

Business Valuations Are Not Commodities



When hiring a business appraiser, you typically get what you pay for. Some business owners may be tempted to seek the offering with the lowest price tag. After all, a business valuation is just a formality, isn't it? Many owners perceive formal appraisals as something required by an outside party -- such as the IRS, a judge or a lender -- in order to obtain approval or comply with a regulatory requirement. But a valuation actually provides insight into a company's current market value, as well as key value drivers to enhance value going forward. A valuation can also serve as a wake-up call for business owners with unrealistic expectations.

Privately-held business owners might need appraisals of their interests for many reasons, including:

- Strategic planning
- Equitable distributions of marital estates
- Bankruptcy
- Gifts and estate planning
- Mergers, acquisitions & shareholder buy-ins (or buy-outs)
- Minority shareholder disputes
- Small business loans

Varying Degrees of Expertise

Many people provide business valuation services, but their qualifications vary significantly. At one end of the spectrum is a valuation professional who has achieved the training, experience and continuing education requirements of one of the following business valuation organizations:

- The American Institute of Certified Public Accountants (AICPA);
- The American Society of Appraisers (ASA);
- The Canadian Institute of Chartered Business Valuators (CICVA);
- The National Association of Certified Valuation Analysts (NACVA); and
- The Institute of Business Appraisers (IBA).

On the other end of the spectrum are online business valuation calculators and fill-in-the-blank software, which are typically based on oversimplified formulas or industry rules of thumb. Computerized models aren't a substitute for an appraiser's professional judgment and training. In short, you get what you pay for.

Is a Calculation a Viable Alternative?

To save time and money, many clients ask for calculation letters instead of full written appraisal reports. Calculations are usually only one or two pages long, and they're only appropriate in limited circumstances.

Calculations may be appropriate, for example, when using a valuation solely for internal purposes or when deciding whether it's financially feasible to pursue litigation. Most appraisers wouldn't recommend a calculation for tax or litigation purposes, however.

By comparison, full written appraisals generally average about 50 pages in length. This level of detail enables outsiders to understand the analyses and replicate the arithmetic underlying a valuator's conclusion.

Sometimes calculations limit the scope of the work an appraiser performs. If so, a valuator's conclusion could change materially if a calculation engagement evolves into a full scope appraisal.

Appraisals Guide Major Decisions

In the words of NASA astronaut Alan Shepard, "I wasn't scared, but I was up there looking around, and suddenly I realized I was sitting on top of a rocket built by the lowest bidder." Shepard got lucky and returned from the moon to tell his tale. But are you willing to bank on the work of an amateur appraiser or computer model? An inexpensive provider may actually cost more over the long-run by skipping steps, overlooking unrecorded asset and liabilities, and failing to support conclusions with real-world evidence.

For most entrepreneurs, their business interests are their most valuable asset. Many important decisions -- such as selling the business, obtaining a loan or splitting up a marital asset -- hinge on business appraisals. If your appraisal is inaccurate, you could lose money or be sued or audited by stakeholders.

For example, if the IRS challenges a valuation prepared for gift and estate taxes, you're more likely to withstand scrutiny with a qualified appraiser. The IRS defines a qualified appraiser as:

An individual who has earned an appraisal designation from a professional appraiser organization, or has met minimum education and experience requirements in the subject matter in which he or she issues appraisals. A qualified appraiser performs appraisals on a regular basis, and receives compensation for his or her work. The professional must not be prohibited from practicing before the IRS.

Obviously, a qualified appraiser isn't someone who bases his or her conclusion on limited information submitted over the internet. It's someone who's dedicated significant time and attention to mastering the business valuation discipline.

Know What You're Buying

You might be thinking, "No one outside the company will ever see this appraisal. Why do I need to use a qualified appraiser?" While valuations prepared for litigation or tax purposes run the risk of outside scrutiny, reliable valuation conclusions are equally important for internal planning purposes. Inaccurate valuations can lead to poor investment decisions.

But hiring a valuator isn't as familiar and straightforward as buying, say, a car. How do you know whether a valuation "professional" is a shiny new Cadillac or a stripped-down jalopy? When evaluating business valuation candidates, price is one indicator of quality, but professional credentials are far more relevant. Investigate the business valuation organizations to which prospective valuers belong. Each organization has its own training, experience, ethics and standards, and continuing education requirements.

Also inquire about your valuator's standard operating procedures, data requests and expected timeline. Comprehensive valuations take weeks (or months) to complete. It takes time to learn how the company operates, conduct site visits, interview management, analyze the data and write a full report.

Likewise, take your time when selecting a valuation expert. Never jump at the first valuation provider you encounter online. Discuss the decision with your trusted financial and legal advisers first.

Gryphon Valuation Consultants is a full-service professional business appraisal firm offering a broad range of valuation and litigation consulting services. If we can serve your valuation needs, or if you have a question about our services, please contact us at 702-870-8258 or visit us on the web at www.BizVals.com. Gryphon is an independent member of the [American Business Appraisers National Network](#).