SN VALUATION
SN CAPITAL SN CONSULTING SN ENGLISH

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November 30, 2012

Business Acquisition Series (BAS): Accounting Considerations

We were looking into an acquisition by Spectrum Pharm and pasted the description from their 10-K below. We will look into the accounting aspects of an acquisition.

The basic idea is assets – liabilities + goodwill = acquisition price. In this particular acquisition, a $27MM goodwill on a $204MM acquisition, implies a ~10% premium to the book value, which is fairly cheap. In closer inspection, we see the bulk of the asset side value ($145MM/$267MM assets, or 54%) is from the distribution rights for the medication.

So, having a lot of goodwill, or essentially premium over the book value of the net assets, is not value adding. Invested capital which is categorized as goodwill is recouped from future cash flows from the acquired net asset, while capital allocated for the net assets acquired assets, dollar for dollar. Or in other words, high goodwill implies capital may be invested in overly priced assets, which may never be recouped or take a long period to realize the target returns.

"Goodwill is calculated as the excess of the purchase consideration transferred over the net assets recognized and represents the future economic benefits arising other assets acquired that could not be individually identified and separately recognized. Specifically, the goodwill recorded as part of the acquisition of Allos includes benefits that the Company believes will result from combining the operations of Allos with the operations of Spectrum and any intangible assets that do not qualify for separate recognition, as well as future, yet unidentified products. The Allos acquisition will also allow us to gain additional expertise and intellectual property for the next generation of anti-cancer therapeutics, an expanded and complimentary product mix, and an assembled sales force, which we believe supports the amount of goodwill recognized. Goodwill is not amortized and is not deductible for tax purposes."

	Pre Target	Post Target	Acquiror	Combined
Cash	50	50	30	80
PP&E	50	50	20	70
Goodwill	0	20	0	20
Assets	**100**	**120**	**50**	**170**
Liabilities	50	50	20	70
Paid in capital	30	70	20	90
Retained Earnings	20	0	10	10
L+SE	**100**	**120**	**50**	**170**

A acquired Target for 70. This would create goodwill of 20, since the book value is 50, or 70-50=20 goodwill. To offset the increase in Assets from goodwill account, Stockholder's equity has to increase by 20 as well. The Stockholder Equity for the Target co. would be zeroed out, and replaced by the 70 from the acquisition. The 30 in Paid in capital, or the seed capital, and the retained earnings are returned to the original owners. The 70 in new capital, will be recognized as the Post-acquisition paid in capital.

This is why we are wary of small firms, attempting to grow by acquiring other competitors, such as Rimage, which acquired a cloud business. Rimage eventually wrote off the goodwill within a matter of a few months. They blew away $50MM, which would have been better used with a share repurchase or cash dividend.

Allos Acquisition

Pursuant to the terms of the Agreement and Plan of Merger dated April 4, 2012 among Spectrum, Allos and Sapphire Acquisition Sub, Inc., Spectrum acquired a total of 96,259,850 shares pursuant to a tender offer, representing approximately 89.98% of the outstanding shares of Allos common stock on September 5, 2012 for an amount equal to the price per share of $1.82 in cash. Allos develops and markets anti-cancer therapeutics in the United States. As a result of the acquisition, we acquired an assembled sales force and anti-cancer therapeutics which enhanced our existing product base.

As part of the purchase consideration, Spectrum agreed to pay Allos shareholders an additional $0.11 per share if FOLOTYN® receives a conditional regulatory approval in the European Union or the EU, by December 31, 2012 and the first reimbursable commercial sale of FOLOTYN® in the lead indication in the third EU major market country is made by December 31, 2013. In January 2012, the European Medicines Agency, or EMA, Committee for Medicinal Products for Human Use, or CHMP, adopted an opinion recommending against approval of Allos' Marketing Authorisation Application, or MAA, for FOLOTYN for the treatment of patients with relapsed or refractory peripheral T-cell lymphoma or PTCL in Europe. Allos submitted a request for the re-examination of the CHMP opinion in January 2012, and, on April 19, 2012, the CHMP confirmed its position and adopted a final opinion recommending against approval of the MAA. On the same day, the CHMP forwarded a copy of its final opinion to the European Commission, or the EC, which is the regulatory authority responsible for rendering a final decision on the MAA. On June 21, 2012, Allos received a letter from the EC stating that the EC had adopted the CHMP's opinion recommending against approval of the MAA. The decision is final and binding. Therefore, Spectrum management does not believe that the milestones triggering the contingent value right are achievable within the specified time frame and accordingly, did not value the contingent value right. We will continue to evaluate the fair value of the contingent value right through December 31, 2013. The Allos related transaction costs expensed for the three and nine months ended September 30, 2012 of $2.2 million and $5.5 million, respectively, were included in selling, general and administrative expenses.

Consideration Transferred

The Allos acquisition purchase price was allocated to tangible and intangible assets acquired and liabilities assumed based upon their estimated fair value at the acquisition date. The following table summarizes the purchase price ($ in 000's):

Cash consideration	$ 205,204
Contingent value right	—
Total purchase consideration	$ 205,204

Fair Value Estimate of Assets Acquired and Liabilities Assumed

Under the purchase method of accounting, the total purchase consideration is allocated to Allos net tangible and intangible assets based on their estimated fair values as of the closing date. The excess of the purchase price over the fair value of assets acquired and liabilities assumed was allocated to goodwill. The goodwill acquired is not deductible for tax purposes. The following table summarizes the fair value of the net assets acquired and included in our condensed consolidated balance sheet is as follows ($ in 000's):

Cash	$ 71,940
Accounts receivable	6,835
Related party receivable	10,482
Inventory	2,246
Other current assets	1,527
Fixed assets	913
FOLOTYN distribution rights – US & Canada	118,400
FOLOTYN license with Mundipharma	27,900
Goodwill	27,550
Total assets acquired	267,793
Accounts payable & accrued liabilities	25,716
Mundipharma R&D expense liability	12,300
Deferred payment contingency	2,200
Deferred tax liabilities, net	22,373
Total liabilities assumed	62,589
Net assets acquired	$205,204

The acquired intangible assets consisted of developed technology for approved indications of currently marketed products. The acquired intangible assets principally relate to the FOLOTYN® distribution rights in the United States and Canada. The weighted-average amortization period for such intangible assets acquired is outlined in the table below:

	Value of Intangible	Weighted-Average

	Assets Acquired	Amortization Period
In-process research and development—FOLOTYN® Distribution Rights	$118,400	(1)
FOLOTYN® License & Distribution Agreement with Mundipharma	27,900	10 years
Total identifiable intangible assets	$146,300	

(1) Acquired in-process research and development ("IPR&D) is an intangible asset classified as an indefinite-lived until the completion or abandonment of the associated R&D effort, and will be amortized over an estimated useful life to be determined at the date the project is completed. Intangible IPR&D is not amortized during the period that it is considered indefinite-lived but rather tested for impairment.

Included in amortization of purchased intangibles expense in the accompanying statement of income for the three and nine months ended September 30, 2012 is $186,000 related to the amortization of these intangibles.

The fair value of the acquired in-process research and development and license and distribution agreement intangible assets was estimated using the income approach. The income approach uses valuation techniques to convert future amounts to a single present amount (discounted). Our measurement is based on the value indicated by current market expectations about those future amounts. The fair value considered our estimates of future incremental earnings that may be achieved by the intangible assets.

Goodwill is calculated as the excess of the purchase consideration transferred over the net assets recognized and represents the future economic benefits arising other assets acquired that could not be individually identified and separately recognized. Specifically, the goodwill recorded as part of the acquisition of Allos includes benefits that the Company believes will result from combining the operations of Allos with the operations of Spectrum and any intangible assets that do not qualify for separate recognition, as well as future, yet unidentified products. The Allos acquisition will also allow us to gain additional expertise and intellectual property for the next generation of anti-cancer therapeutics, an expanded and complimentary product mix, and an assembled sales force, which we believe supports the amount of goodwill recognized. Goodwill is not amortized and is not deductible for tax purposes.

Deferred tax liability reflects taxes associated with the acquired in-process research and development and license and distribution intangible assets recognized as part of the acquisition.

The results of operations for the acquisition discussed above is included in the consolidated statements of operations from the acquisition date. The pro forma results of continuing operations are prepared for comparative purposes only and do not necessarily reflect the results that would have occurred had the acquisition occurred at the beginning of the years presented or the results which may occur in the future. The following unaudited pro forma results of operations for the nine months ended September 30, 2012, assume the Allos acquisition had occurred on January 1, 2012 and for the nine months ended September 30, 2011, assume the acquisition had occurred on January 1, 2011 ($ in 000's):

	Nine Months Ended September 30,	
	2012	2011
	(Unaudited)	
Total revenues	$229,012	$199,329
Income from continuing operations	$ 44,775	$ 13,894
Net income	$ 53,036	$ 7,383
Basic net income per share	$ 0.91	$ 0.14
Diluted net income per share	$ 0.82	$ 0.13

With respect to the acquisition discussed above, we believe the fair values assigned to the assets acquired and liabilities assumed were based upon reasonable assumptions. Our allocations of the purchase price is largely dependent on discounted cash flow analyses of projects and products of Allos. We cannot provide assurance that the underlying assumptions used to forecast the cash flows or the timely and successful completion of such projects will materialize as we estimated. For these reasons, among others, our actual results may vary significantly from the estimated results.

The recorded purchase price amounts are preliminary and subject to change as we are awaiting additional information related to income taxes. The effects of final adjustments, if any, on the purchase price allocation are not expected to be material.

Revenues and net loss of Allos included in our condensed consolidated financial statements from the date of acquisition, September 5, 2012 to September 30, 2012, were $6.0 million and ($1.0) million, respectively, after a provision for income taxes of $1.4 million.

Business Acquisition Series (BAS): Part 6

Business Product: SN Valuation

Business Idea: Back in 2007, the founder, Sung Nam, was laid off from his first job, as the company downsized by 40%. As a result, he began to place minimal trust in job security and started to develop the website focusing on equities, real estate and fixed income products. The entire research process was formed from scratch and after a 3 year development period, the site is publishing 1 new update on U.S. equities, Korean equities, fixed income, real estate, market/economy news and business acquisition series. The site is aimed at providing analytical investment research across the different asset classes and targeted for novice investors, as many of the household financial media may be too broad for the investor to understand the practical subtlety of each news bit. Through the research, the founder and analysts and interns desire to implement real, hard money investments. In the long-term, the founder would like to develop the operations into a small investment/acquisition firm.

Demographic/client base: Novice investors

Google Search Result for Competitors: Tons. Seeking Alpha, blogosphere, established institutional research firms

Product/service highlight: Updated weekly, research reports for each of the 6 topics will be made available on the website. Typically 1 page overview of certain investment ideas, concepts and news.

Distribution/Operations: Hours of research utilizing a number of websites such as SEC filings, investment blogs/forums, stock screeners, Excel financial models, sell side research reports. It is a time consuming task which requires experience in valuation and comfort writing financial related reports. The reports are uploaded to a website building program and basic website coding knowledge is required. The possibilities are endless. One quick step we could take is creating firm awareness by publishing reports in Seeking Alpha under the value investing community.

Financing: None. Only costs $100 to develop.

Ownership burden: The biggest factor of this venture. Unless the acquirer is interested in writing reports, there is no incentive for the owner to purchase the site. The owner will be spending at least 10 hours a week updating the site.

Economically feasible?: Yes, bare bones cost of around $50/year.

Per Unit Spread: N/A

Valuation: Difficult to value in monetary terms with the low traffic volume (1,000 unique visitors in 3 years) and zero intangible asset value of the financial models and research.

Marketable?: No, SN Valuation is closely linked to the founder of the site, so the site will not be marketable, unless a proprietary research process, financial model or intangible asset is sold in association with the firm name and website.

Prototype: N/A

Conclusion: This site will be deemed worthless to potential acquirers unless 1) actual investments are made under the SNValuation name, 2) a proprietary process is developed.