Legacy by Design, LLC

Valuing Closely Held Businesses

Succession Planning

Farmers, Ranchers, & Family Business Owners

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Legacy by Design, LLC
Succession Planning for Agribusiness Owners

VALUING CLOSELY HELD BUSINESSES

Ownership succession is a major component of any business succession plan. Depending on the designated successor, ownership may be transferred by gift, sale, or redemption of the retiring owner's interest. Regardless of the method of transferring the ownership, an accurate valuation of the interest transferred helps ensure the transfer price reflects fair market value and minimizes the risk that valuation penalties will be imposed. Failure to obtain a fair market valuation for a closely held business may result in substantial penalties to the taxpayer, the preparer, and even the appraiser.

In addition to planning an ownership transfer, the closely held business owner may require an estimate of the businesses' worth to help formulate retirement and estate plans, determine the need for life insurance, obtain financing, prepare a personal financial statement, or for prenuptial or divorce agreements.

There is no ready market for determining the value of a closely held business. As a result, a business valuation is required to determine the estimated value of an interest in a closely held business at a given point. This chapter covers the approaches and methods for valuing a closely held business.

UNDERSTANDING THE VALUATION PROCESS

The issue of a business valuation will naturally come up during the course of most business succession planning engagements. The value of the business is important to the successor as well as the owner. If the business is being sold to an unrelated party, the valuation will help determine the purchase price. If the successor is the existing owner's children or other related parties, the valuation helps substantiate the business's value for gift and estate tax purposes. A buy/sell agreement may also require a valuation of the business at the death or disability of an owner.

When Is Valuation Necessary?

Sale of a Business to a Related Party When the business is sold to a related party, a valuation may be necessary to substantiate that the business was sold for fair market value. In many instances, the most important reason to get an appraisal is the possibility that the IRS or another taxing authority might question the value in the future. Valuation is a very fertile area for IRS auditors and will frequently be questioned or challenged in audits involving the sale of a business to a related party.

The IRS carefully scrutinizes related party sales since there is potential for a disguised gift. If the business is sold at less than fair market value, the IRS will assert that the difference between the fair market value and the sales price is a gift to the related party, and assess gift taxes. In most instances, such assertions by the IRS are made several years after the actual sale, and the potential accrued penalties and interest on the gift tax can be significant. Even if there is no concern about the IRS challenging the value, there may be other situations that suggest the need for a valuation. For example, a valuation helps ensure that the sales price is fair if multiple related parties are involved (e.g., several children) and the sale of the business is a part of an overall plan to make equitable transfers to the parties. Likewise, if the owner is retiring and the main source of the retirement income will be proceeds from the sale of the business, a valuation helps the owner quantify his retirement income and ensure he gets a fair price.

One of the disadvantages of obtaining a valuation when a business is sold to a related party is cost. The cost of the valuation will vary depending on the type, size, and complexity of the business. The valuation consultant, the methods used, and the nature and extent of the valuation report can also affect the cost. Closely held business owners may object to the cost of a valuation because they feel they are capable of estimating the fair market value of their businesses themselves. In such situations, it is important to compare the estimated cost of the valuation with the risks associated with not having a valuation done. In many instances, business owners are more willing to spend the money to have the valuation done once they realize the potential for additional taxes, penalties, and interest that might be imposed later.

It is recommended that a business valuation be performed as close as possible to the date the business is transferred to the related party. A valuation performed at this time reduces the likelihood of later disputes and helps support the values shown on tax returns in case of an IRS challenge.

Sale of a Business to an Unrelated Party The business owner selling to an outside party will naturally want to receive the highest amount possible for the business. A business valuation can help accomplish this. With a business valuation, the owner is assured that he is getting a fair price. Additionally, the business valuation may be helpful in attracting potential buyers. Without an independent valuation, the buyer is more likely to suspect that the business is overvalued by the seller, making the sale more difficult. In today's environment, most prospective buyers will insist on a business valuation before the sale is accomplished.

Unfortunately, the cost of a business valuation may be duplicated if the valuation is done before identifying a buyer and the buyer wants an independent valuation from a different valuation consultant. The buyer may suspect the sales price favors the seller since the valuation has been paid for by the seller. He may even object to the valuation method used and prefer a different one. Whatever the reason, there is additional cost involved if the buyer insists on having another valuation prepared. In these cases, both valuations can be used in determining the ultimate sales price of the business.

Despite the potential duplication of costs, it is often preferable to have a business valuation done prior to identifying potential buyers. In addition to assisting the owner in establishing a fair price, it may reveal that the owner's opinion of the fair market value of his business is inflated. In these instances, the cost of a valuation is usually small in comparison to the costs that would have been incurred to find a buyer and enter into negotiations that ultimately fail.

Transfer as a Result of a Buy/Sell Agreement. Buy/sell agreements often specify when a valuation is needed. Therefore, these agreements should be reviewed thoroughly to determine what is required. Many buy/sell agreements contain provisions that are very specific regarding the valuation. There may be a defined valuation method or a combination of methods that must be used. Some agreements contain a mathematical formula that must be used in the valuation process. Reviewing the agreement and making sure the provisions are followed can save time and money. Significant problems can result if a sales price is derived from a valuation that does not conform to the buy/sell agreement.

Transfer by Gift Any time an interest in a business is gifted, a valuation of the interest may be necessary to substantiate the gift or estate tax value and help minimize the risk of change in value upon IRS audit. Generally, the IRS and the courts look more favorably on valuations performed at the time of the gift rather than at some point afterward (perhaps when the IRS is auditing the gift or estate tax return). Therefore, the valuation should be done as close as possible to the date of the gift.

Valuation for Estate Tax Purposes A valuation may also be necessary to determine the estate tax value of a business at the owner's death (or the alternative valuation date six months later). The cost of a business valuation is usually warranted because of the high estate tax rates and increased risk of an IRS audit. In addition, for closely held business interests, a valuation helps ensure that the reported value reflects all applicable discounts.

Valuation upon Transfer to an ESOP (Employee Stock Ownership Plan) There are special valuation requirements for stock transferred to and held by an ESOP.

Working with a Business Appraiser

An appraiser should be informed about the valuation's purpose, scope, and tax considerations to ensure that the appraiser has a solid starting point for valuing the business. A valuation purpose may be for a stock sale, a buy/sell agreement, a gift or estate tax transfer, or a stock transfer to an ESOP. The valuation's scope may be the entire business, an owner's interest only, or a portion of the owner's interests being transferred. Also, the practitioner should discuss tax considerations that effect the valuation. For example, whether an S corporation will pay a salary or return all cash as income distributions affects the owner's self-employment tax liability and thus, after-tax cash flow.

An understanding of valuation terms, approaches, and methods helps a practitioner review the valuation report's adequacy. For example, the valuation terms fair market value and investment value have different applications. Fair market value is based on an arms-length sale between any buyer and seller both being willing and knowledgeable. Fair market value is used in most valuations. However, investment value is based on a specific buyer's knowledge and abilities. Thus, investment value may apply when a buyer is identified or a sale is restricted to co-owners. Also, a closely held business valuation based on the income approach may be more reliable than a valuation based on the market approach. The market approach relies on multiples derived from data obtained on the sale of comparable companies. Often, data on business sales comparable to closely held companies is difficult to obtain. In addition, valuation approaches have different methods. For example, the income approach is based on the capitalized returns method (instead of the discounted future returns method) when future operations are expected to grow at a predicable rate.

Selecting a Valuation Expert

Obviously, the best method of selecting an appraiser is to use someone with whom the practitioner has successfully worked before. However, because this is not always possible, the practitioner may find the need to hire an appraiser with whom he has no prior experience. In that case, a practitioner should locate expert appraisers through professional directories and by seeking referrals from banks, other professionals in the business succession planning area, and dealers in the type of property needing to be appraised. Directories of appraisers can be searched free at the following organizations' websites:

- American Society of Appraisers (ASA), www.appraisers.org
- Institute of Business Appraisers (IBA), www.go-iba.org
- National Association of Certified Valuation Analysts (NACVA), www.nacva.com
- AICPA Management Consulting Services Division, www.aicpa.org

ASA ASA members earn the following professional designations:

- An Accredited Member (AM) has at least two years of full-time or full-time equivalent valuation experience (one year may be fulfilled by five or more years of experience as a CPA in public accounting or as a CFA or CBI) and a college degree (or equivalent experience). Full-time equivalent experience is based on the time spent on business valuation engagements. For example, if the consultant works on business valuation engagements 20% of the time, it will take 5 years to reach one year of full-time equivalent experience. In addition, the candidate must pass comprehensive oral and written exams and submit acceptable appraisal reports.

- An Accredited Senior Appraiser (ASA) has at least five years of full-time or full-time equivalent valuation experience (one year may be fulfilled by five or more years of experience as a CPA in public accounting or as a CFA or CBI) and has fulfilled the educational/examination/ appraisal report requirements.

- The designation of Fellow (FASA) is given an Accredited Senior Appraiser by ASA's International Board of Governors in recognition of outstanding service to the appraisal profession or the American Society of Appraisers.

Information about the ASA designations can be obtained at www.appraisers.org.

IBA The IBA awards the following professional designations:

- An Accredited by IBA (AIBA) member has a four-year college degree or equivalent, has completed an eight-day workshop training program in "Valuing Closely Held Businesses," passed a written examination, and submitted an acceptable demonstration appraisal report.

- A Certified Business Appraiser (CBA) has a four-year college degree or equivalent, completed 90 hours of additional coursework or 10,000 hours of active appraisal experience, passed a written examination, and submitted two acceptable demonstration appraisal reports.

- A Master Certified Business Appraiser (MCBA) has a four-year college degree and a two-year post-graduate degree or equivalent. Applicants for the MCBA must have held the CBA designation for at least ten years, and must have 15 years of full-time experience as a business appraiser.

- A Business Valuator Accredited for Litigation (BVAL) has either a business appraisal designation from the IBA, AICPA, ASA, or NACVA or is a CBA candidate who has passed the CBA exam. Applicants for BVAL provide two letters of recommendation from attorneys who have witnessed the applicant's trial performance, or completed 16 hours of education in areas of law in which the appraiser anticipates providing testimony. Applicants must also attend a five-day course, pass a written exam, and demonstrate competency during testimony clinics.

Information about IBA designations can be obtained at www.go-iba.org.

NACVA NACVA awards the following professional designations:

- **Certified Valuation Analyst (CVA)** Applicants must hold a valid CPA license, be a member of NACVA, complete a five-day course, and pass a lengthy two-part exam, including performing a business valuation for a case study.

- **Accredited Valuation Analyst (AVA)** Applicants must have a business degree or an MBA and business valuation experience, be a member of NACVA, complete a five-day course, and pass a lengthy two-part exam, including performing a business valuation for a case study.

  The AVA certification is also offered to government employees. Applicants must have a four-year college degree and the equivalent of two years of full-time business valuation experience. Applicants must be currently employed by a federal or state government agency and have at least a GS-12 or comparable rating. To receive certification, applicants must complete a five-day training program and pass a lengthy two-part exam, including performing a business valuation for a case study.

Additional information may be obtained at www.nacva.com.

AICPA The AICPA Council established an accreditation program for CPAs performing business valuation services. The program results in the Institute granting an Accredited in Business Valuation (ABV) designation. To qualify for the designation, a CPA must pass a written examination. In addition, a CPA must meet the following requirements to be eligible to take the examination:

- Be a member in good standing with the AICPA.
- Provide evidence of performing ten business valuation engagements to demonstrate substantial experience and competence.
- Provide evidence of 75 hours of learning related to the business valuation body of knowledge.

To maintain the ABV accreditation, a CPA must:

- Demonstrate substantial involvement in at least five new business valuation engagements every three years, and
- Complete 60 hours of related CPE during the same three-year period, of which only 20 hours may be in the form of writing articles and 36 hours may be in the form of lecturing.

Additional information is available at www.aicpa.org.

Before hiring an appraiser, the consultant should keep in mind several key considerations:

- **The Appraiser's Experience with the Type of Company Being Valued** Does the appraiser have any previous experience with the type of company or general industry being valued?
- **The Appraiser's Presentation Skills, Confidence, Credentials and Personal Demeanor** Because many valuations are decided in the courts, these qualities can be critical in determining a favorable outcome for the valuation.
- **Prior Successes in Valuations or Court Testimony**
- **The Appraiser's Independence** If the appraiser has the appearance of being pro-taxpayer, or if the appraiser has an affiliation with the accounting firm associated with the business being appraised, his credibility and objectivity could be questioned.
- **Personal Rapport** The CPA or other professional must be able to communicate and work with the valuation expert.
- **Adaptability** The appraisee should be able to adapt his methodology to the uniqueness of the assignment, instead of relying on a standardized approach.
- **Responsiveness and Timeliness** This quality is especially critical if the case develops into litigation where numerous deadlines must be met.

How to Evaluate a Valuation Report

A good valuation report should be well-written and well-organized and satisfy professional and engagement requirements. The old adage, "It's not what you say, but how you say it," can also apply to valuation reports. As discussed previously, many valuation controversies are decided by the courts. The appraisal report is often the only tangible evidence of how the value was determined. Thus, its appearance is often an influencing factor. If it appears sloppy or disorganized, the courts may take that into consideration and rule in favor of an appraisal that appears more professional.

A well-written report has several distinct qualities. Such a report is:

- **Thorough** It includes all relevant data and analyses that affected the conclusion of value.
- **Balanced** It discusses both positive and negative factors affecting the company's value. Although the client may have a vested interest in the value being relatively high or low, the consultant

should remain unbiased. Accordingly, the consultant's report should be an impartial discussion of all relevant factors.

- **Readable** All the report's readers should be able to follow the work done and the conclusion reached. That means the report should be written in clear and concise terms with minimal use of technical jargon. If technical jargon is necessary, it should be defined. Any data presented in the report should be adequately described so that others can understand it. Remember, most of the readers will not be financial analysts or accountants.

- **Coherent** The report should flow logically from the data presented to the final conclusion. Also, the report's conclusions and analyses should be internally consistent.

- **Well-supported** The authors believe that a report should thoroughly document each valuation process step and conclusion. That means presenting detailed calculations and identifying the data sources used so that another appraiser can follow the process steps and reach a similar valuation.

Common Errors in Valuation Reports

Sometimes more than one business valuation report is prepared. Typically this occurs when parties disagree on the appraiser, the valuation approach, or a valuation assumption. Differences among a decedent's heirs (or between a taxpayer and the IRS) may require a court to determine the value based on differing reports. In this case, courts often ignore a business valuation report with obvious deficiencies. Practitioners can add value to a valuation engagement by critically reviewing the business valuation report for errors. The following are common errors to watch for in evaluating a report.

Failure to Follow the Definition of Value Business valuation terms are used in most valuation reports or appraisals to inform the reader how the value of the business was determined. The stated definition of value in the report is important since the value can vary significantly depending on which definition of value is chosen. For example, the value of a business based on a quick liquidation will be much lower than the value of the same business based on continued operation. One of the most common errors found in valuation reports is the failure to follow the definition of value contained in the report. This can be a costly error and might cause the valuation to be ignored by the courts if challenged by the IRS. Thus, practitioners should carefully examine how value is defined in the report and ensure that it is reflected in the report.

Inconsistencies Practitioners must ensure that the data, analyses, calculations, and conclusions are consistent. Some common inconsistencies include:

- Applying value multiples to the wrong benefit stream (for example, applying after-tax earnings multiples to pre-tax earnings).

- Failure to match the capitalization or discount rates to the proper benefit stream (for example, using a net cash flow discount rate on earnings data).

- Comparing data on the company being valued to guideline data for a different time period without making appropriate adjustments.

- Adjusting financial statements for the company being valued without adjusting guideline companies' financial data.

- Inconsistent use of assumptions. For example, an appraiser cannot assume an orderly liquidation of assets for one purpose (e.g., application of an asset valuation method), and then assume "fire sale" liquidation of assets for another purpose (e.g., calculation of lack of marketability discount).

Arithmetic Errors Surprisingly, one of the easiest errors to prevent is one of the most common. The calculations in each report should be reviewed for accuracy.

Insufficient Support Inadequately documented reports are easier to second guess. Each report should document the data used, calculations made, and conclusions reached. Calculations should tie back to the subject company's financial statements and those of the guideline company's, where utilized.

Inadequate Evidence to Support Discounts Courts often disregard or dismiss discount calculations that do not relate market data to the company interest valued. Discounts for lack of control can be supported by data on minority interest transactions in publicly traded companies. The relevance of the data to the company being valued is usually obvious. However, most data on lack of marketability is based on trades of restricted stock or privately held stock before an initial public offering (IPO). The relevance of this information to valuing other types of companies is usually not convincing. Instead, the lack of marketability discount can be supported by a hypothetical buyer's time and risk assumptions about purchasing the interest. A purchaser makes assumptions about the cash return, the length of ownership, the subsequent cash out price, and the risks these assumptions are not valid. As a holding period increases, the uncertainty increases for the cash return and cash out price which supports a larger discount than if the holding period is short (e.g., an IPO is imminent). However, practitioners should be aware that the longer the assumed holding period, the greater the burden to support that assumption.

Overreliance on Rules of Thumb Rules of thumb are rarely good primary valuation methods. Accordingly, values indicated by rules of thumb used should not be weighted heavily in reaching the value conclusion, unless there is an adequate analysis of market data supporting those rules.

Inadequate Data Some valuation consultants cut corners either because of budget constraints or because of ignorance of available data sources. It is important for the practitioner to be satisfied that the valuation consultant has considered all the data that might significantly affect the valuation conclusion.

Failure to Consider Guideline Company Methods When valuing small, closely held companies, some consultants fail to consider using guideline company methods. Based on Rev. Rul. 59-60, data from comparable companies should always be considered. If a search for guideline companies is conducted, the sources used and the results of that search should be included in the report, even if no comparable companies are identified.

Inadequate Due Diligence The following are examples of inadequate due diligence in the preparation of a valuation report:

- Omitting a visit to the business premises.
- Inadequately interviewing management.
- Failing to consider requirements of state corporate law, articles of incorporation, and bylaws.
- Failing to report or inquire of recent and prospective stock transfers.

OVERVIEW OF VALUATION TERMS AND ASSUMPTIONS

A basic understanding of valuation theory is needed to understand valuation-related issues. This section discusses valuation terms and assumptions that underlie business valuation techniques.

Definitions of Business Valuation Terms

Appraisal This is the act or process of determining value. Accordingly, an appraisal is an opinion of the value of an asset or an ownership interest of a business enterprise. However, a business can have many values, depending on the circumstances. Thus, an appraisal must have a specific definition of value.

Value Value is an imprecise term because its meaning varies in different situations. Some common definitions of value include: fair market value, fair value, investment value, intrinsic value, going concern value, liquidation value, and book value.

Fair Market Value This is the most widely recognized and accepted standard of value and the one discussed most often in this chapter. Many provisions in the Tax Code refer to fair market value (FMV). The IRS defines FMV as the price at which the property would change hands between a willing buyer and a willing seller when the former is under no compulsion to buy and the latter is under no compulsion to sell and both parties have reasonable knowledge of the relevant facts. This definition is commonly used by the IRS, the courts, and valuation consultants. It assumes a hypothetical arm's-length sale without regard to a specific buyer or seller.

Fair Value For purposes of this chapter, this term is not the same as that used in accounting literature. Instead, the term stands for the statutory standard that generally applies in dissenting-shareholder suits and sometimes in corporate dissolutions under some states' laws. Almost all interests valued under this standard are minority interests. In some states, if a corporation agrees to a merger, sale, or other action and the minority shareholders believe they will not get adequate consideration for their stock, those shareholders may have their shares appraised and receive fair value in cash. In such cases the valuation consultant considers the factors established by relevant statutes and case law, which may include market values, individual asset values, methods commonly used in the financial community, and other factors.

Investment Value Investment value is the value of an asset or business to a specific owner or a prospective owner. Accordingly, this type of value considers the owner's or prospective owner's knowledge, abilities, related business interests, expectations of risks and earning potential, and other factors. The key point is that investment value is an owner-specific concept.

Intrinsic or Fundamental Value Some valuation consultants use this term interchangeably with investment value. Other consultants consider intrinsic value to be based on the analysis and judgment of an independent security analyst, investment banker, or financial manager. In court cases, it often is not defined clearly and may refer to FMV, fair value, or some other type of value. The term is ambiguous. Therefore, valuations based on this term need a clear definition of the meaning.

Going Concern Value This term refers to a value that explicitly considers certain intangible factors such as a trained, qualified work force; an operating plant; and the required licenses, systems, and procedures. Going concern value is based on the business being valued as a viable operating entity.

Liquidation Value Liquidation value (sometimes called breakup value) assumes a company's operations will cease and its individual assets will be sold. It usually is determined assuming either an orderly or a forced liquidation. An orderly liquidation means selling the assets over a reasonable period to maximize sales proceeds. A forced liquidation means selling the assets as quickly as possible, such as at an auction. (Forced liquidation value is sometimes called auction value.) Liquidation value (orderly or forced) considers not only the proceeds from selling the assets, but also the selling costs, the costs to hold the assets until their sale, and other expenses. Typically, the liquidation value of a business represents the lower limit of value.

Book Value Book value is an accounting term. For a specific asset, book value is its historical cost reduced by any allowances for depreciation, amortization, unrealized losses, and impairment. For a company, book value is its shareholders' equity (the excess of total assets over total liabilities on the balance sheet).

Observation: Generally, investment value and FMV are the most significant of these valuation concepts in transactions involving the disposal of a business.

Basic Business Valuation Assumptions

Business valuation methodology is built on the following basic assumptions:

> **Value of Business Equals Present Worth of the Future Benefits of Ownership** The preceding statement is a fundamental assumption of business valuations. A rational buyer normally will invest in a company only if the present value of the expected benefits of ownership are at least equal to the purchase price. Likewise, a rational seller normally will not sell if the present value of those expected benefits is more than the offered

selling price. Thus, the value of an ownership interest in a company is equal to the present worth of the future benefits of ownership.

Defining Future Benefits In business valuations, the benefits an owner receives are normally represented by the net cash flows from operating the business through dividends, draws, and/or salary and benefits beyond a normal level. This assumes the business retains enough cash to fund its expected level of operations. In the valuation process, the valuation consultant estimates the amount of the benefits accruing to the ownership interest being valued.

Value Can Be More Than One Number Any business valuation is full of judgments and estimates, and as discussed earlier, several definitions of value exist even if the buyer and seller can agree on all the facts. No one can predict with certainty the amount of future benefits that will be received by the owners of a business. Informed investors may have different opinions about the amount of those benefits. Also, investors may require different rates of return based on their opinions about the risks of owning that company. A company's value depends on each person's assessment of the benefits and risks.

Value Is Based on a Specific Point in Time An investor's required return and the amount of available benefits usually is estimated at a single point in time. Also, the estimate of value is based solely on the information available at the valuation date.

UNDERSTANDING VALUATION APPROACHES AND METHODS

The value of a business depends on the stream of future benefits that will be reaped by the owners of the business. However, those benefits cannot be measured with certainty. Businesses have different risks and earnings characteristics. Their owners' goals and expectations vary. No single formula can be used to determine the value of every business in every situation. Therefore, different fundamental valuation approaches have been developed. For each fundamental approach, there are various valuation methods that have evolved for estimating future benefits and the resulting values of businesses.

The three basic approaches that form the framework for specific valuation methods are (a) the income approach, (b) the market approach, and (c) the asset-based approach.

Overview of Valuation Engagement Steps

Choosing the appropriate valuation method or methods is ultimately the valuation professional's responsibility. However, practitioners should be familiar with the different methods and the situations in which they would generally be appropriate. A practitioner who has been involved with a business for many years may have insights that would be helpful to the valuation professional as he or she considers the various methods and their application to that particular business.

Obtain (or prepare) financial statements. If an income approach is used, these statements will be used to quantify the stream of benefits that are capitalized or discounted. If a market approach is used, the financial statements will be used to compute the various ratios that are compared to similar businesses for which selling prices are known. If an asset approach is used, the financial statements are used to identify the net assets upon which value is based.

Adjust the financial statements as necessary. Depending upon the basis on which they were prepared, the financial statements may have to be adjusted, (e.g., for financial statement departures from GAAP). In some cases, the financial statements have to be normalized (i.e., if unusual circumstances exist, the statements are adjusted to what they might have looked like under normal circumstances). The impact of nonoperating or excess assets may also create an adjustment. If cash flows are being analyzed (e.g., a capitalized cash flow approach) additional adjustments will be required. When the asset approach is used, the financial statements amounts are adjusted to FMV. Also, the effect of state and federal income taxes may have to be computed or recomputed.

If a market-based approach is used, identify guideline (comparable) companies. If the business being valued is a relatively small, closely held company, this may be a very difficult task. Documenting why the guideline companies were chosen is critical.

Estimate the business's operating value. This is the valuation expert's job and will involve determining what general approach to use and making decisions about how that approach is applied. Typically, the valuation professional should also perform "sanity checks" (usually by using another valuation method) to determine the reasonableness of the preliminary estimate.

Determine if the initial estimate of value should be adjusted for any premiums or discounts. Depending on the valuation approach used, adjustments such as a lack of marketability discount, a control premium, a built-in gains discount, or a minority interest discount may be appropriate.

The Income Approach

The income approach attempts to measure the present worth of the future benefits of business ownership. The two methods used to apply the income approach are (a) the capitalized returns methods and (b) the discounted future returns methods. Both methods use the business's projected operating results to estimate its value. Thus, both methods use earnings-based methods.

The capitalized returns methods may be used when the future operations of a business are not expected to change significantly from current normalized operations or are expected to grow at a predictable rate. To apply these methods, current annual returns from operations (either earnings or cash flow) are divided by a capitalization rate to estimate value.

The discounted future returns methods may be used when the future returns of a business (a) can be reasonably estimated and (b) are expected to differ significantly from current returns because of factors, such as expected changes in industry or economic conditions. To apply these methods, the future returns of a business are projected out until the year they reach a stabilized level. The earnings at this point are capitalized at an appropriate rate and the result is referred to as the terminal value. The terminal value and the projected earnings or cash flow for the periods before operations are stabilized derive a value for the business.

A value determined by either the capitalized returns or the discounted future returns methods may need to be adjusted for control premiums, built-in gains discounts, minority interest discounts, or marketability discounts.

When to Use Capitalized Returns Methods versus Discounted Future Returns Methods Capitalized returns methods are appropriate when current operations are indicative of future operations (assuming a normal growth rate). On the other hand, discounted future returns methods are appropriate when future returns are expected to be substantially different from current operations. (Substantially different means materially greater or less than a normal growth rate.) It may be desirable to use both of these methods to estimate the value of a business. Appendix 15B provides a comparison of valuation methods and relevant factors to consider when selecting a method.

Specific Valuation Methods The most common valuation methods under the capitalized returns methods and the discounted future returns methods are as follows:

- Capitalized Returns Methods.
    1. Capitalization of earnings.
    2. Capitalization of net cash flow.
    3. Capitalization of gross cash flow.
- Discounted Future Returns Methods.

1. Discounted net cash flow.
2. Discounted future earnings.

Using Guideline Company Data to Estimate Value (the Market Approach)

The market approach assumes an asset's value can be estimated from data obtained by analyzing recent sales of comparable assets. (In everyday life, this approach is generally used to value single-family homes.) In business valuations, the value of guideline businesses and/or comparable transactions may be used to determine the value of a business. The market approach is applied by conducting a thorough search for guideline data followed by an analysis and adjustment of the guideline data.

Once financial information for guideline companies has been obtained, it is used to calculate various value multiples or ratios for the guideline companies (the price/earnings ratio is the one most often used). Then the guideline companies' value multiples are applied to the company being valued. For example, the average or median price/earnings multiple for a list of guideline companies may be identified. Then that multiple is applied to the earnings of the business under consideration to estimate its value. It is important that earnings are measured in the same way and that the same period is used for both the business being valued and guideline companies. That period could be the latest 12 months, latest fiscal year, estimate of the next 12 months, or average or weighted average of some number of past years.

Commonly used value multiples or ratios include the following:

- Price/earnings.
- Price/dividends.
- Price/gross cash flow.
- Price/book value.
- Price/revenues.
- Price/net asset value.

Each of the above multiples or ratios constitutes a separate valuation method. The price/book value and price/net asset value methods can be characterized as asset-based methods, while the other value multiple methods can be characterized as earning-based methods.

Observation: In practice, truly comparable guideline businesses are difficult to find—especially for the typical relatively small closely held business. The valuation report should discuss the steps taken to search for comparable guideline data, the sources used, and the results of the search. The reports should also describe the population(s) from which the guideline transactions were drawn and the criteria for selection. If comparable guideline companies were identified, the report should give a brief description of each one, with relevant financial data (such as ratios, trends, and prices and valuation multiples).

Using the Underlying Assets Methods to Estimate Value (the Asset-based Approach)

Underlying assets methods determine a value for a business based on individual asset values. To apply these methods, the company's assets and liabilities are adjusted to either fair market value or liquidation value, depending on the method used.

Under the net asset value valuation method, the company's assets and liabilities are adjusted to their appraised values (usually FMV) to determine the value of the business. This method assumes the value of the business will be realized as part of a going concern (as opposed to a liquidation value method).

Adjustments also may be necessary to account for income taxes. If the valuation involves a C corporation, entity-level taxes from operations should be accrued and taxes calculated on the differences between FMV and tax basis of assets. For partnerships (including limited liability companies treated as partnerships for tax purposes) and sole proprietorships, there will be no entity-level taxes to consider. For S corporations, deciding whether to tax-effect earnings is more complicated.

Valuing Intangible Assets Many businesses have intangible assets, which may or may not be reflected on the financial statements. A valuation using an asset-based approach must consider these assets. Intangible assets are assets that lack physical substance but possess economic value. They may be purchased, such as franchises, or developed internally. For example, a company may patent a unique product that it develops. (See Appendix 15E for a list of common intangible assets.)

Intangible assets are identifiable or unidentifiable. Identifiable intangible assets have a determinable economic life, may be sold separately from the business, and can be destroyed. Examples of identifiable intangible assets are patents, trademarks, copyrights, assembled work force, and customer lists. Unidentifiable intangible assets have no determinable economic life and have no value apart from the business. Common examples are goodwill and going concern value. Unidentifiable intangible assets are commonly referred to as mass assets and are the residual that exists after all the assets of a purchased business have been valued.

Intellectual property is an identifiable intangible, but is unique because the owner can protect the asset from unauthorized use under enforceable laws. Patents, trademarks, copyrights and franchise agreements are examples of intellectual property.

The following three approaches are commonly used to value intangible assets:

- The cost approach primarily focuses on the replacement cost to develop the intangible asset. Patents, product development, and an assembled and trained workforce are often valued using the cost approach when alternative value approaches are not available.

- The market approach requires information on sale transactions (where similar intangibles represented the key component) or licensing transactions (that disclosed licensing fees and/or royalty rates on similar intangible assets). Licensing information is disclosed in public filings, franchise memoranda, and trade publications. Multiples can be derived from sale transaction data and applied to the subject intangible asset. Royalty rates from licensing transactions can be applied to projected income produced by the intangible asset, which are then discounted to present value at an appropriate discount rate. Royalty rates are commonly expressed as a percentage of selling price or total revenue. Sometimes royalty rates are applied to units sold or a level of profit, such as gross profit.

- The income approach is the primary approach used to value most intangible assets. The value is based on the present worth of future benefits. However, careful analysis is required when applying the income approach because the benefits attributable to the specific intangible asset must be separated from the benefits attributable to other assets of the enterprise.

Using the Liquidation Value Method To determine value using the liquidation value method, the net proceeds available after liquidating the business assets and paying off the liabilities are discounted to present value using a suitable discount rate. This method assumes the value of the business will be realized through either a forced or orderly liquidation of its assets instead of as a going concern. Generally, the orderly liquidation method will be more appropriate unless there is a lack of funds or other factors that prevent the business from holding its assets long enough to affect an orderly liquidation.

Engaging an Asset Appraiser Use of the NAV or LV methods may require the owner to hire an asset appraiser in addition to the business valuer. Although an asset appraiser creates an additional cost to the company it may be necessary if assets are significant and hard to value.

Several factors affect the decision about when an asset appraiser may be needed when the net asset value or liquidation value method is used. Some of the more obvious factors are:

- **An Asset Appraiser Is Usually Needed When the Liquidation Value Method Is Used** Qualified asset appraisers generally are better informed about market conditions for certain assets than valuation consultants. Thus, the authors suggest using an asset appraiser when the liquidation value method is used.

- **An Asset Appraiser May Be Needed If There Are Large Amounts of Inventory or Property and Equipment** A company's balance sheet normally presents inventory, property and equipment at their book values, which may be significantly different from their market values. Accordingly, an asset appraiser may be needed to determine the market value of significant assets, especially real estate and equipment.

- **An Asset Appraiser May Be Needed for Companies in Certain Industries** Some asset-intensive companies in specialized industries are more likely to require asset appraisers. For example, a real estate investment company with large inventories of undeveloped properties probably will require appraisals from a qualified real estate appraiser. Likewise, an oil and gas production company will normally require a reserve report of developed and undeveloped oil and gas reserves as of the valuation date.

Applying Other Valuation Methods

Other specific valuation methods exist that cannot be readily classified into one of the approaches previously discussed. These methods generally are based on a combination of methods and include:

- Excess earnings method (essentially, an earnings-based method).

- Multiple of discretionary earnings (an earnings-based method).

- Rules of thumb.

- Business specific methods, such as transactions in a company's stock and valuations based on enforceable contracts, such as a buy/sell agreement.

Using the Excess Earnings Method The excess earnings method is commonly used for valuing small businesses or professional practices. The method was developed by the IRS and is outlined in Rev. Rul. 68-609. First, the value of the net tangible assets of the business and a reasonable rate of return on those net tangible assets is determined. Then the excess earnings—which is the difference between the actual net earnings and the reasonable rates of return on net tangible assets—are calculated and capitalized using an appropriate cap rate. Effectively, this second procedure computes the value of the business's intangible assets. To determine the business's total value, the value of the intangibles is added to the value of the tangible net assets. The excess earnings method is not, however, viewed favorably by the IRS if used to value the intangible assets of a business when another valuation method is available.

Using the Multiple of Discretionary Earnings Method The multiple of discretionary earnings method (also known as the sellers' discretionary cash flow method) is best suited to businesses where the salary and perquisites of an owner represent a significant portion of the total benefits generated by the business and/or the business is typically run by an owner/manager. Accordingly, this method can be a good way to value very small businesses (normally businesses with less than 20 employees and values less than $250,000). The vast majority of those who acquire very small businesses are purchasing both a business and a job. These people tend to think in terms of income to replace their previous paycheck or income to support their family. They look at the total discretionary earnings to see if it is sufficient to pay all the operating expenses of the business, carry the debt structure necessary to buy and/or operate the business, and provide an adequate wage.

Until recently, the term discretionary earnings has not been universally used or defined. Some professionals prefer to use other terms, such as owner's discretionary cash or owner's cash flow. The problem with these other titles is that they are not fully descriptive and contain terms that have different meanings in the accounting and financial professions. The Standards Committee of the International Business Brokers Association (IBBA) has defined discretionary earnings as a company's earnings prior to the following items:

- Income taxes.
- Non-operating and nonrecurring income and expense.
- Depreciation and amortization.
- Interest income or expense.
- Owners' total compensation.

To determine the value of a business under this method, discretionary earnings is multiplied by a value multiple derived from sales in the market. Again, because discretionary earnings include the owner's compensation and benefits, the value derived really represents the value of the business to a prospective owner/manager.

Using Rules of Thumb Rules of thumb are formulas used to value businesses in certain industries. Rule of thumb formulas are derived from guideline business sale transactions and generally are multiples of gross revenues, operating income, or some other measure of earnings power. For example, a rule of thumb for a casualty insurance brokerage might be a multiple of retained gross commission income, plus net tangible assets. Professional practices are often roughly valued at some multiple of billings.

In general, rules of thumb should not be used as the only valuation method. However, they are useful in evaluating the reasonableness of the values indicated by other methods. Limitations on rule-of-thumb methods include inability to identify enough comparable transactions and inability to ascertain information about financing terms for comparable sales and specific factors (such as the fact that a sale was a distress sale, for example) affecting sales of comparable businesses. In other words, the basic limitation of rules of thumb is that they are intended to apply to "typical" businesses. However, in actual transactions, there is no such thing as a "typical" business as far as the buyer and seller are concerned.

Using Business Specific Methods Sometimes information can be obtained about a business that gives a good indication of its value. For example, transactions involving a company's stock may be helpful. Often such transactions are among family members (which may not provide the most useful information), but sometimes there are true arm's-length transactions.

Another example of a business specific method is using enforceable contracts such as buy/sell agreements to establish the value of a business. If any such contracts are between related parties, the valuation consultant should strongly consider whether they provide indications of the value of the business.

SELECTING APPROPRIATE VALUATION METHODS FOR VERY SMALL BUSINESSES

What Is a Very Small Business?

Although a small business is generally closely held, a closely held business is not necessarily a small business. A common example of a very small business is a single store pizza parlor. Because businesses like these are usually owner operated, they are often referred to as "Mom and Pop" businesses. For purposes of this section, these businesses will be referred to as very small businesses.

Very small businesses tend to have certain common characteristics. Following are some of the more important shared features:

- Usually the owners are also the managers of the business. Therefore, if the business succession plan is to sell a very small business, both the return on the owner's labor (the owner's "salary") and the return on invested capital must be considered. Prospective buyers of very small businesses are often motivated by a desire to "purchase" a job or career.

- The financial reporting used by a very small business usually is based on the business's taxable income—which owners attempt to minimize. Therefore, earnings may tend to be understated.

- Business owners often set compensation and benefit levels for themselves (and other family members on the payroll) to manipulate income. Generally, compensation will be set high to minimize income in a C corporation and thus avoid double taxation of corporate profits. However, in S corporations, shareholder/employees tend to favor low salaries to avoid self-employment tax. Also, some owners may attempt to maximize profit by taking a reduced salary while the business is for sale. The appraiser should make adjustments to normalize salary expense if these factors are present.

- Accounting records may be on the cash basis and typically are not very detailed or sophisticated.

- The legal form in which the business is conducted is often relatively unimportant. Many very small businesses are sole proprietorships, others elect S or C corporation status to limit owner liability.

Common Elements of a Very Small Business Purchase/Sale Transaction

As stated earlier, purchases of very small businesses generally involve buyers who are motivated by the purchase of a job as well as a business. Owner/operators often measure their total return by including salary, benefits, and profits. Therefore, purchases and sales of very small businesses tend to have some of the following characteristics:

- The buyer's (not the seller's) perception of the business's potential is the key factor in its marketability. This is always true, but this fact is abundantly clear in the purchase of a very small business.

- These businesses are usually sold via an asset purchase rather than by purchasing the ownership interests in the business entity (if any).

- The terms of the sale (for example, whether the seller will take back a note) and collateral required for any loans are key factors in deciding the price eventually paid.

- Both buyers and sellers may be ruled by emotion.

Which Valuation Methods Are More Appropriate?

Most very small businesses are quite risky. Many fail within the first year of their existence. Some of the reasons include:

1. Lack of capital.

2. Poor management and planning.

3. No business experience on the part of the owners.

In view of these considerations, certain valuation methods are more appropriate for valuing very small businesses. These are discussed in the following paragraphs.

Multiple of Discretionary Earnings Method The multiple of discretionary earnings method is often used to value very small businesses. In fact, this method has been used so frequently that it may constitute an industry norm.

Excess Earnings Method The excess earnings method is also frequently used to value very small businesses. It can be viewed as a combination of the underlying asset methods (in which an amount is paid for tangible assets of a business), plus a negotiated amount for intangible assets based on capitalized excess earnings (if any).

Guideline Company Methods Valuation methods using guideline company data are also useful. In this case, this means sales of other very small businesses. To apply this method, business brokers, business owners, and other professionals should be contacted in an effort to develop transaction information. Comparative data on sales of very small businesses is not widely available. However, BIZCOMPSr, the IBA Market Database, and DoneDealsr are three sources of comparative information that may be useful in valuing very small businesses.

- **BIZCOMPS** is a study of recent small business sales compiled by a business broker. The data is divided into Western, Central, and Eastern editions. As an example, the Central states study, published in 2004, contains information on more than 1,500 actual sales. There is also a National Industrial Study that covers sales of manufacturers, wholesalers/distributors, and business-to-business service providers. For information on purchasing BIZCOMPS, call (702) 454-0072, or visit their website at www.bizcomps.com. Owners of PPC's Guide to Business Valuations may purchase an electronic version of BIZCOMPS. Contact PPC at (800) 323-8724 for more information or visit ppc.thomson.com.

- **IBA Market Database** is a computerized database compiled by the Institute of Business Appraisers (IBA) for its members. The database contains information on over 23,000 sales of small and mid-sized closely held companies. For more information, contact the IBA at (800) 299-4130, or visit their website at www.go-iba.org.

- **DoneDeals** is an online database of over 5,800 mid-market transactions that provides data such as price, term, and seller financials and ratios for every transaction reported. Approximately 50% of the deals are under $14.5 million, and approximately 78% of the selling companies are privately owned. The database is updated weekly. For more information, visit ppc.thomson.com or contact PPC at (800) 323-8724.

Note: Because of the limited sample sizes and other data limitations, the authors recommend that the above resources be used only to establish guidelines. The data from these resources is not a substitute for other in-depth research on the specific business and the market factors that impact that type of business in its geographic area. In the valuation of very small businesses, it is important that guideline information be timely, relevant, and sufficiently detailed to allow meaningful comparison. Although the above resources are limited with regard to timeliness, relevance, and detail, they still can provide useful information—in particular the data may be useful as a sanity check.

Valuation Methods That May Not Be Useful

Stock prices of seemingly comparable publicly traded corporations are usually not helpful in valuing very small businesses. The differences between the publicly traded firms and very small businesses are usually too great to allow meaningful comparison. The practitioner should look for comparable transactions, but it is unlikely they will be found in the sales prices of publicly traded companies.

Since very small businesses are usually risky, their future performance is uncertain by definition. The mortality rate of very small businesses is so high that a prediction of long-term performance may not be possible. Accordingly, a discounted future earnings or discounted net cash flow method using, for example, a five-year or 10-year time horizon is often not appropriate.

APPLYING DISCOUNTS AND PREMIUMS TO CLOSELY HELD BUSINESSES

One of the most challenging areas in the valuation of closely held businesses is the application of discounts and premiums. Typically, the issue involves whether a discount or premium is appropriate and, if so, the amount of the discount or premium. The following is a list of some premiums and discounts that may be appropriate in the valuation of closely held businesses:

- Lack of marketability discount.
- Key person discount.
- Minority interest discount.
- Control premium.
- Assignee interest discount.
- Built-in gains discount.

Note: Valuation discounts should be applied and calculated separately in an appraisal not combined.

Lack of Marketability Discount

Ownership interests in closely held businesses are typically not readily marketable compared to similar interests in their publicly traded counterparts. For example, a share of stock in a privately held company is usually worth less than an otherwise comparable share in a public company. Discounts for lack of marketability usually should be applied to any ownership interest that cannot be easily sold in a timely manner (e.g., phoning your broker and receiving the proceeds within three days). Such discounts are applicable to most investments *not* listed on an organized exchange or traded in an active over-the-counter market.

Key Person Discount

The success of many small businesses is directly attributable to the efforts of the owner or another key person. Thus, the loss of this individual may depress the value of the business, especially if the business lacks trained personnel to take the key person's place (Rev. Rul. 59-60). The factors that should be considered in determining the size of a key person discount include—

- The nature of the business and its assets.
- The effect on future profits from the key person's loss.
- The existence of a current employee to take over the key person's responsibilities.
- The availability of competent new management members that can be hired at the salary and benefits formerly paid to the key person.
- The amount of key person life insurance proceeds payable to the corporation (assuming valuation is after the key person's death). The lack of adequate life insurance coverage increases the need for a key person discount.

Minority Interest Discount

A minority interest discount is a downward valuation adjustment reflecting the absence of the power of control of a minority interest. Since a minority interest cannot direct the activities or policies of the business, this interest is worth less than one that can control policy decisions.

A minority interest discount is different from a discount for lack of marketability. A minority interest discount relates to the lack of control inherent in the interest to be valued. In contrast, the discount for lack of marketability is allowable on the theory that a closely held business interest is not easily liquidated. The discounts are applied separately. However, they may both apply to the valuation of a particular business interest.

Voting power held by family members does not have to be aggregated to determine whether the transferred interest is valued as part of a controlling interest. Accordingly, a minority interest discount is not disallowed solely because a transferred interest, when combined with other interests held by family members, is part of a controlling interest (Rev. Rul. 93-12). In the case of a gift, this is true even if the donor owned 100% of the business interest prior to the gift(s).

The IRS position is more beneficial to taxpayers who are gifting or selling their business interest to other family members than to a taxpayer whose interest is being valued for estate tax purposes. Each gift or sale is valued separately, even if several gifts or sales are made simultaneously. Thus, without family attribution, the cost of gifting or selling a controlling interest in a business to family members can potentially be reduced substantially if each recipient receives a minority interest. In contrast, estate tax values are determined at the decedent's level. Thus, even though family attribution does not apply, a minority discount still is not available for estate tax purposes if the decedent owns a majority interest at death. However, if a business interest is held as community property, the estate should be entitled to a minority discount for the business interest since the decedent's community property interest in the business can never exceed 50%.

The IRS has ruled privately that when there is no single controlling interest in a corporation owned entirely by one family, the value of a transferred minority interest, which combined with the interests of the other shareholders was enough to control the corporation, had to be increased by its "swing vote" potential.

However, the True case indicates that the IRS's theory of a swing vote premium may not apply to transfers of a minority interest in a closely held business owned entirely by one family. This decision provides important precedence for taxpayers attempting to preserve a minority interest discount in transfers of closely held family business interests.

The concept of the swing vote premium relies on the assumption that the hypothetical buyer may be able to join forces with other owners to control the entity or block others from control. Therefore, the likelihood that the hypothetical buyer can form a coalition is critical to the application of a swing vote premium.

In True, the Tax Court rejected the IRS's argument that a decedent's 38.47% interest in a general partnership held entirely by one family was not entitled to a minority interest discount because it could be combined with any other single block to create a controlling interest. The Tax Court based its decision on two premises:

1. In determining whether a minority interest discount applies, it cannot be assumed that a hypothetical buyer would be a member of the transferor's family.

2. It can be assumed that the hypothetical buyer would recognize the identity of the other partners and consider it unlikely that he would be able to form a coalition.

Given these assumptions, the Tax Court found that a hypothetical buyer would view the minority interest as lacking in control and thus be entitled to the appropriate discount.

In this and other cases, the Tax Court seems to take the position that the minority interests owned by family members may be considered a single majority block by an unrelated third-party purchaser. Therefore, if the family forms a majority block, the unrelated buyer must be purchasing a minority interest and be entitled to an appropriate discount.

Control Premium

In contrast to a minority interest discount, a controlling interest usually commands a premium over a minority interest because the holder of these interests has virtual control over all aspects of the business's operations. Thus, if the interest in a closely held corporation constitutes voting control, the value of the stock is usually increased to reflect the premium placed on such control.

Determining the amount of a control premium or minority discount is difficult and involves a great deal of judgment. The degree of control is what is important and it is that degree that must be evaluated. Factors to consider that affect the degree of control that can be exercised, and therefore affect the amount of premium or discount, include the following:

- **Cumulative versus Noncumulative Voting** Many companies have noncumulative voting provisions, which means a majority owner has the ability to elect the entire board of directors, and that ability cannot be blocked by minority interests. Some companies, however, have a cumulative voting system in which all voters (shareholders) are given votes in proportion to their ownership percentages. This system often allows minority shareholders to gain some representation on the company's board of directors. Thus, a control premium may need to be applied to an ownership interest in a company with noncumulative voting provisions, or a smaller minority discount may apply to a minority interest in a company with a cumulative voting system.

- **Contractual Restrictions** Companies may give up certain control rights through contractual provisions. For example, a bank may require certain activities of a company be restricted or prevented in order to fund a new loan or continue an existing debt relationship. Some of the more common restrictions involve the payment of dividends, liquidation of assets, or changes in the direction of the business, not to mention compensation of controlling shareholders. Therefore, the control premium for a majority interest may be less in a company that gives up control rights through contractual provisions.

- **Effects of Regulations, Including State Statutes** Statutes concerning the rights of minority and majority owners vary from state to state. In about half of the states, major actions, such as mergers, sales, liquidation, and recapitalization can be approved by a simple majority. Other states require a two-thirds or greater majority to approve such actions. In those states, a minority who owns just over one-third of a company's stock (or even less in a few states) has the power to block significant actions. Because statutes vary from state to state, the valuation consultant should always research the laws of the state of incorporation in determining what, if any, premium or discount applies. For example, the minority discount would be less for a 35% interest in a state where a two-thirds or greater majority is required to approve actions than for a 35% interest in a state that requires majority approval.

- **Effects of Distribution of Ownership** The amount of stock a person (or group of people) owns in relation to other shareholders is often important in determining control issues. For example, if each of three stockholders or partners owns a one-third interest in a company, no one has complete control. However, no one is in a relatively inferior position unless two of the three have close ties with each other that the third does not share. The minority discount applicable to each one-third interest would be less than the discount applicable to a 10% ownership interest.

A control premium or a minority discount is appropriate if the method used to value the interest does not already reflect the discount or premium. For example, if the capitalized returns methods are used, the resulting value will represent a minority interest, but if the client needs to know the value of a controlling interest, a control premium may be added. Alternatively, if a control value has been determined, but the client needs to know the value of a minority interest, a minority discount usually should be subtracted.