

**PRESIDENT'S MESSAGE
 JUNE 2007**



To my fellow I-CBC Members:

Welcome to summer! June 21st marks Summer Solstice and this is an opportunity to review your progress against your business and personal plans. I hope that you are on track but you may, like me, need to make a mid-year correction. Our I-CBC membership is comprised of multi-disciplinary professionals who by and large provide service to businesses. And, I suspect, we also share the common ground of being rewarded based largely on our results and not our activities.

Are you on track? If yes, *well done!* If not, who are your resources to help you? Networking and mentoring with other successful professionals has always been a key to success. Of course, you can always pull yourself up by your own bootstraps but it's so much more fun to work with others! *Are you having fun?*

My mid-course correction is exactly along these lines. I'm re-challenging myself to examine the networking and referral relationships that drive my business and personal life. As an example, I am a member of a service organization: Rotary International. I-CBC includes members who are involved in Kiwanis, Lions Clubs, Rotary and other worthy organizations. These associations provide a way to share our time, energy, leadership and/or wealth in the service of others. During May, I hosted 4 Peruvian business professionals as part of a Rotary International exchange. I encourage you to get involved and make a contribution of your personal resources in an avenue that fits your family and business interests.

Changing gears ... your Board of Directors and Committee Chairs had a telephonic board meeting on May 10th. Our committees are active and always welcome participation and input ... please contact a committee chair for more information.

Your Board is also considering forming an Ad Hoc Committee to consider our 10 year vision for I-CBC. I welcome your input or comments. Our next Board Meeting is June 20th and we hope to propose a forum during our National Conference in Annapolis, Sept 20-22.

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Get involved and make a difference! Thank you for your continued support and, for Goodness Sake, take a kid fishing!

Jeff Adam, MCBC
 ICBC President

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Editorial Office

18615 Willamette Drive
West Linn, OR 97068
Phone: 1-877-422-2674
Fax: 503-292-8237
email: maryann@westsidesecc.com

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EDITOR'S COLUMN

Welcome to the June edition of the ICBC Newsletter. As you may notice, we have received a few more articles for this edition. We encourage all members to use this as a forum to share ideas with your colleagues. So if you have an article you would like to share with the membership, please send us your article and we will do everything we can to get it published.

If you have a contact in a related industry that you feel has something that would be beneficial to our membership, please feel free to contact the ICBC office to see if it would fit into our newsletter schedule. Be sure and look in the next couple of newsletters for a series of articles from a marketing professional that I have asked to share some ideas with our membership.

Also, this issue has the first in a series of articles by Past President Bob Ross. Be sure to catch this one and the ones that will follow.

Start planning now in attending the 2007 ICBC Conference in Annapolis, Maryland. We will have updates in our newsletters.

Get creative—and submit some articles!!

Ray Hanson
Newsletter Editor



BUSINESS BROKERAGE AND THE INTERNET

By Bob Ross, MCBC

Twenty years ago I would advertise a retail business, a service business, and a manufacturing business each Sunday in the Dallas Morning News classified ads section. So would all of the other brokers in the area. Business Opportunities ads were a full page and a half on Sunday. Today there are usually only about two columns. Back then the phone would ring on Monday and Tuesday with a few buyers calling each week. As time went by fewer and fewer potential buyers were calling and there were less and less classified ads. It was costing me about a \$1,000.00 per month. This was in late 1980's dollars.

Today, we live in an electronic world that is dominated by the internet. Nearly everyone who is involved in the sale of a business has their own web site and also has their business listings posted on several additional sites. Based on two recent polls, the average broker is participating in six web sites. The average monthly cost for these averaged slightly less than \$250.00. We talk about how all costs are going up. Advertising businesses for sale has actually gone down drastically. What other expense in your business has been reduced to one-fourth of what it was even a decade ago?

If someone walked up to you today and said "If you will give me \$500.00 I will bring you a real buyer for one of your listings," I do not know anyone who would not take him up on this deal immediately. Most web sites cost you less than \$500.00 per year and we get upset if we only get one buyer that actually purchases a business in a year's time. Searching for real buyers is just like fishing. You must continue to cast out the bait. The more hooks you put in the water the more fish you are going to catch.

My point is that if I were going to go back to active brokering I would have my business listings on ten or more web sites. I would still only be spending less than half of what I was spending on newspapers twenty years ago. Web sites do not work like the old days of the classified ads. The classified ad was good for 2 or 3 days at the most. The internet web sites work 24/7 and 365 days a year.

Another thing that I have noticed is that the quality of the buyer inquire has improved from most of the web sites I used. One web site, that will go nameless, produced a lot of "tire kickers" toward the end of my brokerage career but I continued with them. After two years of paying their monthly fee a real buyer contacted me. He purchased a business and I made a commission of \$87,500.00. During those first two years I had paid them about \$750.00 with nothing to show for it. If I had stopped using them, look what it would have cost me. Patience and diversity is what I am preaching. Individual web sites are really very inexpensive and they all pay off in the long run if your listings are properly presented.

This is the first in a series of articles on how to get the most out of the internet that I have been asked to write by the ICBC board. Since I am in the web site business with my Brokers Network Group web site (a commercial for my site) and maintain the ICBC web site along with several other web sites I do have an internet background and experience that can help you get more out of the internet.

I am working on future articles on the difference in what benefits you get from different types of brokerage web sites; how to make your company web site work better for you; and other ways to use the internet to improve your efficiency and save you time and money. If any one has a topic related to the internet that they would like for me to discuss send an e-mail to bobross@bbn-net.com.

Next Time: Getting More Traffic From Your Internet Ads

Bob Ross is immediate past-president of ICBC. Even though he has retired as an active broker, he is still involved in helping brokers, with advice and assistance, who participate in his company's web sites.

Failing to Fail

By Monty W. Walker, CPA, CBI, BCB

So much is said about the wonders of becoming an entrepreneur while so little time is spent discussing the fact that failures do and will occur. The key question to be pondered by every person who may choose to pursue an entrepreneurial path is --- What if I fail?

You see, failure to some is the inability to grow their business to the level they want. Failure to some is the inability to meet the opinions others have of them. While for others failure is the necessity to close the business down and suffer some financial loss.

It is this sense of potential failure that keeps many people from pursuing their entrepreneurial dreams.

Oliver Wendell Holmes was quoted as saying:

“What lies behind us and what lies before us are small matters compared to what lies within us.”

This is a truism which rings loudly for Entrepreneurs.

The thought of becoming an Entrepreneur is somewhere in the recesses of most people’s mind. The “What-Ifs”, The “I bet I cans”, The “I know my idea is good”, ring in the ear of most people at some point in their life. Some people react and take control of these thoughts by taking the path less followed and begin to pursue their entrepreneurial calling while others take a less risky path and do nothing only to find themselves years later in life simply saying --- I wish I had _____. With this being said, becoming an Entrepreneur is not a calling meant for everyone.

People who decide to pursue an entrepreneurial activity, especially those who decide to Start a Business, must be willing to accept failure. The failure of a company is a gut-wrenching experience for an entrepreneur. Though failing will teach a person a lot about what can go wrong in an **entrepreneurial** venture.

Microsoft, one of the nation’s most successful companies, looks for people who have failed because these people add significant value to Microsoft because of what they learned when they failed. They know what can go wrong and thus they will most likely not travel the path which they know can lead to failure.

Failure is not an end. Many entrepreneurs who don't succeed the first time do indeed try again. They often bring to their second venture a wisdom, business savvy and humility that may have been lacking in the first venture.

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The one thing inside every entrepreneur that will ultimately help lead him or her to success is the ability to stay the course even when failure is eminent.

Entrepreneurs who fail often come to view failure as a valuable learning experience. For these people, they do not let their business failure cause them to fail personally. They realize that it is not their business that makes them who they are but it is who they are inside that is most important.

For these people and many like them ---- The only real failure is not try.

So for entrepreneurs:

Any failure that lies behind them and any opportunity which lies before them are small matters compared to what lies within them because it is what lies within that will ultimately lead them to success.

About the Author:

Monty W. Walker is the senior principal of Walker Advisory Associates and Hutcheson Walker Advisors. These firms provide strategic business and transaction advisory services to the closely-held business market with the focus of Hutcheson Walker Advisors being innovative retirement strategies. Monty Walker works with Entrepreneurial clients throughout the country advising them in the areas of Business Transactions, Business Structuring & Design, Business Tax Planning and Business Exit Planning. He can be found on the Internet at ---- www.waa-online.com

**ICBC CONFERENCE
Wednesday, September 19th – Saturday, September 22nd
Annapolis, Maryland**

The ICBC Board Members and I are very excited as we plan ahead for the upcoming conference. This will be a great setting to network and renew old and not-so-old friendships. Your spouses and friends will love the trip here, as you will find abundant waterfront dining, entertainment, shopping, and sites to see. May I suggest that you come early and/or stay after the conference. However, some advance planning is needed, if you intend to do so. The Naval Academy has home football games on both the Saturday before the conference and Saturday 22nd, our last day. If you enjoy college football, you will want to be there. Make your weekend reservations as soon as possible. The Historic Inns book well in advance for these events. You will be pleased to know that the Naval Academy, the football stadium, and everything else mentioned above is within walking distance of the Historic Inns.

On behalf of the Board and myself, Mary Ann Gray sent all members an email on May 21st requesting their input to the conference agenda. For those who have responded, we thank you. Your input will help to focus a program that meets your requests. If you have not taken the short time to respond to the survey, please do so in the next few days, as we value your input. We are currently in the process of committing to presentations and speakers. If you would like to provide input directly to me, I may be reached at 410-266-7110 or drew.smith@themortongroup.biz. Additional details of the conference will be presented next month.

Buy-sell Agreements – A Valuator’s Perspective

**By Brian A. Wendler, CPA-ABV,
CM&AA, MCBC, CFP**

May 25, 2007

Increasingly, business appraisers are being called in to value businesses whose value is subject to a buy-sell agreement. Most often, the purpose of the valuation assignment (to name a few) occurs when there is an event, such as: the admittance of a new partner/shareholder, the buyout of a dissident shareholder, buyout of a deceased shareholder’s business interest, or the purchase of life insurance in cross-purchase agreements by and among the other owners of the business. By the way, many life insurance companies require a formal valuation to insure that the appropriate amount of insurance is being purchased. Instead of the buy-sell agreement providing a roadmap in navigating the corporate and emotional dynamics that are prevalent in these assignments, it often causes confusion, ambiguity, and uncertainty. Our experience has been that most of these agreements were drafted ages ago – and usually have never been updated – so there are usually a host of deficiencies.

Because of space limitations, let’s assume in this case that the assignment is to value a deceased shareholder’s business interest. Some of the common issues usually include:

- 1) Unclear Standard of Value – How is value defined? Is it Fair Market Value? Fair Value? Book Value? Or some other value, such as Investment Value?
- 2) Undefined Level of Value - If valuing a minority business interest, are the discounts that would normally be available in gift and estate tax situations, applicable? Or, is the business interest valued on

a pro-rata share of the whole enterprise value?

- 3) Which source of business data is utilized – financials and/or tax returns?
- 4) As of Date – Is it the date of death? Or, is it the date of the last monthly financial statement, year-end, or some other date?

Again, there are usually more deficiencies than we’ve identified above, but because of space limitations, we will only review them in this space below.

1. Standard of Value

Fair Market Value

We all have heard of the most common standard of value “fair market value”, as it is applicable in most of our business sale transactions assignments, as well as gift and estate tax valuations. Fair Market Value is usually referred to as it is used and defined in Revenue Ruling 59-60

“ as the amount at which the capital stock would change hands between a willing buyer and a willing seller, when neither is under any compulsion to sell or buy, each having reasonable knowledge of all relevant facts, neither being under any compulsion to act. Court decisions frequently state in addition that the hypothetical buyer and seller are to be able, as well as willing, to trade and to be well informed about the property and concerning the market for such property”.

Fair Value

“Fair Value” is a standard of value that is most often used in accounting, statutory or in judiciary matters. Examples are financial reporting purposes, bankruptcy and shareholder disputes. Fair Value used in state statutes is usually determined from judicial decisions, as there is no specific guidebook telling one how to use Fair Value.

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Book Value

“Book Value”, net book value, or owner’s equity is an accounting convention, not an appraisal standard or method. From an accounting standpoint, it is the historical cost of all the firm’s assets less its liabilities. Valuation is a forward-looking concept – not a backward review of the historical costs of a business’ assets. It would be naïve to assume that the value of a business are the assets/liabilities listed on the balance sheet, as there may be several assets and/or liabilities that are not shown on the balance sheet, such as a host of intangible assets: patents, trademarks, or liabilities such as pending lawsuits, etc.

Other-Investment Value

Investment Value is the value of an asset or business to a specific or prospective owner. Accordingly, this type of value considers the owner’s or prospective owner’s knowledge, abilities, expectations of risks, earning potential and other factors.

2. Undefined Level of Value

When valuing a minority business interest, which has been the case in many of our buy-sell agreement assignments, the question becomes whether we should apply applicable discounts, such as lack of control and marketability discounts that would normally be available in gift and estate tax situations. Or, alternatively, is the business interest calculated as a pro-rata share of the whole enterprise value? For example, if a deceased shareholder estate has a 10% stake in a business whose enterprise, fair market value has been determined to be \$1 million, is this 10% interest worth \$100,000 (\$1 million x 10%), or some lesser amount? In some cases, we’ve seen management want to apply both a minority discount and a lack of marketability discount. Carrying our example above a little further, if we applied a minority discount of 25% as well as a discount for lack of marketability of 30%, the resulting 10% interest could be worth as little as

\$52,500 (\$100,000 less a 25% minority discount), then the resulting minority interest of \$75,000 reduced additionally by a 30% lack of marketability discount, yields a 10% minority, non-marketable interest that is only worth \$52,500. As can be seen, the difference in value of the 10% interest can be substantial depending on whether the value is calculated on pro-rata basis of the enterprise value or if reduced by the lack of control and marketability discounts.

One of the greatest areas of disputes in valuations is the amounts of discounts that are applied for lack of control and lack of marketability. Interests in closely held businesses are not liquid relative to many other investments. For example, if one exclusively holds stock or other interests in a publicly traded company, it is comparatively easy, quick and inexpensive to convert the holding to cash at the owner’s discretion – usually in three business days. Such is not the case for an interest in a privately-held business. There are very few avenues to cash-out one’s interest.

On the other hand, the discount for lack of control is a succinct way of saying that investors expect higher rates of return when they cannot control the use of a business’ resources, the risk at which assets are placed, and the amount or timing of distributions. Just as in publicly traded securities, the buyer of a minority business interest is in a minority position. He does not have a say in the management of the business, cannot demand distribution of available cash flows and has no ability to liquidate the underlying assets. A buyer would undoubtedly consider these negative factors before making an investment as a minority investor. Because a minority interest would lack the elements of control that a majority interest usually can hold, it is necessary to apply a lack of control discount to the ownership interest.

Obviously, if you are the company, you would like to buy-in at a low price and sell at a high price. Applying the above discounts could

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drastically lower the value of the interest. But is this the way it should work if it is your estate that is trying to sell back shares to the company or its shareholder upon the death of a partner/shareholder? On the other hand, most businesses would like to pay a “fair” price that it can afford to pay – not pay such a high price or “premium” - that it could permanently affect the overall financial health of the business.

3. Source of Business Data

Obviously, an appraiser needs the business’ updated financial information and future outlook to complete a credible valuation, but which information do you use? It depends on which is the most reliable. We prefer accrual based financial statements as close to the date of death as possible. If it is other than near the year-end financials, be aware that the interim or stub period financial statements may not be that reliable because not all expenses and adjustments have been made. From a more practical standpoint, usually we receive the financial information that is the easiest for the business to produce, unless there is too long of a gap, or major changes have occurred from the year-end data. You have to have a cutoff date at some point. We also take into consideration information that is known or knowable at the date of death through question and answer interviews with management. Remember, the appraiser does not audit anything. However, they should make reasonable inquiries of management to cover their bases, such as inquiring if there are major lawsuits pending, undisclosed offers on the company, non arms-length transactions between shareholders and the company, non-productive family employed by the company, securing a significant contract that could be a windfall to the company, to name a few.

4. As of Date

The “as of” date in appraisal terminology is known as the “valuation date”, “appraisal date”, or the “effective date”. It means that the appraiser’s opinion is specific to that date in time - not a date that is 6-months later. This date is important because appraisers should

consider company, financial, industry, economic and other factors that are known or knowable at the “as of” date. Much of the company and financial information may be accomplished through question and answer interviews with management and an analysis of the financial statements. Remember, the appraiser does not audit anything. However, the appraiser should make reasonable inquiries of management to cover its bases, such as inquiring if there are major lawsuits pending, undisclosed offers on the company, non arms-length transactions between shareholders and the company, non-productive family members employed by the company, securing a significant contract that could be a windfall to the company, to name a few.

We have presented in the limited space above only a few of the issues that affect buy-sell agreements. Believe me there are more. We believe that it is imperative that valuation professionals be part of the team when creating or navigating thorough buy-sell agreements. Otherwise, unintended results, hardship, and possibly litigation might develop from a poorly drafted buy-sell agreement. Stay tuned for the next ICBC newsletter as we will discuss in a second article additional buy-sell agreement issues.

About the Author:

Brian A. Wendler provides business valuation and transaction advisory services nationally, across a wide variety of industries and company size including manufacturing, distribution, retail, medical, finance, engineering, hi-tech and low-tech firms. He is the principal and founder of National Business Valuation Services, Inc. (NBVS).