Word to the Wise: Business Valuation Basics

What's your company worth? This is a question business owners love to ponder — and many have a dollar figure in mind. But before banking on that number, remember that an objective, professional appraisal will likely differ from your estimate. For those considering a valuation, here's a look at the process.

What's Involved?

A professional business valuation determines the value of an enterprise — either the entire business or an interest in it — at a particular point in time. To arrive at a value, business valuation professionals look at every aspect of the business: its competition in the manufacturing and distribution arena, performance, management and, most importantly, its operational results.

They consider what distinguishes the business from other manufacturers and distributors: cash flow, customer base, technology, market strength and growth potential, among other elements. They also rely on a number of research tools and databases to compare one company's value to another.

As members of the AICPA, CPAs must follow specific standards to ensure the consistency and quality of valuation services. The AICPA recognizes two types of engagements relative to value: a full valuation engagement or a less involved calculation engagement.

For a valuation engagement, the AICPA standards permit two types of written reports — summary and detailed. A calculation engagement results in a calculation report summarizing the calculated value. For all engagements, oral reports are permitted and are sometimes preferable, especially in cases involving litigation.

Why and When?

Most owners consider a valuation when it's time to sell the company. But there are many other reasons for a valuation, including divorce litigation, bankruptcy, retirement and estate planning, calculation of damages, succession planning, the addition of new partners, buy-sell agreements and financing applications.

Different circumstances require different standards of value. Fair market value is the most common standard and is used in virtually all federal and state tax matters. It is defined by the AICPA as the "price, expressed in cash equivalents, at which property or business would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, where neither is under compulsion to buy or sell, and when both have reasonable knowledge of the relevant facts."

Knowing the value of your business can be enlightening. But being aware of the specific factors driving that value may be even more important because it allows you to make strategic decisions about how to better manage the company moving forward.

It's critical to work with a business valuation professional who is experienced and certified in the field — especially if his or her valuation report will be scrutinized in tax or divorce court.

Who's Qualified?

Note that while many accounting firms offer business valuation services, not all CPAs are certified in business valuation. Several organizations offer credentials in business valuation, including the American Institute of Certified Public Accountants (AICPA), the American Society of Appraisers (ASA), the National Association of Certified Valuation Analysts (NACVA) and the Institute of Business Appraisers (IBA).

It's critical to work with a business valuation professional who is experienced and certified in the field — especially if his or her valuation report will be scrutinized in tax or divorce court. Consult with your CPA for advice on choosing the right valuation professional for your situation

We hope you find this information valuable. As always, we are here to help. Please contact John Oeltjen at 314.862.2070 to discuss your sustainability initiatives.

John E. Oeltjen, CPA
Shareholder | Director of Manufacturing & Distribution Services
joeltjen@muellerprost.com
314.862.2070

Click here to view previous articles and hot topics

Looking for more on business valuation?

Check out ThrottleNet TV's two-part interview with Mueller Prost shareholder and Director of Consulting, Adam Herman, CPA/ABV/CFF, CVA, ASA,CFE.

http://www.youtube.com/playlist?list=PLYec6MnBnupMxTtM0XgSxR5pzovQVc7YD