

# *Burkert Valuation Advisors, LLC*

VALUATION AND LITIGATION CONSULTANTS

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## **Spotlight on Value: There Are Many Ways to Define Value**

*by Rod P. Burkert, CPA/ABV, CVA*

Depending on the purpose of the valuation, or the context within a valuation, one definition of “value” may be more appropriate than another. The standard of value (as we say in the industry) answers the following general but very basic questions: “Value to whom?”; “Valued how?”; and “Under what circumstances?”

The question of “**Value to whom?**” can be defined by four different standards.

**1. Fair market value** - The price a hypothetical willing buyer would pay to a hypothetical willing seller with neither party under compulsion to transact and both parties having reasonable knowledge of the relevant facts. This standard of value is universally used in all income-, gift-, and estate-tax purpose valuations.

**2. Fair value** - The price that fairly compensates an owner who was involuntarily deprived of the benefit of his/her ownership interest where there is neither a willing buyer nor a willing seller. This is a state specific, statutory standard used in cases involving dissenting stockholder and other types of shareholder litigation.

**3. Investment value** - The price that an identified buyer (or class of buyers) would be expected to pay with consideration given to any unique benefits or synergies that the buyer is purchasing. This value is most appropriate in business purchase/sale transactions where the buyers and sellers are likely to know each other and, in fact, may be cooperating through the due diligence process.

**4. Intrinsic value** – Is an analytical judgment of value based on the perceived characteristics in an investment, without regard to the identity or characteristics of a particular investor. It represents the “true” or “real” value of an asset. Security analysts compare the intrinsic value of a stock with its current trading price to assess buying and selling opportunities.

The notion of “**Valued how?**” is primarily a function of the approach used to value a business and the methods thereunder that are appropriate for the business being valued.

**5. Book value** – An accounting term that represents the “accounting value” of assets minus liabilities at the balance sheet date. Because balance sheets are normally prepared in accordance with generally accepted accounting principles (GAAP), the book value of a company does not consider the fair market value of its underlying net assets nor its economic earnings capacity.

**6. Adjusted book value** – Is an indication of value developed by adjusting the reported book values of a company’s assets and liabilities to their actual or estimated fair market value. The “assets” referred to in this definition are tangible assets, such as accounts receivable, inventory, and fixed assets, and occasionally, identifiable intangible assets such as non-compete agreements or patents; unidentifiable intangible assets, such as goodwill, are generally not considered. However, any off-balance sheet and/or contingent assets and liabilities would be included at their actual or estimated fair market values.

**7. Asset accumulation value** – Takes adjusted book value and adds the value of all the other intangible assets such as going concern value (e.g., the company name, its in-place work force, and its customer list) and goodwill. These intangible assets can be valued by using any combination of the cost, income, or market approaches to valuation. Business appraisers have classified and valued over 100 different kinds of intangibles.

**8. Business enterprise value** (aka invested capital value) – Is the value of 100% of the equity plus the market value of interest-bearing debt. This value is normally derived when a weighted average cost of capital is applied to cash flows of debt and equity holders or when guideline company price-to-revenue, price-to-EBIT, or price-to-EBITDA multiples are applied to similar metrics of the subject company.

**9. Equity value** – Is the value of all tangible and intangible assets of an enterprise, less its liabilities; it represents the stockholders’ claim on the net assets of the company. This value is normally derived when an equity cost of capital is applied to cash flows of stockholders or when guideline company price-to-book or price-to-earnings multiples are applied to similar measures of the subject company.

Finally, “**Under what circumstances?**” can be thought of as the assumption about what is going to happen to the business and the “level” of value of the business interest that is the subject of the report.

**10. Going concern value** – Assumes that the business was operating yesterday, is operating today, and will be operating tomorrow, and the value of that business is best determined by the earnings or cash flow it generates for the benefit of its investors.

**11. Liquidation value** – Assumes that the business is worth more broken up, its assets sold in an orderly or forced manner. If the holder of the appraised interest can force such an action to occur, the liquidation value of assets less liabilities could be an appropriate measure of value. Depending on the existence and value of goodwill this may, in fact, be the case.

**12. Control value** – Is the additional value inherent in a greater than 50% interest, reflecting the power of a shareholder over the business. Different levels of control value are possible depending on the rights and/or restrictions that are associated with a particular sized block of stock under state law, e.g., simple vs. supervoting majority.

**13. *Lack of control value*** – Generally refers to the value of a two 50/50 interests or the value of any non-voting interest, e.g., non-voting stock or limited partnership interests.

**14. *Minority value*** – The value reflecting an ownership position of less than 50% and the associated inability to make decisions that affect corporate policy. Different levels of minority value are possible, e.g., a minority interest that is the largest equity interest due to fractionalization of ownership and a minority interest with swing vote attributes.

**15. *Marketable value*** – Is the value of a debt or equity interest assuming an existing market where that debt or equity can be exchanged. Active public markets, such as listed exchanges, are examples where a debt or equity holder can receive a known amount of proceeds with minimal transaction costs and waiting time.

**16. *Private company value*** – Incorporates a discount from the marketable value owing to the lack of a ready market of buyers and sellers for closely-held stock.

There you have it – 16 different ways to define value. Yes, as in other things, value is in the eye of the beholder. The important thing to remember? At a given point in time businesses (and business interests) can, do, and always will have different values for different purposes. Thus, the standard of value must be matched to the purpose of the valuation in order for a reasonable conclusion of value to be reached.

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Rod is a co-founder of Burkert Valuation Advisors, LLC. With over 25 years of combined experience in public accounting and private industry, he has provided business appraisal and litigation consulting services for companies operating in a wide variety of industries and for various purposes. He is also an instructor for the National Association of Certified Valuation Analysts and a past chairman of its Executive Advisory Board and its Education Board.

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