

DUE DILIGENCE AND PROCEDURAL CHECKLIST FOR THE INDEPENDENT FINANCIAL ADVISER SOLVENCY OPINION

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Secured lenders often require that a solvency opinion be issued at the time of certain leveraged corporate transactions. These corporate transactions may include leveraged merger and acquisitions (M&A), stock redemptions, dividend payments, and others. Other parties (such as corporate directors, joint venturers, and M&A targets) may also request a solvency opinion related to certain debtor corporation transactions. Typically, these parties want assurance that the corporate transaction does not involve a fraudulent conveyance. Also, solvency opinions are sometimes performed before and after bankruptcy filings. These solvency opinions may relate to claims of either fraudulent conveyance or preference payments. With regard to leveraged corporate transactions, these solvency opinions are typically prepared by independent financial advisers. This discussion presents a "checklist" of due diligence procedures that financial advisers typically consider in a solvency analysis. This particular checklist relates to a leveraged M&A transaction solvency analysis. This checklist can be used as a procedural tool for the independent financial adviser. Or, it can be used by the debtor corporation management, the secured lender, or others involved in the process of reviewing the financial adviser's solvency analysis and/or solvency opinion.

INTRODUCTION

Independent financial advisers perform solvency analyses and issue solvency opinions for various transaction, financing, bankruptcy, taxation, and litigation purposes. In a solvency opinion, the financial adviser opines on the solvency of a debtor corporation at the time of certain corporate actions.

Typically, the solvency opinion is intended to demonstrate that the subject debtor corporation is solvent at the time that a debt is incurred, a dividend is disbursed, a distribution is made, an expense or liability is paid, an asset is purchased, a security claim is issued, a class of equity security is redeemed, one class of security is exchanged for another class, and so forth.

Sometimes, the solvency opinion may be intended to demonstrate that the subject corporation is insolvent on a specific date, or at the time of a specific event. An example of an insolvency analysis relates to when a corporate taxpayer may (or may not) recognize cancellation of debt (COD) income for federal income tax purposes.

This discussion will focus on the solvency analysis and the solvency opinion related to a corporate financing trans-

action. For example, a solvency opinion is often prepared at the time of a corporate merger and acquisition (M&A) financing, such as a leveraged acquisition transaction. In such instances, the financing source will want protection against claims of an avoidable fraudulent conveyance related to the leveraged transaction. In the leveraged M&A transaction solvency opinion, the financial adviser will perform the three generally accepted solvency tests.

Related to a leveraged M&A transaction, the three generally accepted solvency tests are:

1. the balance sheet test,
2. the cash flow test, and
3. the capital adequacy test.

First, this discussion summarizes the objectives of the three generally accepted solvency tests. And, this discussion describes the practical application of the three solvency tests.

Second, this discussion presents a checklist of the due diligence and analytical procedures that the independent

financial adviser will typically consider when performing a solvency analysis. This procedural checklist may also be used by the debtor corporation management, the secured lender financial institution, and other parties to the corporate action. These parties may use this due diligence checklist in their good-faith assessment of the financial adviser's solvency opinion.

OVERVIEW OF THE SOLVENCY OPINION

A solvency opinion is a financial adviser's opinion that the debtor corporation will not become insolvent as a result of the proposed financing transaction. For purposes of this discussion, we will consider the case where the proposed transaction is a leveraged acquisition or recapitalization transaction.

The objective of the solvency analysis is to determine whether the leveraged corporate transaction will result in any one of the three specified financial conditions. The importance of these three specified conditions is that they can be the basis for a claim that a fraudulent transfer occurred at the time of the proposed corporate financing transaction. The three conditions that are typically studied in the solvency analysis are defined in the United States Bankruptcy Code (section 548), the Uniform Fraudulent Transfer Act, and the Uniform Fraudulent Conveyance act.

A solvency opinion analyzes whether any of the following three conditions exist at the time of the corporate transaction (after giving effect to the proposed transaction financing):

1. The balance sheet test: Does the recorded amount of the debtor corporation liabilities (specifically including the proposed financing) exceed the fair value of the debtor corporation assets?
2. The cash flow test: Does the debtor corporation have adequate cash flow to service all of its liabilities (specifically including the proposed financing) as those liabilities come due?
3. The capital adequacy test: Does the debtor corporation have an unreasonably small amount of capital to run its business operations (after the proposed corporate transaction)?

Together, these three tests are identified as the solvency tests. In order to be considered solvent for purposes of a leveraged corporate transaction, a debtor corporation must pass all three tests. It is important to note that a solvency

opinion is based on the information that is available to—or reasonably foreseeable by—the financial adviser as of the proposed corporate transaction date.

Next, this discussion will summarize the principal procedures that the financial adviser will typically consider in each of these three solvency analysis tests.

The Balance Sheet Test

The balance sheet test determines whether, at the time of the proposed corporate transaction, the fair value of the debtor corporation assets (both tangible and intangible) is greater than the recorded balance of the debtor corporation liabilities.

For the purpose of the balance sheet test, first, the independent financial adviser will analyze the highest and best use of the debtor corporation assets. The highest and best use analysis will indicate the appropriate premise of value for the fair value analysis of the debtor corporation assets. The premise of value that the financial adviser will typically conclude for a solvency analysis is value in continued use, as part of a going concern business enterprise.

For purposes of a solvency analysis, fair value is typically defined as the price at which the 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, with both parties having reasonable knowledge of relevant facts.

Second, the financial adviser will estimate the fair value of the debtor corporation assets as of the date of the corporate transaction. This fair value analysis includes consideration of all of the debtor corporation financial assets, real estate and tangible personal property, and intangible assets.

Third, the financial adviser will consider the recorded balance of the debtor corporation liabilities. The debtor corporation liabilities include all current liabilities and all long-term liabilities.

Fourth, the financial adviser will subtract the recorded amount of the debtor corporation total liabilities from the fair value of the debtor corporation total assets. It is noteworthy that the amount of the liabilities includes the debt related to the proposed leveraged corporate transaction.

The balance sheet test is “passed” if the fair value of the debtor corporation total assets is greater than the recorded balance of the debtor corporation total liabilities. There are three generally accepted approaches (i.e., the income approach, the market approach, and the asset-based approach) that the financial adviser may consider

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in the aggregate valuation of the debtor corporation total operating assets. Within each generally accepted valuation approach, the financial adviser will consider one or more generally accepted valuation methods.

A detailed description of each generally accepted valuation approach and method is beyond the scope of this discussion. However, the Exhibit 1 checklist accompanying this discussion includes the procedures that the financial adviser will consider in each of the generally accepted valuation approaches and methods. The financial adviser performing the balance sheet test should be familiar with both the conceptual foundation and the practical application of all three generally accepted valuation approaches.

The income approach, market approach, and asset-based approach may all be applicable to the aggregate valuation of the debtor corporation total operating assets. Each of these three generally accepted approaches can be used to perform the balance sheet test.

However, the component analyses of the income approach will also be applicable to both the cash flow test and the capital adequacy test. Therefore, the income approach is typically used in every solvency analysis in order to (1) perform each of the three solvency tests and (2) ensure the consistency within the three tests of the valuation (and other financial) variables used in the solvency analysis.

The Cash Flow Test

The cash flow test analyzes the debtor corporation ability to meet its debt obligations as they become due. The financial adviser will typically project the debtor corporation expected cash flow for several periods into the future.

The term of the projection period typically corresponds to the repayment period for the proposed financing.

The cash flow test analysis will consider the repayment of all of the debtor corporation debt (both principal and interest) obligations, including the proposed transaction financing. Next, the financial adviser will analyze the debtor corporation cash flow available to meet debt obligations by estimating:

1. any excess cash balance available on the solvency test date,
2. the available cash flow expected to be generated during the projection period, and

3. the availability of any unused credit commitments available to the debtor corporation.

The cash flow test is “passed” if, in each prospective period, the debtor corporation can pay its projected debt obligations from one of the three aforementioned sources of cash. As part of the solvency analysis, the financial adviser will typically perform sensitivity analyses as part of the cash flow test.

In the sensitivity analysis, the financial adviser will “sensitize” or “stress test” the various cash flow projection variables. The objective of the sensitivity analysis is to determine whether the debtor corporation can meet its debt obligations under a variety of alternative financial circumstances and economic conditions.

“The cash flow test analyzes the debtor corporation ability to meet its debt obligations as they become due.”

The Capital Adequacy Test

The capital adequacy test (sometimes also referred to as the reasonable capital test) determines whether the debtor corporation is engaged in (or is about to be engaged in) a business or a transaction for which it has an unreasonably small amount of capital. The capital adequacy test determines whether the debtor corporation will have an adequate amount of capital to meet its:

1. operating expenses,
2. capital expenditure requirements, and
3. debt repayment obligations.

The capital adequacy test is related to the cash flow test. The cash flow test involves a long-term sources and uses of funds analysis. Typically, the term of

the cash flow test is the term of the proposed transaction financing. The capital adequacy test involves a short-term sources and uses of funds analysis. Typically, the period analyzed in the capital adequacy test includes the four fiscal quarters after the solvency date.

If the debtor corporation has a reasonable (i.e., adequate) level of capital, then it will be able to meet its financial obligations as they come due under various operating scenarios. The objective of the capital adequacy test is to assess whether the debtor corporation is likely to survive, assuming reasonable future business fluctuations.

The financial adviser will typically assess and analyze various operating scenarios, including the following:

“The capital adequacy test (sometimes referred to as the reasonable capital test) determines whether the debtor corporation is engaged in (or is about to be engaged in) a business or a transaction for which it has an unreasonably small amount of capital.”

1. debtor corporation management's best estimate of future financial and operational performance,
2. no change from the debtor corporation recent historical financial performance, and
3. reasonable variations in the debtor corporation revenue growth rate and profit margin assumptions.

The capital adequacy test is "passed" if the debtor corporation is expected to have sufficient cash on hand to pay its (1) operating expenses, (2) capital expenditures, and (3) current liabilities/current portion of long-term debt. In other words, after the proposed corporate transaction, the debtor corporation should be able to fund its ongoing business operations for the foreseeable future.

FINANCIAL ADVISER CAVEATS REGARDING RELIANCE ON ANY PROCEDURAL CHECKLIST

It is important for the financial adviser to consider several caveats regarding the use of any checklist of due diligence procedures.

First, no checklist should ever substitute for the independent financial adviser's professional judgment.

Second, the checklist presented in Exhibit 1 below is not intended to be a comprehensive and all-inclusive procedural list that should be followed without exception.

Third, the terminology (i.e., names of methods and/or procedures) used in the checklist presented in Exhibit 1 may have several interpretations.

Fourth, the facts and circumstances regarding a specific corporate transaction and a specific debtor corporation should always be considered when determining the appropriateness of any item on any checklist.

Finally, the Exhibit 1 checklist should not be used to derive a "quantitative score" to evaluate the quality of a solvency analysis or a financial adviser's solvency opinion.

For example, the fact that a particular solvency analysis did not receive a "score" of 100 percent does not imply that the financial adviser's solvency analysis is not complete or not in compliance with professional practices.

Also, the fact that a particular solvency analysis does receive a "high score" does not necessarily imply that the financial adviser's solvency analysis is complete and in conformance with professional practices. Such a "high scoring" analysis may still be lacking in professional competence or may be inadequate for the assessment of debtor corporation solvency.

The checklist presented in Exhibit 1 is a tool that the financial adviser can use as a procedural reminder in conducting a solvency opinion analysis. However, no checklist can evaluate the analytical quality and the professional judgment involved in the performance of the procedures.

The checklist presented in Exhibit 1 is not a substitute for the due diligence, prudence, and rigorous analysis that the independent financial adviser should perform.

Finally, the experienced independent financial adviser will understand that not all of the listed procedures are applicable (or even possible) for every solvency analysis. The professional judgment of the experienced financial adviser will determine which procedures are appropriate in each case.

It is noteworthy that the Exhibit 1 checklist excludes a description of the asset-based approach valuation procedures in the balance sheet test discussion. This is because, in practice, the asset-based approach is the least commonly used solvency opinion valuation approach.

However, this exclusion does not imply that the asset-based approach is inappropriate in a solvency analysis. Rather, the asset-based approach asset accumulation method and/or adjusted net asset value method may be used in a solvency analysis balance sheet test.

Practically, due to data constraints and other reasons, these asset-based approach valuation methods are performed much less frequently than either income approach valuation methods or market approach valuation methods.

SUMMARY AND CONCLUSION

The legal and financial issues related to a leveraged corporate transaction fraudulent conveyance and/or a debtor corporation solvency are complicated. A contemporaneously prepared solvency opinion from an experienced independent financial adviser is an important component in the secured creditor's defense against claims of a voidable capital transaction fraudulent conveyance.

The Exhibit 1 checklist enumerates the due diligence procedures that are typically considered by an independent financial adviser in the preparation of a solvency opinion. This Exhibit 1 procedural checklist should serve as a useful tool to the financial adviser, the debtor corporation management, and the secured lender involved in a leveraged corporate transaction.

In particular, the Exhibit 1 procedural checklist is intended to be applicable to the solvency analysis of a leveraged corporate M&A transaction. However, this solvency opinion procedural checklist should never substitute for the professional experience and reasoned judgment of the independent financial adviser.

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Exhibit 1
Checklist of Analytical Procedures Typically Considered in the Preparation of a Leveraged Corporate Transaction Solvency Opinion

A. Engagement Purpose and Objective

1. Identify the purpose of the solvency opinion (i.e., the reason to conduct the solvency analysis)
2. Identify the objective of the solvency opinion
3. Define the solvency analysis assignment
 - a. Identify the parties who will use the solvency opinion
 - b. Identify the effective date of the solvency opinion
 - c. Identify the solvency tests that apply to the subject assignment
4. Define the engagement fee structure, opinion content, delivery date, and professional qualifications of the engagement analysts in a written client engagement letter

B. Due Diligence and Collection of Data

1. Collect and review the transaction documents related to the subject leveraged corporate transaction
2. Collect and review the credit facility documents related to the subject corporate transaction
3. Collect and review the debtor corporation documents including:
 - a. Historical financial information (typically, the last five fiscal years and any interim statements) including:
 - i. income statements
 - ii. balance sheets
 - iii. statements of cash flow
 - iv. statements of changes in stockholders' equity
 - b. Pre-transaction and post-transaction debt structure
 - c. Current debtor corporation financial budgets, projections, and forecasts
 - d. Description of the debtor corporation business
 - e. Ownership structure (pre-transaction and post-transaction)
 - f. Legal documents relevant to the proposed corporate transaction
 - g. Other relevant operational information including, but not limited to:
 - i. product and/or service information/brochures
 - ii. list of major customers
 - iii. list of major competitors
 - iv. list of senior personnel
 - v. list of locations in which the debtor corporation operates
 - vi. description of any off-balance-sheet intangible assets and contingent liabilities
4. Conduct debtor corporation management interviews in all relevant functional areas, regarding:
 - a. historical operations and results
 - b. current operations and results
 - c. prospective operations and results
 - d. competitive environment
 - e. industry outlook
 - f. technological changes/developments
 - g. pending litigation and/or contingent liabilities
5. Conduct debtor corporation plant/site inspections
 - a. Inspect representative plants/sites and consider:
 - i. capacity limits and physical condition of the existing plants, facilities, and equipment
 - ii. functional and technological adequacy of the existing plants, facilities, and equipment

- b. Discuss plant/site with debtor corporation management representatives and consider:
 - i. current/future facilities expansion and capital investment plans
 - ii. competitive effects of any planned plant/facility changes
 - iii. expected operating cost effects of any planned plant and facility changes

C. Economic Environment (as of the Solvency Date)

1. Consider the national and international (if relevant) economic environment
2. Research and analyze the national and international economic environment and outlook
3. Consider the historical and expected relationship of the relevant economic environment to the performance of the debtor corporation

D. Industry Environment (as of the Solvency Date)

1. Research and analyze the history and nature of the industry in which the debtor corporation operates
2. Research the current outlook for the subject industry

E. Fundamental Position of the Debtor Corporation

1. Consider the debtor corporation capitalization and ownership (both pre-transaction and post-transaction)
2. Review the debtor corporation history
3. Review and analyze the debtor corporation current business operations and financial position
4. Consider the debtor corporation financial and strategic outlook
5. Perform a historical financial statement analysis
 - a. Consider financial ratio analysis
 - b. Consider trendline analysis
 - c. Consider common size analysis
 - d. Consider benchmark comparative analysis
6. Perform historical financial statement normalization adjustments, as necessary
 - a. Consider nonrecurring financial statement adjustments
 - b. Consider extraordinary financial statement adjustments
 - c. Consider change in accounting method financial statement adjustments
7. Perform a prospective financial statement analysis
 - a. Identify the key financial variables that drive the debtor corporation prospective results of operations
 - b. Analyze debtor corporation management-prepared projections/budgets/forecasts
 - c. Assess reasonableness of projections relative to historical debtor corporation results
 - d. Assess reasonableness of projections/budgets/forecasts relative to subject industry data

F. Solvency Analysis

1. Consider the appropriate solvency tests required for the subject solvency opinion
2. Perform the cash flow test to determine if the debts incurred post-transaction are beyond the debtor corporation ability to pay as such debts mature
3. Review the terms of the post-transaction debt obligations
4. Prepare detailed cash flow projections through the term date of the secured credit facilities
5. Prepare monthly or quarterly projections for several periods after the proposed transaction and annual projections thereafter
6. Develop the appropriate economic income fundamentals for the analysis of the debtor corporation cash flow available for debt service, including:
 - a. Sales
 - b. Cost of goods sold
 - c. Operating expenses

- d. Capital expenditures
 - e. Net working capital requirements
 - f. Depreciation and amortization expenses
 - g. Interest income and interest expenses
 - h. Federal and state income taxes
 - i. Debt principal payments
 - j. Dividend payments
 - k. Annual cash balances
7. Determine the debtor corporation quarterly/annual ability to meet its:
 - a. Operating expenses
 - b. Capital expenditures
 - c. Net working capital requirements
 - d. Interest expense
 - e. Debt principal payments
 8. Perform a series of sensitivity analyses related to the cash flow projections to test the sensitivity of future debtor corporation financial performance
 - a. Test the fundamental financial variables, such as:
 - i. sales growth
 - ii. EBITDA profit margin
 - iii. EBIT profit margin
 - iv. capital expenditure requirements
 - v. net working capital requirements
 - vi. weighted average cost of capital
 - vii. terminal year cash flow multiple
 - b. Consider the debtor corporation past performance, current economic condition and future financial performance in the sensitivity analyses
 - c. Review the debtor corporation ability to meet its financial obligations under each sensitivity analysis scenario
 9. Analyze, for each projection period:
 - a. Excess cash on hand
 - b. Available net cash flow
 - c. Debtor corporation unused credit availability
 10. Consider debt covenants of lenders and determine whether debtor corporation can meet the debt covenants in each year of the cash flow test
 11. Conclude whether or not the debtor corporation “passed” the cash flow test
 12. Perform the balance sheet test
 13. Estimate the fair value of the debtor corporation total operating assets
 - a. Identify the generally accepted valuation approaches and methods
 - b. Select the valuation approaches and methods appropriate to the subject debtor corporation
 14. Perform an income approach valuation analysis—such as the discounted cash flow method
 15. Review and analyze financial projections related to prospective results debtor corporation of operations for a relevant (e.g., five year) discrete projection period
 16. Develop the appropriate economic income fundamentals for the analysis of invested capital (i.e., long-term debt and stockholders’ equity) net cash flow, which considers:
 - a. Earnings
 - b. Noncash expenditures (e.g., depreciation expense, amortization expense, etc.)
 - c. Capital expenditures
 - d. Net working capital requirements
 17. Develop a discounted net cash flow analytical model with projection variables and assumptions that are consistent with the cash flow/debt repayment model employed in the cash flow test

18. Develop the appropriate yield capitalization discount rate for the present value calculation, with consideration to:
 - a. Risk-free rates of return
 - b. Equity rates of return (and/or equity risk premiums)
 - c. Systematic risk (e.g., beta)
 - d. Company-specific risk premium/required rates of return, with consideration to:
 - i. expected attainability of debtor corporation financial projections
 - ii. degree of post-transaction debtor corporation financial/operating leverage
 - iii. degree of diversification of debtor corporation business/product base
 - e. Capital structure
 - i. mix of debt and equity components of the debtor corporation “invested capital”
 - ii. typical capital structure in the subject industry
19. Develop an estimate of the terminal/residual value, with consideration to:
 - a. Terminal/residual year financial fundamentals (e.g., net cash flow projection for terminal year)
 - b. Terminal/residual year direct capitalization rate (e.g., dividend discount model)
 - c. Terminal/residual year market-derived pricing multiple (derived from capital market information of companies similar to the debtor corporation)
20. Apply the derived yield capitalization discount rate to the discrete period estimated economic income projections (e.g., net cash flow) and the terminal/residual value estimate
21. Perform an income approach valuation analysis—such as the direct capitalization method
22. Analyze the appropriate measure of economic income subject to direct capitalization
23. Estimate a normalized amount of future period economic income subject to capitalization
24. Estimate the appropriate market-derived direct capitalization rate calculated as:
 - a. The debtor corporation yield capitalization rate for the selected measure of economic income
 - b. The debtor corporation expected long-term growth rate in the selected measure of economic income
25. Divide the debtor corporation normalized future period economic income by the selected market-derived direct capitalization rate, to conclude a direct capitalization method value indication
26. Calculate an income approach estimate of the debtor corporation business enterprise value (i.e., invested capital value) that includes:
 - a. Value of all interest-bearing debt, plus
 - b. Value of total stockholders’ equity
27. Perform a market approach valuation analysis—such as the guideline publicly traded company method
28. Identify guideline publicly traded companies, consider:
 - a. Same or similar line of business
 - b. Size
 - c. Trading activity/pricing evidence
 - d. Financial condition
29. Adjust the financial statements of the selected guideline publicly traded companies, if applicable
30. Identify appropriate financial and operating fundamentals
31. Calculate market-derived valuation pricing multiples for the selected guideline publicly traded companies
32. Analyze the range of guideline company market-derived valuation pricing multiples
33. Compute and analyze financial ratios and operating ratios for the selected guideline publicly traded companies, including:
 - a. Size ratios
 - b. Growth ratios
 - c. Liquidity ratios
 - d. Profitability ratios
 - e. Return on investment ratios
 - f. Turnover/activity ratios
 - g. Leverage ratios

34. Compare the debtor corporation to the selected guideline publicly traded companies
35. Select the appropriate market-derived valuation pricing multiples for the subject debtor corporation
36. Apply the selected valuation pricing multiples to the appropriate subject debtor corporation financial and operational fundamentals
37. Perform a market approach valuation analysis—such as the guideline merged and acquired company method
38. Identify and select guideline merged and acquired company transactions
39. Identify the merged and acquired company financial and operational ratios
40. Calculate market-derived valuation pricing multiples for the selected merged and acquired companies
41. Analyze the range of market-derived guideline transaction valuation pricing multiples
42. Calculate financial and operational ratios for the selected guideline transactions, including growth rates, profit margins, and return on investment ratios
43. Compare the debtor corporation to the selected guideline transactions
44. Select the appropriate market-derived valuation pricing multiples for the subject debtor corporation
45. Apply the selected valuation pricing multiples to the appropriate subject corporation financial and operational fundamentals
46. Synthesize a market approach estimate of the debtor corporation business enterprise value (i.e., invested capital value) that includes:
 - a. Value of all interest-bearing debt, plus
 - b. Value of total stockholders' equity
47. Ensure that all debtor corporation invested capital value indications are presented on the same level of value
 - a. Consider that, typically, a marketable, controlling ownership interest level of value is appropriate for a solvency analysis
 - b. Apply all appropriate systematic valuation adjustments (i.e., discounts and premiums) to each value indication in order to conclude a consistent level of value
48. Consider any appropriate nonsystematic (i.e., company-specific) valuation adjustments appropriate to the debtor corporation invested capital value indication
 - a. Consider such nonsystematic valuation adjustments as key person dependence, key supplier dependence, key customer dependence, etc.
 - b. Apply any appropriate nonsystematic valuation adjustments either (1) within each individual valuation method analysis or (2) as an overall adjustment to an overall synthesized value indication
49. Prepare a synthesis of all applicable value indications from all application valuation approaches and methods
 - a. Determine the relevance of each valuation approach and method used in the balance sheet test
 - b. Conclude the appropriate fair value of the debtor corporation business enterprise (i.e., invested capital)
50. Estimate the aggregate fair value of the debtor corporation total operating assets, by:
 - a. Adding the recorded value of the debtor corporation current liabilities to the fair value of the business enterprise (i.e., invested capital) to estimate the fair value of debtor corporation total liabilities and total stockholders' equity
 - b. Calculating the "stepped up" asset value adjustment, using the following equation:
 - i. fair value of total liabilities and total stockholders' equity
 - ii. minus: accounting book value of the total operating assets
 - iii. plus/minus: any other accounting adjustments (if applicable)
 - iv. equals: aggregate fair value of the debtor corporation total operating assets
51. Compare the aggregate fair value of the debtor corporation total operating assets to the recorded value of the debtor corporation total liabilities in order to evaluate the positive or negative balance of the debtor corporation total net assets
52. Determine whether the aggregate fair value of the debtor corporation total operating assets exceeds the recorded balance of its debtor corporation total liabilities

53. Determine if the debtor corporation “passes” the balance sheet test
54. Perform the capital adequacy test
55. Review the cash flow/debt repayment analysis performed in the cash flow test to determine whether the debtor corporation has adequate capital to meet its short-term:
 - a. Operating expenses
 - b. Capital expenditure requirements
 - c. Debt service interest obligations
 - d. Debt service principal obligations
56. Review the sensitivity analysis scenarios of the cash flow/debt repayment analysis to determine whether the debtor corporation has adequate capital to meet its short-term:
 - a. Operating expense requirements
 - b. Capital expenditure requirements
 - c. Debt service interest obligations
 - d. Debt service principal obligations
57. Determine if the debtor corporation has adequate capital to run its business under a range of financial circumstances and economic conditions
58. Review each valuation approach and method performed for the balance sheet test to determine if the debtor corporation has an unreasonably small amount of capital to allow the debtor corporation to meet its operating needs in the short term
59. Review and consider the level, nature, and sources of funds for expected capital reinvestment
60. Determine if, in the short-term, the debtor corporation can:
 - a. Pay its current liabilities and the current portion of its long-term liabilities
 - b. Pay its payroll, research and development, and other operating expenses
 - c. Make required capital expenditure investments
61. Determine whether or not the debtor corporation “passes” the capital adequacy test

G. Reporting the Results of the Solvency Analysis

1. Prepare a leveraged corporate transaction solvency opinion, as requested
2. State the purpose and objective of the solvency opinion
3. State the effective date of the solvency opinion
4. Define the standard of value and the premise of value used in the solvency analysis
5. Describe the proposed leveraged corporate transaction
6. Describe each of the solvency analysis methods employed
7. Describe the financial, operational, economic, and industry information considered
8. Define any limiting conditions that affect the solvency analysis and/or the solvency conclusion
9. Include a summary of the professional qualifications of the principal analyst(s) performing the solvency analysis
10. Opine on the solvency of the debtor corporation immediately after, and giving effect to, the consummation of the proposed leveraged corporate transaction

H. Documentation of the Solvency Analysis

1. Prepare and maintain engagement workpapers
2. Include a copy of the signed engagement letter/statement of work
3. Document the due diligence procedures performed in the solvency analysis
4. Document the information considered in the solvency analysis
5. Document the analytical models created in the solvency analysis
6. Document the reasoning that supports the solvency conclusions reached
7. Include in the engagement workpapers sufficient analytical detail so that the subject solvency analysis can be replicated at a later date, if necessary
8. Include a copy of the final, signed solvency opinion in the engagement workpapers