

Do you know what your business is worth?

Most business owners will agree that the most valuable asset they own is their business. When asked what their business is worth, most business owners are not able to provide an answer, or their figures are considerably off the mark. There are two ways business owners might address this question:

- Look at the book value (*book value* is an accounting concept that usually will significantly underestimate the value of an ongoing business);
- Quote a multiple of revenue which nearly always results in an overestimation of value.

Many business owners believe the need for a business valuation only arises before or during certain qualifying events, such as when gifting ownership interests to children or grandchildren, upon death (for estate tax purposes) or divorce, or when buying or selling a business. This viewpoint can be very short-sighted. By consulting with a valuation analyst regarding the factors that determine the value of your business in advance, you can focus on those particular value drivers that may increase your company's profitability (and value).

Communication is key to this process. It is imperative that the valuation analyst spend time with you, studying your business in order to gain an understanding of the business. Conversely, you need to spend time with the analyst in order to understand the valuation process specific to your business.

Business Valuation defined

How do you determine the value of a thousand shares in your family-owned, privately-held business? If you owned one thousand shares of Microsoft stock, you could look up the stock price listing in a newspaper, go online to a financial website, or call your broker for the price per share. Simply multiply that price by one thousand and you have the value of your ownership interest.

But the stock price of your business cannot be located in any financial table or by calling any broker. That's where business valuation analysts come into the picture - they utilize the information found in the public markets and apply it to a privately-owned business in order to determine its value.

Business valuation is a forward-looking concept. In simplified terms, the value of an ongoing business is dependent upon:

- The amount of cash flow a business generates today;
- The amount of cash flow a business is expected to generate in the future;
- The rate of return a buyer would require for an investment in your business.

In order to determine the value of a business, the valuation analyst looks at these factors in the context of economic and market conditions.

Be wary of multiples to "estimate" value

Business owners often ask, "Last year my competitor sold his business for four times earnings, why can't I sell my business for the same multiple?" It would be highly unlikely that the multiple used last year would be relevant to your business this year without consideration of certain facts and circumstances. First, it would be purely coincidental, even if the

businesses were similar, that the financial operations, conditions, and future earnings would be identical, creating an identical multiple. Second, economic conditions which are in a constant state of flux, are a component used in the determination of any multiple and have an impact on value. For example, if the prevailing interest rates are higher now than they were last year, this would have a negative impact on the value of the business. Conversely, if interest rates are lower, the value of the business may be higher. So any multiple applied to the earnings of your business (or any other valuation method for that matter) has to be developed specifically for your business and as of a specific valuation date.

When to consider a Business Valuation

The business valuation process can you in addressing critical business and succession planning issues with family members, co-owners, or key employees. It can provide for the life of the business beyond its current owners, and through proper planning eliminate the need for costly litigation. A qualified valuation analyst can explain the valuation process as it specifically relates to your business and will ultimately be able to answer your most pressing question: "What is my business worth?"



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