



## THE VALUE OF A BUSINESS VALUATION

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Today's business owners and professionals have come to realize that businesses have values in excess of their tangible assets. However, one of the most common mistakes is they assume there can only be one "value" for a given business.

It is logical for a business owner to think of value in two ways. The first way is to identify what is acceptable, by whatever criteria and parameters they choose. This will result in an "intrinsic value." The second is to identify what potential buyers are willing to pay, or the "market value." In the same respect, a potential buyer will have the same two ways of valuing the business. It is these factors, in conjunction with ever changing economy, supply and demand, industry trends, etc. that prevent a standard formula that will produce a reliable conclusion about the value of any particular business or practice at any given time.

For many situations, as is the case in valuations for virtually all federal and state tax issues, the mandated standard of value is "fair market value." However, in other cases it could be a function of the wishes of the parties involved. For example, the "investment value" to a particular investor could vary greatly from that of another investor due to differences in perception of risk factors, estimates of future earnings, tax status, synergies with other operations, etc. Other standards of value include, but are not limited to, book value, replacement value, or liquidation value. It is the duty of the valuator to distinguish between the various standards of value and determine which to apply to the given engagement.

Franklin Pierce Adams once said, "There are plenty of good five-cent cigars in the country. The trouble is they cost a quarter. What this country needs is a good five-cent nickel." With factors changing almost by the minute, it is a must to know what is being valued, why it is being valued and when it is being valued. With any one of these overlooked, a "five-cent cigar" could easily be valued at a quarter.

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Of course any value can be stated, however, it is not valid until the other party involved accepts it. The true value of having a valuation report is being able to withstand the challenge of another. In a buy/sell environment, it has to be accepted by the other party. In an estate or gift tax setting, it is the IRS that must be satisfied. In other cases, such as partner disputes or divorces, it could be the judge or jury. In any case, having a valuation report issued by a certified valuator tremendously strengthens the defense of an assigned value.

A business valuation is much more than assigning a dollar value to a business. It's the application of standards, formulas and judgment that comes from training and experience to arrive at an accurate and defensible assessment of value. The process of establishing the worth of a business requires a multidisciplinary examination of the business, including pertinent financial, tax, economic and industry data. A defensible valuation report includes why a business is worth a particular amount and can be explained and justified to an owner, a judge or jury, a banker, an IRS agent, a purchaser and others who rely on the valuation.

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