

Glossary of Business Valuation Terms

International Glossary of Business Valuation Terminology*

Adjusted Book Value – The value that results after one or more asset or liability amounts are added, deleted, or changed from their respective financial statement amounts.

Asset (Asset-Based Approach) – a general way of determining a value indication of a business, business ownership interest, or security by using one or more methods based on the value of the assets of that business net of liabilities.

Benefit Stream – any level of income, cash flow, or earnings generated by an asset, group of assets, or business enterprise. When the term is used, it should be supplemented by a definition of exactly what it means in the given valuation context.

Beta – a measure of systematic risk of a security; the tendency of a security's returns to correlate with swings in the broad market.

Blockage Discount – an amount or percentage deducted from the current market price of a publicly traded security to reflect the decrease in the per share value of a block of those securities that is of a size that could not be sold in a reasonable period of time given normal trading volume.

Business Enterprise – a commercial, industrial, service, or investment entity, or a combination thereof, pursuing an economic activity.

Business Valuation – the act or process of determining the value of a business enterprise or ownership interest therein.

Capital Asset Pricing Model (CAPM) – a model in which the cost of capital for any security or portfolio of securities equals a risk-free rate plus a risk premium that is proportionate to the systematic risk of the security or portfolio.

Capitalization – a conversion of a single period stream of benefits into value.

Capitalization Factor – any multiple or divisor used to convert anticipated benefits into value.

Capitalization Rate – any divisor (usually expressed as a percentage) used to convert anticipated benefits into value.

Capital Structure – the composition of the invested capital of a business enterprise; the mix of debt and equity financing.

Cash Flow – cash that is generated over a period of time by an asset, group of assets, or business enterprise. It may be used in a general sense to encompass various levels of specifically defined cash flows. When the term is used, it could be supplemented by a qualifier (for example, "discretionary" or "operating") and a definition of exactly what it means in the given valuation context.

Control – the power to direct the management and policies of a business enterprise.

Control Premium – an amount (expressed in either dollar or percentage form) by which the pro rata value of a controlling interest exceeds the pro rata value of a non-controlling interest in a business enterprise, that reflects the power of control.

Cost Approach – a general way of estimating a value indication of an individual asset by quantifying the amount of money that would be required to replace the future service capability of that asset.

Cost of Capital – the expected rate of return (discount rate) that the market requires in order to attract funds to a particular investment.

Discount – a reduction in value or the act of reducing value.

Discount for Lack of Control – an amount or percentage deducted from the pro rata share of value of one hundred percent (100%) of an equity interest in a business to reflect the absence of some or all of the powers of control.

Discount for Lack of Marketability – an amount or percentage deducted from the value of an ownership interest to reflect the relative absence of marketability.

Discount Rate – a rate of return (cost of capital) used to convert a monetary sum, payable or receivable in the future, into present value.

Economic Life – the period of time over which property may generate economic benefits.

Equity Net Cash Flows – those cash flows available to pay out to equity holders (in the form of dividends) after funding operations of the business enterprise, making necessary capital investments, and reflecting increases or decreases in debt financing.

Equity Risk Premium – a rate of return in addition to a risk-free rate to compensate for investing in equity instruments because they have a higher degree of probable risk than risk-free instruments (a component of the cost of equity capital or equity discount rate).

Excess Earnings – that amount of anticipated benefits that exceeds a fair rate of return on the value of a selected asset base (often net tangible assets) used to generate those anticipated benefits.

Excess Earnings Method – a specific way of determining a value indication of a business, business ownership interest, or security determined as the sum of a) the value of the assets obtained by capitalizing excess earnings and b) the value of the selected asset base. Also frequently used to value intangible assets. See Excess Earnings.

Fair Market Value – the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.

Forced Liquidation Value – liquidation value at which the asset or assets are sold as quickly as possible, such as at an auction.

Going Concern – an ongoing operating business enterprise.

Going Concern Value – the value of a business enterprise that is expected to continue to operate into the future. The intangible elements of Going Concern Value result from factors such as having a trained work force, an operational plant, and the necessary licenses, systems, and procedures in place.

Goodwill – that intangible asset arising as a result of name, reputation, customer loyalty, location, products, and similar factors not separately identified.

Goodwill Value – the value attributable to goodwill.

Income (Income-Based) Approach – a general way of determining a value indication of a business, business ownership interest, security, or intangible asset using one or more methods that convert anticipated benefits into a present single amount.

Intangible Assets – non-physical assets (such as franchises, trademarks, patents, copyrights, goodwill, equities, mineral rights, securities and contracts as distinguished from physical assets) that grant rights, privileges, and have economic benefits for the owner.

Invested Capital – the sum of equity and debt in a business enterprise. Debt is typically a) long-term liabilities or b) the sum of short-term interest-bearing debt and long-term liabilities. When the term is used, it should be supplemented by a definition of exactly what it means in the given valuation context.

Invested Capital Net Cash Flows – those cash flows available to pay out to equity holders (in the form of dividends) and debt investors (in the form of principal and interest) after funding operations of the business enterprise and making necessary capital investments.

Investment Risk – the degree of uncertainty as to the realization of expected returns.

Investment Value – the value to a particular investor based on individual investment requirements and expectations.

Key Person Discount – an amount or percentage deducted from the value of an ownership interest to reflect the reduction in value resulting from the actual or potential loss of a key person in a business enterprise.

Levered Beta – the beta reflecting a capital structure that includes debt.

Liquidity – the ability to quickly convert property to cash or pay a liability.

Liquidation Value – the net amount that can be realized if the business is terminated and the assets are sold piecemeal. Liquidation can be either “orderly” or “forced”.

Majority Control – the degree of control provided by a majority position.

Majority Interest – an ownership interest greater than fifty percent (50%) of the voting interest in a business enterprise.

Market (Market-Based) Approach – a general way of determining value indication of a business, business ownership interest, security, or intangible asset by using one or more methods that compare the subject to similar businesses, business ownership interests, securities, or intangible assets that have been sold.

Marketability – the ability to quickly convert property to cash at minimal cost.

Minority Discount – a discount for lack of control applicable to a minority interest.

Minority Interest – an ownership interest less than fifty percent (50%) of the voting interest in a business enterprise.

Net Book Value – with respect to a business enterprise, the difference between total assets (net of accumulated depreciation, depletion, and amortization) and total liabilities of a business enterprise as they appear on the balance sheet (synonymous with Shareholder’s Equity); with respect to an intangible asset, the capitalized cost of an intangible asset less accumulated amortization as it appears on the books of account of the business enterprise.

Net Cash Flow – a form of cash flow. When the term is used, it should be supplemented by a qualifier (for example, “Equity” or “Invested Capital”) and a definition of exactly what it means in the given valuation context.

Net Tangible Asset Value – the value of the business enterprise’s tangible assets (excluding excess assets and non-operating assets) minus the value of its liabilities.

Non-Operating Assets – assets not necessary to ongoing operations of the business enterprise.

Orderly Liquidation Value – liquidation value at which the asset or assets are sold over a reasonable period of time to maximize proceeds received.

Premise of Value – an assumption regarding the most likely set of transactional circumstances that may be applicable to the subject valuation; e.g. going concern, liquidation.

Portfolio Discount – an amount or percentage that may be deducted from the value of a business enterprise to reflect the fact that it owns dissimilar operations or assets that may not fit well together.

Rate of Return – an amount of income (loss) and/or change in value realized or anticipated on an investment, expressed as a percentage of that investment.

Report Date – the date conclusions are transmitted to the client.

Replacement Cost New – the current cost of a similar new property having the nearest equivalent utility to the property being valued.

Reproduction Cost New – the current cost of an identical new property.

Residual Value – the prospective value as of the end of the discrete projection period in a discounted benefit streams model.

Risk-Free Rate – the rate of return available in the market on an investment free of default risk.

Risk Premium – a rate of return in addition to a risk-free rate to compensate the investor for accepting risk.

Rule of Thumb – a mathematical relationship between or among variables based on experience, observation, hearsay, or a combination of these, usually applicable to a specific industry.

Special Interest Purchasers – acquirers who believe they can enjoy post-acquisition economies of scale, synergies, or strategic advantages by combining the acquired business interest with their own.

Standard of Value – the identification of the type of value being utilized in a specific engagement; e.g. fair market value, fair value, investment value.

Sustaining Capital Reinvestment – the periodic capital outlay required to maintain operations at existing levels, net of the tax shield available from such outlays.

Systematic Risk – the risk that is common to all risky securities and cannot be eliminated through diversification. When using the capital asset pricing model, systematic risk is measured by beta.

Unlevered Beta – the beta reflecting a capital structure without debt.

Unsystematic Risk – the portion of total risk specific to an individual security that can be avoided through diversification.

Valuation – the act or process of determining the value of a business, business ownership interest, security, or intangible asset.

Valuation Approach – a general way of determining the value indication of a business, business ownership interest, security, or intangible asset using one or more valuation methods.

Valuation Date – the specific point in time as of which the valuator’s opinion of value applies (also referred to as “Effective Date” or “Appraisal Date”).

Valuation Method – within approaches, a specific way to determine value.

Valuation Procedure – the act, manner, and technique of performing the steps of an appraisal method.

Valuation Ratio – a fraction in which a value or price serves as the numerator and financial, operating, or physical data serve as the denominator.

Weighted Average Cost of Capital – the cost of capital (discount rate) determined by the weighted average, at market value, of the cost of all financing sources in the business enterprise's capital structure.

* Five professional organizations whose members provide business valuation services have adopted this glossary of definitions for terms used in business valuation. This glossary is designed to provide guidance to business valuation practitioners as well as users of business valuation services. The professional organizations that have adopted this glossary are the American Institute of Certified Public Accountants, American Society of Appraisers, Canadian Institute of Chartered Business Valuators, National Association of Certified Valuation Analysts and the Institute of Business Appraisers.

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