

Building a Defensible Business Valuation

You have decided to have your business valued. What documents and information should you expect to share with the appraiser for them to prepare a defensible business valuation?

Your Privacy

You or your client have a closely held business where information is typically kept private and shared on a must-know basis only. As CPAs and members of the American Institute of Certified Public Accountants (AICPA), we adhere to the AICPA's Code of Professional Conduct that includes a Confidential Client Information Rule. We cannot disclose any confidential client information without your specific consent in writing. In addition, we maintain a highly secure portal for the easy sharing of all information.

What Information Will be Requested? Why?

The information request will be tailored to your specific situation, reflecting your business and the purpose of the business appraisal. For valuations for tax related or other regulatory purposes, the Internal Revenue Service has issued detailed guidance regarding the approach, methods and factors to be considered in valuing interests of your business (Revenue Ruling 59-60).

The type of information requested falls into several categories:

- **Financial documents** – both historical financial information as well as projections in some cases.
- **Ownership information** – who owns the company? Are the owners the operators? What is the owner/operator's compensation?
- **Management information** – who manages the company? Is the owner supported by key management that are employees (non-owners)? What are the responsibilities of key executive/officers and managers? Are non-compete agreements in place?
- **Governance documentation** – is there an operating/shareholder/buy-sell agreement or other agreement between owners? Do the agreement(s) in place dictate restrictions on transfers of ownership that would impact the valuation conclusion? What is the legal and tax structure of the company? Is there more than one class of stock? Are shares or units designated as voting and non-voting? Who holds what?

The tables that follow provide insight regarding some the documents commonly requested and how they are used by the business appraiser.

Sample Financial Information Requests	
Information Requested	How It's Used
Tax returns, financial statements – last 5 years and interim periods, if applicable	Often, history is a predictor of the future. We analyze a historical period long enough to observe the business' ebbs and flows. This helps us to determine sustainable cash flow.
Financial projections	If a company is a start-up, in a growth stage, or in decline, historical financial performance may not be available or relevant. We work with the owners to develop reasonable projections, and possibly multiple scenarios of outcomes used to value the company.
Accounts receivable and payable agings as of the Valuation Date	We assess operating and liquidity risks, which impact the valuation. We compare receivable and payable turns to the company's peers and assess relative effectiveness.
Schedule of sales to top 10 customers – last 2 years	This allows us to assess customer concentration risk, customer turnover, level of annuity business – all of which impact the valuation. This information impacts the risk factor used to value the company.
Schedule of purchases from the top ten suppliers – last 2 years	This allows us to assess vendor concentration risk, which impacts the risk factor used to value the company.
Loan agreements including owner and other related party loans	We analyze a company's leverage and assess its risk, which impacts the valuation conclusion. We also look to related party loans/terms and loans from the owner to assess whether these meet the definition of a loan or equity.
Lease for office(s)/facility(ies)	We identify if the leases are with related-party entities and where possible work to assess market rent vs. the expenses recorded by the operating company. This impacts cash flow and the valuation conclusion.
Compensation to owners/family members	We assess market compensation paid to the owner/operators and other family members, which impacts cash flow and the valuation conclusion.

Other Information Requests	
Information Requested	How It's Used
Schedule of shareholders and their holdings	We document ownership using articles of incorporation, operating/shareholder and other owner agreements. The characteristics of the ownership (controlling, non-controlling, voting, non-voting) impacts the valuation conclusion.
Governance	We look to the governance documents to identify restrictions on the transfer of ownership interests and determine how it impacts the valuation.
Schedule of key management	We analyze the key management structure including the owners and employees. We determine the relative responsibilities of the owners and key employees. In addition to assessing market compensation to the owners, we assess the risks pertaining to a key person. Does the majority owner control the key customer relationships? Is there thin management outside the majority owner? Do key employees have employment agreements with non-compete clauses? Can a buyer successfully operate the business?
Prior transactions	We'll request recent letters of intent and/or terms of recent transactions pertaining to the equity of the business. These are possibly strong indicators of value depending on the date of the transaction and changes since.
Goodwill/intellectual property	Are there royalty/franchise agreements in place? Is goodwill recorded from prior transactions? We will analyze cash flows and assess the related market value.

The Final Step

The requested information is provided... then what?

At JBVAL, once we receive and analyze the requested information, we reach out to schedule a due diligence interview with you. Since we are well prepared, our due diligence interview typically lasts an hour or two. If in person, there may be a facility tour. If by video conference, this tour may be virtual. After the interview, our valuation professional will be ready to complete your valuation. We issue a draft report to you and your professional advisors to review for factual accuracy. The report will be completed in no more than 20 to 25 working days from when we receive the information.