What Kind of Value Would You Like?

Typically, when an attorney feels it is necessary to value a business, he/she believes that a clear and unequivocal decision has been reached – the need to get the value of the business. However, what is the appropriate "standard of value" for the matter at hand? Is it fair market value, fair value, investment value, liquidation value….? All of these points are relevant in how the business valuator proceeds and, certainly, in how the business valuator concludes. Let us briefly discuss these various terms of art.

⇒ **Fair Market Value** – the classic definition of fair market value has long been memorialized along the lines of:

  - The price at which a business would change hands between a willing seller and a willing buyer, neither under any compulsion to sell or buy, and both equally informed of all relevant facts.

    The classical arm's length transaction. Furthermore, the reference to price in that definition is generally understood to mean a cash price – money up front. This is the standard of value we typically see for gifting and estates.

⇒ **Fair Value** – the major difference as contrasted with fair market value is that as to a minority interest, a lack of control discount is not applied. There is also some question as to whether a marketability discount should be applied (assuming that it is appropriate at all for the specific matter at hand). Fair value is usually the standard of value utilized in a shareholder oppression suit, and for divorce matters (in New Jersey).

⇒ **Value to the Holder** – this is not any form of "Value". It is a fiction created by those who mistakenly believe it actually means something. Nowhere has it ever been clearly defined, and is "junk science", with potential value extremes of shocking dimensions.

⇒ **Investment Value** – generally meaning the value to a particular investor or group of investors – as contrasted with value to a wide range of (or the ultimate hypothetical) investors. This type of value brings into play aspects and issues of interest or relevance to a particular investor, rather than to the general investing public. Generally this means that additional value may be place on the business entity by that individual, value in excess of what a dispassionate hypothetical investor would consider.

⇒ **Intrinsic Value** – in some sense, intrinsic value is similar to investment value, but may call upon the valuator to be more analytical – it is a less "personal" sense of value. When (if) this approach to value is adopted by a sufficient number of investors, intrinsic value can become fair market value. We see intrinsic value used by stock analysts when they argue that the market doesn't yet appreciate the real value of a company, or conversely, when they argue that the market has overvalued a company. These analysts will then refer to the intrinsic value of a company as being the "real" value that the market has yet to recognize.

⇒ **Buy Sell Agreement** – this is not a standard of value, but depending on the nature of the assignment, may very well be the most important method of valuing the business entity. It could also be totally irrelevant. This is especially so if it has not been used in the past, if the amounts are unrealistic, if it is essentially a death buyout plan… However, in a non-divorce situation, a shareholder's agreement may carry great weight – after all, it is a contract. Nevertheless, even if the valuation proceeds under the provisions put forth in that shareholder's agreement, it is not a standard of value.

⇒ **Liquidation Value** – generally this is only a consideration when the business is truly in poor shape, or barely (not at all) profitable (in relationship to its invested capital). Also, this is the putative value we often hear from the business owner (in a divorce), or the majority owner (in an oppressed shareholder's suit). Essentially, this value is the sum of the parts (assets, at realizable value, less liabilities) – with no goodwill.