

Body Shop - How to Appraise

Many smaller body shop owners have asked, "How do I appraise my body shop?" In the last month I have been asked to do two appraisals on body shops. The first appraisal was to assist in partnership dissolution; the second appraisal was for marriage dissolution. (That is what the attorneys call a divorce.) Would you like to know how to appraise the value of a body shop business?

Before we begin, I would like to make one comment. Whenever a CPA has done an appraisal of a body shop, I find that their opinion of value is much greater than the actual value the market place will pay. This is not because the CPA's do not know what they are doing because they do; it is just that the market place places a much higher risk on buying a body shop than the accountants do. The following is an excerpt from one of those appraisals.

THE THREE WAYS TO APPRAISE A BUSINESS

1. The ASSET VALUATION METHOD. This method is basically used when a body shop does less than \$400,000 a year in gross income and the seller is making wages, but no real profit above what he would be paid if working for another. On this size business, a buyer is willing to pay for the assets of the business but little or nothing for goodwill. The equipment is usually worth between \$50,000 and \$100,000, depending on how many frame machines the business owns and how nice a spray booth the business owns.

I have seen some specialized shops sell for more than the above number because they have a truck spray booth or another business attached to the main business. Examples of attached business might be an auto repair shop or towing operation. Also the location, size and real estate rental amount will influence the value of any business, to some degree.

2. The second method, I call the GROSS SALES METHOD. This is used when the sales are over \$1,000,000 a year but the profit is unknown or financials are not available or reliable. Because of experience, a Body shop buyer can make reasonable estimates of future profits, if they have some basic information. The basic information includes rent, source of business (DRP, STREET, or a CAR RENTAL AGENCY), and the desirability of the location.

When this method is used, the value appears to be about 3 months sales or 25% of the last 12 months sales. This method is not very reliable on businesses with sales of less than \$1,000,000, because the question of being profitable is very questionable. Why is this breaking point \$1,000,000 in annual sales? Multi-store buyers will have well paid managers, so many figures their breakeven point is around a million.

Less than \$1,000,000 in sales is not even worth their time. Of course we know that there are exceptions to the rules. Some of the exceptions are A. when a new location will be a satellite store to a bigger location. B. The buyer must have a location in a specific area to please a DRP. C. To get rid of a competitor.

3. The third and most used method of evaluating any business, including body shops, is the NET PROFIT METHOD. This method is based on the idea that a business is worth what it generates, in profit and benefits, for an owner. Body shops, like so many other small businesses, often do not show a profit, at the end of the year. Strange, how so many businesses of different sizes all just happen to end up with little or no profit. What I find really amazing is that the IRS doesn't audit more businesses than they currently do.

As a result of showing poor profits, on the books, it becomes very difficult to use the NET PROFIT METHOD for appraising many small businesses. Luckily for me, I can quite often find hidden profits, of a business, by adding to the books, items we call owner's benefits. These include: Owners salaries, if a corporation. Personal autos and all the related expenses used by the owner and his family that are written off against the business, life insurance and health insurance for the owners.

Depreciation is also a hidden profit that is usually added back in to the taxable profit to help build up the total owners benefits. And lastly, personal utilities, phones, trips, etc. that are deducted on the tax return but are not really costs to run the business.

After saying all this, what is the value of a business based on the Net Profit Method? Automotive businesses, especially auto body shops appear to sell for between 1.5 to 2 years adjusted profit (book profit plus owners benefits added back in). Larger body shops doing over \$2,000,000 in annual sales may sell for much more, because the owner is making much more money, than just his salary and a buyer will consider part of the profit a return on his financial investment.

Very large body shops that are being bought by public corporations are evaluated primarily on their return on investment (Percentage profit that is being made on the cash purchase price of the business.) These big buyers can afford to pay between 5 times and 10 times annual net profit, after

deducting all officers' salaries and perks.

Often these, public corporations, high purchase prices include two important restrictions, which is really why they are buying the business in the first place. First: The business is bought for little or no real money. They use restricted corporate stock that is not negotiable for two years. And second: The management is required to stay and run the company for some period of years.

The bottom-line, as I see it, is that you sold your soul, not your business. One last comment on selling to large corporations; heaven help the seller who sells his business for corporate stock or the buyers bonds and the buying company goes broke or the stock market crashes. I had a close friend sell his company for mostly cash and some seller carry back financing in Dec 1997. By Feb 1998 the buying company was in bankruptcy, making the paper my friend held worthless.

CONCLUSION: Appraising a business, especially body shops, is an art not a science. No two people will appraise the value of a business the same. I am amazed that the same thing one buyer thinks is a great asset is what another buyer thinks is a major negative. Differences of opinion are what make life interesting.

About the Author

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