Valuing Your Business

As a business owner considers placing his or her company on the market, ascertaining the proper value for the company is critical. Too often the owner assigns an unrealistic and unachievable arbitrary value then proceeds into the sale process only to be disappointed with the market's response. As a result, the asking price is reduced several times. During this unfortunate period buyer prospects and valuable time is lost. A company's value is determined by a compilation of factors such as the company's sales, earnings, performance, market outlook, personnel, net book value, and fair market replacement value of equivalent operating assets. But it can also be influenced by intangible assets like the company's image, reputation and goodwill.

To maximize the fair market value of your business, it's vital that you capitalize on those intangible assets.

- **Develop key employees**. Buyers generally aren't interested in paying a premium if the business relies on you for its success. Remember to delegate responsibility to key employees and involve your key staff members in the decision making process. Demonstrating that your company's success is reliant on your capable, well-trained employees – not just you – will pay off at the time of sale.
- **Document what you do**. Be sure that job descriptions, operation processes, and strategic plans are documented. Documented records and plans give a buyer greater comfort that

he or she will be able to emulate your successful growth and will help your buyer obtain financing. Also, be sure to keep business records like sales and expense reports, internal profit and loss statements/balance sheet, and tax returns clean and well-organized.

- **Build relationships**. Name recognition, customer awareness and your reputation are all part of your business value. Even if your company doesn't have many hard assets, your relationships are key. Consider diversifying both supplier and customer accounts.
- **Improve cash flows**. A potential buyer wants to see the "true cash flow." And, of course, in the business world cash is king. Be sure you are driving all income to the bottom line.
- **Review your assets**. Sell off or dispose of unproductive assets or unsalable inventory. Remove or buy off any assets that are primarily for your personal use.
- **Find and build your niche**. You don't have to be everything to everyone. Buyers will pay a premium for a niche that has barriers to competitive entry.
- **Remodel, clean, and organize**. What's the first thing anyone does when they put their home on the market? They spruce things up and make sure everything is in its right place. Yet, in business, that's rarely considered. A well-maintained facility will get the best price. Even businesses that lease space can benefit from a thorough cleaning and organization to convey a feeling of quality and efficiency.

There are several approaches to valuing your business.

BALANCE SHEET VALUE

There are several balance sheet valuation methods, including adjusted book value, book value and liquidation value. The adjusted book value is determined by revising the asset's book value to reflect the cost it would take to replace the assets in their current condition. This method requires the total values to be offset against the sum of the liabilities. The book value considers the figures from the company's financial records, as depreciated at the time of the sale. The book value can pose some difficulties for sellers, particularly if the seller has depreciated the assets too much to gain prior tax advantages. The liquidation value is the amount that could be realized if all assets – equipment, furnishings and inventory – were sold separately. This value is typically much lower since it doesn't consider a company's intrinsic value.

INCOME APPROACH

The income approach takes into consideration the company's level of earnings using a capitalization rate, discount rate or multiplier. Several income approach methods are frequently used. Each method requires a level of earnings and a conversion factor to translate the earnings into a company value. Selecting the proper level of earnings – after-tax, pretax, discretionary or cash flow – and matching it with the proper conversion factor – discount rate, cap rate or a multiplier – is critical to calculating a reasonable value.

MARKET APPROACH

The market approach sets a value based on the values of other businesses that have been sold. Setting the market value involves researching the sale prices for similar businesses in a geographic area. In some cases, however, finding a company that is similar in many ways to your company may be difficult. Whatever your goal, I can help you value your company. Don't be impressed by the person who presents the highest value – you may only be setting yourself up for failure during the sale process.