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Word to the Wise

Valuation 101: What You Need to Know

It's normal to muse upon the value of your business. How much is it *really* worth?

Unfortunately, many manufacturing and distribution business owners think their companies are worth more than they really are. Your business means everything to you, but if you sell it, a potential buyer sees it only as a transaction.

When you ask yourself, "What's my company worth?" the answer is, "It depends."

What Buyers Seek

Plain and simple, buyers are looking for return. They're looking for future cash flow and earnings. But they may also be seeking synergy with their other holdings, a new market presence, a better handle on supply chain and distribution, or other benefits.

Buyers don't like risk. And though all purchases have some risks, generally speaking, the lower the risk the higher the price a buyer will pay.

While you know your company well, it's the hard numbers that will help buyers determine the potential return on their investment.

Valuation vs. Calculation

The only way to truly determine value is to engage a credentialed analyst for either a full valuation or more limited engagement called a calculation of value.

By definition, the outcomes of a valuation and a calculation are different—and a calculation can be considerably less expensive.

According to the American Institute of Certified Public Accountants (AICPA), a "valuation engagement requires more procedures than does the calculation engagement. The valuation engagement results in a conclusion of value. The calculation engagement results in a calculated value."

Further, in a valuation engagement, "the valuation analyst estimates the value of a subject interest and is free to apply the valuation and methods he or she deems appropriate in the circumstances."

Regarding a calculation engagement, the "analyst and the client agree on the valuation methods and approaches the valuation analyst will use and the extent of the procedures the valuation analysts will perform ..."

While a full valuation is generally required for court cases and tax filings, a calculation is useful for owners in other circumstances.

For example, a calculation is helpful if you are considering retirement or sale and want an estimate of what the company might bring in terms of value. A calculation can also be useful if you want to vet an unsolicited offer for the company or for periodic reviews of buy-sell agreements (see page 4).

A Starting Point

If you are interested in a valuation, contact your CPA to discuss which type of service best suits your circumstances. Your CPA will discuss with you the scope of the engagement—what is required in terms of documentation and input from you, and how the valuation analyst uses that information. He or she will also discuss schedule and timing.

Regardless if a sale is imminent, a valuation or a calculation can be an excellent point of reference for owners looking to build value. The information in the analyst’s report will help you identify risks and position your company for the future.



Our valuation team has worked with many manufacturers and distributors. Call us today to start a conversation.



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