled, direct margin from 0 to 32.5%
- BTP to 37% of revenues, 30% of revenues from new brands of existing clients
- Headcount reduced by 50%, developed integrated software system
- Major clients; Colgate, Nestle, Pepsi Foods, L'Oreal, Texaco

Area Manager for Central America 9/91-6/92

- Guatemala, Costa Rica, Honduras, El Salvador, Panama
- Reorganization of Guatemala, El Salvador offices

FCB Malaysia (Kuala Lumpur) 1/89-2/90

Managing Director, CEO

- Revenues increased 33%, direct margin increased from 3% to 19%
- 20% of revenues from new business
- Clients; Colgate, Matsushita, Proton Saga, Ajinomoto, Parkson Grand Dept. Stores

FCB Latin America (New York) 1/87-12/88

Sr. Vice President, Regional Client Service Director

- Developed FCB professional working skills program
- Major Clients; Colgate, Citibank, Nestle
- Director of pan regional creative campaigns for Colgate

FCB International (New York) 6/85-12/86

Vice President, Regional Account Director Latin America for Colgate Palmolive Co.

- Regional direct margin 11% to 19%

- Direction of major regional brand advertising campaigns
- Designed computerized regional media planning and buying system

FCB/Siboney Puerto Rico (San Juan) 2/82-6/85

General Manager 1/84-6/85

Client Service Director 2/82-1/84

Siboney Advertising, Colombia (Cali) 7/79-2/82

General Manager

Siboney Advertising, Venezuela (Caracas) 1/77-7/79

Regional Marketing Coordinator

EDUCATION/PERSONAL

MBA in International Management, American Graduate School of Intl. Management (Thunderbird)

M.A., University of Iowa, B.A., Purdue University, Deuxième Degré D'Université de Strasbourg, France

Address : 1935 Secoffee Street, Coconut Grove, Florida 33133

Email/Phones : MCOMCORP@gmail.com, Phone 305 453 3731, Cell 305 942 6035

Site Visit Notes and Questionnaire

July 20, 2000

Mr. John Smith

CEO, President

ABC Construction

5529 ABC Construction Blvd

Any town, California 91365

Dear Mr. Jones,

In connection with our assignment to value a 100% interest in ABC Construction Company, please provide us with the documents listed on the attached schedule.

Upon receipt of the requested documents by our office, we will schedule a meeting with you at the Company's place of business.

Your cooperation in this matter is appreciated. If you have any questions, please call our office at 305 453 3731.

Sincerely,

Michael Cannon

MCOM Corporation

Enclosure

MCOM Corporation

SCHEDULE OF REQUESTED DOCUMENTS

Financial Statements and Income Tax Returns:

1. Federal income tax returns for the last 5 years.
2. Annual financial statements for the last 5 years.
3. Interim financial statements for the period ended June 30, 2000 or the closest date for which financial statements are available.

Other Financial Data:

1. Accounts receivable aging report with payor detail, if available
2. List of inventory and description of accounting treatment (LIFO, FIFO, etc.).
3. Estimate of the number of days on hand of prepaids/office supplies as of date of valuation.
4. List of fixed assets. For each fixed asset the list should indicate the date of acquisition and the purchase amount.
5. Schedule of real estate investments.
6. List of all subsidiaries and their annual financial statements for the last 5 years.
7. List of all other businesses in which the Company has a financial investment and their annual financial statements for the last 5 years.
8. Accounts payable aging report.
9. List of all notes payable. For each note please provide the name and address of the lender, the original amount of the note, the interest rate, the term of the note, any scheduled balloon payments, and any loan covenants.
10. List of all shareholders in the Company and the amount of shares owned by each shareholder.
11. If not shown in income statements, a breakdown of sales, by product or service, for each of the last 5 years.
12. If not shown in the income statements, a breakdown of cost of goods sold and operating expenses for each of the last 5 years.
13. A schedule showing, by Company officer, all direct compensation for the last 5 years.

14. A schedule showing, by Company officer, all payments made by the Company into a pension fund on behalf of the officer for the last 5 years.
15. A schedule showing, by Company officer, all payments made by the Company for health insurance on behalf of the officer for the last 5 years.
16. A schedule showing, by Company officer, all payments made by the Company for life insurance on behalf of the officer for the last 5 years.
17. Copies of forecasts or projections made by the management of the Company or its consultants.
18. Copies of appraisal reports that opine to the value of assets owned by the Company or its subsidiaries.

Other Requested Data:

1. Copies of leases where the Company is either the lessee or the lessor.
2. Copies of buy/sell agreements involving ownership interests in the Company.
3. Copies of articles of incorporation, bylaws, and amendments
4. Copies of partnership agreements.
5. Details of any pending litigation involving the Company as either plaintiff or defendant.
6. Details of transactions involving purchase or sale of ownership interests in the Company.
7. Copy of all employment agreements, partnership agreements, shareholders agreements, buy/sell agreements, consulting agreements, management agreements, and income distribution plans in use

PREMISE INSPECTION FACT SHEET

Site Visit

Company Name: ABC Construction Company

Valuator's Name: Michael Cannon

Date August 3, 2005

1. **Company's primary address:** 5529 ABC Construction Blvd, Any town, Cal 91365
2. **Date of Company's inception:** 1985
3. **Type of entity (C-Corp., S-Corp., LLC, LLP, etc.):** C-Corporation
4. **State Company organized:** California
5. **Company's primary SIC code number:** 1731 Electric Work **Secondary SIC code number(s):** 235310 NAICS Electrical Contractors
6. **If corporation, number of shares authorized:** 55 (,000) **Number outstanding:** 0
7. **If corporation, number of shares of treasury stock:** 0
8. **Describe other classes and/or types of stock:** None
9. **Briefly describe the history of the company from its inception to the date of valuation** June 30, 2000.

This Site Visit was conducted individually with Mr. John Smith, President of ABC Construction and other employees of the company including Shirley Smith, Office Manager, and Lee Williams, Construction Manager. Impromptu conversations were also held with a variety of employees on the company premises.

Background

The company was started in 1985 by John Smith' father, Reginald. Reginald was an English merchant marine sailor who disembarked in San Diego shortly after World War II. His tanker ship had been destroyed by a Japanese U-Boat and he was one of a few survivors picked up by an American convoy returning to the west coast after re-supplying US troops in Hawaii. He was only 20 years old and fell in love with California and shortly afterwards with a California girl. They were married and had a son, John, in 1945.

Reginald and his young family moved to the small towns in the mountains inland from San Diego and settled in the town of Any town in 1946, as far away from the sea as he could get. Having worked in electricity in the merchant marine Reginald began to look for work as an electrician's assistant, and

this became his trade for the next 40 years. He worked for electrical contracting companies in the area and when his son graduated from high school, he too joined the trade. Reginald and John worked together as a team for a local electrical contractor for over 20 years while John married and started his own family. Not wanting his grand children to have the same difficulties as he had had in starting out, Reginald decided to start his own electrical construction business. He wanted to leave something tangible for his grand children before he died.

By 1985 Reginald was turning 60 and his son 40. They were both master electricians and, over time, had built up a loyal clientele of construction companies who preferred to work with them as a team on jobs. The move to open their own business was a natural one. Both father and son prospered and enjoyed working together. Having been employees of the same industry for a long time, they deeply understood the problems that workers had to live with. Consequently, they based their business on some sound principles; Develop and maintain strong relationships with customers, develop repeat business, treat employees fairly and pay union wages and benefits, compete based first on quality work, done on time and within budget, and only then on price. This formula was very successful and ABC Construction became known as a quality company that delivered on time and within budget. There was none of the labor strife that plagued some of the other contracting firms in the area and the high quality staff at ABC Construction were happy and generally did not leave for work in other companies. This low turnover and high quality gave ABC Construction a big advantage when bidding for new jobs.

The company was successful and served to provide a good living to Reginald and John and the handful of employees they had. By 1996 Reginald was approaching 71 and he had no desire to expand the business further, but John could see that there were many missed opportunities to profitably increase the size of the business. Just as Reginald was contemplating retirement from the business he and his wife were killed suddenly in a car accident coming home from church on a Sunday morning.

Growth and Expansion

John vowed to continue the business as before but also to find ways to expand it and make it more profitable. Over the next 4 years John worked hard to further develop the business based on the sound principles forged with his father over the previous 10 years, and by 2000 the business had reached very high levels of revenue and profit with a stable clientele and group of employees. This expansion and growth came because of John's insistence in systematizing the operation and focusing on good planning and execution. John standardized all the trucks to the same brand, engine displacement and general features to simplify maintenance. He built and standardized what he called work "kits" that included all the tools and parts crews would need to work on a job. This eliminated the tremendous wasted time most crews face when they start a job and then have to stop to go and get either parts or tools or return to home base before the job was done. John estimated that this alone made his work crews 25% more efficient than his competitors. This made ABC Construction more profitable and gave them margin to bid competitively on jobs.

Customer satisfaction was high when John took over the business. Many of the customers were friends of Reginald and, at first out of pity, they continued to work with ABC Construction. But when they saw that John maintained the high level of quality and service and kept prices reasonable, they passed their allegiance along to him. John's easy and reliable manner helped immensely in this. Surprisingly, a lot of ABC Construction's business came to them without competitive bids or price haggling. Industry research shows that this is not an isolated phenomenon. The "Guide to the Electrical Contracting Market" from 1999 states that fully 44% of all jobs come from no bid jobs from established customers. GC's and construction companies often develop relationships of trust with key suppliers and routinely work with them without the hassle of the bidding process or strong price negotiations. John was always careful to never abuse this relationship of trust, making sure that the prices he charged were always within the reasonable range. This was crucial in communicating to customers that ABC Construction was a trusted partner.

While ABC Construction had done an excellent job in maintaining established business, John reminisced that it had been hard work to expand the business beyond the locally owned general contractors and establish relationships with the state wide construction firms that typically had larger projects

with a more consistent flow. John had had to demonstrate ABC Construction's strong record of project completion on time and in budget and back it up with performance guarantees that sometimes kept him awake at night. State wide construction firm contracts were instrumental in doing two things that greatly expanded ABC Construction's business. First, they helped expand their business in Nevada and secondly and most importantly, they gave ABC Construction an opportunity to compete for government construction business. While Nevada contracts added a growing 15% to 25% to the revenue line, the government construction jobs, all of which had no problem paying the union wage and benefit premiums charged, added another 10 to 15% to the growth of the business. All in all, John was satisfied both with the growth and the diversity of the business. No one client represented more than 10% of the overall business. The growing pains they experienced going from a small operation to a medium sized one were mostly overcome and with 12 three man crews ABC Construction had the flexibility to react quickly to the market and solve problems. John was particularly proud of Shirley's contribution to the success of the business in that she helped John develop a forecasting plan and organize work so that ABC Construction had a continuous backlog of booked projects that projected an average of 3 months into the future. This early warning system allowed ABC Construction to carefully plan staffing needs and add crews when the work load was going to be greater and move them out when the load diminished.

John's wife Shirley participated fully in business developments by taking over all the office and administrative work. While neither she nor John were financial experts they felt that the person they had hired shortly after Reginald's death, Joe Wilson, would do a good job.

Current Situation

By 2000 John began to feel some concern for his own health and he and Shirley decided to sell the business. After more than 35 years as a master electrician of which 15 years were in his own business, John felt he could say he had done it all. His grown children had never shown an aptitude or interest in the business so he felt justified in selling it to a third party. Reginald had moved as far away from the sea as possible but John had always held a desire to retire and cruise the west coast on a boat.

John is a mature businessman who is characterized by his steady and unruffled way of doing business. He has taken a careful and cautious approach to the sale of the family business. He is not in a hurry nor will he make a rash decision to free himself up from his daily responsibilities. John feels that the business is in great shape and he can take the time he needs to sell it in the best way possible for him, for his clients, and for his employees. If John had been able to go to college he would have made an excellent engineer.

John and Shirley spoke frankly to me and revealed that neither of them were knowledgeable about how to sell or price a business for sale. They advised me that the Construction Manager, Lee Williams, had expressed a strong interest in buying the business but that there was no commitment on either side. John determined that he would make his decision to sell based on the best, fair estimate of the business value. If that were to coincide with Don's interest and ability to pay he would be happy to see the business go to someone who knew the company and understood how it was run. John also expressed concern that the loyal clientele that ABC Construction had built up over the years be adequately served after his departure.

10. List all locations where the Company performs business activities. Briefly describe the activity at each location.

Location

ABC Construction provides electrical contracting services to residential and industrial new construction, existing construction and new build outs of out dated properties. ABC Construction provides these services primarily in Southern California but also serves Nevada. John Smith is a licensed electrical contractor in both states.

11. Describe the products or services provided by the Company.

The best way to describe the services provided by ABC Construction is to quote the California Occupational Guide number 121 on electricians.

“Electricians plan, lay out, install, repair, and maintain electrical equipment that provides light, heat, communications, and power. Electricians perform electrical work required in the building and remodeling of structures. They assemble, install, and connect lighting and power systems, thermostats, intercoms, signaling systems, and ventilators. Electricians follow blueprints and specifications to install electrical wires, cables and conduit systems. Electricians must have good mechanical ability, a thorough knowledge of the principles of electricity, circuitry, and power distribution within a building and familiarity with the materials and techniques of construction. For safety, electricians follow local electrical building and safety codes. On small jobs they may work alone with minimal supervision, and they may supervise an apprentice. On large jobs they may work under the direction of the electrician supervisor or foreman.”

More specifically, ABC Construction provides all these services to both the residential and industrial markets. While ABC Construction revenues come primarily from new construction, remodeling jobs have begun to take a small but growing part of the business. Mark has supported the growth of this business to offset the potential slow down in work that comes when the construction industry takes a cyclical dip.

Common residential jobs can be the electrical installations for a new sub development of homes built by a customer general contractor. The contract is usually done between the general contractor and the electrical company. The residential developer approves the GC overall budget but most often does not intervene in the choices the GC makes for sub contractors. Consequently, the relationship between the GC and the sub contractor is extremely important.

Typically, ABC Construction would receive a call from a GC advising of a housing development going up and a timetable for when structural framing would begin and be ready to receive electrical installation. Shirley and John would chart the size of the development, dates and optimum mix of crews and timing to complete the project and then develop a project budget. John would review this budget with the customer along with the timing schedule. With a signature from the GC, ABC Construction would book the job and prepare staff as well as review inventory, schedule trucks, work crews and “kits” and back up in case something fell through. This process occurs generally with enough lead time for ABC Construction to purchase inventory and have it delivered just in time so that it can be included in the “kits” and used on the job site.

Industrial jobs are done through very much the same process with the exception that they can often be larger and require a higher degree of expertise to comply with all the complexity an industrial or office building can demand. These jobs are managed by the most expert crews and often John himself and Don as well as the foremen pitch in and work directly on them.

12. Describe the Company’s competition in the marketplace. Include competitors who provide a substitute for the Company’s product or service.

Based on statistics produced by the Guide to the Electrical Contracting Market published in 1999, there are more than 7,500 electrical contracting companies in the State of California. The vast majority of these companies are comprised of 4 or less employees including the owner. They comprise an astonishing 58% of all companies. Another 19% of these companies are comprised of 5 to 9 employees, including the owner. This means that fully 77% of all electrical contracting companies in California are small, almost individual firms. The surprisingly fragmented nature of this market means that ABC Construction faces very stiff competition for work. Since most of these smaller firms will not have the resources to provide the infrastructure, materials, or the experienced personnel that ABC Construction offers, they typically compete on price alone. In many cases they employ illegal aliens at rock bottom wages to compete better. This represents a segment of the market that ABC Construction is consciously avoiding.

John estimated that he had approximately 500 direct competitors in his geographical and local market area. As with the national averages, the vast majority of these competitors are the smaller, less capitalized, shoe string type operations that often bid jobs as lowest cost bidder. These small firms stay in business by picking up the smaller jobs and the rock bottom priced jobs that other, more established firms will not take. They are characterized by average to poor work, few or no work quality guarantees, lack of timeliness and an ever changing cast of characters as bottom rung employees. In many

cases these firms are not used because they are not able to commit to completion times on larger jobs. They just do not have the size or manpower to handle them. They do not pay union wages or benefits.

From the other end of the spectrum there are the very large, state wide firms that have great economies of scale and employ several hundreds of electricians. These firms are successful on large projects for the speed with which then can complete a job and the generally good quality of work they do. However, in many cases, they truck crews in from other parts of the state and local General Contractors are not always comfortable working with people they don't know.

There is also a small group of direct competitors that are more or less the size of ABC Construction, with more or less the same kind of pedigree; local electricians who have worked hard and built up a steady and consistent work product and clientele and who hire them consistently. John is friendly with this group of competitors and they often refer work to each other when they are overbooked. This is true but friendly competition. There has always been enough work for these firms to prosper. John estimates that the competitive set looks like this, but he had no statistics or research studies to back it up.

Total California

	Competitive Firms	Description	Number	Estimated % Firms
Total	Entire California Mkt	all firms, all sizes	7500 est	100%
	1-4 employees	smallest firms	4350	58.4%
	5-9 employees	next smallest	1455	19.4%
	10 -19 employees	mid sized	900	12.0%
	20-49 employees	mid sized	532	7.1%
	50-99 employees	large	150	2.0%
	100+ employees	mega	82	1.1%

Source: Guide to Electric Contracting Market, US Census 1999,

California estimate of establishments

John Smith estimates

Southern California/Western Nevada Local Area Market

	Competitive Firms	Description	#	Estimated % Firms	Sales Est.
Total	Entire SoCal/Nev	all firms, all sizes	500	100%	460MM
	1-4 employees	smallest firms	292	58.4%	<i>both combined</i>
	5-9 employees	next smallest	97	19.4%	<u>30MM</u>

10 -19 employees	mid sized	60	12.0%	90MM
20-49 employees	mid sized	36	7.1%	108MM
50-99 employees	large	10	2.0%	82MM
100+ employees	mega	6	1.1%	150MM

Source: Guide to Electric Contracting Market, US Census 1999,

California estimate of establishments

John Smith competition estimates

There are no statistics to measure sales by company but John's estimates are that the smaller jobs, the lowest margin jobs are handled by the smallest and next smallest firms. This, he estimates does not represent more than 20% of total market sales volume. The remaining 80% of the market is divided unequally between the rest of the companies in the local area market. As follows most industries, margins increase as sales volume goes up. Thus, companies in the 10 to 19 employee range will have sales revenues averaging about \$1.5MM per company. This makes margins razor thin and these companies are usually not very profitable. The large and mega companies will be working with margins in the 15 to 25% range, depending on the job.

13. List advantages/disadvantages to Company’s products and/or services to those provided by its competitors.

Advantages

ABC Construction has some significant advantages over its competitors. The long term commitment to on time, within budget work has paid off. They are well established in the market after 16 successful years of operations. They have a wide variety of customers with none representing more than 10% of the overall sales. The quality of the work is excellent. Happy well paid employees at union rates are stable and there is low turnover. ABC Construction has a strong reputation in the market, with excellent facilities and equipment. Importantly, they have a high degree of repeat business from existing customers. Over 50% of the business comes in the door from existing customers that do not require costly new business visits, sales pitches, and low-ball bidding. Finally and most importantly, ABC Construction’s system of work trucks with work “kits”, the innovative way they plan work and employee quality and permanence give them a competitive advantage over firms of all sizes. This allows them to work faster and more efficiently and produce a better margin than competitors.

Disadvantages

Supervisory staff is overextended with so many work teams and projects to manage. Union wages are automatically approximately 20% higher than non union competitors. This is mostly offset by the higher degree of efficiency that ABC Construction demonstrates on projects. Competitive threats are significant and come from larger firms constantly working to develop relationships with ABC Construction’s customers. The pace of innovation is increasing and requires constant vigilance that, in an average size firm like ABC Construction, is more difficult to invest in and manage. Finally, the maquiladora and illegal alien problem has increased dramatically over the past few years. When interest rates rise and construction budgets are squeezed, General Contractors need to cut corners in every area. During these times it is very difficult for GC’s to continue paying higher amounts for work that they could get for very much less with illegal workers. In these cases, ABC Construction cannot compete. ABC Construction plans for these situations and so far has been able to avoid them but it is an ongoing issue.

14. List the Company’s primary customers and an estimate of the total revenues represented by each customer.

<u>Customer Name</u>	<u>Estimated Volume</u>	<u>Comments</u>
Newhaul Homes	650K	Tract home builder, requires fast, Accurate and inexpensive work
Jackson Brothers	700K	Office construction, warehouses, 16 year relationship is excellent
Depot Construction	350K	Referral business installation jobs of retailer merchandise. Possible to expand this business into more areas
Fortune Development	750k	High end apartment buildings and Luxury single family and town-

State of California	500k	Homes., High margin business With top of the line materials and Systems. Premium price for the Best quality work. Excellent and Growing relationship with Red Bluff Various projects from rewiring Existing bldgs to new const.
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<u>Customer Name</u>	<u>Estimated Volume</u>	<u>Comments</u>
County of Any towm	500K	1 st year of a 10 year long plan To rehabilitate county schools, Hospitals, and offices
Nevada Gaming Inc	375K	New resort and casino wiring And refurbishments
Reno Development	450K	Single family tract homes and Town home developments
Any towm Homes	725K	16 year relationship with this Successful local builder who has Land ownership to continue At the present rate for the next 7 years
Sun City Retirement Community	700K	Long term project of mid level and quality assisted living homes And apartments
EEZZ Storage	595K	Air conditioned storage units with

220volt current.

All others 1,000MM Composed of new construction
 And remodeling, residential and
 Industrial. No one customer
 Exceeds 200K

Total 7,295MM

15. List the Company's primary suppliers and the product or service they provide. Indicate whether or not suppliers can be easily replaced.

<u>Supplier name</u>	<u>Inventory supplied</u>	<u>Alternate?</u>	<u>Comments</u>
Essex Wire	all types of wiring	Many	Dependable, good price, partial Lots
Johnson Wire	wiring products	Many	Bulk discounts and special orders Not a problem
Conduit experts	Conduit	Many	Bulk and small shipments Friend of Mark Smith
ABC Panels		Two	Standard and custom panels For switches
Jackson Switches	Switches and breakers	3	Standard switches and breakers for Single and multi family

16. Briefly describe the industry in which the Company operates. Is the industry in a period of growth or decline? Are there many providers of the product/service or a few? Are companies acquiring one another? Does the industry follow the national economy?

According to a variety of predictions grouped in the magazine *Electrical Contractor*, the housing and industrial construction market will remain flat for the years 2000 and 2001. Estimates made by major industry resources McGraw Hill, Potable Cement Assn, Home Builders Assn, Fannie Mae, Paine Webber, and a variety of bankers and Wall Street firms, predict the markets will remain flat to slightly up. This information contrasts with the unscientific survey we conducted in the Any towm area of Califomia. Here we see a slight increase year over year of 4% growth. The construction

industry is benefiting from a period of low interest rates and low inflation. These overall macro economic factors are expected to continue into the future and provide a stable backdrop for economic expansion in California and other major destination states.

The electrical contracting segment of the construction industry demonstrates a higher degree of resilience and resistance to economic downturns than the construction industry itself. Electrical contracting services are required for new construction, refurbishing, residential and industrial markets, highway projects and any other number of installations where electricity is required. The industry, as shown previously, is peppered with a whole gamut of competitors. Most are in the very small size range and do not present serious competition to larger firms. Mid sized and larger firms do compete seriously for work and this keeps a strong lid on price rises and inflation. Up until now the industry has resisted serious consolidation. This is in part due to the fiercely independent nature of most construction companies and general contractors, as well as the nature of the business. We do predict, however, that in the next 10 years there will be an irresistible move toward consolidation in the industry. This will leave the very large and the very small still alive. The economies of scale for consolidation of the mid to large companies will be too attractive for owners to pass up and the very small companies will continue in their niche. The industry follows the national economy in that the primary determinant of housing starts is interest rates. Since we predict stability and low interest rates for the foreseeable future, this presents a favorable outlook for the industry.

17. List trade publications pertaining to the industry. Include publisher’s name and address.

<u>Name</u>	<u>Publisher</u>	<u>Address</u>
Electrical Contractor	McGraw Hill	112 South Way, Los Angeles
RS Means Estimating	RS Means	234 Capital Drive Wash DC
Federal Reserve Bank Beige Book	Same	San Francisco, Federal Reserve
California Economic Indicators	Cal. Dept Finance	Sacramento, Cal
Nevada Economic Indicators	Nev. Dept Fiance	Carson City, Nev.
Construction Fiancial Management Association	US Gov.	Washington DC

List public companies that may be considered comparable “guideline” companies.

<u>Company Name</u>	<u>Industry</u>	<u>Exchge</u>	<u>Description of Services</u>
EMCOR Group, Inc	Capital Goods	NYSE	Mechanical and Electrical Construction
TechLite, Inc.	Capital Goods	OTC	Retrofitting of existing lighting systems
Helionetics, Inc.	Capital Goods	OTC	Manufacture of consumer Lighting
Noga ElctroMech	Capital Goods	NASD	Electrical Contracting and Engineering
Cerbco, Inc.	Capital Goods	OTC	Pipeline/Sewer rehabilitation
Chemed Corp	Capital Goods	NYSE	HVAC, Plumbing services

Comfort Sys. USA Capital Goods NYSE HVAC, repair, replacement services

19. Number of Employees:

Full-time 14 Part-time None Temporary Varies by season Contracted 37

20. Are any employees covered by a collective bargaining agreement? Yes No

If yes, briefly describe agreement and attached a copy.

No copy of the collective bargaining agreement was available for me to include here, however, Lee Williams was kind enough to outline the key elements of the union contract. ABC Construction is a member of the *National Electrical Contractors Association* (NECA) and the union that ABC Construction employees belong to is the *International Brotherhood of Electrical Workers*. It covers all foremen, and electricians. Lee Williams, who formerly was a member has now moved into a management position. Both these organizations contribute to a *Joint Apprenticeship Training Committee* that provides ongoing training for entry level employees. The basic terms of the collective bargaining agreement are as follows;

- 7. Hourly wages ranging from \$14.00 to \$24.00 based on seniority and job title
- 8. Medical insurance split 50%/50%
- 9. 401K program with 50% contribution of ABC Construction for every \$1 of employee contribution
- 10. 2 week paid vacation, increasing to 4 weeks after 10 years of service
- 11. Paid time off for apprenticeship programs
- 12. 50% contribution to continuing education programs in general electrical area

ABC Construction has been and continues to be very respectful of the union and willingly meets union demands that are negotiated on a statewide and national basis. Based on this good relationship, there has been labor peace throughout the life of the company. Electricians know ABC Construction to be a top tier company to work at and when a position comes open many apply for it.

21. List members of management team. Include title, duties, and compensation.

NAME	TITLE	DUTIES	COMP.
John Smith	CEO/President/Co-Owner	Bidding, marketing, mgmt	120k
Shirley Smith	VP/CO-Owner	Office Management	120k

22. List all other key employees. Include their title, duties, and compensation.

NAME	TITLE	DUTIES	COMP.
Lee Williams	Construction Manager	Supervise 4 foremen Quality control	60k
Jack Schwartz	Estimator	Job Costings & budgets	40k
Steve Gonzalez	Maintenance Foreman	Supervise 2 mechanics	45k

Maintenance all equipment

Joe Wilson Office Manager, Controller Supervise 2 staff; AP/AR 55k

23. Briefly describe the premises from which the Company operates. Is the facility owned or leased? If, leased what are the terms? Briefly describe lease. Are premises large enough to allow for expansion? If not, what is management's solution?

The facility is leased from the Smith Family Limited Partnership. This limited family partnership was set up by Reginald shortly before his death in 1996. It appears that he had two brothers and one sister who still live in England. Reginald did not have the money to start the business in 1985 so he made a deal with this brothers and sister to start and fund a partnership to buy the property and building on ABC Construction Boulevard. He made a long term agreement to rent the property at a competitive rate from the family partnership and his brothers and sister agreed to a long term contract and a transferable right of first refusal if they ever decided to sell the property. As the business prospered Reginald offered on several occasions to buy the property from the family partnership but neither his brothers nor his sister wanted to change the arrangement. Sensing that one day the company might have a problem, Reginald wisely bought the property adjacent to the current property just prior to his death. He reasoned that, if the family partnership ever decided to increase the rent beyond a reasonable amount or sell the land for an amount beyond his means, the company would have the resources to quickly reconstitute an operational base next door.

The current, rented facilities are 5400sq feet of building space on a two floor building that is on three acres with a full acre paved for vehicle parking and equipment storage. Administrative offices are on half of the second floor. The other half of the second floor is used for storage of inventory. The first floor is made up of two mechanics bays for truck and machinery maintenance. Adjacent to this are two workshops. The first is a machine shop with lathe, drill press, shapers and sophisticated pipe bending machines. The second is a metal fabricators shop equipped with a shearing machine, hand bending presses and rivet guns for fabricating the various electrical boxes and custom units that cannot be bought as inventory. Additionally, there are two small cubicles with desks that serve as offices for the construction manager and the estimator. The estimator also serves as dispatch for job teams and is responsible for replenishment of inventory in the trucks that go to the job sites. At the extreme end of the building on the ground floor are 4 stand up dispatcher podiums. These are used by the four foremen to direct the activities of the work teams that they direct to the job sites.

This site set up provides ABC Construction with a competitive advantage over other firms since they can quickly build custom electrical boxes to solve problems. Teams at the job site call in the dimensions of the custom work and the maintenance foreman and his mechanics build the required units and drive them to the site.

The current premises are adequate for the current work load. John Smith advised that he had resisted the temptation to expand the facilities and invest more money in assets. He had felt that, given the cyclical nature of the industry, it would be better to deal with a bit of discomfort from time to time rather than have additional overhead charges to cover. The current rental contract is valid for an additional 9 years with annual review of rental amount based on a local rental survey done by an independent firm. So far these reviews have been done by Sue Land at Commercial Realty Company. My review of the rental agreement shows that it is a firm contract for the next 9 years. Unless there is mutual consent to eliminate it, both parties are obliged to abide by it. This is to the advantage of ABC Construction since the rental amounts are incidental as relates to overall revenues and represent a very small portion of expenses. This amount, even as it grows over the coming years, will continue to be less than the carrying costs of new construction on the additional land the company owns. This advantage could be negated if the additional land were to be developed so as to produce revenue to ABC Construction.

The adjacent land that ABC Construction purchased is a 5 acre parcel with equal ease of entry and exit. It is undeveloped. On several occasions customers have suggested ABC Construction build a larger building for themselves and rent excess space to construction companies. ABC Construction

has considered doing this as it would provide additional revenue to the operation and hedge revenues from operations. But this has not been done so as to respect the agreement made by Reginald with his brothers and sister. John recognized that if the business continues to grow at over 10% in the following year as it did in the past year, his seasonal space pressure would begin to become a permanent space problem. In that case, he would be forced to begin to develop the adjacent property. John said that he frankly hoped to pass that issue on to the new owners. Having the additional land ready for development and owning a long term reasonable contract on existing facilities represented a very stable basis upon which to run and expand the business.

John also felt that in a selling situation he did not want to distract himself from the operations of the business or embark on a new project of that magnitude.

24. Briefly describe age and condition of any major pieces of equipment used in the Company's business.

Most of the \$1.35 million in equipment is made up of rolling stock and electrical construction "kits" that accompany each truck when it goes out on a job. There are a total of 18 trucks and 20 electrical construction kits. These kits include ladders, wire cutters, bolt cutters, soldering equipment, portable welding equipment, electrical generators, spare parts and tools of all types. The kits are standard for each truck and are maintained and tested weekly by the maintenance team. Any tools that fail are reported by the work crews and replaced immediately. Employees who abuse equipment are reprimanded. All kits are in excellent condition and provide lasting service. The life of a kit generally exceeds 5 years. The maintenance group replaces kits and kit equipment as it completes its useful life. The rolling stock is carefully maintained by the maintenance crew. This has been a source of pride for John as it was for his father. Full mechanical review of the rolling stock is done every 30 days or 3000 miles, whichever comes first. Trucks are equipped with bypass oil filters which has virtually eliminated engine wear and breakdown. Average mileage per truck per year is 25,000 miles. In 4 years trucks that reach 100,000 miles are assessed for quality and value. In most cases the maintenance crew overhauls engines, suspensions and transmissions and puts them back in service for another 2 years. As the vehicle approaches 150,000 miles of service it is retired from the fleet and sold at auction. The maintenance team works shifts that do not conflict with the truck's use during the daylight working hours of the work crews. Approximately \$300k of the equipment is made up of the machine and fabrication shop tools and presses. This equipment is robust and requires less maintenance and generally does not need replacement. Lathes and drill presses routinely are in service in companies for 30 to 40 years, with an occasional change of an electric motor; which, in the case of ABC Construction, are rewound by staff and reinstalled. Office equipment and computer equipment is replaced every 5 years. ABC Construction's software is up to date and compatible with the latest advances used in the industry.

25. Describe contingent liabilities.

ABC Construction has no legal liabilities pending. In this regard the company has an excellent record. The only contingent liability the company has in the long term contract signed for the rental of the company premises. This contract is reviewed every year and the rent is established at a true average of comparable space for the area. If the company were to decide to move (highly unlikely given the stability of the customer base) it is estimated that the premises could be sublet and this would be agreeable to the owners.

26. Describe any offers to buy or sell business interests in the Company.

From time to time over the course of the years, larger firms have inquired as to John's interest in selling the business. Up until now, he has always refused. Having observed the way these companies operate, he knows that they will acquire the client base, the best employees and will eliminate all the duplicated departments like accounting, administration, special services, maintenance teams. The purpose of this tactic is to wring as much profit from the business as possible and reduce overhead as much as possible. John has always felt that this would be a betrayal to his clients and it wouldn't be long before they left for another company. John feels strongly that the success of ABC Construction has always been the trust and commitment the company has shown to customers. John wants to pass this along to the new owners and do his utmost to assure customer service to his client base.

27. Concluding Points

My overall assessment of ABC Construction is positive. It is a well run company by honest and forthright owners who have worked hard to develop a reputation of quality and fairness. Staff are the best of the best and remain loyal to the company over the long term. ABC Construction is a quality operation.