

Pricing a Business

You'll probably combine many factors and methods when setting a price for your business.

1. Value of tangible business assets.

Tangible assets are physical, such as furniture, equipment, and inventory. If the tangible assets are in reasonable shape, there may be a ready market for them. An appraiser can help you put a value on these tangible assets.

2. Value of intangible business assets.

There may be value in your business name, or in patents, copyrights, or customer lists you own. And favorable long-term contracts with customers or suppliers or a transferable long-term lease in a good location can also be valuable intangible assets. Employees can also be important intangible assets.

3. Sale prices of comparable businesses.

The closest to an ideal way to set a value on your business is to see what other small enterprises like yours have sold for. In the real estate business, this is called looking at comparables.

4. Industry formulas.

In some businesses, it is often said that you can arrive at a sales value by multiplying either gross sales or net earnings by an accepted number. If you're considering buying a business in a field where formulas like this are part of the culture, look at what the price would be using that formula, but don't ignore other factors.

5. Market demand.

If a number of similar businesses have just been put on the market or there's been a recent spate of factory closures in your area, there may be no interested buyers at your price or within what you believe is a reasonable range.

6. Your personal needs.

If financial pressures are forcing you to sell your business quickly, you'll probably have to take less than the optimal sale price. Or, if you're unable or unwilling to work for the buyer -- even for a short time after the closing -- that fact may diminish the value of the business in the eyes of a buyer.

7. Type of buyer.

For a buyer who will be relying on the business for a livelihood, the sale price and the terms of payment need to result in cash flow that is sufficient to cover paying the buyer a decent salary -- in addition to covering operating expenses and installment payments to you. But for a buyer who is considering your business as a strategic addition to a similar business he or she already owns, the benefits of scale may allow a lower price; bookkeeping expenses, for example, may increase only slightly when the buyer adds a second location.

8. Terms of payment.

The terms you require, such as the amount of the down payment, the repayment period, and the

interest rate, can all affect how much a buyer will agree to pay. And you may want to charge more if you'll be paid over five rather than three years, for instance, since during the repayment period, you'll be exposed to more risk of buyer default.

9. Appraisals.

Appraisers excel in assigning values to tangible property such as land, buildings, and equipment. However, in most cases, a business is worth more than the sum of its assets, so if you choose to use an appraiser, pick one who understands and has had experience in including the nontangible factors, such as a favorable lease or excellent goodwill.

10. Put it all together.

All or some of the above factors can be used in pricing your business. But keep in mind that the overall deal -- price and payment terms -- has to be realistic, even though you'd like the sale price to be as high as possible. You need to feel reasonably certain that the buyer is unlikely to falter and that the odds are that in three or five years, the buyer will make the final payment. This means that, during the years the buyer is making payments and also probably working in the business, the business must produce enough income to pay the buyer a decent salary in addition to covering the monthly payments to you.

For more information about valuation methods, business brokers, and the sales process, go to http://www.inc.com/guides/buy_biz/24005.html.