Front Cover

How Much Is My Web Site Worth?

Overview on how to establish the value of an Internet Business

Web sites can be bought and sold just like any other piece of property, and can have a valuation just like their brick-and-mortar business counterparts, or jewelry and art. What is needed, however, is a systematic method to place a value on Internet companies because traditional valuation processes do not always apply. This book gives a comprehensive overview of the process that explains how to establish the worth for your Internet Company. There are three primary reasons to have your business valued:

1. **You want to monitor the performance and growth of your company.**
2. **You need financial support to grow the business and financial capital from some source other than yourself.**
3. **You want to sell your business.**

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BuySellWebsite.com Publishing

Published 2003 United States of America

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Section 1: Introduction

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Chapter 1: Valuation Overview

Introduction

"Appraisal" and "valuation" are often used interchangeably. However, the historical distinction between these two words is that an appraisal can be a part of a business valuation. Normally, appraisals are for objects and property, whereas valuations are for businesses that have both tangible property (appraisals) and intangible property.

The focus of this book is on business valuations that may or may not have appraisals of physical objects. Internet businesses frequently have more intangible value than tangible value. Internet businesses, up until now, are not capital and real estate intensive businesses.

The valuation process is used to determine the worth of something – in our case it is an Internet business. There are a number of reasons to perform a business valuation:

1. To sell the Internet business.
2. To finance the business.
3. To establish the progress of developing a company by periodic valuations.
4. To establish the value of an Internet business to be transferred at the death of the owner.
5. To establish the value of business for insurance reasons.
6. To establish the value because of legal reasons i.e.: divorce, minority ownership position change and etc.

We need to define property and objects that are to be appraised or evaluated. There is no question that real estate is property and that it can change hands and have value. Real estate appraisal has had a long history and is well established. The appraisal process has a validation process because there are numerous properties bought and sold which help establish the appraisal value.

The subject here is Internet businesses. The questions we are trying to answer pertain to the fact that the Internet is a new medium of exchange where the nature of property and the value of that property need to be delineated. We are dealing with some tangible objects of an Internet business and many intangibles. For a start, we can turn to the dictionary for denotations of the words relating to appraisals and valuations.

Formal Definition of Appraisal and Valuation:

The definition for any property, tangible or intangible, can be approached in a variety of ways. The issue we are facing here is that Internet businesses are a new phenomenon and the dictionary does not yet use Internet businesses in the definition examples of the word "appraisal" and "value."

Nonetheless, referring to the dictionary definition can be very useful in understanding what valuation and appraisal mean in the context of Internet business. The dictionary definition of appraisal, appraise, valuation, valuator and value are as follows:

Appraisal:

? An act or instance of appraising, a valuation of property by the estimate of an authorized person

Appraise:

? To set a value on: estimate the amount of
? To evaluate the worth, significance, or status of, to give an expert judgement of the value or merit of

The appraisal definition refers to property. Therefore, once we have the definition of appraising, we need to understand the definition of property. The dictionary definition of property is as follows:

Property

? A quality or trait belonging and especially peculiar to an individual or thing
? An effect that an object has on another object or on the senses
? Virtue
? An attribute common to all members of a class
? Something owned or possessed, specifically: a piece of real estate
? The exclusive right to posses, enjoy, and dispose of a thing: OWNERSHIP
? Something to which a person or business has a legal title
? One (as a performer) under contract whose work is especially valuable

An article or object used in a play or motion picture except painted scenery and costumes

Valuation

? The act or process of valuing specifically: appraisals of property
? The estimate or determined market value of a thing
? Judgement or appreciation of worth or character

Valuator

? One that valuates, specifically one that appraises

Value

? A fair return or equivalent in goods, services, money for something exchanged
? The monetary worth of something: marketable price
? Relative worth, utility or importance

? A numerical quantity that is assigned or is determined by calculation or measurement

What we are interested in here is that property belongs to someone or some company. The owner has the exclusive right to possess, enjoy and dispose of a thing (property). It has to do with ownership of the thing (property). The other element of property is that the work is especially valuable. This could also give the Internet business value in addition to the property that can be touched – which would be like an art object.

The art value here is related to that increase in value that will cause the business to be worth more in the future. Investors are not looking to buy an Internet business and hang a portrait of that business in an art museum. They will want to know the "emotion" the business will elicit from potential customers. Therefore, particular attention is paid to the intangible aspects of an Internet business.

Art Appraisals

Appraisals in the art business are an essential part of that industry. Most people do not want to sell something to determine the value--especially if all they want is a value number for insurance purposes. Art is renowned for being rife with fake property. Therefore, one reason to have an appraisal is to determine the authenticity of an art piece.

The art can have greater value than the materials that make up the object and the labor that it took to create the artwork. Therefore, it is necessary to establish what an art object is worth. This must be accomplished with parameters, which are not dominated by materials and labor costs. Artwork has established markets where the objects are sold and these property exchanges help in the process of determining the value at any given moment for an individual art object.

Real Estate Appraisals

Appraisals in the business world have to do with determining the worth of the business as it relates to the future financial capability of the business. Therefore, there are a number of aspects to a business valuation. The business investor wants to know both the economic worth of the business at present and what the future projected value will be. There are two fundamentally different kinds of assets in an Internet business: tangible and intangible assets. Thus, some portion of the Internet business valuation is like a real estate property, where the value is mostly tangible. And there are elements of the Internet business that are like art, where most of the value is intangible. So in an Internet business there are real estate property parameters to measure (tangibles) and art appraisal types of parameters to measure, (intangibles).

So Internet business appraisals are a mix of real estate appraisals, art appraisals, and traditional business appraisals. Some of the appraisal is subjective and "in the eye of the beholder," while another aspect can be concretely compared to similar businesses that have been sold on the Internet. In order to create a model of how to evaluate Internet businesses, we can reference concepts used in all three of the appraisal processes.

The nature of Internet business valuation is a combination of several approaches. The task here is to look at the past, and adapt and invent as needed to derive meaningful valuations for the Internet business world of today.

Business Valuation

The valuation process for an Internet business is complicated by this fact that the business is comprised of the intangibles of an art form-- more than traditional business-- coupled with some real property and some traditional business. It is that balance that must be established in order to have a relevant and accurate valuation.

There are a number of business types. The types of businesses we are most interested in are the following:

1. Traditional businesses
2. Internet businesses
3. Combination of Traditional and Internet businesses

Traditional businesses are those that need brick and mortar property to conduct transactions with customers who physically walk through their doors.

Internet businesses are those that only interface with customers electronically, either via the Internet or telephone.

A combination of Traditional and Internet businesses are those that have both brick and mortar stores and can also conduct customer interactions by electronic means.

A. Traditional Business Valuation Overview:

1. Traditional business valuations have many elements, including financial audits
2. Financial audits give a substantial view of a traditional business
3. Traditional businesses have industry standard values to draw from if value is to be determined
4. Lots of traditional businesses have already been sold over the years

There is not much in the form of art in most traditional businesses, though there is some intangible property, such as in high technology companies B: Internet Business Valuation Overview:

1. Valuations are a form of audit
2. Financial audits give a financial view of the business, but not a complete business view
3. Valuation can come in many varieties and levels of completion.
4. Valuations give a more comprehensive story then just a financial audit
5. The ultimate valuation is an auction or a sale
6. Auctions are only valid for the people in the auction
7. A different set of people at an auction will give a different result

8. The ultimate use of the valuation process is as a business improvement tool

C: Combination Internet and Traditional Overview:

1. Valuations will be far more difficult
2. Accomplish one valuation for the traditional portion
3. Accomplish one valuation for the Internet portion
4. Combine the two valuations into an integrated process

Internet Business Valuation Requirements:

Valuation requirements are not an exact science at this point in the Internet business arena. Different uses of an Internet business valuation are evolving and will eventually level out and become standardized.. As the Internet ages and business models solidify, we will likely find that most of the reasons for doing a valuation are already established, since they are predominately driven by human nature's need to ascertain value. Our fundamental need for valuation will remain a constant, even in this emerging technology. What will change, however, is the language we apply to the Internet's specific form of valuation and its process.

The requirements for Internet business valuations will be addressed in this book by answering a series of questions. Future releases of this book will begin to list the exact requirements for the purposes and the process of accomplishing the valuation.

Why should an Internet Business accomplish a valuation?

The Internet business owner should use the valuation as a way of determining whether the business is making progress towards increasing its net worth. The work of valuations can be accomplished in real time on the Internet. This may well be the future for most of the valuations for Internet businesses. So much of the parameter data can be measured with little human intervention that the automatic valuation algorithms could be used more frequently to obtain the real time value of the business.

However, Internet businesses need valuations for a variety of reasons. There are business reasons, such as performance, borrowing and investing. There are personal reasons, including divorce and death. There are government reasons, such as income taxes, property taxes, and estate taxes. Yet the most frequent reason for a valuation is that external investors are involved in the business. These investors may have money to loan to an owner or to buy the business, but may not have the expertise of running an Internet business.

What requirements are driving the Internet business to accomplish a valuation?

Investors will probably be the first economic reason to drive a small Internet business to seek outside help in financing the company. Most entrepreneurs do not understand that personally they do not have the skills to manage the business for the long term. Skills to manage the business, after the business is established, maybe in shorter supply then financial resources. Most often entrepreneurs assume that they will be able to run the business if they just had the funding. Therefore, a dance occurs between the investment

community and the new business community. One is overstating the value and the other is understating the value. Therefore, an arbitrator may very well be appropriate – an Internet business valuator.

How often must an Internet business have a valuation?
The frequency of appraising is a function of the use of the valuation. If the valuation is for personal gratification, then the owner/creator has been growing the business and it should be often, as the owner desires. If the owner is seeking financing, then the valuation needs to be current. Current on the Internet does not mean not every few years, but every few months.

Sooner than every six months is probably too often, while once every decade is not remotely often enough. The best recommendation is to have a partial valuation often for business performance issues and a complete valuation annually.

What are the valuation process requirements for a traditional business?
The valuation for a traditional business gives us insight into valuation for Internet businesses. It will not be long before all traditional businesses will also have at least a presence on the Internet and therefore, by definition, will be combination types of business. However, we must address how much business must be accomplished on the Internet before there is an impact on the value of the business.

Some traditional businesses just use the Internet as another form of advertising. The techniques of visitors to customers will be difficult to follow in that form. Therefore, a traditional business valuation process would be accomplished, treating the Internet element as merely another advertising medium.

What are the business design requirements for a traditional business, which will impact the valuation process?
Because so many businesses today are a combination of Internet business and traditional business, most of the parameters used to evaluate a traditional business are needed to accomplish the valuation of a combination business type. Nonetheless, there are parameters that can be used directly from a traditional business in a valuation of an Internet business. This is especially true of those parameters relating to the business support structure required regardless of what kind of business you have.

Business support structure refers to the support departments of a business – shipping and receiving, procurement, finance, communications support, etc. The act of doing business requires a certain amount of business regardless of what type of business you have. There are still items to be ordered and received. There are storage issues. There are employee issues. None of these elements disappear just because you have an Internet business.

How often does a valuation need to be accomplished for a traditional business?
Most traditional businesses do not have a radical change in the performance because the business is limited by the amount of people that can walk through the door. Because the

rate of change is limited, the frequency at which the business must be evaluated for business worth is not as high as an Internet business.

Audits of traditional businesses only occur annually and are really closer to financial audits rather than business valuations. The owner is probably not looking to sell the business, and the local banker can obtain sufficient data from the financial statements to determine whether a loan to the business is risky or not.

Internet Business Systems and the Valuation Process

If valuations are to include the future value of Internet business systems there needs to be an integration of the two. The Internet business structure allows for a lot of the concepts of a valuation process to become automated. Once the process is automated, the process can be used to help make business decisions. This is because the value is available in real time. It further allows business owners to explore potential scenarios to help predict how they should modify their business for increased performance.

Valuation parameters need to be measured. The importance of some of these parameters can be implemented into the design of the Internet business. The parameters that can be automated will be identified later. There are two types of parameters: absolute and arbitrary. The absolute parameters are things that can be measured with certainty and these can be automated. The arbitrary cannot be measured with certainty and cannot be automated.

In what Internet business would this valuation process apply?

This valuation process was started to determine the value of Internet businesses that one of the authors owned. There was no intention in the original design of the process to include traditional businesses. The nature of the Internet is changing and as time goes on there will also be a move to include the traditional business valuations because these business are arriving at a point where they all have Internet activity that is more than just advertising. The question is how much Internet activity and whether that activity has a significant contribution to the overall success of the business.

The Internet business allows for many valuation parameters to be measured automatically. Therefore, is it less difficult to measure these parameters in Internet businesses than to measure similar parameter values in a traditional business. So for the moment this valuation process is addressing mostly the Internet portion of the business.

How does the valuation process account for businesses that have a substantial traditional business component?

Traditional auditing and valuation processes of traditional businesses still apply. Over time, this element of the business will also be integrated into the total valuation process. It will become increasingly difficult to separate what element of the combination business caused the increased income.

The reason it will become more difficult is because the advertising in traditional advertising media will impact the Internet portion of the business and the Internet will help the traditional element.

How is the current buying and selling of Internet businesses incorporated into the valuation process?
The Internet offers places were every hour of every day there could be an auction. The buying and selling of anything is the only way to validate the real value. There must be an event where someone is willing to pay for that object at some price. That price has to then be reflected into the valuation process.

In the real estate market there are usually several other comparable properties that have recently sold and are used for comparisons. No two houses are exactly alike and no two businesses are exactly alike. Some judgement needs to be made as to how the comparison values reflect on the present business that is being evaluated.

This is accomplished on the Internet by tracking valuations and selling prices of businesses that have already been through the process. Competent valuator thus far reflects this knowledge. This type valuator has been in the business and understands the meanings of some of the parameter values that go beyond what mere automation of the valuation process would provide.

Can accountants develop all of the business parameters needed for a valuation?
We have used accountants in traditional businesses to evaluate and audit parameters. Many accountants have gone on to understand and include the more subjective elements of the process. However, numbers are just numbers until some emotion of the business is captured and put into the numbers. The numbers that accounting creates can take some of the emotion out of the buying or investing process, but those numbers will not reflect the emotion that can be generated in the marketplace.

There needs to be an integration process that takes the absolute parameter values of the accountants and integrates them into the arbitrary parameter values of the marketing department of the business. It is this integration that allows for a greater understanding of the company. There are accountants that can learn this integration process.

What is the process of accomplishing a valuation on an Internet business that only has a service and no product to offer to their customers?
A service is a product that does not need a manufacturing element to support. It is a product that once delivered is hard to find in the business it is delivered to. It is a product that does not necessarily have intrinsic value because it exists.

There are a lot of service businesses on the Internet, such as consulting. There are also a lot of services offered on the Internet that are an extension of a traditional business (i.e., medical advising by doctors, consultation and document preparation by lawyers, etc.).

The service may or may not be delivered over the Internet. But the income parameters are the same whether the deliverables are products or services. At the end of the day, the business expended a quantifiable amount of dollars to attract the business and the business received a measurable amount of dollars for delivering the product or service. Either there is more income than what went out or more expenditure than income. What matters is the efficiency of the logistics between the expenses and the income, as well as how much emotional and physical effort was involved in the process of accomplishing the business.

Chapter 2: Historical Perspective

Historical View of Valuations

As long as humans have exchanged goods and services there have been appraisals of the value of the goods and services provided versus the cost of obtaining those goods and services. The valuation process happens every time you go to purchase any item. You may not accomplish a formal valuation that is written down, but you will have accomplished one nevertheless. Most times this purchase process is accomplished by some emotional decision without the support of more detailed numbers.

It is not difficult to make these valuations if you know a lot about the goods and services that you are trying to purchase and the goods and services are items that you are familiar with on a daily basis. However, it is a different story when you must purchase or invest in a new technology or business type that you do not know well. It is far more difficult to determine if the deal is good or bad without access to someone who can translate this new business into ratings and words that you can recognize and understand.

The valuation profession is divided into categories of the items that need to be evaluated or appraised. A common set of these categories is:

a. Business Valuation
b. Gems and Jewelry
c. Machinery & Technical Specialties
d. Personal Property (art)
e. Real Property (houses)

These are broad categories of items. Some of these categories are more organized and regulated than others and some appraisal specialties even require a certification process. Nonetheless, all categories require a person or persons knowledgeable about the subject being appraised. Business valuations may require several specialties to arrive at an accurate business value.

Some non-profit associations have developed standards by which valuations and appraisals should be accomplished. Internet business valuation processes are being built on that foundation. The Internet is such a fast moving industry that specific standards are going to be difficult to pin down. However, the fundamentals are close to those in all business valuations. The single objective of the valuation is to achieve a consensus about the value of the Internet business value. All valuations need to contain five fundamental elements:

a. Come to a conclusion (a dollar value or range of dollar values)

b. Consider applicable relevant information (parameters in this valuation process)
c. Accomplish appropriate procedures (algorithms in this valuation process)
d. Consider appropriate conceptual approaches to compare the values generated to historical data (rating in this valuation process).
e. Write an appropriate report to document the findings and results (reporting in this valuation process).

Traditional Business Valuations and Audits

The surprising collapse of many large traditional companies can show how difficult it is to measure the value of a company from the outside. Large conglomerates are even hard to evaluate from the inside. The financial numbers can be manipulated to fool most people for a period of time. All these failures indicate that an investor needs more than just the financial numbers to know the value of the business. The integrity of the present management is also a factor in determining the value of a business. Along with knowing that, the board of directors is also independent of the management and can correct abusive behavior.

There are just some fundamentals of the business that need be established, regardless of the business type or category. These fundamentals must be continuously monitored. Some businesses can change rapidly while others change more slowly. Notwithstanding business performance is either going up or going down. The static state does not hold very long because uncontrollable, external stressors on a business are changing. If the business does not change in response to those external events, the performance of that company will change.

A business valuation or appraisal can be accomplished from a number of different viewpoints. In the past, these approaches have been:

a. The asset-based approach
b. The income approach
c. The market approach

The type of business helps determine the approach. In the case of an Internet business, we need to understand that physical assets do not drive many of these businesses. After all, you can set up a business with a table, computer and Internet connection in your home. You don't even need a chair to sit on if you don't mind standing up. The physical resources can be very minimal. Your storefront can be located on some other company's server if you are only selling electronic information. The shipping and handling can be electronic.

The other two traditional approaches to business valuation are income and market. If an historical perspective is taken, then this process here is an outgrowth of a combination of income and market approach specifically tailored to the Internet business. As valuations evolve and traditional businesses devote large portions of their businesses to being Internet business, then the valuation will need an expanded approach concept that

borrows processes from existing valuation approaches to develop new and more applicable valuation processes for these developing business entities.

There are two excellent measures of the survival rate of a small business in the marketplace. These two measures are the amount of income a small business is making and the longevity of the company. By this metric, young businesses not making very much money will fail. At least one out of every two will fail within two to five years. But companies that have been around for a few years have a substantially higher probable survival rate than companies less then two years old.

So what is the goal here? Make more money and stay around long enough to reduce the probability that you will fail. When your business surpasses the one million dollar mark and you have been in business longer than five years, then your probability of failure within the next five years after that is less then ten percent. If you are in the category of less then ten thousand a year and less then two years in business, then the probability goes to the fifty-percent range for failure within the next five years.

Poor business management is the most frequently sighted reason for business failure. The valuation process developed here provides the business owner an objective way to know and understand the progress of developing the business so that the probability of success goes up as the income goes up and the longevity increases. Moreover, you have to have the income before you can have the longevity.

Business valuations have been going on as long as there has been business and those businesses needed to be bought or sold or needed financing. The valuations may have come under different names, but nonetheless it is still a valuation process. What is different in the Internet business world is that portions of the valuation process can be used as an automated business management tool to measure and ascertain the progress that the company is making.

Real Estate Appraisals

Most homeowners are familiar with this appraisal process. They may not have understood the process or the report. This is especially true if the value of the appraisal resulted in something different than expected and the bank required a greater down payment in order to secure the mortgage based on the low valuation. This process is accomplished by comparing similar homes that have recently sold in the neighborhood. Where this process becomes very subjective is when there have not been many homes sold in the neighborhood that develops the equivalency to the home.

This is the issue we are working with on Internet business valuations. The neighborhood has not been around very long and there have not been numerous businesses changing hands to develop a database to validate the valuation process. However, as this market approaches the age of ten years of activity, this lack of comparisons will decline substantially.

The difference is that most Internet business value is not in real property (tangible). These businesses do not hold a lot of real estate. The value is in the intangible elements of the business.

Personal Appraisals (Art Appraisals and similar objects)
Art, for example, may not have similar comparable items to help establish its value. Internet businesses are in many respects an art form at this stage of the business development cycle. We don't quite yet know how to categorize these businesses. There is some mystique about how these businesses even hope to operate and whether they really work. After all, what do most people know about electrons flowing around the world and the underlying technologies that make this happen? The vocabulary of the Internet core technologies is not even understandable by most people using the Internet today.

Therefore, in some respects the Internet business has some art appraisal issues (intangibles). It is not the cost of the canvas and the oil paint that makes the painting valuable. The same is true with the Internet small business. There can be considerable value without necessitating real or personal property to create and substantiate that value.

Present Perspective of Business Valuation History

The Internet creates a new type of business. Creating a new type of business may or may not change the way valuations and audits are accomplished. The history of this period, when reviewed in the future, will tell us for sure whether the Internet was a technology watershed that radically changed the way we accomplish business and the way we evaluate those businesses dominated by Internet activity.

Yet we do not have the historian's luxury to wait twenty-five years before we decide whether we should be changing the way we accomplish business valuations. We are in the midst of the transition, and there is every indication that it will have substantial impact. On account of this appearance that this technology will continue to change and will have an enormous impact, we need to develop the tools that allow us to evaluate and appraise the worth of these new types of businesses now.

Internet Business Valuations
Internet business is not yet a decade old. Yet many businesses on the Internet have become household names. Many have promised much and returned nothing. Returning nothing is not a new characteristic of business. More businesses fail than succeed, especially if they are small and young. Picking the few winners is what the investment business is all about. Moreover, picking winners is based upon a track record. It is hard to have an historical track record when we do not yet have even a decade of business for the total industry--not to mention that most of the companies in existence today where just not here in 1995.

It is predicted here that the Internet business will change the frequency of the valuation process, and the amount of instant data will modify the valuation and audit history. We

have had ways to track customers in the past, but electronic transactions allow a whole new level of data availability. This data availability will need to be translated into something with perspective, or the sheer volume of numbers will overwhelm the valuation process and we will return to guessing. This return to guessing will occur because the data will not have meaning to the individuals accomplishing the valuation process.

Most especially, business owners and investors will not understand what they are being told if there is not an education process simultaneously developing with the expansion of this branch of the business valuation process. There will be a new set of parameters created for measuring; a new set of algorithms for processing those parameters; and a new set of ratings established so that non-technical people can understand and make intelligent decisions based on the information provided.

The language of the final numbers of what the value of an Internet business will be - will probably not differ much from the language used today to describe traditional business. What will change is the intermediate language of the report that addresses the parameters, algorithms, conversions and ratings used to get to the final number. The language will be an outgrowth of the core technologies being applied to the Internet today.

One of the major shifts of the valuation process will be the revolution of real time data and analysis. It is the real time nature of the parameter measurement and application of the algorithms that will move the appraisal from a primary financial tool to a business management tool.

The Internet business may drive the definition of business property. The intangible element needs to be discussed in depth before that definition has meaning for more then a few people with specialized knowledge. We have real property and we have personal property. However, what will we call an Internet business that is dominated by intangibles? What kind of words will we use to designate the assets of an Internet business and determine the value?

Some elements will be real estate and some elements will be personal. Then there is the bulk of an Internet business: intangible property. So much of what has value in this setting is more like intellectual property. This asset has value because it can be used to generate income. When all is said and done, we are after income and will need to figure out how to describe the assets generating that income.

Chapter 3: Business Types

Overview
It is helpful to differentiate business by type. Different business types will be treated differently in the valuation process. This chapter addresses the types of business of interest when discussing accomplishing valuation of Internet businesses. It has already been mentioned that this book is addressing three types of businesses:

a. Internet Businesses
b. Traditional Businesses
c. A Combination of the two businesses

There are established valuation methods for addressing traditional businesses. Valuation of traditional businesses can be challenging at times, even though valuations for these types of business have been accomplished for decades. The novelty of the Internet makes the valuation of the other two types of businesses more difficult because we do not have historical data to help solve the problem. This is especially true for valuators unfamiliar with the Internet and the dynamics of the Internet in sufficient detail to allow accomplishing a valuation of these types of business.

This chapter addresses each type in more detail so that the reader can begin to identify the business type and valuation approach appropriate for their own business.

All systems have limitations. Understanding the larger system within which the valuation system is being described helps the reader understand the valuation system process limitations. This will also allow the reader to know and recognize when the process is being used outside the original design boundaries.

Traditional Business Type
Overview
Customer Interface
Marketing
Advertising
Support Systems

Overview
If you took business classes in college you will know about the traditional types of businesses. These are businesses that existed before the Internet (prior to 1995). There are many different categories of these kinds of businesses and numerous books written about many different forms of these businesses. There are courses taught on how to manage many of these companies and financial and performance norms for most of these businesses.

These are the businesses that you frequent often in your city that have a brick and mortar storefront. These may also be businesses that you have dealt with through receiving catalogs in the mail. They may be the businesses that manufacturer the products you use both at home and at work.

Customer Interface, storefront, phone, operating hours

The traditional business has a storefront, which allows the customer to physically visit the company. When there is a physical storefront the interface with the customer is controlled by how and where the doors are placed to allow customer access. There is signage that must be in place to direct the customer to the store.

Traditional businesses normally do not have much of a discussion about whether the phone is answered or not. Someone generally answers the business phone. This is because the phone call is often about immediate concerns – like how do I get to your store – or do you have a certain item in stock. Phone interaction is normally about immediate sales in one form or another.

A traditional business is not about using the Internet. So primary forms of communications with the customer are in person, phone, fax and mail.

The operating hours of a traditional business are dictated by local custom and what the competition is doing. We must note that hours for all businesses are getting longer. Staffing physical spaces to directly interface with customers or answer the phone is expensive.

For example, the cost of a bank transaction in a physical bank where a teller interfaces with a customer lies in the dollar per transaction range. Having the customer interface with the bank through an automatic teller machine puts the cost of transaction in the half-dollar per transaction range. Having the customer interface electronically over the Internet puts the cost in the low pennies per transaction range. Not all bank transactions can be accomplished over the Internet, but when it can be, there can be a substantial cost reduction.

Nevertheless, a traditional business must supply the support for the customers' preferred method of interface in order to survive in the marketplace. Sometimes the telephone is the only way to interface with the customer; therefore staff is necessary to answering the phone.

Using the phone as the major form of communication has advantages and disadvantages in terms of the cost and the benefits. If you are in the retail business, then that is probably the one link you have to the customer other than foot traffic. If you are in the manufacturing and distribution category, then communication with your customer base is more complicated because it is distributed over a wide area and is more complex.

A lot of the business internal direct calls can be handled by voice systems of one kind or another. In contrast, the customer needs to have some understanding of the options for contacting your business.

Support Systems

No matter what the business type, support systems, which allow the business to function, need to be in place. Support systems are about managing the business' resources to enable the company to be efficient at accomplishing its objectives. The types of support systems we are talking about here are:

a. purchasing
b. product control and distribution
c. manufacturing
d. receiving
e. shipping
f. finance
g. facilities
h. employees relations

All businesses need to have processes that allow these functions to be accomplished. In a small business it may just be the business owner and the procedures are not written. However, most often the procedures need to be written. Written processes allow for the everyday events in the business to be repeated in a standardized manner. Customers want consistency and that is what procedures accomplish, if followed. Successful traditional businesses will have these procedures because it establishes management of the business. Failure is most often a management event.

Written procedures and policies are set up to handle the routine tasks that must be accomplished almost every day in a business.

Items for every business need to be procured, necessitating purchasing. Purchasing means spending company money. Spending company money needs to have controls, such as an approval process.

The product control and distribution system involves the items being sold. These items need to be stocked and displayed in a traditional business. Displaying the product to the customers can be a very expensive item for a traditional business. The other limitation besides costs is the space required for displaying the products.

Manufacturing issues are the same whether the business is an Internet business or a traditional business.

Receiving product is also the same for traditional and Internet businesses. It is the shipping that is radically different. In the traditional retail business, the customer takes care of the shipping to his/her place of need. In an Internet business, the product needs to be delivered by some third party shipping method.

Keeping track of the finances is a straightforward task until you consider government regulations and laws. Then those things that used to be simple can become very complex because every decision appears to have a tax or legal liability or both.

If you are just starting a business and do not have an accountant, keep all the receipts and an excellent accountant can help figure out what you did in your business from a financial viewpoint. You will need this when it comes time to interface with government tax departments.

If you are a small business, there are plenty of systems that can either use paper to account for your financials, or if you are so inclined, use a computer to record and balance your finances. You will not need a full financial department – just someone responsible for this element.

Account receivables are those monies that others owe you for product or services rendered. This is one area that small businesses need to consider. Delays in account receivables can mean the difference between success and failure. A small business most often does not have a lot of operating cash available to carry through the very rainy days. For a traditional retail store, the account receivables are customers in the neighborhood. Securing account receivables from the neighborhood is lot easier than over the Internet.

Facilities to accomplish the business in can be radically different between the traditional business and the Internet business. The facility for a traditional business needs to have a physical space, which needs to be cleaned and repaired immediately. The Internet business can be a facility that has very little beauty.

Employees in a traditional business have to come to the business and have to be somewhat local in order to work there. That is not true of an Internet business, where the employees can reside all over the world.

Internet Business Type
Overview
The definition of an Internet business, for the valuation process, involves the inception point where most of the income is derived. Internet businesses have a very different customer interface than traditional companies. The marketing and advertising are very different. The storefront is very different.

The characteristics of an Internet business system are such that there are some very marked differences between traditional business and an Internet business.

System	Traditional Business	Internet Business
Customer Interface	Physical storefront	Electronic storefront
Customer communications	Face to face, phone, fax, mail	Electronic mail, phone
Hours of operation	Local	24 hours/7 days a week

Purchasing	Person	Person
Finance	Person	Person
Employees	Local	Worldwide
Marketing	Local	Electronic
Advertising	Local, newspaper, TV, radio, brochures, sales persons	Electronic
Facilities	Local	Anywhere
Shipping	Local	Anywhere

Internet businesses are in the early development stage and the exact characteristics have not yet been defined. Therefore, the following discussion about Internet businesses is in a questions and answer format. Frequently Asked Questions (FAQ) is a common and useful tool for Internet businesses. The FAQ technique is often used on the company web site.

How do you recognize and categorize businesses into business types for valuation of an Internet Business system?

Many elements of the Internet business system are in development. One of those elements is the business valuation system. The Internet business systems did not existed prior to 1995. It has only been in the last couple of years that Internet businesses have grown and have been operating for enough time to determine that a valuation system was even needed.

The two main types of Internet businesses today, from a valuation viewpoint, are those that only use the Internet and those that are a combination traditional business and an Internet business. These are further divided into businesses that provide a product and business that provide a service. There are also those businesses that provide both products and services.

The industry is not yet old enough to determine additional types and categories of Internet business from a valuation viewpoint. However, just like traditional businesses have many categories, so too will Internet businesses. Data will aggregate to substantiate the valuation process as businesses are bought and sold.

What constitutes a successful Internet Business system?

The rating process used in the valuation system will help identify a successful Internet business. This will be especially true if the valuation is accomplished on a periodic basis. The history of the business's performance will be established. Valuations are looking backwards in time at historical data. Valuations are normally not used as a predictor of the future. A business can be successful in the past and have used up all the market availability and therefore not be successful in the future. This rating--comparisons to other companies in the marketing niche--is far more difficult to ascertain for Internet businesses today because there is not enough historical data. The question of having a successful business will be established by using multiple valuations of the same and comparisons, where available, to other Internet businesses.

What constitutes a failed Internet Business system?
Internet businesses fail when they do not adhere to business fundamentals in making business judgements. Nevertheless, how do you know about an Internet business system? There is one excellent indicator of failure: No Visitor Traffic. If there is no visitor traffic to the web site, there is no possibility of success. Therefore, one of the first indications of Internet business failure is a lack of web site traffic.

The effort to get visitor traffic is another indicator. Many dot com business like Amazon.com had enormous losses trying to establish market share. Holding market share on the Internet has to be built on more than just startup advertising and operating losses. There also needs to be fundamental business support systems to insure that the business will not fail. There has to be some unique element to the business in order to survive. This uniqueness impact is discussed in Chapter 7.

What is the average length of time for an Internet business system to become profitable?
Just because there are millions of people on the Internet does not mean that your business will have access to all those customers. All markets should be treated as niche markets in the beginning. If you want to have a profitable business, you need to find 200,000 to 700,000 people that are accessible in order to have a niche market. You can measure this accessibility on the Internet by reviewing the company customer electronic newsletter mailing list. If you have that size market and a series of products or services that can be repeatedly sold to this market, then within two to three years a business can see some profitability.

Do Internet businesses all have the same industry category from a valuation viewpoint?
The top category is Internet business and from that standpoint they are all in the same category. However, when you start to look at the number of visitors at a web site for different businesses you will find a few with millions and millions of visitors. Most Internet businesses, for example, are not in this category. Small Internet businesses can have a lot of visitor traffic, but most businesses are not in that kind of traffic category.

The number of links and the types of businesses that will allow linking also helps establish the category of business your company is in. Having good links to other successful complimentary Internet businesses is also an indicator of a successful Internet business.

Do Internet businesses need different industry valuation criteria depending on what products or services are being sold?
The valuation criterion has two basic elements: the parameters and the value of the parameters. The parameters may be the same but the value needed to be a successful small Internet business is radically different from what it takes to be a large Internet business. Therefore, there will be different success criteria for different kinds of Internet businesses.

One of the success criterions needs to go back to the competition in that niche market. The competition will help establish the values in the different parameters. Furthermore, the analysis algorithms will have different coefficients applied.

How are the algorithms of the analysis of arbitrary/absolute parameters changing from product category to product category in Internet businesses?
Parameters, algorithms and ratings are used in a valuation process. The parameters may mostly be the same for different niche markets of Internet businesses. For example, there is the parameter of number of visitors, which is applicable to all Internet businesses. What will differ are the coefficients of the algorithms and the ratings comparisons to other companies in the same niche market. For instance, it may be that two small Internet companies are addressing the same market. The comparisons of these two companies would be radically different if you were accomplishing the comparisons for two Internet businesses that were addressing radically different niche markets.

The need to use Internet businesses in a valuation that are addressing radically different markets will only be a short term problem with the valuation of Internet businesses. Categories of Internet businesses will emerge and comparisons of two companies that are selling fish, for example, online will become more doable.

How will the shipping of the business products to customers be handled?
When it comes to getting physical products to customers the delivery of products for Internet businesses will be similar to the mail order catalog business. In the case of the mail order catalog system, there is a catalog. In the case of an Internet business, there is a catalog online. The catalog online is part of the web site.

When the product can be delivered in electronic format, then the shipping of product to the customer has a form and method not found in traditional businesses. It is this selling of electronic products that makes the Internet such an interesting marketplace. People still need to have specific information, even though there is a lot of information available for free on the Internet.

How will the financial department be set up?
The support systems for an Internet business are really not much different from those businesses that are traditional businesses. In this case, the receipt of payment from the customer and qualifying the customer for credit are long distance functions. The advent of credit card security over the Internet has substantially improved the capability of Internet companies to sell their products.

The addition of systems like PayPal has markedly increased sales on the Internet. PayPal is a third party collector of account receivable for a fee. There are public auctions like ebay that have essentially made credit card merchant accounts available for millions of people.

It was not long ago that getting a merchant account to do business on the Internet was almost impossible. Now it is normal.

How will the account receivables be handled?
Account receivables is a must for any business. If the customers are all hundreds or thousands of miles from your business and you have accounts that are not collected, it becomes very difficult to accomplish this element of your business. That is why Internet businesses are generally not in the business of extending individual credit to customers.

If account receivables are in arrears, it is a red flag in any business, but this is especially true in an Internet business because the customers are not local.

Will the company answer the phone?
You will find on the Internet today companies that do not publish a phone number. Time will tell if those companies will succeed in the marketplace. It was not long ago when we would not buy gas at the local service station if we had to use a credit card at the pump and to pump our own gas. Now that is the preferred method by many customers and these customers will drive past a gas station that demands that we go inside to pay.

At this juncture in Internet business development, it is imperative that customers have multiple methods of contacting the Internet business. One of the most common today is the phone. However, having a phone interface means that someone needs to answer the phone.

How many hours a day is the phone answered by a person?
Needing to answer the phone is a double-edged sword. If you answer it, then it costs money. If you do not answer the phone you may miss important communications that will change visitors into customers. There are some products that can be sold without a personal interface. If that were not true the auctions on the Internet, that have become so popular, would not be so successful.

Therefore, answering the phone has an impact on a business valuation, but depends on the kind of products the Internet business is trying to sell. Some products and services need the personal selling, others do not.

What business processes will be used?
It is important to have business processes that help make decisions easier and tasks repeatable. There is a portion of the valuation that comes back to the question, "Is this a professional web site?"

A professional web site is the integrated process of an Internet company. The more complete the processes are within the Internet business, the more complete the web site. An experienced valuator will learn a lot about a business just from the web site. The web site is the first process that a customer will see. If that process is complete, then the business support process can be examined for completeness. If the web site is disorganized, then the supporting business processes are not of much value.

Will there be business policies and procedures set up in order to handle most routine tasks in the company?
The routine business interfaces to the customer should be on your web site. The customer should know how you want to do business. Having the customer interfaces defined with your policies on how to accomplish business with you is not everything. However, if there is a professional web site, then there will probably be other policies and procedures intact in the Internet business. Having the right product or service will help determine if a business will succeed. More important is having the right management; a professional web site is an indicator of the management capability.

In how many ways can you deliver your products to your customer?
Product delivery can happen in a number of ways. What is important is that the customers know that you are working to deliver the product. What is neat about Internet businesses is that it is easy and inexpensive to send the customer notification of how and when the product has been shipped. This is true whether it is a physical product that UPS is delivering or an electronic product that you are delivering electronically.

How quickly are unique, Internet business parameters changing as the Internet is changing?
It was one thing to be unique with a traditional business. It is quite another to stay very unique very long on the Internet. Copycats abound. People are willing to take your web site code in a heartbeat.

Nonetheless, there is a uniqueness that most copycats never quite get and that is consistent quality service and products. If you have the intent to go the distance and develop a clientele, then your business will succeed. Moreover, uniqueness will need to be developed and created over and over again in this marketplace.

Combination
The combination business is one that has both the traditional storefront and an Internet storefront. Many companies will fall into this category. They first will use the Internet as an extension of their advertising campaign, then determine that the Internet can be another revenue stream.

How are businesses characterized that have half their business from the Internet and the other half from a traditional business?
There are methods to evaluate traditional business and, with this book, we have a way to evaluate Internet businesses. As time progresses these two valuation techniques will begin to merge as companies begin to integrate the Internet as part of their business.

Therefore, some businesses started as traditional business and decided to expand to the Internet and now have half their business there. The other end of the spectrum is starting as an Internet business and finding that it is advantageous to find more customers to open an additional interface to the customer by opening a traditional business.

At this point, the valuation process treats these two ways of doing business as separate businesses. Algorithms do not exist to integrate these elements into a single analysis.

What are the characteristics differences in an Internet businesses from traditional valuation processes?
The dominant difference between the two different types of business comes down to being dominated by the customer interface. The interface differences are in communications, marketing, advertising and exchange of goods and services and the methods that are used to pay for those goods and service. Take those elements away and a lot of the business support structure needed for a traditional business is also there for an Internet business. The exception is that having the right kind of physical facilities in the right locations does not drive the Internet business.

What are the differences in customers between traditional businesses and Internet businesses?
Customers of traditional businesses are seen. Customers of Internet businesses are never seen. You do not know for sure whom you are dealing with as an Internet business. If the communication is all done electronically, you really do not know whom you are dealing with. This may not be important as long as you get paid, but how do you know what your customer wants next in goods and services?

What are the differences in customer loyalty between traditional businesses and Internet businesses?
Loyalty is about giving your customer reasons to do business with you again. We are not talking about the human nature of doing business. This human nature of business is not always very clear as to the rationale of what has transpired.

Loyalty for traditional business can be controlled by location. The competition needs to establish their business in your neighborhood. This is not true of the Internet. The neighborhood is the world.

Nevertheless, it has been shown repeatedly that there is such a thing as brand loyalty if you have a replicable way to reach your customers with items they need and want to buy.

Is there a difference in the rate of acquiring the parameter information between the traditional process and the Internet business systems?
A number of items in the traditional businesses are easy to measure. These include the items that are within the control of the owner. What happens at the customer interface level is far more difficult to evaluate. This is where it becomes more difficult for the average traditional owner to have the same level of data as is available on the Internet about the customers of those businesses.

What is the cost difference of understanding the valuation parameters with a traditional business versus an Internet business?

The cost of getting traditional business data is enormous, while the cost of getting Internet data is very inexpensive, easy and efficient. This is why Internet business valuation will eventually become the way to manage Internet businesses.

Are brick and mortar traditional businesses easier to evaluate and appraise then Internet businesses?
Traditional businesses are harder to evaluate, when gathering the data, than in analyzing the data after you get it. The opposite is true of the Internet business. It is easy to get a lot of data, but it is hard to understand what the data is telling you. The reason Internet data is more difficult is because we do not have a very long history to help put the valuation information in perspective.

What elements of the valuation and valuation process for an Internet business is much easier to accomplish than a traditional business?
Gathering electronic data is much easier with the Internet than with traditional business. Tying this data back to known customers is substantially easier. It may not turn out to be important, but we can begin to build a story of how we got where we are. The above is true of some parameters. Arbitrary parameters that require human intervention to gather and understand are as difficult in an Internet business as in traditional business. All of the arbitrary parameters can be difficult whether it is a traditional business or an Internet business.

Systems
What percentage of the business' income needs to be accomplished on the Internet before a company is considered an Internet Business system?
There is a continuum between traditional business and Internet business as to the combination types of business. Time, we believe, will show that there will be many levels of this combination type of business form. Traditional businesses that have existed for decades will figure out how to use the Internet effectively for their business.

For the purposes of this book we are mostly talking about businesses that are Internet businesses. These are businesses that have no storefront for customers to enter the business establishment. That is a pure Internet business in this discussion. It turns out that it just doesn't make much difference what the amount of traditional business you have is. The Internet business can be treated as a separate identity from a valuation process. If you own a traditional company and are using the Internet to increase your business for local walk in traffic, then the Internet is like another form of advertising for the traditional business. If the customer has to come to the physical storefront to acquire the product, then the Internet is an advertising tool.

Even though a local market, for example an automobile dealer or a large apartment complex, dominates the business, they will find ways to have their customers interact with them through the Internet portion of their business.

These businesses will have to rethink how they compensate their sales people if they pay on commission. Who gets the credit if most of the sales work is accomplished over the Internet?

How is an Internet Business system different from a Traditional Businesses system?
The dominant difference between the Internet business and the traditional business is the interface to the customer. The second dominant difference is the physical facilities needed to operate the business.

If the business has a substantial traditional business component, is the business evaluated as two separate businesses?
At this point in the development of the valuation system, the valuator uses two different approaches and generates two different values of the company. It is treated as two separate and distinct profit centers.

How quickly are traditional parameters that can be used to evaluate an Internet business being modified because of the changing Internet environment?
Even traditional businesses need to rethink their vocabulary when it comes to the customer interface. Customers who require interface will require time and effort on someone's part within the company. The types of people in the business will be changing.

Uniqueness
How fast do the marketing trends occur in an Internet business that makes it unique from a traditional business?
Core technology changes on the Internet occur faster than in a traditional business. Therefore, the time frame in which marketing events and advertising events happen changes the business strategies. Customers that would come last month to your web site won't come this month because there is nothing new for them to see.

This is true unless the product you are selling is a consumable and the customer is not interested in new data as much as consistent and repeatable service to supply that product.

Chapter 4: Integration: Business Systems and Valuation Processes

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Overview

Business valuations have been viewed as single events that are used to determine the value of a business when there needs to be a change in ownership, there needs to be more investment into the business or a list of other reasons. The advent of the Internet has changed business in that a lot of the data needed to generate a valuation can be generated automatically. Numbers by themselves need interpretation. It is the interpretation of that data that needs expert analysis.

It is because of this reduction in effort to acquire the information that more energy can be expended on the interpretation of the data that allows this business valuation tool to be considered as a management tool. This can be a management tool that can be used often to help manage the business and the employee tasks that need to get accomplished. The valuation is not a total valuation but a limited portion of a very complete valuation.

Valuation as a Financial Tool

Overview

A number of things can be accomplished with a valuation as a financial tool. One of the firsts is to know the value of your business. You have created something and you do not know what it is worth. You may not want to sell or get third party financing – you just want to know what it is worth so that you know what your business creation performance has been.

The next instance that you would need a certified valuation is when you want to grow the business and you need to convince the investment community that you have something worth investing in or loaning resources to.

The next is that you need to sell the business to move on to other things. Or you may want to sell your company through an auction. You need to know before the auction instead of after the auction the minimum price you will accept. You may want to set a reasonable minimum price before the auction begins.

Knowing the Worth of Your Business

The income you receive is one thing, but what is the business worth? Circumstances change rapidly on the Internet. Your business can be going great one day and not the next. There are slow times and there are fast times. It is not clear yet on the Internet when the slow times are; what is a normal business cycle. It may be that your present slow condition will change just because the overall activity on the Internet is down.

There are a number of reasons to know the present value of your business. Some of these reasons are as follows:

a. Understand how your company ranks in general on the Internet.
b. Know how your company ranks in your selected niche market.
c. Understand how the site traffic impacts the value of your business.
d. Know whether the value of your business is better this year than last year.
e. Establish realistic business goals in your niche market.

You set out in building your business for some reason. The reason was most probably more than just making money. Moreover, there was some dream that you had before you went to all this work. A valuation is about knowing some of the milestones along the road that helps keep you focused on your original goal of building a business and building that business well. This is about knowing what you have done in more concrete data form and knowing you have a process that will help you establish realistic goals and how you are making progress in reaching them.

Growing Your Business

You want to grow the business, but the business needs more resources. This is a critical stage of every company. It is answering those fundamental questions about what size of company do you want in sales, in employees, in market penetration, and etc.

If you decide that your business goals are realistic in your niche market, and now you want to grow the business and need more resources – what do you do? This is in addition to having all the right business plans.

This is when a valuation can become a very valuable tool in your quest for more resources. It becomes an even more powerful tool if there is a track record of valuations that show progress toward your realistic goal. You can use this to show what has been possible and what the potential return of this investment will be.

What financial implications to borrow resources would occur if the value of the company fell below certain level?
Now if you borrow the resources and the next several valuations show you are going in the downward direction, there can be implications to your loan just like there would be in a traditional business. Banks don't like loans that are not repaid. Loans are just their product just like you have product to sell.

There may be no bad consequences for you if you can continue to make the loan payments and the business is the collateral. If the bank uses the business as collateral and they ask for a periodic valuation to show that the collateral is still in place, then the consequences can be the same as investment in the stock market when you have borrowed money on margin and the stock value goes down. If the stock price goes down the collateral goes down and you must find additional monies to support the margins.

Selling Your Business
There will come a time when you will want to sell the business. Your children are just not interested in running the business and you want to retire. Or perhaps you just want to go do something else in life. Now you need to establish the value of the business. If you have not been accomplishing periodic valuations, then the first one may come as a surprise.

The surprise could be either way. The business could be worth more than you thought or it could be worth less than you thought. It will only be worth whatever someone will pay. Nonetheless, you need a value to start with when beginning to talk to potential investors or potential owners in your business. Valuations give you a starting point. They give you references as to how your business value rates compared to other Internet businesses.

Tax Implications of Valuations
Two things in life are certain: death and taxes. The government is always looking to know where the money is. Where the money is, dictates where the taxes should be, according to the politicians. All governments have endless needs for financial resources. Businesses are just one of those resources. Sometimes government agencies demand a valuation to establish the worth of a business. These normally are very complete valuations.

What impact does the valuation have on taxation by local governments?
It is not clear what the local implications of an Internet business are. We are sure that the local governments will figure it out. There is a general cry already for local governments to tax the Internet business community in some manner.

Time will tell all the creative ways this will occur. Normally it takes governments about 14 years to figure out how to begin the taxation of a new technology. We are about at that stage for the Internet.

It is not yet clear how valuations will impact these kinds of local government taxation issues.

What impact does the appraisal have on the estate of an owner who passes away?
The rules of estate taxes are in transition. The value of the Internet business may be tough to pinpoint. For instance, where is the business located? Internet businesses can reside in many locations. It does not even need to be in the same country. There will be legal battles in the years to come to establish what the estate of an Internet business is and where that jurisdiction resides.

A valuation is just one element in helping decide how much the estate is worth. Nonetheless, the value could be zero in a short period of time because of the rate at which the Internet business is changing. Courts take a long time. In the length of time taken to resolve the issue the company will probably cease to exist.

Valuation as a Management Tool
Overview
Using the valuation process, or part of the process, as a management tool for the business is a concept that can have validity only in some businesses where the process can have some form of automation. If there is no automation, then it is a costly tool because it will need to be completed often enough for information to allow real-time decisions to take place.

Would a business owner consider a valuation as a management tool?
A business owner who wants to grow the business will always be looking for additional management tools. The primary reason that businesses fail is because the business did not have the right management.

There is another truism: That which is measured – improves. If your employees do not know what is important to you they will not accomplish what you want. Knowing the direction of value is important. This will be especially true if you tie employee compensation to the value of the company. This has happened over and over again in traditional companies. Companies have given their key employees bonuses of one kind or another in relation to the stock value of the company.

Incentive for Employees
It has been an eternal quest as to how employees should be motivated. It is also true of business owner. Business owners need to know the direction of their business in order to be motivated. Value of the company is one way to determine where you are on the journey. This is true no matter who is associated with a company. We like to be associated with the up-and-coming successful companies. We like to universally bash the big and strong companies that were once our heroes.

Would a business owner consider a valuation as an incentive to employees that would get a bonus once the company arrives at a given value?

Small businesses look for all kinds of ways to attract and retain key employees. Internet business valuations accomplished on periodic bases, which are related to bonuses for the employees, should be a consideration in today's marketplace.

Establishing Marketing Strategy

Parameters used in the creation of the valuation very well could be tools from a management viewpoint to allow a valuation of the marketing strategy. The parameters can be used in an automated method to create and analyze. This data then would need to be compared to past marketing strategies and determine the effectiveness of the present strategy.

Customer interface is not everything in a business, but it is a sure guarantee that if the business has no customers to have an interface with, then there is no business. You don't have to be an Internet company in order for that to be true.

A close look at the parameters discussed in later sections will lead to the conclusion that some of these parameters and analysis can be very useful in accomplishing a limited valuation on just the marketing strategy. If this is so, then the marketing strategy will have a valuation rating that can be used to improve the performance of the company. It is like having a valuation inside a valuation.

Valuation of Advertising Campaign

The advertising campaign is an extension of the marketing strategy. Measurement of the parameters of visitor response used in the valuation process can also be tied to the advertising campaign if the advertising campaign has tags placed in the advertising so that you know where your effectiveness is being accomplished.

This effectiveness has to do with visitors being converted to customers and customers being converted to repeat customers.

Determination of Customer Satisfaction

One of the more extensive elements of a valuation is to determine customer satisfaction. The contrast of this is the lack of customer satisfaction resulting in a lack of business. Automation of customer satisfaction is not entirely possible. Someone needs to look at more than numbers only. One needs to look at the words and decide what the tone of voice is in the written responses. One of the difficulties of the Internet is that it is sometimes hard to read the emotions of the customer.

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Chapter 5: Valuation Functional Parameters

Overview

There are three categories of valuation parameters we want to discuss in this chapter. These involve the business, marketing and finance valuation parameters. In order to accomplish a business valuation, data is needed. A systematic approach to identifying and collecting the data is important. If the valuator does not have the appropriate information from which to create the final value of the business, then we are back to the "garbage in and garbage out" routine, which doesn't do anyone any good.

If you determine what data you need to create the valuation and whether that data is represented by nameable parameters, then the task of collecting the data is much easier. Now, if you know whether those parameters are absolute or arbitrary, it helps in the valuation process. In addition, it will become apparent that some of the valuation parameter values will change at a faster rate than other parameters. Knowing which parameters change the most frequently helps determine the periodicity of the measurement of that parameter. If the data is changing quickly, then the valuator must look more frequently at the latest values for those parameters if he or she wishes to have a valid valuation. This constant, rapid change also places a limit on how long the valuation is good for before obsolescence sets in.

Business Valuation Parameters

Business parameters have to do with the business structure needed to support the business. There is some minimum set of functions that need to be in place to have a business at all. The validity of the business can be determined by examining these parameters to determine if the fundamentals of the business structure are adequate to support the mission statement of the Internet business.

Some, but not all, of the business valuation parameters are as follows:

a. Business stability
b. Time in business
c. Management team
d. Maximum to minimum income ratio
e. Hours of business operation
f. Financial resources
g. Number of employees
h. Organizations structure
i. Business operating policies
j. Customer satisfaction

Business stability is a parameter that in some respects is subjective and in other respects is absolute. There are a number of interrelated valuation parameters that go into a figure of merit about how stable a business is. In the end, the bank or investor wants a yes or no answer to the question of stability. This is because stability comes back to risk of failure. It is the risk that needs to be quantified and a plan made to mitigate that risk to tell the investor that it is a known risk and the business knows how to control or avert it.

The amount of time a company is in business is one parameter that is used in Internet business valuations. No business can claim that they have been in business for a century, or for that matter a decade. Therefore, as a buyer of an Internet business, you do not have any comfort with this type of business being a long-term existing business with a history of values that have been recorded and established. So here the time in business is measured in single digit year numbers. If a business on the Internet has been there less then a year, then there is a need to look at the management team of the business. If the management team has had a track record someplace else, then it may be possible to correlate something to this new business. That is assuming the past businesses and the present business address the same market niche.

The management team and the board of directors (if it is a corporation) are very important elements. This is because most businesses fail because of poor management team than for any other single reason. Boards of directors need to be independent.

Looking at the maximum to minimum income ratio gives a reflection of the month-to-month volatility of the business. It may be that the business, by nature of the products being sold, is that kind of business. Nevertheless, large fluctuations in income indicate that the business is notably more unstable than one in which the income variance is small. Stable businesses are built on repeat customers that have learned to trust the business. There is seasonal variation that needs to be accounted for, but all business in that market niche will reflect the same variance.

Customers for an Internet business are more global than for a traditional business. Therefore, one needs to consider the hours of operation and how the interface with the customer over the Internet will be accomplished. Most unique products require some other form of customer interface than the Internet. This denotes that someone must interface with the customer. People are still people and would like to talk to someone, especially if the product is very unique. Therefore, the hours of operating the business need to be considered. The stability of the interface to the customer is important. If the customers are worldwide and they must always use off-business hours in their time zone to talk to someone in your company, then this will impact the value of the business.

If the day-to-day operation of the business is cash flow restricted, then the flexibility of the business to respond to variations in the marketing responses will be stressful and limited. So one of the parameters that needs to be examined from a business stability factor is the financial resources needed to meet day-to-day operations.

The number of employees and how these employees have been organized have a reflection on the stability of the business to meet changing business needs. There have been many studies of small businesses that show the greater the number of employees, the more stable the business.

The business structure of how the employees are organized to accomplish business is very important. This valuation parameter has to do with how information flows in the company, especially if we are interested in how information flows in response to applied stresses on the business. There are fundamentally two different organizational charts in every business. There is the one that the top leader draws up and says this is how our company works and there is the one that people follow when the company is in a stress mode and needs to solve the problem or suffer severe consequences. The further these two organizational charts are apart from each other, the lower the morale of the employees. The published business organizational chart is sometimes affectionately called "the thin line" and how the company really works, when it is stressed, is called "the thick line."

The business valuation parameter that addresses business policies comes back to a very basic fundamental, which is that businesses that have written procedures and policies which employees read and follow will generally do a lot better than business that don't have effective procedures and policies in place.

The overall customer satisfaction with the business, the product and the way the customer must do business with the company is an important valuation parameter. This is separate from the specific customer complaints about a specific order. These go back to the fact that the business has long termed customers and those customers continue to provide repeat business.

Marketing Valuation Parameters

Some of the marketing valuation parameters related to web site visitors and customers are listed below:

A. Visitor/Customer

1. Visitors/Customers
    a. Number of
    b. Threshold number of
    c. Repeat visits
    d. Visitor to customer conversion ratio
    e. Number of visits before purchase
    f. Time on web site
    g. Value

2. Visitors directed by
    a. Search engines
    b. Other web sites - links

c. Non-Internet advertising

It is easy to determine the value of an Internet business if nobody visits the web site; the value is zero or close to zero. Your web site needs to have visitors before they can become customers. Seldom do first time visitors turn into customers. Normally there needs to be more than one visit by the potential customer before the status of first time customer is achieved.

Your web site can have lots of visitors and never have a customer. Just because some search engine directed visitors to your web site does not mean that those visitors are targeted potential customers. It is not yet clear what the rate of conversion is for web site visitors. We need to develop the conversion data over a lot more businesses than what we have today to begin to know what the numbers are for conversion of visitors to customers. There are claims of high conversion rates, but the average will always be low single digit numbers. When mail order was king the business was happy with a one-percent return. One half percent was not a bad day.

It appears that there is some inertia to a web site from a number of visitors' viewpoint in order to succeed as a business. There appears to be a level where your business has enough recognition that you get visitors at a regular and constant rate depending on the niche market you are in. Therefore, there needs to be some minimum level of visitor activity before anything begins to happen with your Internet business. Furthermore, this rate of visitors needs to be over some period of time.

There is beginning development of the number of repeat visits a potential customer must make to your web site before there is a commitment to spend money with your business. There needs to be a level of trust established. This is a parameter that an Internet business needs to track as a figure of merit to determine the daily performance of your business.

The ratio of visitor to customer conversion is another important parameter to understand about the value of an Internet business. The total number of visitors divided by the total number of customers is this ratio. It now depends on whether you can sort out how many of the visitors are repeat visitors before turning into customers.

Therefore, you have the number of visits, the number of visitors, and the number of times the visitors visited before converting to a customer. All of these parameters are very important to understanding the efficacy of your business marketing strategy and advertising campaign.

Another parameter that can be measured is the amount of time that the web site visitor is spending at your web site. If this time is less then ten seconds, there is not much going on in terms of connecting with that visitor. Visitors will read long copy if the long copy is addressing their particular issue that they need solved.

At the end of the day, we have to get back to how we value the customer. It is about how many sales and what those sales totals are. We need to answer whether there can be back-end sales to improve the value of the customer to your business. A business cannot overpay for potential customers too long, or the business will have a cash flow problem.

The value of a customer is not only what that customer has spent with your business but also how much discretionary income the visitor possesses in order to spend something on your products. This is where you need to understand the limits of your customers before committing to paying too much for acquiring them individually. Therefore, if a customer is worth tens of dollars a year, that is one scenario, but if the customer is worth thousands a year then the approach can be radically different.

Visitors can come from a variety of sources. In the initial days of the Internet the source of your customers for an Internet business would only be from marketing on the Internet. Since that time it has become apparent that we need to have a more comprehensive advertising campaign to expose your business to potential customers. Therefore, as one of the valuation parameters, it is important to look at the other aspects of attracting potential customers.

Today's advertising world requires payment no matter what method is used to attract customers. The eternal battle as to, which of these methods is the most cost-effective, will not end just because the Internet is the new way to reach the customer. You will find web site addresses on the side of shipping trucks today instead of phone numbers even for traditional businesses.

B. Web site

1. Design Issues
    a. Professionally designed web site
    b. Customer friendly web site
    c. Domain name
    d. Browser compatibility
    e. Web site load time
    f. HTML
    g. Meta Tags
    h. Web Site Description
    i. Images per page
    j. Image file size
    k. Page file size
    l. File transfer rate
    m. Server space

2. Language Use
    a. Spelling
    b. Grammar
    c. Language use

d. Different languages
e. Acronyms
f. Specialized vocabulary
g. Slang use

Your web site has a number of design issues that show up as valuation parameter drivers. A web site is not just a web site that can be put together any way you can. Web sites need to have some marketing thought associated with the web site. There needs to be an integrated strategy as to how visitors and customers navigate your web site to find the information that they need.

The first issue that needs to be addressed is the need to have a professional web site. This is a subjective parameter and the value that is needed to reach this level is constantly changing. What was a professional web site in 1995 is not a professional web site in 2002. This will continue to evolve as Internet technology evolves. But your web site needs to be attuned to the niche market and needs to have some fundamental elements to be viable in the marketplace.

The domain name needs to reflect the niche market that you are in. It needs to be recognizable and average customers need to be able to at least have a shot at remembering the name or knowing how to find the name with the right kind of search. It will become more and more difficult to have short, memorable names. Therefore, your domain name needs to be a logical name that potential customers would think to ask for in a search for your company.

One of the downsides of the Internet is that you do not have much control over the way your potential customer will look at your company's electronic brochure. You do not choose the browser or the hardware that the customer will use. Therefore, what looks good on one computer will look very bad on another. Even the display size is different for each customer. Testing is essential to effective web site design.

Although fast Internet connections are more common, it is still not universal in the United States. Therefore, web site load times are critical. Fancy, high bandwidth web sites are still negatively impact business valuation processes. Long load times are directly related to very short patience on the part of the customer.

The use of the HTML coding for web sites is becoming more and more derived from the web site design tools rather than being learned by the programmer of the web site. Nevertheless, there is a need to understand the code because in understanding the code you can create more efficient web site designs.

Meta tags and the web site descriptions are ways to help people find you in the use of search engines to get to the right information for the potential customer. These items can have a significant impact on the ability to find your business. It is these kinds of fundamentals that will make or break the business.

As much as we like images, there is a price to pay for them: bandwidth. The more images you have and the more complex these images are, the longer the download to the customer's machine. A great deal of attention needs to be paid to the use of images. Images can be powerful communication tools, but they can also destroy the customer interface patience.

The trend is toward smaller page sizes so that the customer does not have to download so much information at one time. Making multiple versions of a site available is one option for inviting the user to select the ideal site format for their system. Yet there is constant debate as to what is the right way to display information. Short copy is easier to digest than long passages and smaller pages with good navigation allow a quick load and the ability to consume the information in smaller increments.

The total size of the web site impacts the server space required to host it. But this is not as much a driver as to business valuation as it once was.

There are a number of language issues related to the web site and the value of the Internet-based business. These issues include the use of a language typically used by the potential customers. These issues include the fundamentals of any language, including spelling, grammar and language use. When the Internet only belonged to technical people, there was a considerable margin on the use of the language. Most of the regular users were thinking of other topics than how they used the language.

As the Internet moved from a technical communications tool to a marketing tool the need for improved language skills increased. Now the Internet is easy enough to work on so that even very non-technical people use it daily. The view of non-technical people can be radically different from technical people when it comes to the use of language. Here now we are talking about business and the language usage needs to have the fundamentals of spelling, grammar and language use. Place these elements in the context of niche marketing that is being addressed and you can hurt the value of your business by using language that does not have the fundamentals. It does not need to be perfect – only serviceable.

The Internet is global and you may need to have several language versions of your business web site. The use of multiple languages can impact the value of the business. For example, you intend to sell to a country where most of the potential customers do not speak English. If you don't you use their language, then this is equivalent to having zero visitors.

There are the special aspects of a business where acronyms are common. If you know your customer base and they can handle the acronyms, then it is all right. Though generally it is better to stay away from that use of the language. If the valuator has trouble reading and understanding your web site, then he will not think much of your business.

Every niche market has a set of unique and specialized words. A definition page on your web site is in order to accomplish education about your business.

The use of slang is not appropriate in today's Internet business unless that is what your customer base is using to communicate. You need to know your market on this issue. Still, generally speaking, slang will decrease the value of a web site. It just does not come across as professional.

C. Web Site Marketing Parameters

Web site marketing parameters are divided into three categories: web site links, web site advertising and search engine/keywords.

1. Web site links
    a. Link content
    b. Link friendly
    c. Non-competing link
    d. Competitors – two links away
    e. Link page rank
    f. Link popularity
    g. Link promotion
    h. Link ranking
    i. Quality site link
    j. Dead/Failed links

There is a whole marketing and advertising strategy that must be thought through in order to have links be a friend of your business and not a detriment to it. The nature of the links on your web site can tell a lot about your business. A very knowledgeable Internet business user will characterize your business in just a few moments by noting and following the links that are on your web site. You are known by whom you are associated with in the Internet world. You are also known by whom you are *not* associated with in the Internet world.

The use of links can lead customers away from your web site or towards your web site. You can find that by chasing down the links from your web site to the next two links away that your customers are slipping out your link doors to your competitors.

Therefore, before you use a link to some other place on the Internet, you should not only visit the link but also the links from the first link. Also know that just because you visit a link today and found no competitors there, it does not mean that tomorrow there will not be a competitor's link there.

The site that you are linking to will not help you if there is no visitor traffic to that site. Because no one knows about it, links from that site will not come to you. Therefore, you need to understand the overall ranking of the linked web site in terms of visitors. More specifically you want to understand if the visitors to that web site have any interest in

what you are selling. Just because you have visitors to the web site does not mean that they are targeted visitors to your marketing niche. Therefore, the value of your business is not increased with that link.

There needs to be a balance between too many links and too few links for your niche market. Sometimes there are so many other links on a web site that the customer gets confused as to what the web site is selling. There are some of the web sites that have just turned into an advertising page for other companies. If that is the intent of your business, then that is all right. If that is not the intent of your business, then that is not all right and it impacts the value of your business.

The quality of the web site is also of concern to your business value. If you associate with very unprofessionally presented web sites, then that image is reflected on your business. Quality in this sense is in the eye of the customer.

One of the most customer unfriendly elements you can have on your web site is to have links to dead or failed web sites, known colloquially as "link rot." It is very annoying and deterring result of site design negligence. You will lose value and credibility in a very short period of time if you do not keep your links updated.

2. Advertising
    a. Individual page value
    b. Product placement in web site design
    c. Advertising resources applied
    d. Advertising campaign effectiveness
    e. Customer exhaustion – no more customers
    f. Long term advertising campaign
    g. Changing customer needs and habits
    h. Targeted traffic parameter
    i. Best selling products
    j. Selling other's products
    k. Evolutionary product path
    l. Re-directs

There is a marketing strategy and an advertising campaign. The advertising is the tactical work of making something happen to draw in potential customers. Businesses have had numerous ways to advertise to potential customers. Each method has pros and cons. All cost money to make it happen. It appeared to early Internet business owners that advertising on the Internet was cheap and easy. There were millions of customers and they would succeed with very little effort in attracting those customers.

That is when the reality set in. The initial potential customers on the Internet were seekers of information--not buyers of products and services. The people on the Internet were primarily technical people who were normally not in the business of buying

products. The second reality that set in was that all the potential customers were not the same as the number of customers that would be available for a niche market.

With those two reality checks, it became apparent that advertising was still needed and that we needed to learn a whole new advertising medium to very different potential customers that responded in different ways to that advertising. Nevertheless, the fundamentals of advertising are the same as other mediums. You still need to find the target customer. It is still hard work to make that happen.

Now we are down to finding what works and what doesn't work to bring in customers. Web sites are normally made up of pages. Not all pages sell as well as others. Some may need to be there for contact information and have no product data at all. Each page of the web site has a different advertising value. Therefore, it is important to know the advertising pulling power of every page of your web site. Too much information is just as detrimental as too little to the value of an Internet business.

It is not only important to the value of the business where on the page the product is placed. If the customer needs to scroll down the equivalent of several pages to find the best selling products – your company value just went down as well.

The amount of advertising resources applied to attracting customers cannot be zero. If an Internet business claims no advertising dollars in their expenses, then reality has not come to that company – yet.

The effectiveness of the advertising campaigns needs to be established. In the purest sense it is that you spent this much money and acquired this many customers. Still, it is never that simple and measuring and understanding the effectiveness of the advertising campaigns is very important to the value of the Internet business.

An important parameter if you are an investor or outright buyer of an Internet business is whether the market has been saturated for the product being offered. If the market is saturated and there is no more growth in the marketplace, then the future value of the company is impacted. The trend line of visitors visiting the web site is one indicator. It may be that the advertising campaign has failed to identify how to reach the potential customers--not that the customer base has been exhausted.

Advertising needs to be carried out over the long term. Failure to have a long term campaign strategy is very detrimental to the value of the company. The Internet does not need a five-year strategy in advertising; it needs a six-month strategy and a process that will continue to modify that strategy.

Some products are new to customers and the customer needs to be educated to the value of the product. Having to educate customers will delay the response of customers, and therefore the value of the business. The other side of the issue about new product is the need to educate about the uniqueness that differentiates your company from the

competition. You need to measure and understand how long it takes to educate your customers. The number of visits before buying is an indicator of this effort.

Finding the targeted customer is more important than finding visitors. Targeted customers are those who have the authority and the means and the interest to purchase your products. If you conduct surveys of your customers about suitability of your product to their needs, and/or desires, then you will get a measurement of how targeted your advertising has been to get to the right customers.

Identifying the best selling product is easy. Identifying the right back-end sales products and how to substantially improve the effectiveness of your business is another issue. Nonetheless, the value of your business goes up substantially when you have back-end sales.

Another issue is whether you are selling your own product or selling someone else's. There are advantages and disadvantages to both. However, in the long term, if you are selling uniqueness in the marketplace you will want your own products. Whether you have your own product or are selling some one else's you will need a product improvement path that will accommodate the changes in the marketplace. Failure to demonstrate that path will impact the value of your Internet business.

Re-directs means that the customer goes to what he thinks is the web site and in reality he or she ends up at another domain. When you do this you lose brand recognition. It may be convenient to the technologist but it is devastating to the marketing aspects of the business.

3. Search Engines/Keywords
    a. Keywords use
    b. Keyword latency
    c. Products to keyword match
    d. Web site ranking and search engines
    e. Direct traffic
    f. Re-register

The Internet is driven by words. More specifically, it is driven by keywords. Internet technology does not care what the string of letters is in the keywords. Computers can find the duplicate of a string of letters with ease. The string of letters may not mean any thing to a human, but the computer can find it in a search mode. The keywords we are interested in here are not what the computer can do but what the keywords are that people would use to search for you and your products.

Therefore, keyword usage becomes very important to the value of the business. Using a popular keyword that is competed for heavily in the marketplace can end up costing more than it is worth to your business. Not because those who are biding up the cost are in

your niche market, but because they use the same keyword to get people to their web site to see their products.

Whole books are written on Internet search engines and how to get the most value out of this kind of tool. What it boils down to is that effective use of keywords increases the value of the company.

A search engine company ranks keywords according to those who are willing to do the paying today. Therefore you need to monitor how your customers are arriving at your web site. Are search engines directing them or are they finding you in some other way?

Another aspect of the search engine is re-registering your web site as you change it. Failure to re-register can be devastating to your business.

Finance Parameters

The finance parameters are normal accounting data that look at a company expenses, income and financial resources. It is not yet clear what the normal expenses are for a certain niche market business on the Internet. Neither is it clear what the normal income levels should be. Furthermore, the sources of financial support are not yet well established.

It is possible to add up all these numbers and balance the books, but knowing what is normal is a far more difficult task. What is needed is historical data for the business being evaluated. What is not in question, after all, is that the income and expenses have been accounted for. The question is whether the business made money in the time period evaluated.

The following are some finance valuation parameters:

1. Expenses
    a. Monthly operating expenses
    b. Fixed expenses
    c. Unexpected expenses
    d. Capital requirements
    e. Debt
    f. Large one-time expenses

This book is not a tutorial on accounting. There are plenty of books on that subject. It is the value and trend of certain kinds of expenses that help establish the value of an Internet business.

There are the monthly operating expenses and the fixed expenses. With historical data these can be established. What are not so clear are the unexpected expenses in these kinds of businesses. The expense risks and variability of those risks are not yet clearly identified.

Capital requirements can be very little for this kind of business. An Internet business can really be run out of your basement office. The other side of the capital investment is the debt to accomplish the capital investment. In this case, the capital needed is more labor investment then equipment.

2. Income
    a. Income monthly average gross
    b. Income monthly average net
    c. Income multiplier over nine months
    d. Income multiplier net over twelve months
    e. Maximum to minimum income ratio
    f. Method to receive payment
    g. Credit card payments
    h. Credit card merchant accounts
    i. Fee rate of merchant accounts
    j. Account receivables
    k. Aged account receivables
    l. Third party payment collection
    m. Postal payment
    n. Third party fees
    o. Income levels

The question about income is what are the methods of payment identified and used by the Internet business. In the very beginning days of the Internet this was a great struggle because there were not secure ways to send financial information over the Internet. This issue has been largely solved through encryption– which is until someone figures out how to break it.

Income averaging helps to understand the trends of the business. The maximum to minimum income ratios helps to understand the seasonal nature of the business or the volatility of the business.

How you collect the money that is owed you and the fees that need to be paid to accomplish that task are important aspects of the value of a business. Not having a way to collect what is owed you in a timely manner is devastating. The fees you need to pay to collect the monies owed you and the lateness of the account receivables are significant indicators of business value.

3. Financial resources
    a. Financial reserves
    b. Bank financing
    c. Venture capital financing
    d. Customer finance

A reason for doing a business valuation is to establish the credibility and the need for additional financing. The financing and its reserves are very important to the building of any business, not just an Internet business. What is difficult today is to have people understand the nature and ramifications of the Internet business in the investment community.

In reality this is the same as any new technology business. Only this time it is the use of someone else's technology to accomplish business, rather then the selling of the technology itself.

Customers always finance a business if it is successful. What has not been fully explored is how customers could help a business with uniqueness, which they want, financially. This is a funding source that entrepreneurs should not overlook.

Chapter 6: Valuation Product/Service Parameters

Overview
There are measurable parameters that have to do with the product being offered and its manufacturing. Similarly, there are parameters that address the service being offered if that is what the Internet business is offering instead of a product.

Product parameters for an Internet business are not much different from product valuation parameters important to a traditional business. Manufacturing valuation parameters important to a traditional business are just as important to an Internet business. A service offered by an Internet business with the valuation parameters that measure that service are just as important and similar to the traditional business parameters.

Therefore, the parameters used in a valuation for an Internet business will not be any different from those used in the valuation of a traditional business for the most part for these types of parameters. The major difference between the Internet business and the traditional business is in the marketing and customer interface arena. You will find greater difference there between the types and methods of measuring valuation parameters for marketing and customer interfaces.

Product Valuation Parameters
Product valuation parameters involve the acceptance of the product as the customer views it. The manufacturing valuation parameters deal with the production of the products being offered. Some of the product valuation parameters are as follows:

a. Customer view of product acceptance
b. Customer view of product quality
c. Customer view of product uniqueness
d. Customer view of product usefulness
e. Shippable product
f. Consumable product
g. Product sets up back end sales

The product needs to be useful to the customer. It can be the greatest product in the world but it does not have much value if the customer does not find it acceptable. Product acceptability is an arbitrary parameter that is measured by customer surveys.

Customer view of quality is different from quality manufacturing. Quality manufacturing is about building the product to the requirements the first time. Manufacturing quality is about reducing the waste products of the manufacturing process because the process is under control and defects are mostly eliminated. The product may be designed and

fabricated with excellent quality, but that does not satisfy the needs of the customer if the customer does not need the product. Monitoring the material return department tells volumes about what customers think of the quality of your product.

There are products that are commodities, which the customer wants for the lowest price, and that price is the only uniqueness that will distinguish one product from another. The other desire of product uniqueness from the customer's viewpoint has to do with the customer being unique among his or her friends because of your product. This is measured by customer surveys to determine how customers feel about your products.

We started this discussion by talking about product acceptability. Product acceptability is a lower level of customer approval then product usefulness. A customer can find that the product is acceptable for the price that you have asked. What is being measured here is the fact that the customer wants to use the product frequently because it solves some problem the customer has.

By definition, being in the Internet business means that the product needs to be shipped to the customer. Some products do not lend themselves to being shipped by normal shipping carriers. As soon as the product has to go by freight truck instead of package carriers, the barriers to marketability just went up a lot.

There are two product-related valuation parameters that have to do with selling more than once to the same customer in short periods of time. It takes a lot of effort to get the customer the first time. Now they have bought from you and want to buy more, but the product you are selling does not get used up and you do not have any back-end sales items to present to the customer. Not having repeated sales options is a negative impact on the value on an Internet business.

There is a composite image that needs to be developed about the value of an Internet business that shows how the repeat sales are made to the same customers. The success of this marketing strategy will be measured by looking at the invoices to customers. This is an absolute valuation parameter that is easy to measure and to track. This parameter should not be a once in a great while parameter to measure but one that is measured every day or every week.

Manufacturing Valuation Parameters

Manufacturing valuation parameters have to do with the capability to create the products and to deliver those products to the customer. It also deals with using third party products for sale on your web site. Some of the manufacturing valuation parameters are as follows:

a. Product availability
b. Timeliness of product delivery
c. Quality of manufacturing processes
d. Internally manufactured
e. Externally manufactured

f. Special skills required
g. Special machines required
h. Long lead components
i. Real estate required
j. Floor space required
k. Personal property required

One of the difficulties of the Internet is that the timetable of business has decreased substantially. People do not write letters that are then sent by the postal service, have the company write a letter and then wait for the letter to be delivered by postal service. Therefore, the product availability requirements have changed. The availability has to be clearly marked on your web site. If it is not clearly marked, then the assumption will be that it is in stock. Keeping inventory in stock is not necessarily a good business practice because of the cost. So product availability becomes a valuation parameter because there are conflicting requirements. The customers want it now and the business cost reduction concept wants just in time inventory.

Timeliness of the product delivery has to do with what it takes to get the product to the customer. Normally companies do not hire the brightest employees to run shipping and receiving departments. Therefore, the business needs a systematic process of handling the shipping of product to the customer. Errors in the shipping department are very costly. This valuation parameter is measured by looking at the success of the shipping department and of getting the product to the customer.

Waste in the manufacturing process is measurable and should be used as a valuation parameter when doing business valuations. Poor manufacturing quality when the product numbers are low is one thing, but when you need to produce large quantities and the manufacturing quality is not there, then there is considerable waste and the probability of the customer getting a bad product is very high.

There are a number of issues that must be addressed when it comes to where the product is manufactured. If the product is manufactured internally within the company, then there are capital equipment issues. If an outside vendor manufactures the product to the company's specifications, then you have the issue of subcontracted manufacturing. You also do not have control over the priority of the vendor's manufacturing line and therefore may not be able to control ramp up of product manufacturing when needed.

Another aspect of external manufacturing is if you are using someone else's product to sell on your web site. Now you do not have control over that product. That may be all right if you are selling books, but it may not be all right if the manufacturer decides to get into your marketing business.

Needing special skills and machines to create product gives uniqueness but also drives costs. So the issue here is what is the impact which goes both ways. Uniqueness in skills and machines increases the cost of competition entering into your market but also drives the cost of your product. Another issue along this line is that of long lead components

that you do not manufacturer, which need to be part of your system. Long lead items manufactured by other companies for integration into your products will probably decide for you that you cannot move fast enough in the marketplace. You now have an extreme negative to the value of your Internet business if you have a need to produce product quickly.

There is also the issue of the facility requirements to accomplish the manufacturing. There is the real estate needed, the buildings needed and the personal equipment necessary to accomplish the business. Capital intensive businesses can have an advantage in some ways, but extreme disadvantages in others. High capital requirements denote inertia to the business system and inertia to the business system denotes time delays.

Service Parameters

We are familiar with services that can be rendered to a customer in traditional business. Some examples of these kinds of services are those provided by doctors, dentists, lawyers, plumbers and etc. There are many other personal services that can be rendered like childcare and housecleaning.

Therefore, at one extreme we have a traditional business that is offering a service. The service is probably local and requires the customer to come into a location to receive the service. Many service businesses are using the Internet to create additional interfaces to their customers. So the business looks more like a combination of a traditional business and an Internet business. However, the question that we need to address here is how payment is being made. If the payment is only in person at the office then the Internet is just another way to advertise. If the service is accomplished over electronic means and the payment is made through the Internet, then you have the makings of an Internet service business.

If you create an Internet business, which furnishes a service over the Internet, then you have a true Internet business. Internet service valuation parameters needed to measure this kind of activity are now different from traditional businesses in the implementation. This is true except for the people part of it. People are still people and no matter the method of interfacing with the customer there needs to be the same attention given to the needs of the customer from the viewpoint of the customer. That never disappears. We just need to find a way to determine if this remote customer is happy with the service and will return for more services.

Some of the valuation parameters of interest for measuring the performance of a service Internet business are as follows:

a. Customer base that needs the service
b. Customer view of service acceptability
c. Customer view of service quality
d. Customer view of service uniqueness
e. Customer view of service usefulness

f. Consumable service
g. Service that sets up back-end sales

Service normally denotes that the provider of the service is in close physical proximity to the customer. But the Internet business world is beginning to show that some services can be delivered over long distances. This will not be true if you are fixing someone's teeth as a dentist, but there are other services that can be rendered at a distance. The size of the customer base is what is at stake here. It is proximity that controls the ultimate size of the business. It has yet to be determined if proximity to the customer is a limiting factor in the growth of the Internet service business.

The customer needs to find that the service is at some minimum level acceptable at all. If you do not meet that requirement, then there is not much happening in terms of business value.

The quality of the service is one of those subjective valuation parameters, which needs survey answers from your customer to know that they find the quality level they need in your products.

The customer needs to be either buying a commodity whose price is the only driver or there needs to be a reason why your service is different from or better than someone else's. There needs to be some uniqueness to the service.

Once the customer has found you after looking at many other companies do they continue to come back again and again to receive your service?
If the reason they return is because they have no other place to receive the service that is one answer, but it is quite another if there is competition. This is measured by asking your customers in surveys.

Service usefulness goes beyond acceptability. The customer really does like the service and returns over and over again. There needs to be some emotion on the part of the customer that there is something really here.

There are services that are consumable and there are services that are a once in a consumer lifetime need. Having consumable services impacts the value of the company. Back-end sales of additional services also are necessary to have repeat sales to the same customers. It is not a good thing to have every sale require a new customer. The Internet business strategy for long term value needs to have repeated sales to the same customer in order to show consistent income and consistent growth.

Chapter 7: Valuation Uniqueness Parameters

Overview
Internet business uniqueness parameters address a number of different concepts associated with the valuation process. There are a number of uniqueness parameter areas that are of interest to business owners. These areas include intellectual property, marketing and products/services/manufacturing.

Patents are the most common forms of intellectual property that can be considered as uniqueness, but there are others as well.

Marketing also has areas of uniqueness in how you find unique visitors, which turn into unique customers. The unique use of keywords will help this element as well as a unique domain name that your customers can remember.

Uniqueness in the products and services offered is another form of uniqueness for the company. Patents may not protect the products and services or copyrights, but they still may have value in the marketplace because of uniqueness. This is especially true if the uniqueness can be modified with time to stay current. Manufacturing process can be unique also. These unique manufacturing processes may show up in the products as unique benefits or just in the quality of the product, which is a long term uniqueness in the marketplace.

Uniqueness Definition
Uniqueness in a business has to do with setting that business apart from other competing businesses in the marketplace. Therefore, that uniqueness definition we are seeking here has to do with the uniqueness that would be perceived by the customer. If the customer does not perceive uniqueness, then the value of the business is not enhanced. What we are seeking here are elements of the business that will increase the value.

The dictionary definition for “unique” has to do with:

a. Being the only one
b. Being without a like or equal
c. Distinctively characteristic
d. Unusual

Searching on the Internet helps to establish uniqueness if uniqueness is claimed. The effort is not as great, to verify the uniqueness, as it is with traditional businesses claim of such uniqueness. Just because a business claims uniqueness does not mean that it really

has it. The business thinking that they have uniqueness does not mean that the customer holds the same opinion.

Uniqueness in an Internet Business

The customer needs to recognize that the product or service that the Internet business is offering is unique and will bring unique benefits to the customer. Uniqueness in web site design is rapidly decreasing as a distinguishing element in any business. (Unless the uniqueness is because your web site design is so bad that everyone recognizes it.) Software design tools are becoming so sophisticated in checking your web site that blatant errors should not be there.

Therefore the uniqueness in the Internet business does not have to be that your business is on the Internet and that you have a unique customer friendly web site, but you must also have a unique element that the customer cannot obtain as easily somewhere else.

Uniqueness Parameters

Again, uniqueness in an Internet business can be divided into three major areas: intellectual property, marketing and manufacturing. Most often uniqueness parameters are arbitrary parameters. Arbitrary parameters make it so that the values are subjective. Subjective values have uncertainty.

Unique Intellectual Property

Intellectual property has a number of parameters that fall under this category. These include, but are not limited to, the following:

a. Patents
b. Proprietary data
c. Secret formulas
d. Authorship of information
e. Copyrighted materials

Patents are often cited for being uniqueness in a business. Normally the patent makes several claims. These claims are then validated by defending these claims in the marketplace and in courts of law. Often a company will have one or two patents and then attempt to use those patents to defend all the company's products, whether they apply or not. Patents have limited lives and have to be defended in court to become valid.

However, there have been some patents that have turned out to have high value. Sometimes patents do not have value until the market is right and the right company is promoting the benefits to the customer.

Proprietary data is unique industry information to the company. It is only as unique as it is marketed and defended in the marketplace.

Secret formulas or secret processes are a common technique to try to keep competitors from gaining the advantage of the product or service. This then is hard to verify, from the outside of the company, as to the uniqueness of the secret element of the business. This is a hard parameter to put any value on. This is especially true if it falls in an area in which very few people have any expertise.

The Internet is driven by information and authorship by people within the company, which is one way to establish uniqueness in the marketplace. The disadvantage of publishing is that some of your secret processes will also get out – unless you are just in the business of selling information – and then in that case you want to get the information out to the customers – as a sold item.

Copyrighted material is common. We sometimes forget that software is not patented but copyrighted. What we are looking for here is product being sold or processes that are unique to the business which allow some advantage in the marketplace that allows one to control costs or are perceived advantages by the customer.

Unique Marketing

Marketing has a number of parameters that fall under the category of uniqueness. These include, but are not limited to, the following:

a. Unique visitors
b. Unique marketing advantage
c. Unique web site design
d. Unique web domain name
e. Unique use of keywords

At some point, marketing uniqueness comes to having unique visitors. For example: Apple Computer, no matter what, appears to have unique customers. There are those visitors and customers that consider your product and service so unique that they will do anything to do business with you. These are the kind of visitors and customers all companies would love to have.

The unique marketing advantage has to do with your business' unique approach to a niche market. For this book we are addressing the valuation of businesses that address unique markets. Not very many companies have universal markets. If there is a universal market, then there will be a lot of competition in that market. The best-valued businesses are those companies that have a niche market in which they rank number-one, and that market is large enough to have a customer base. Especially a customer base large enough to support you in the manner in which you wish to grow accustomed.

The unique web site design is related to having a professional web site. It is having one of the web sites that customers find enjoyable to use. But having a web site that is professional does not mean the web site has uniqueness. There are a number of ways to acquire uniqueness. One of those is with technologies. Another way is to have multiple ways for the customer to receive information about your products or services. Not all

customers learn in the same way. Some like to read while others like to listen, and still others like to see animation of some kind.

The uniqueness of the domain name can help customers remember the Internet address. Although there is a need to be careful that your domain name is not so close in likeness to another company's domain address that your customers go there instead of to your place. Too long a domain name is death to any company.

There are a variety of ways to have customers arrive at your web site. One of these methods is the use of keywords and search engines. There are some keywords that are used a lot and are very expensive to purchase customers through their use. One of the uniqueness elements of a business in a niche market is to find keywords that your unique customers are using that are not the most common keywords. That way your customers will eventually find your web site. This will control your web site keyword acquisition of visitors. This increases the value of the business because it is controlling the cost and going after unique customers for your niche market using unique keywords.

Unique Manufacturing

Unique manufacturing involves having a method of creating products in such a way that the customer has a perceived benefit. A lot of manufacturing processes can be unique and are never patented. Nonetheless they give the business an advantage because of cost containment or the competition does not know how you built the product. This is a hard parameter to measure and put value on in the market place. However, still not harder than some other customer-driven parameters that need to be measured in order to have a valuation of the business.

Chapter 8: Valuation Determination

Overview

Once the data is collected in terms of parameters and parameter values, it needs to be converted into a final value or range of values. Therefore, there is an input to this portion of the valuation process and there is an output. The inputs are the values of the selected parameters and the output is a single or range of values for the stated purpose of the purpose of the valuation.

A valuation does not have to be comprehensive. The purpose of the valuation will determine the number of parameters and amount of effort to find the data for those parameters that will be expended. Therefore, the amount of data analysis that goes on between the inputs and the output can vary considerably depending on the purpose of the valuation. If the purpose is for a court of law that is allocating the value between different parties, then the extent and completeness will be radically different from a valuation being used as a business monitoring tool.

If used as a business-monitoring tool, then the effort should be limited to a select number of parameters and the valuation should occur more often. The analysis that is accomplished between the inputs and the outputs is also different if it is a complete valuation that has essentially become an expert witness for a legal proceeding.

The analysis takes the different parameters, absolute and arbitrary, and integrates those to some value while keeping in mind the characteristics of the niche market, the industry comparison rating and the general economy. The analysis can range from the simple to a very complex mathematical formula. The best analytical processor at this point, though, is an experienced Internet businessperson to take the subtitles and tie them together in a way that others can make a decision from the valuation report with confidence that they understand what they have been told.

Parameter Integration

There are many parameters in many categories. There are absolute parameters where we can know the number with a lot of certainty. There are arbitrary parameters that will require the skill of a very experienced person to determine a reasonable value or range of values from the very fuzzy input data.

It is the integration of these parameters that helps determine the value. For example, the absolute parameters normally do not carry the emotion of the business. The arbitrary parameters have a lot of uncertainty and risk as to what the values mean. Parameter

integration is taking those two types of parameters from different categories and integrating them into a plausible business valuation story.

The integration process in traditional business valuations has been evolving for decades. The Internet business valuation process is only just beginning. Some elements can be borrowed from the traditional business valuation process, yet new and intriguing elements are evolving as the Internet business story itself evolves.

There are four ways the integration can be accomplished:

1. There is integration across only the absolute parameters from the different categories.
2. There is integration across only the arbitrary parameters from the different categories.
3. There is integration of mostly absolute parameters with some influence of the arbitrary parameters.
4. There is integration of mostly arbitrary parameters with some influence of the absolute parameters.

Depending on the niche market, there can be lots of gradations of the above four main integration processes. If ever there was a business where the phrase "it depends" is appropriate, then this is the business. There is always another "what if" scenario or another variation on the purpose of the valuation which impacts the final value and what that value means.

Analysis and Conversion of Parameters Values

The analysis has two fundamental parts. One part is the algorithms that take parameters and accomplish some mathematical manipulation of the values. The other part is the conversion of the values to other measurement systems. We do this later when we convert a parameter such as volume of an object from one measurement system to another. We may want to use inches in one country and centimeters in a different country. The object has not been changed, but the measurement system used has been changed to describe the same object.

Therefore, in a valuation process one analysis tries to understand the data in mathematical terms and another analysis process converts the information from one viewpoint to another viewpoint. The change in viewpoint makes the information more readily understandable to the intended reader.

The same input data can be used to create a business valuation used for different purposes. The conversion of that data, to be understandable by the end user, is what we are discussing here. Just showing the math does not make the numbers understandable. These values need to be converted into something that the intended audience can understand.

Analysis processes:

a. Internet business algorithms
b. Changing of Internet business algorithms
c. Traditional business algorithms
d. Absolute parameters algorithms
e. Arbitrary parameter algorithms
f. Absolute/arbitrary parameter algorithms
g. Arbitrary/absolute parameter algorithms
h. Changing of absolute parameter algorithms
i. Changing of arbitrary parameter algorithms
j. Changing of algorithms from market niche to market niche
k. Distortion caused by absolute parameter algorithms
l. Distortion caused by arbitrary parameter algorithms
m. Time requirements of algorithms

Internet businesses are primarily different from traditional businesses because of the interface with the customer. This difference drives the nature of the valuation analysis. The algorithms used for evaluating these kinds of businesses are dominated by this interface. It is the way customers do business. If the valuation analysis does not address this interface, then it is not possible to determine the value of the business. The first valuation requirement of the analysis is the number of visitors to your web. This number drives everything in the analysis. The second element is the number of visitors that are converted to customers. The third requirement is the number of customers that are turned into repeat customers.

The ease of being able to accomplish the conversion of visitors to repeat customers is a very good measure of the value of a business. If this conversion process is not happening, then there is no value for the Internet business.

The fundamentals of how a business makes this happen for the Internet business world is under constant change. The method of the process will continue to change for decades to come. Nevertheless, the fundamentals of finding visitors and converting these visitors to customers will still be imperative. The Internet allows for this process of monitoring the visitor-to-repeat-customer conversion to be monitored with a great deal of automation.

Traditional businesses have this same fundamental problem of getting visitors to the storefront and converting those visitors to repeat customers. The difficulty that a traditional store has with this is the lack of individual customer data about how successful they have been in this converting process. Therefore, the data that goes into the analysis is different from that in an Internet business.

The nature of absolute parameters allows for the mathematics of the analysis to be based on exact numbers. With this type of analysis there are two possible errors. The first is with the data itself. The data can be bad for two reasons. The first is that the parameter value is wrong because someone did not have the right number for whatever reason. The second is that the data is not relevant because of data latency. The data is too old to be of value.

The other type of error here is that the analysis combines the parameter values in a way that does not reflect what is really happening in the business.

The nature of the arbitrary parameters and their analysis incorporates so much subjectivity to the values. These values are determined best by having an experienced valuator. Short of that, the values do not have much meaning. Therefore, whatever analysis is accomplished on these kind of bad values to start out with only makes the final values worse.

The analysis process uses both the certainty of the absolute parameters and the uncertainty of the arbitrary parameters to create a more realistic interpretation of the state of an Internet business. Whether the valuator uses a dominant amount of absolute parameters or dominant amount of arbitrary parameters to help establish the final value is dependent upon the business being evaluated and the valuator accomplishing the task.

The analysis used for evaluating Internet businesses is a constantly changing process. The exact algorithms are being established as businesses are increasingly being evaluated for value. This change will continue for decades because the nature of the business is to increase automation.

What is also not fully established yet is how the analysis algorithms will change from niche market to niche market. The one thing we do know is that these algorithms will change, as more parameters become available for evaluation and more data as to what those parameter values mean to the final value of an Internet business.

Valuators are constantly looking for distortion in the analysis created by the wrong elements in the algorithms. These distortions occur when the data is taken beyond the resolution of the original data. Analysis tends to fill in missing data. Analysis is a way to smooth the data so that it is easier to understand. However doing that may create a false sense of everything being all right when in fact the missing data might reveal a radically different conclusion.

Old data on the Internet can cause a lot of misunderstanding. There is nothing wrong with old data – as long as it is treated as historical data. The Internet business world is demanding that currency of the data is weeks or months old - not years. A business may appear to be perfectly evaluated correctly, except the marketplace has changed and the customers have gone somewhere else because the company did not stay with the changes.

Conversion processes:

a. Internet business
b. Traditional business
c. Absolute parameters
d. Arbitrary parameters

There are three levels of data we are talking about in this chapter. There is the raw parameter value data. There are the algorithm output values that have combined some of the parameter value data together. There is the converted data that takes the algorithm output and converts that data into the language of the valuation customer.

If you were to read valuation reports of traditional businesses you would also find these three levels of parameter information. So from that standpoint there is no difference between a valuation for an Internet business and a traditional business. Both kinds of businesses need to take the raw data and convert that data into something the intended reader can understand.

Many times the users of valuation reports are people without skill in business or finance and those people need to be addressed in some manner. The purpose of a valuation report in the ultimate sense is to teach the reader enough about a business so that they can make intelligent decisions. If the final report does not have a section that translates (converts) the data to a reader's comprehension level, then the valuation report has missed the mark.

If the person reading the report could understand the raw data prior to analysis and conversion to the reader, then just give that person the raw parameter data. What the converted data gives to the reader is a summary and overview that he would not have otherwise.

Niche Market Comparisons

General business comparisons are interesting, but niche market comparisons are exciting to the managers involved in that niche market. So what we are struggling with in Internet business is defining the categories of niche markets. How do we define the markets and the characteristics constituting a description of that market?

As businesses are bought and sold, the categories of businesses will become established. Auctions are great places to learn about how people interact with items being purchased at auctions. The auction process begins to categorize the objects that need to be sold. So it is also true that categories attract the people that are interested in those objects. Having interested parties' only look at objects they are interested in buying speeds up the process.

It is also true of businesses. A business many want to define itself in a special category for marketing reasons. However, from an investment viewpoint it may just be part of some larger category. These larger categories will begin to have values created for comparison reasons. There is always someone looking to categorize businesses. It may be no one other than vendors who are trying to sell to these businesses.

Comparison Ratings

Comparison ratings have to do with how this business stacks up to business in general and to business in a specific niche market. Values standing alone do not give a perspective unless there is some form of comparison to other values. The lay of the land is just not apparent unless there is some comparison.

The difficulty here is that many of the values that a valuator would like to use for comparison purposes are buried in a closely held business and are difficult to obtain. Numbers that can make or lose the business money are normally held closely within that business. That is the meaning of a closely held business. It is the opportunity to not be so public. A business that is a corporation that is traded on the open market is easier to compare because there is more data in the open. That is not true of closely held businesses. So the task here is to find the comparison data and to use that data in a relevant way. The difficulty with a lot of the data is that the values come without the context in which they were developed.

There are a lot of parameters that can be compared. In fact, if one had all the data from several businesses, it would be very instructive to a business manager to understand the comparisons of all the detailed data that goes into a total business valuation. This would be especially true if his numbers where compared to the three top competitors in his niche market.

The general investment market wants to know, for example, how the final value of a business stacks up. What a loan officer or business investor wants to know is the details of why this is a good deal versus other good deals.

General Economy Impact to Valuation

No business is an island on the Internet. Furthermore, to continue the analogy, the ocean is the world for the Internet business. That world is getting larger but customers are closer – time wise. Therefore the general world economy as well as the national economy have impacts on the Internet business. The impact can be positive or negative. It you are creating businesses to sell and people are wanting to get into their own business then it is possible to have a market like the Cadillac dealers had during the depression. The dealers of the Cadillac model did not have a major reduction in the sales of luxury automobiles. Just because the general economy is bad does not necessarily mean that the niche market you are working in is following the general trend of overall economic factors.

Nonetheless, a business valuator needs to address the general economy and how that impacts this specific business at this particular time. Turbulent economic times impact many businesses differently than more tranquil times. The link from the general economy to the particular niche market and then to the business being evaluated needs to be determined and characterized.

Section 3: Validation of the Valuation

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Chapter 9: Risk Assessment

Overview

There are two kinds of risk that we wish to discuss here:

1. Those risks that have to do with the Internet business being valued.
2. Those risks associated with the valuation process.

Just because the valuation process establishes a value for the Internet business does not make it a good investment if the business has inherent high risks. Valuation processes historically have not tried to put risk values on the business. Those kinds of risks have been created and used by business brokers. Nevertheless, today there are many business brokers who perform the function of business valuators.

Therefore, the concepts of risk of the company have been associated with the process. There are many reasons to discount the value of a business and risk may be one of the biggest discount elements to impact the value of a business.

The Internet is new and therefore will have more risk than other traditional businesses just because we do not have enough business history. There are factors and ratios that have stood the test of time in the traditional business world but we do not know yet for sure if those same ratios and parameters and values will be the same or radically different for this new type of business.

The other risk has to do with the risks in the valuation process. The process is dependent on data. The uncertainty of that data puts the valuation process at risk. Many values of the parameters needed in the valuation process may not be readily available. The data may be old or sorted in the wrong way to be of use in this process.

In addition to these issues there is the fundamental element that some of the parameters are absolute and some of the parameters are arbitrary. Arbitrary means that there is human subjectivity to create the value used. This means the number is no better than the valuator's experience in creating the number.

It is because of this, that experienced valuators have said that you cannot evaluate a business until you have fifteen years experience. They say that after having twenty years experience. Then, those same valuators, at thirty years of working this business say the valuator needs twenty-five years of experience before he or she knows the business. Therefore, if ever there was a profession that needed experience, this Internet valuation business is one where experience is essential. So there is a dilemma – you need a twenty-

five year experienced valuator in a business that is less then a decade old. Therefore, you identify the risks and do the best you can under the circumstances.

So the Internet, from a marketing viewpoint, is not yet ten years old and we are trying to evaluate the value of businesses when those who have evaluated traditional business say you need at least fifteen years to start. Where does this leave us in reducing risk to the potential customers of the valuation? We believe in these beginning years we will need to evaluate more often and be more willing to change the parameters, algorithms and ratings as the market changes as we learn more about these kinds of businesses. The valuation created last year with a process may not be the same process used this year because we have discovered elements that are different. Risk management will need to occur because we were willing to learn and to modify the process as we learn to give better valuations. Access to the data associated with buying and selling of Internet business will be a huge improvement in the valuation process.

Valuation Process Risk

The valuation process has risks associated with the process being repeatable and consistent. There are the following types of risks:

1. The difference that occurs because two different people with two different sets of experience accomplish a valuation of the same Internet business at the same time.
2. The uncertainty of the process that occurs because of valuations that are separated because of time and the process itself has changed and the values produced this year can not be related to last year directly.
3. The uncertainty in the parameters themselves because some of the parameters are arbitrary and are arrived at subjectively.
4. The uncertainty of timelines of the data that is used. Three-month-old data on the Internet may be just ancient history and have no relevance at all.
5. The uncertainty about picking the right parameters in the analysis and combining those parameters in the right way.
6. The uncertainty that the parameters measured actually measures the risk of the business itself and therefore will impact the value of the business.
7. The uncertainty because the parameters and values generated are not viewed in context of the larger economic system and therefore will become misleading.

It is not uncommon in traditional business valuations to have multiple valuators. This is especially true if the valuation is going to be used in a legal proceeding. That is one of the reasons why there are appraiser associations developing industry valuation standards. Standards are a lot tougher to have in a new type of business. Therefore, the probability of there being a difference between two individual valuators will be higher for Internet businesses than for traditional business.

The uncertainty will be higher for small businesses than for large businesses. The risk is higher for closely held businesses than for companies traded on the stock market. The

risk is also there because the probability of finding two different valuators of Internet business, who have sufficient experience to be compared, is low.

The way to approach this issue of not having the right talent is to have valuations more often and begin to fine-tune the valuation over time. The task will get better for the business owner and the valuators will begin to learn more about the unknowns of this business and more businesses will be bought and sold so that the process is validated.

The uncertainty of the analysis needs to be identified for the reader of the final report. There are uncertainties that cannot be removed from the process. This is not uncommon when the process includes trying to characterize the future responses of people. The valuation is looking at historical data and the price of a business is what it is worth to someone in the future.

If you wish to turn the uncertainties into understandable and recognizable business risks, that is currently accomplished in the development of the process by having a discussion in the report about those risks that are recognized at this point. All of this data and the analysis of the data will need to be placed in context of the larger business world. Failing to put all of this in context will be one of the largest risks to proceeding with the value on the last page of the valuation report.

Financial values by themselves without the marketplace values can develop large risks about the business and the process of valuation. For example: The company I just sold you has made a lot of money making buggy whips. That is the good news – the bad news – now that you have bought the business - starting next year – nobody will need any new buggy whips because the marketplace has changed.

Low Risk Elements (low uncertainty)

The parameters of the valuation process that are absolute are low risk elements. These are measurable values. If there is uncertainty in these values then it is because of latency of the data or the data is not available over a long enough period of time to know what is normal.

The part of the valuation that only uses absolute parameters will have low uncertainty. The uncertainty of this part only increases if the rest of the business valuation about the marketplace dynamics (emotions) may not be putting the generated values in context.

In the end, valuations are subjective and therefore the final value can be very subjective. Trying to predict the future is difficult. There is low uncertainty in the history of the company if enough data is available for the valuator to see the whole picture.

Historians, for example, have the job of looking at data and drawing conclusions and insights about that data which allows understanding of the past. The advantage that historians have is that they normally wait at least twenty-five years before they examine

the data and draw conclusions. They have a chance to look at more data than a newspaper reporter would have to write the story for the next day.

The valuator is caught in between these two extremes. They cannot wait decades for the data to surface and time to show what was really important to the events of the day. The valuator is not trying to do the business of a news reporter that is trying to get a story out in the morning that has enough interest for someone to read. What we have here is an interested reader, or the valuator would not be commissioned to do the valuation. However, companies can have a lot of data hidden to the valuator. This is because of two reasons: 1. The business managers do not know it is important to the valuation and 2. Someone knows it would impact the valuation in a negative way and therefore suppresses the information.

The short-term uncertainty in the valuation, though, is probably a smaller uncertainty than the future of the Internet. The core technologies supporting the Internet concept continue to change. Furthermore, those technologies continue to evolve at a high rate and this allows for very different business possibilities. The continual change in the bandwidth of the Internet allows larger and larger files to be transferred. The evolution of data compression technologies allows for more efficient information transfer.

These will cause uncertainties in what the valuation numbers mean today to the reader. The business valuation numbers are all right for the short term, if an experienced valuator accomplishes them. However, the uncertainty moves from low to high in a very short period of time. This is because of the technology and marketing dynamics of the Internet. This is one more reason why the authors of this book recommend that the valuation be performed more often.

High Risk Elements (high uncertainty)

The very nature of the arbitrary parameters gives these elements higher uncertainty. There is a range of uncertainty with arbitrary parameter values. The risk associated with these parameters is because the valuator needs to make subjective decisions about whether the parameter should be considered and, if so, what value to assign to that parameter.

Arbitrary parameters reflect the marketplace importance. Marketplace is a human-driven requirement. Human-driven requirements are subjective. Moreover, if business owners are not willing to address those requirements, then there also can be no rewards when the owner correctly identifies those needs and then creates responses that fill those needs.

Therefore, the arbitrary parameter portion of the valuation analysis is categorized as a high-risk element – which is high uncertainty. If the uncertainty is too high the final numbers are meaningless. The owner might as well take a dart and a wall with lots of numbers on it in a random way and then just throw the dart at the wall and pick the number that it hits.

The high uncertainty in a valuation is contained with two techniques: 1. Get all the relevant and related data about the business activity and 2. Use an analysis methodology that combines the certainty of the absolute parameter values with the emotion of the marketplace of the arbitrary parameters to create a credible report.

Emotions Associated with Valuation Risks

The human race has the ability to take a lot of subjective, conflicting information and turns it into something meaningful. When Neal Armstrong was landing on the moon, the computer was telling the engineers on earth that there were errors in the system. The question was raised as to whether the errors should terminate the mission just before landing on the moon. The engineer who understood the system watched the data and concluded that this set of errors was not detrimental to the landing. The errors were just not coming often enough to cause a high risk to the mission. No computer program could have made that judgement in real time because no one had thought that that particular sequence would be important to the mission.

The emotions of the valuation process exist because of the customer's emotions about their decisions to buy or not buy from this business. They are there because of the business structure that people are running to support the business and they are there because of the experience and talent of the valuator. All of these emotions need to be brought together into a meaningful final value.

The hard numbers of the financial parameters are normally not subjective and therefore do not have much emotion. The numbers may cause an emotional response, but the data is not subjective. The marketing parameters on the Internet can be divided into two different categories:

1. Those parameters that can be measured directly.
2. Those parameters that are subjective (arbitrary).

It is the taming of subjective values that requires the experience and skill of the valuator. There is no substitute for experience and the willing attitude of the valuator to look across a wide spectrum of information before saying what values should be used in those parameters.

Uncertainty Management

Business management is about managing risks. Risks are elements of the uncertainty of accomplishing business. There are whole books on the subject of risk management. It is not the intent here to address all those methodologies of identifying and managing risk.

It is the intent here to point out that if the nature of the Internet business has high risks the valuation process will have a greater uncertainty in the final value than if the business were a low risk business. The valuator needs to understand the nature of the business being evaluated. There are those in the investment community who would consider that all Internet businesses are high-risk ventures. However, that is not necessarily true for

certain classes of people. For example, companies in the aerospace business are accustomed to a lot more risk than businesses that are making trinkets for the tourist industry.

The valuator manages the risk of coming up with a wrong valuation by developing a process that is repeatable within some limits. The refining of that process will eventually give a higher certainty to the valuation.

The process has got to have more than elaborate algorithms to help it. The downside of algorithms and believing them is that the output of an analysis can be no better than the input data. Therefore, one of the input needs to be the real time marketplace data of closely held Internet businesses being bought and sold. This single element goes a long way to managing the risk of valuation process.

Chapter 10: Measurement Methods

Overview

Parameter measurement denotes that there are parameters to measure. Often in business, we select parameters to measure because we can measure the parameter. The parameters that we can measure are not necessarily the parameters that we need to measure. It is sometimes like looking at where the light is and not where we lost the object. We are looking at where the light is because there is where we can see. We won't find the lost object there because it is not there.

There are other parameters that we really need but have difficulty measuring. Therefore, we do not measure those parameters. New measurement tools are always being created. Therefore we should find the time to always be examining to see if measuring the parameters that we really need can be accomplished with more efficiency method.

We need to pay close attention and revisit often the selection of parameters we are using to measure the performance of a business. We may be measuring very accurately the parameter, but it is the wrong parameter. If we measure the wrong parameter and then use that information to manage the business, then eventually the business will falter.

The two continuums that we are interested in have to do with the difficulty of measuring and the accuracy of the measurement. There are some parameters that are easy to measure and there are some that are hard. There are parameters that are scattered along that continuum. So there are also parameters that we can measure with accuracy and there are parameters that have high uncertainty. Again, there are parameters along that continuum.

So on one axis we can plot accuracy and on the other axis we can plot difficulty of measurement. If we are to accomplish a complete valuation, we need to measure all the parameters. However, that is not what we necessarily need each time we accomplish a valuation. Therefore, the type of valuation comes back to the parameters that need to be measured. The measurement method then becomes very important. The goal of valuations is to find more and more parameters that can be measured automatically and then get more and more information out of those parameters.

Absolute Parameters

If you are a detail-oriented person then you like absolute parameters and you like even better absolute parameters that are easy to measure. The nature of accomplishing an Internet business allows for the measurement of many parameters.

Just because a parameter is easy to measure does not mean the parameter is what we need to understand the value of the business. What we measure is eventually what we respond to in the management of business. In this case, management means directly by running the business or investing in the business.

Internet marketing methods are getting better and better at measuring customer responses. There is a limit, though, to how much a customer will tell you in an automated way. Next comes the more subjective measurement parameters of asking customers what they like and don't like. Then you have moved from absolute parameters to arbitrary parameters.

Arbitrary Parameters

Arbitrary parameters are those parameters that have subjectivity associated with measuring the value. Subjectivity means uncertainty and uncertainty means risk. These parameters are not about adding up columns of income numbers and expense numbers. These parameters have a lot to do with the intangibles of a business.

The intangibles of a business are many times the most important elements if there is uniqueness to the business. However, uniqueness is in the eye of the customer, not the owner of the business or the inventor of the product or service. Therefore, if you want to measure these market-driven arbitrary parameters, it comes back to having someone with experience in the marketplace.

A partial list of arbitrary parameters is listed below. A quick review of these parameters shows that there is a very subjective nature to them. Yet these parameters are very important to the value of a business. This type of parameter is dominated by the marketing and customer elements of a business. It turns out that if there are no customers, then there is no business. So although these parameters are subjective, it becomes apparent very quickly that if the number of visitors to the web site is zero, the value of the business is zero and these subjective parameters have no meaning at all.

1. Marketing
    a. Advertising versus Number of Customer Visits
    b. Domain Name Uniqueness
    c. Keyword Space
    d. Keyword Uniqueness
    e. Market Potential
    f. Traffic: Value
    g. Traffic: Targeted
    h. Traffic: Targeted Value
    i. Traffic: Unique Traffic Value
    j. Product Uniqueness Value
    k. Proprietary Software Value
    l. Customer Base That Needs Product

    m. Customer Base That Needs Service
2. Link
    a. Non-Competing
    b. Promotion
    c. Quality of site linked to
    d. Content Relevance
    e. Friendly
3. Web Site
    a. Individual Page Value
    b. Content Value of Site
    c. Marketing Appeal
    d. Uniqueness
    e. Browser Compatibility
    f. HTML Design Value
    g. Professional Designed Site
    h. User Friendly Site
4. Customer
    a. Benefits
    b. Satisfaction
    c. Customer perception of quality
    d. Customer perception of product
    e. Customer perception of service
    f. Service Uniqueness Value
5. Company Organization

These arbitrary parameters are tough parameters to measure in great detail every day. Many need to go on customer surveys that take time to evaluate and to know what the responses mean. These are the parameters that are very difficult to automate. For example, it is easy to count the number of links that a web site has in the design of the web site, but much more difficult to evaluate the ability of that link to help the business being evaluated.

Even if the measurement is more difficult, the process of trying to discover the value of each of these parameters can be very helpful in understanding an Internet business. This Internet business is in many ways so remote from the customer, that if the effort is not expended to get to the real value numbers of these parameters it will not be long before there will be a disconnection with the customer.

Automation of Parameter Measurement

Arbitrary parameter measurement is difficult to automate. Therefore, the measurement of these parameters requires a human in the loop to accomplish the measurements. Once you have a human measuring the intentions of humans, uncertainty in the measured value is created.

Domain Name Impact
There have been studies which show that a domain name over twenty-two letters results in a very negative customer acceptance impact. The problem with the Internet is that all the very short domain names are already spoken for by this time. So we are in the business of generating ever more complex names.

It is easy to measure the number of letters in a domain name. What is hard is to determine is the value of that domain name in the marketplace. Even if you have a domain name that has many letters – it maybe that the name can be easily remembered – like the phrases of songs we remember forever.

Visitors
Measuring the number of visitors to a web site is easy and can be automated. What is not so easy is to determine the value of each visitor. The search engines are beginning to put advertising value on each customer that you must pay to participate in the game of keyword search. However, the search engine dollar value of a visitor may not yield the same results. If no visitors turn to customers for that keyword, then the value to you of those visitors is zero.

The search engine owners can tell you how many visitors they sent your way but cannot tell you the value to your business. They can set a price, and after a while, if no one is buying, then there will be no desire to purchase that keyword as an advertising tool.

Visitors and Customers Privacy
A lot of data can be generated about visitors and customers. What companies do with that data is coming under scrutiny by various government agencies. There will be more and more impact of what a business can do with that data. There will be laws that will govern what you can ask for in the first place.

Therefore, customer privacy laws and ethics will force restrictions on the measurements of certain parameters. There will be customers that will consider certain responses to surveys and questionnaires an invasion of privacy.

Valuation Ratings Comparisons
Turning arbitrary parameter values into ratings so that one company can be compared to another or to an industry will have the same uncertainty in the value created out of several parameters as was in the original measured data.

This is not a new subject. Businesses have struggled with these marketing issues for a very long time. They have struggled to understand why customers do what they do.

Turning arbitrary parameter values into ratings that can be used to run a business or buy a business is difficult to automate. We are back to requiring a human as the valuation measurement tool.

Uniqueness of Business

Business uniqueness is an arbitrary parameter and is made up of a lot of subjective factors. The problem of uniqueness on the Internet is that uniqueness does not last very long if others perceive that this uniqueness has value.

Therefore uniqueness will be a moving target. The competition will force you to continually change in order to hold your uniqueness. For example web site design in 1995 that was unique would be old fashioned in 2002. The same is true of products and services. The idea that one can maintain the uniqueness position by standing still does not bode well. Normally in a traditional business you are either going forward or going in reverse. The same is true of an Internet business – only it happens faster.

The measurement method of uniqueness is a subjective measure and comes from experience. On the Internet, this does not mean experience only in the long distant past, to know the historical perspective, but also continual experience today. This forces a valuator of Internet businesses to need to be in the marketplace daily looking at businesses from many different viewpoints.

Timing of Measurements

Having the value of a business change rapidly is not new. The element that is new is that there are many more businesses in the category. Business is not local. Customers are mobile and it is difficult to measure the demographics of the customer and how you get to the customer and get the customer to respond is a constantly changing parameter.

Let's look at what has happened to the stock market as communications have increased. There used to be delays between customers buying and selling stocks. The buying and selling in real time was for the few brokers. Now buying and selling is in real time for the masses. Thus the market can reflect the perceived value of a business in seconds. For publicly traded businesses this certainly demonstrates the value of a company. It may not be the total value because there may be residual assets that have value. However, residual assets are never worth as much as these values plus the goodwill asset values.

The nature of communications today and the ability of someone to cause harm by publishing false information can make a business valuation accomplished in one month totally invalid the next month.

The reason we are talking about this is that business value has a timing function. That timing function needs to be addressed. There are some parameters that can be measured minute by minute as the activity on the Internet interacts with your web site. These

parameters may not give you the most insight as to the value of the business. Except it is certain that if there is no activity on your web site, there is no value.

Therefore, from timing viewpoint businesses needs to specify how often various portions of the Internet business valuations needs to be accomplished. This timing issue has two major elements that drive when and how often. One is the internal use and the other is external use. Internal use is because you are trying to increase the value of the business because you want to make more money. You want to know if an advertising campaign has changed the value of your business. The other reason is external and normally involves money in some way. This is because of wanting to borrow money or to have the value for insurance reasons. The reasons for the valuation will drive the timing. A valuation that is six months old even in traditional businesses may not mean much.

The timing of Internet business parameter measurement can be from real time to months of effort to measure the value. If you are an investor in Internet businesses you want both the real time and the longer perceptive measurements.

Measurement Requirement Impact of Web Sites

Some parameter values are associated with the web site. If they are associated with the web site then they will impact the web site design. Technologies will be developed that will allow more and more measurement of Internet activity. Government will restrict some of this activity because of privacy concerns. This will be a constantly changing element of the Internet and therefore the design of a business web site.

One of the parameters valuators measure is whether the web site has a professional design. If ever there was a subjective parameter, this is it. Nevertheless, it is the subjective parameter that customers use to decide whether to click and go to the next site and never return to your site.

Other parameters can have impacts that are a lot less subjective. These include such web site design elements as:

1. Link content relevance
2. Link promotion
3. Quality site link
4. Direct traffic
5. Individual page value
6. Dead/failed link
7. Re-directs
8. Re-register

A lot of marketing valuation elements can be introduced into the web site. The measurement methods of monitoring these elements can have some automation applied. Other elements will need human intervention and thus uncertainty in the accuracy of the measurement.

Chapter 11: Substantiation Methods

Overview

The selling price of a business is a composite number. It is made up of the absolute parameter and arbitrary parameter values combined together in some unknown manner in the minds of the buyer and seller. The process of selling and buying a complex system like a business has many factors. The valuator may or may not have included the right parameters in the valuation process.

As valuators try to identify the driving elements and then determine if there are parameters that can be measured to quantify those parameters. However, there is always in the back of the mind, that there may be some parameter, which is even more important then, any on the present parameter list.

Therefore, it is necessary to validate the process. As part of the valuation process there needs to be a method that periodically validates the model. This validation process needs to have data coming from different aspects and different viewpoints to help insure that the final numbers have some measure of certainty.

All valuations need a purpose for which the valuation was rendered. For example, if the valuator is tasked to provide a value for an insurance company, the replacement cost of the business will have a different value than if the business is sold to an investor. Therefore, the process will need substantiation that is also relative to the purpose for which the final value was established.

Systemic Substantiation Data

The valuation process of an Internet business needs to be viewed as a system. In this system there is more than one category of business. There is more than one purpose for the valuation. Therefore, there will eventually need to be a system of substantiation data that will support the valuator and the process.

It is too early yet in the world of Internet businesses to even know how many categories of businesses there are. So that is one source of error in the valuation process that turns into a risk. At the moment, Internet businesses are treated as a class of businesses with most of the parameters being applied to all businesses. There will be recognizable categories of businesses as more business valuations are being accomplished and as more and more businesses are bought and sold.

The purpose of the valuation is still being driven by the needs that traditional businesses need to be evaluated. There are insurance values, divorce settlement values, borrowing money values and selling values, to mention a few. Therefore, the purpose and the value must be correlated. If the purpose and final value are not correlated, then the value will be misleading and we will have lending institutions using insurance replacement values for loaning purposes.

The value of an Internet business to a lending institution is considerably less than the selling price of the business. The lending institution has to deal with the probability that the selling of the business assets may occur after the business has failed. Assets of a business after it has failed are substantially less valuable than if the business still has a future.

Therefore, the data needs to come from many sources to substantiate the process. Moreover, the nature of the fast changing Internet is that it must be recent substantiation data. Hence, the data that is being used to substantiate the final value needs to be recent. Lending institutions may want to reconsider how often they reevaluate the collateral that is there for the loan, as an example.

Substantiation of absolute parameters is different from substantiation of the arbitrary parameters. If the final selling price is used to substantiate the process that price is made up of absolute parameters and arbitrary parameters. The valuator needs to accomplish some analysis to determine what was allocated to absolute parameter information and what was allocated to arbitrary parameter information.

Therefore, from a valuator viewpoint, it may be difficult to determine what part of the process needs re-calibration in order to have a valuation process that represents the marketplace. The substantiation and re-calculation of absolute parameters can often be automated and therefore the periodicity of the re-calibration can almost approach real time for an Internet business.

This is not necessarily true of the arbitrary parameters. These parameters will be far more difficult to validate. There is the element of what is called “goodwill” in the business. Goodwill is a difficult element to determine and to validate.

The valuator uses algorithms to determine how to integrate the parameter values to a final rating and value of the business. It turns out, from a systems viewpoint, the buyer, for example, is using an algorithm of his/her own to determine the value of the business. These algorithms may be different. Furthermore, the nature of why a business is purchased will change. Therefore, there will need to be a systematic accumulation of substantiation data if valuations of businesses are to be taken seriously.

Historical Data

We have not yet determined what is historical data on the Internet as it relates to business valuations. After all, the Internet business history is not very long--less than a decade.

Most of the businesses are less than five years old. So there is not the historical data you would find in the traditional business environment. The business ratios are just not established that have proven to be valid and consistent parameters to use to know the health of a business. Of course, none of this historical data is helpful in evaluating business data if someone is "cooking" the books.

We are still struggling with the categories of businesses on the Internet. Therefore, the historical data will need to be broken down into the different business categories. This is no different from trying to evaluate the home building industry by only looking at the gross national product.

Internet businesses are not going away. They are just really new. The historical data is being developed every day. Right now historical data that is valid is probably not considered historical data in other more established businesses. Six months in the Internet business world can be a long time.

It is because of this need to establish the historical data that the authors of this book recommend that the valuation be accomplished often. It does not need to be a complete valuation of the business. It does not need to be for all purposes of a valuation.
But a business owner needs to begin to understand the sensitivity between the parameters being measured and the final value of the business.

Industry Data
There are Internet businesses and there are industries within that business. It is not clear yet for Internet businesses what industry they are in. For businesses that are combination of Internet and traditional then there will be a debate as to the industry category. Do we follow the traditional categorization or do we create a new, more descriptive industry category?

Once the industry category is decided there is the issue of determining the industry norms for valuation comparisons. This will also need to be developed over time. The norms will be established as businesses are created and bought and sold in the marketplace.

Niche Market Data
Most businesses do not compete in large markets. The markets they compete in are niche markets. A market can appear to be large but it may be further divided into different ranges of prices for the same functional product. For example, cars appear to be a large market. But each vehicle is not competing with all other vehicles. The luxury class of cars is a niche market, so there are fewer customers and fewer businesses competing for those customers.

Niche markets on the Internet can be identified by the keywords used to find the businesses in that market. It may be in the future that is the method of defining a niche market. Already the search engines have defined certain keywords to represent certain

markets. The value of that keyword has a value. A set of keywords could also be an identifier of a niche market. Traditional businesses were defined into categories by a variety of other means, but it may turn out that keywords are the defining categories for Internet businesses.

The substantiation data is being built. As more and more companies are bought and sold, the value of those businesses will be established. Niche markets will be identified and the data will be available.

Traditional Business Data

In the beginning of this book we defined three types of businesses. These were traditional businesses, Internet businesses and a combination of these two. Traditional business substantiation data will be used for the traditional businesses. It can also be used for those companies that have a combination business – at least for part of the combination business. It is the Internet business that we are discussing here – mostly.

The standardization of the valuation process that is used in traditional business valuation can be used as a starting point for Internet business valuations. The element that is not in traditional businesses is the use of the web site as an interface to the customer. Being able to use that interface radically changes the dynamics of the business and therefore the valuation process. If the process is changed, then the substantiation of the numbers generated by that process need to change.

Items that used to take a considerable length of time are now completed in seconds in an Internet business. It has yet to be shown that data that has long gestation periods, like traditional businesses, can be used along side data that has only been here for a very short period of time.

Auction Data

Auction data has always been an excellent source of information about the value of whatever is being auctioned. The concept of using the Internet as a tool for communication between buyer and seller has been very successful. This concept started with selling of low cost items.

The concept has now expanded to buying and selling businesses. What happens every trading day on the stock market is that a portion of a company is put up for sale and someone buys a portion of that company. What is beginning to happen in the Internet business is an equivalent concept except that it is not a portion of the company but the complete company. It will not take long for these exchange locations, on the Internet, to help the buying and selling of businesses become as well established and accepted as the stock market. The exception is that this is a niche market and the community involved will be a lot smaller than the stock exchange.

What you have in the Internet auction concept is a place where you offer to sell and where someone, maybe from around the world, offers to buy. Now the only thing that you are arguing about is the price and the terms and conditions of that price. The Internet auction allows for a larger audience to see the product if someone wants to sell and place the object in the marketplace.

Auction data is not all the data you need to accomplish a valuation. There are other data that need to be generated to substantiate all the different types of valuation requirements. Nevertheless, the auction is a great substantiating source of information. You may not know all the particulars about the payment method of any given sale of a business but you will calibrate the price range of that kind of business. Auction data does not help an insurance company, for example, need to understand the replacement cost of a business. Replacement costs can be radically different than the auction price.

Management Data

One of the advantages of Internet businesses in the valuation of businesses is that many of the absolute parameters can be monitored often. If management uses some of the valuation data on a day-to-day basis, then that data can be used to substantiate a portion of the business valuation effort. This will allow information that is used in business to show the validity of the valuation report. Information that is seen more frequently and tested against day-to-day operations becomes substantiated in terms of the user of the report because the information is familiar and easier for the readers to validate in their own minds.

It is not the nature of many startup companies to generate everyday testing data about their own business. That is normally something that happens later in the development of a business. What is happening on the Internet is that in order to survive at all, this kind of valuation data needs to be generated and used.

Section 4: Investment Community Perspective

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Chapter 12: Marketing Uniqueness

Overview
Value can be derived from uniqueness. This is especially true in the marketing aspects of a business. There needs to be something that differentiates your business from all the other businesses on the Internet. However, the differentiation needs to be a desirable characteristic. You can differentiate your business by having a very bad web site design. This is not the kind of uniqueness we are talking about. After all, it is hard to get uniqueness with a bad web site design – because there are plenty of those on the Internet today.

The investment community is looking for some way that shows your business has a unique set of customers. That; you have a web site which uniquely addresses the needs of that set of customer; that your business has some unique intellectual property that sets you apart; and that, in the final analysis, the intellectual property is translated into unique products and services.

Once your business has some or all of these marketing uniqueness characteristics, it is imperative that you translate this uniqueness into measurable business value. The measurable business value is apparent because there is a management strategy in place that will take advantage of these unique characteristics in the marketplace.

Customer Uniqueness
Prior to having unique customers, a business needs to attract unique visitors. Unique visitors are those visitors that can be converted into customers. A lot of web sites have visitors. Some of the most visited web sites have lots of visitors, but not very many customers. Perhaps the visitors are customers of their advertisers. At least that is why the advertisers are paying them for the space on their web site.

That is not the question to answer here. We are trying to find qualified customers who have the resources available to become buying customers.

How do you determine the value of the unique visitors that come to your web site?
Unique visitors are those visitors who eventually acquire the status of customer. The value of the customer depends on your Internet business activity, what products you sell to these customers and how many back-end sales are possible. The cost of selling to an individual customer continues to decrease as more and more back-end sales are sold to that customer.

Web Site Uniqueness

Web sites are built from a few fundamental-programming options. The list of the programming commands available is a limited set. Plug-ins function is constantly being added to give a program some way to differentiate the web site. Many times the plug-ins disrupts the customer's experience and irritates the customer instead of giving the business uniqueness.

How does a business develop a unique web site?
Uniqueness in web site design is a moving target. A unique web site in 1995 would be very old fashioned today. Having unique products and/or services helps drive web site uniqueness. So does explaining those unique products to potential customers in innovative and creative ways. Once those customers can relate to the uniqueness of the web site, then they buy your products or services.

Uniqueness in web site design has to be viewed through the eyes of the customer. What makes the customers of that niche market comfortable with the web site makes it unique. When you get to niche markets, the web site needs to reflect the uniqueness of that market niche. If it reflects that customer class uniqueness then it will not be driven so hard to have the latest Internet technology whether that technology makes any sense for this set of customers.

How will the uniqueness of the site and the products of the web site impact the Internet business valuation results?
At this point in Internet business, the value is driven by uniqueness. Price and availability drive those sites selling commodities. That is the uniqueness of those sites. Therefore, the value for those sites will show up in the ratio between income and expenses because of the volume of items being sold. It is volume that drives the value of these businesses.

There is the other category of Internet businesses in which uniqueness is driven by the uniqueness of the product or service and the unique way that those items are presented to potential customers. It is because the Internet business has a unique set of customers that are loyal and the repeat business is very important.

Repeat business costs less to acquire and the return is substantially higher. Therefore, the value of the Internet business is higher because there are products that have uniqueness going to a unique customer base that can have repeat sales. The repeat sales occur for two reasons: a. either from the product being consumable or b. the business having a continuous supply of new products for the customer to purchase.

Intellectual Property Uniqueness

How does a valuator determine if a patent is relevant to the value of the Internet business?
If a company has patents, they tend to list them on everything that they do. This is true whether that technology is directly applicable to that particular product. Most patents

have lots of claims. Most of these claims have never been challenged. If these claims were challenged in court of law, the strength of a claim would seriously erode.

Normally the claims are written in a way that it is difficult to know what the claim of uniqueness is. Part of this is due to the inventor wanting to accomplish two conflicting desires at the same time. The first is to have enough claims that even if some of them are challenged later there will be sufficient left to protect the unique ideas being patented. The second has to do with not wanting to give too much away in the patent about what the real uniqueness is so that the idea is protected by industrial secrets.

Nonetheless, patents are not always the best routes to protect uniqueness in a product. The classic example is the formula for Coke. After many decades the formula is still secret.

Why would one pick the patent route over the industrial secret route? Patents get your idea in the public domain with some protection. It is easier for outsiders to see if you have true innovation. The downside is that the time of protection is limited. The patent has a set amount of time for protection.

An industrial secret is more difficult to prove to the general public that your product has uniqueness. The secret may also be disclosed in some unexpected manner and in that case there is no legal protection. Someone could then patent the idea. However, industrial secrets do not have a legal time limit.

So back to the question: How does the valuator know the true uniqueness of a product patent? The valuator may need to hire experts in the field.

How do the patents give the Internet business uniqueness in the marketplace?
Exclusivity is what patents are about. There is a period of time when the patent is valid. If the business is willing to defend the uniqueness, then there is, in fact, uniqueness. Patents are only as good as the defense of the patent. The patent can erode because others have filled similar claims and those claims went unchallenged.

The uniqueness is maintained and sustained in the marketplace because the idea is unique and the business is willing to defend that uniqueness. Governmental prosecutors will not be policing the patent office looking for violators of patents. The system is such that patents needed to be defended by the patent holder if that patent is to maintain uniqueness.

What is the uniqueness of the products in the niche market that the Internet business is operating?
Products do not have to have legal protection for uniqueness. If the product cycle is short, patents do not yield much advantage. This is because the patent approval cycle is long. Therefore, the uniqueness in a niche market needs to drive the business. This is how the business derives value. The valuation of Internet businesses at this point is

driven by what has and will happen in the marketplace. If nothing happens in the marketplace, then there is no value.

Determining uniqueness of an Internet business is an arbitrary parameter that takes years of experience to even consider how to determine the worth of this parameter. Since the Internet is young, in comparison to other business types, then the experience is not yet there in the general valuator community. Therefore, someone having what he would consider a unique business needs to find a valuator that has sufficient experience to identify and quantify that uniqueness into the valuation report.

Does the Internet business have unique software that is either sold stand-alone or is used in the processes of the business to give an advantage?
Internet businesses are electronic businesses driven by computers. Computers are driven by software. The use of software in the business can have a tremendous impact on the Internet business. This impact can be positive or negative. The software we are speaking about here does not necessarily have to do with products being sold.

The software can be buried in the processes of the business that allow major elements of the business to be automated. This automation has a lot to do with the expenses an Internet business will experience. Therefore there can be automation that can accomplish the tasks of running the business and there is the software that can be used to measure the performance of the business. Both of these types of software can have uniqueness in the niche market. That uniqueness has value.

Does the Internet business have a unique service that is protected with some intellectual property for the marketing niche in which the business is operating?
Services are very different from products. Products have legal protection if you decide to use the patent route as a form of uniqueness protection. Services become more problematic from a uniqueness viewpoint. If the service is a process, then that can be patented. If the service has elements that can be copyrighted, then that is an approach to uniqueness protection.

This service uniqueness needs to be determined. However, once the uniqueness of the service is identified then it must also be determined how long that uniqueness can be defended in the marketplace. This identification and the ability to defend that uniqueness are elements of the valuation process that have the most uncertainty in the value given to that parameter.

Product Uniqueness
Product uniqueness is a difficult parameter to identify and measure. A lot of unique products have been created that did not make it in the marketplace. So it is not just the uniqueness of the product, but also the uniqueness of the business that supports the product. Failure in the marketplace is driven more often by failure in business management than because of product uniqueness failure.

There needs to be a new definition of product uniqueness. Product uniqueness would have a lot more value if it included the business delivery system of that product to the customer.

The business delivery system is comprised of all those support functions that a business needs to find, sell and supply products and services to the customer. In the case of the Internet business there are more options to create that business delivery system.

Therefore, when accomplishing business valuations on Internet businesses, it is not just the product but how that product is delivered that determines uniqueness. This means that the niche market must be identified and the method of reaching that niche market must be very apparent.

Service Uniqueness

Service uniqueness is driven even harder by the business delivery system than product uniqueness. Uniqueness of the service may only be the business delivery system. This system needs to have an identifiable method of attracting visitors and turning those visitors into customers. Nonetheless, it will not take long for a competitor to visit your site and determine from a customer perspective what you are accomplishing.

Therefore, there needs to be a way to protect that service uniqueness. This may mean that some of the ways in which this uniqueness is accomplished need to be kept as industrial secrets.

Which of these services are unique in the niche marketplace?

To understand uniqueness for services there has to be a survey of the competitors in the marketplace. There is one advantage of the Internet business in that it is much easier to find and survey from the Internet what the competition is offering to the customer base. Therefore, the uniqueness of a service has to be evaluated in terms of the competition in order to know the value of a particular company's service uniqueness.

Chapter 13: Financial Implications

Overview

The implications to the financial community of a business valuation can be from no reaction at all to total belief that the numbers mean something. Businesses are not built without resources. Most other resources needed to build a business are traced back to financial considerations. The very nature of our business community is based on expending one amount of money and receiving in return an increased amount of money.

The investment community has known their share of failures. There are plenty of stories about failures in the business community. There have also been some successes. It is because of those successes that there is enough faith to invest resources again.

In this dance, which must occur between the investment community and the business development community, there are duties and responsibilities on the business owner side and there are duties and responsibilities on the investment side. What is happening on a larger scale is that the accepting of financial resources means turning over some of the control of the business to others. There can be a little turnover of control or a lot of turnover. In the case of failure, there are laws that also govern the control of a business if it seeks certain bankruptcy options.

It is not a happy day when businesses fail, for whatever reasons. There are a lot of given reasons for failure but one that is most difficult to understand is the true value of the company at any given time. This is one of the reasons the business community is spending one billion a year on having outside people accomplish business valuations.

It is not just the state of the company, it is how that company is doing in the marketplace compared to other companies in the niche market and to the larger economy that everyone is a part of, whether they want to be or not. Another reason to accomplish these valuations is to look at industries outside the niche market that could decrease the value of this niche market because of technological advances. Just look at how many different audio recording mediums we have had in the last forty years. We have gone from tape reels, to eight tracks, to cassettes, to CDs to MP3s. and DVDs. Each change eroded the market for the preceding technology.

Owner/Manager Responsibilities

Periodically in the business cycle we have a reset in the business community and the investment community. There was one in 1929 and there was one in 1987. The year

2002 may go down as another year of reset for these two communities. There are owner/manger responsibilities to the investment community. These responsibilities include some straight talk about what the present state of the company is. External valuation by credible sources is one of the tools available to establish the credibility needed.

When does an Internet business seek outside investment?
Most entrepreneurs do not have sufficient resources of their own to build a business. Therefore, if the business grows to millions in sales, then somewhere along the way a need to find additional external resources will appear. The triggering event is driven generally by two different needs:

1. Cover existing operating expenses and/or debt
2. Expansion (growth) of the business.

At what point do you know that you want to grow the business faster than you have personal resource capital to expand?
One of the issues is to know when the opportunity is really there and when to wait for the opportunity to expand the business. There is a certain amount of luck in finding the right timing in the marketplace. Too early and you have expended resources that you did not get a return on; too late and you never recover the number one position in your niche market.

All the analysis in the world will not turn the timing issue from an arbitrary parameter to an absolute parameter. This arbitrary parameter, timing, can be helped by using some absolute parameters to improve the timing prediction. Nonetheless, timing often has to be instinctual--a hard thing to explain to the investment community.

At what stages of an Internet business development is it just not appropriate to have outside financing?
All businesses start with some money other than the money generated by that business. So every business has outside financing. Businesses can expand with inside money, but not start with it. So the issue is after the initial source of outside financing when does a business seek additional financing?

The second, third and future rounds of outside financing are driven by a number of items. Every business wants a grant from someone of monies they do not have to account for later. However, that is rare and most types of financing need accounting of some kind. Therefore one must consider what kind of accounting you as a business owner/manger want to live with on a daily basis. Hence, once the business is established, you need to establish whose money you want to have and when to request that money.

Startup costs and expansion costs are two of the major drivers for seeking increased funding. Therefore, these are two of the stages when you care about this the most. Nevertheless, during a startup phase with no customers it is difficult to establish a value for the company and therefore valuation of the business does not have much merit. In the

expansion mode, the valuation process can help establish the stage at which the business needs to seek additional financial support.

What autonomy will the owner of an Internet business give up when third party financial resources are accepted?
There is always the question of control when accepting third party financial resources. The ability to make decisions in the business like you did before the financing is very different after the financing. So many business owners elect to remain small because they do not want the complicating factors of third party financial resources. It is in this last case that the valuation process may very well help the business owner discover ways that automation and business parameters measurement methodology will improve the performance of the present resources and no control is lost to external third party interests.

How do you identify the right kinds of resources for your Internet business?
Each type of financial resource has the established return on investment that the source is willing to receive for participation. It comes down to cost of the money and the amount of control you wish to relinquish.

Why would an entrepreneur ever care about the financial markets view of his business?
The language of the financial markets is different from the language of business interests. If the business wishes to participate in the financial markets there needs to be an established set of information that will go to the financial community that they will recognize as something they can understand. There is no need to understand the language of the financials markets if the Internet business is never going to need outside resources.

How does a business owner organize his Internet business to have the best opportunity to sell the business in the financial markets?
There are business structures that the financial markets are familiar with and there are business structures with which they are not familiar. The big growth is almost always in business structures that most of the financial market is not comfortable with to do investing. Therefore, it is the task of the business owner to shape the business to what is understood, if the maximum value is to be received during the selling process.

What educational materials must be given to the financial market to educate the market people about your specific Internet business?
Communications is not everything but it is close to everything. There are a lot of mediums in which to communicate. The issue today is that there is so much information that most people are overloaded about what information to pay attention to in the first place. It is necessary to evaluate the audience of the materials and determine what they need. Too little information and your message goes nowhere; too much and the audience is overwhelmed.

How does a business owner keep financial market people from wanting to run his business their way?
Trust is the name of the game when it comes to control. No trust and the lending source will want control. It again comes back to business management.

Investor Responsibilities
Investors in Internet business have responsibilities in the valuation process use. The words of the valuation process cannot be translated entirely to words that mean something to an investor in other businesses.

The Internet world is changing rapidly and has a set of technologies that require some understanding before the terms of the parameters being measured begin to mean anything to the investor. Therefore, the valuation report is saying one thing and the investor is reading something entirely different.

The investor has a responsibility to develop some knowledge of this business world. It is too easy to say it is just like some other business except with minor changes. This is just not true because the thought process of how to create, operate and maintain an Internet business is radically different. Yes, there are a number of elements that are the same, but this can sometimes get you as an investor into a miscalculation because you think you understand the business.

Owner/Investor Interactions
There will be a set of interactions between the owner and the investor. Sometimes these are friendly and sometimes these are not. Lots of investors have been successful elsewhere in business. They therefore know and understand the need and nature of excellent management. Most entrepreneurs are not excellent business managers. Business management needed to run and operate a business after it is established is normally different from what it takes to get it started.

Hence, there is a very different opinion of what is right for a business. Normally the starter of the business is still excited with the idea – whatever it is that sparked the creation of the business in the first place - and the investor sees the money portion of the business and what it takes to get a return on that investment.

Normally there is a time difference as to when things should happen. The owner normally has a longer time frame than the investor. This difference in time to investment return will cause tension between the owner and the investor.

What are the Internet business parameters that are the most important to venture capitalist?
There is only one thing that venture capitalists are interested in and that is assessing when there is going to be a return on investment. They like to be proud of how quickly they turned the money and returned a profit to the owner of the money. Normally venture capitalists want a substantial return on investment. This in necessary because they have difficulty predicting which business will make a return on investment. Therefore, they

will have some failures along the way where they need to have some successes that pay more then twenty percent.

What is the relationship between venture capitalist and Internet business entrepreneurs?
Normally lots of business meetings need to take place before a venture capitalist will turn loose of his money. The venture capitalist wants to ensure that there will be a return of the principal at least and a target of thirty five percent return per year on the investment. The owners will at some point object to the high price of venture capitalist money unless the company is expanding at a rate and with a return that it is just not that big of an issue.

Other owners and venture capitalists become good friends – and this friendship will last for the rest of their lives.

How do you sort out the desire of venture capitalists to want to manage your business when you know best?
A business can have too many cooks. Too many cooks will destroy a business. Valuation experts are looking for conflicting directions from management of a business. There is also the question of what process the business uses to decide what issues are the most important. There must be a process by which a business decides which items have the highest priority.

Venture capitalists can be a way to save a company or grow a company, but venture capitalists may not have sufficient management knowledge and skills to manage the business for this particular niche market. However, this may also be true of the owner. There will need to be an exchange between the two to discover the comfort zone.

How can a valuation help the prospective investor understand this Internet business?
Understanding comes from teaching. If the valuation process creates a document that teaches, then there will the Internet investor will have acquired an understanding.

There can be a question as to whether this is a perfect understanding and whether that understanding is sufficient to make intelligent decisions about the future involvement with a particular business.

Business Control
Direction has to come from somewhere. After all, poor business management is the number one reason for business failure. Therefore, the control and direction of the business is very critical. This is one of the reasons why selling a business to someone who does not understand the business will probably result in failure of the business at some point.

From a business valuation viewpoint there needs to be parameters that measure the management capability of the present management and the future management if a change is contemplated.

Investment Sources
There are lots of places where there is money to lend. However, that does not mean that any of that money has your name on it. If you are to be successful at finding money to support your specific business then you need to get to a funding source that understands your business.

Will local banks loan money to Internet businesses?
In 1995 the answer to borrowing money from a traditional bank for a very non-traditional business like the Internet was not looked at by banks as an excellent opportunity. As the Internet business market grows there will be more and more local banks to loan money to Internet businesses just like what is accomplished by banks working with local businesses.

Are there special companies that only deal with Internet businesses and understand how to finance these kinds of businesses?
You can find companies on the Internet that will finance your business. The question you need to ask is can you afford the money?

How do the financial markets view the Internet business?
The early 2000s dot com failures made investors want to look more closely. Other recent failures in traditional businesses have caused financial markets to be jittery about almost every financial market.

The view will change as Internet businesses begin to be defined and successful.

How did the dot com failures of the early 2000s change the way the financial markets view the Internet business?
Investors discovered that there is no substitute for doing homework on businesses. Entrepreneurs will always argue that this is different. This may be true but it may not be true. The financial markets are more careful now then before.

What financial parameters are the most important to the financial markets?
Return on investment. Any parameter that addresses the risk in that parameter is important to the financial markets.

What business parameters are the most important to the financial markets?
Good management and market uniqueness are very important business parameters to the financial markets.

Chapter 14: Valuation Reporting

Overview

Business valuations are subjectively built on a set of absolute and arbitrary parameter values. Each reader who looks at the valuation answers has their interpretation of them. Add to this the issue of the range of valuations that can be accomplished on a business and you have set up a possibility that the numbers given will have no meaning.

Let's start with the fact that the valuation process may have been only for part of the business and not the business in its entirety. It will be common for businesses that are part traditional and part Internet to want a valuation of the Internet portion only. However, if you are buying the business, the traditional aspects may need a different valuator.

The duty of the valuator in writing the report is to match the intended readers' ability of understanding the report as to what was accomplished during the valuation process. There are five steps to the valuation process. The extent to which each of these steps is accomplished must be clearly addressed in the report. This will reduce the probability of reading more into the report than the data and analysis can deliver.

The five steps of the valuation process are:

1. Define the extent of the valuation (partial or complete)
2. Gather the data (define the sources)
3. Analyze the data (extent of algorithms)
4. Determine the value (single, or range with conditions)
5. Write the report (focused to proposed readers)

The data from these five steps needs to be reflected in the report in a manner that the intended audience can understand.

Defining the extent of the valuation is important because full valuations are not always accomplished and therefore the number or numbers given in step four of the process needs to be bounded by the amount of valuation that was accomplished.

The report needs to address the parameters used in evaluating the business and the source of the values used. There can be a long list of parameters that can be measured in the valuation process. The subjective nature of generating the final value may mitigate some of the uncertainty of these parameters. One must be careful of the concept of "Measure

with a micrometer, mark with a piece of chalk and cut with an axe." We can get so precise in our parameter values but forget the subjective nature of the whole process.

There has been considerable effort over the decades to generate different sets of mathematical algorithms to describe the parameters being measured. These algorithms are an attempt at taking absolute parameter information and arbitrary parameter information and convert it into understandable economic business terms. All algorithms have limits. So the extent and limits of the analysis needs to be stated.

Most people affected by the process do not understand it, but they understand the one number at the end. They may not understand that the number needs to be discounted because the nature of the business or the economy or the speed with which the business needs to be sold. Nonetheless, they will understand that single number or range of numbers. What they will probably not understand is the "what if" scenarios that are associated with the number. In the business valuation business the final value given will always have the underlying response of "Well it depends" when asked if some element of the valuation process was considered differently.

The report needs to be written. Reports can become very dry material and the readers will jump to the end game to find the single value. The report should convey the extent of the valuation, the data gathered, the analysis and the method by which the value was determined. Then the report writer should consider who the readers would be and render a report that is in a language they can understand.

Readers of Valuation Reports

So in writing the report let's start with the reader viewpoint instead of the valuator viewpoint. The readers of the report are not as interested in the details of the valuation as the valuator. What they want to be able to do, at the end of reading the report, is to understand what they have been told and the extent of the valuation. Once the reader understands these two elements then he or she will be able to put the final number in context. It is very important for a reader to put the number in context. The number is not the end of the journey for the reader. The reader must now go forward with the number and determine what financial and legal consequences are associated with that number.

If the writer of the report considers the viewpoint of the reader when writing the report then the format of the report will change as the valuations change between different categories of Internet businesses and potential readers. The sellers of business and the buyers of businesses can be very different from each other. Nevertheless, different classes of business investors can be very different. How these different groups absorb information can be very different.

Communication methods today are many and varied. There may need to be some form of valuation communications other than written. Sometimes the subtleties of the valuation can be carried in spoken form or video form better. This does not substitute for written

form but not all readers absorb the context of the numbers as well in the written form as in some other communication forms.

Different readers with different expertise will have different views of the data. An executive summary in the beginning of the report may be very appropriate for one set of people where as others will want to know the details.

The details of the parameters used can be overwhelming to the casual reader of the report. Therefore it is important to treat the absolute and arbitrary parameters at a higher level than would be accomplished in a technical report. The valuation report is not a time to impress the world with your complex knowledge of the craft of your valuation business if your are the valuator.

If you are going to be the reader and you are also the person making the decision about who will perform the business valuation, you may want to look at previous sample reports of what the valuator has accomplished. Valuators will want to limit the number of formats and styles of writing the report. Readers, though, need to ensure that they can read and understand the reports. Therefore, having read the report, the reader needs to ascertain whether he or she understands any of the data presented.

The world is complex – but sometimes we make it more complicated then it needs to be. There are three fundamental reasons for making the report complex:

1. The writer does not understand the business and the business valuation process for the industry.
2. The writer is not a good teacher to explain the data in understandable terms.
3. The writer wants to impress the reader with his or her knowledge.

The report is about education. If it does not educate then it has not accomplished the reason for its existence at all.

Valuation Parameters

There are hundreds of parameters that can be measured. Not all of these parameters are needed all the time in any given valuation. It is very important in the initial stages of defining a valuation task to decide the extent of the valuation. Therefore, looking at the parameters being measured will give an insight into what is needed. The glossary in the back of this book lists some, but not all, of the parameters that valuators may use in determining the value of an Internet business.

If you are the valuator and take the perspective of the reader then you must help the reader understand which of all these parameters make sense for this particular Internet business. It is not necessary to list all the parameters used. However, the categories of parameters used in creating the value should be delineated.

It is not only the parameters but also the source of those parameters that matter. One of the great difficulties in accomplishing a valuation is that the input data is wrong. It is

wrong because it is not the right number for the parameter or it is wrong because it is the right value for the parameter but the information is very old and irrelevant to the present conditions.

Valuation Algorithms

Analysis is accomplished by using algorithms. Algorithms are mathematical formulas, which allow the combination of parameters to create a variety of more understandable outputs. Raw data is difficult to put into perspective for most people without some manipulation. What you want to accomplish here is to take absolute parameters and arbitrary parameters and combine them. This needs to be accomplished in a way that takes some of the emotion of the arbitrary parameters and instills some life into the absolute parameter values so that absolute values have some relevancy to the spirit of the business.

The arbitrary parameters will need to have some of the uncertainty of the values modified by the absolute numbers. Some of the emotion of the arbitrary numbers will be toned down to make the values more realistic with what is going on the business. The algorithm outputs take some of the hype of marketing and the business and tone down and integrate some of the hard cold facts of accounting.

There are algorithm output values that have to do with internal data and internal ratings of the business and there are algorithm outputs that have to do with external data and external ratings of the business in regard to other businesses in the market niche. It is the placement of these values in terms of the specific industry that will begin to make the raw data understandable to the reader. The reader will need perspective in order to know how much he or she should care about the number the value represents.

Valuation Ratings and Final Values

Valuation ratings have to do with how this business compares with itself if there has been more than one valuation and how the business compares with the market niche industry. The final Internet business values have to do with a single number or range of numbers that would be the fair market price, if that is what is asked for, of the business.

It is the recommendation of these authors that the business have frequent valuations to help not only in knowing the present value of the business to help in managing the business of growing the company. One of the great difficulties of most valuation processes is that the data necessary to go into the valuation is difficult to find and organize in a manner that is useful to the valuator.

This data acquisition with an Internet business can be substantially improved because many of the parameters needed are parameters that can be automated by the technology. Another difficulty of valuations is to find the data about other companies in the marketing niche with which to compare. Most of these Internet companies are small, closely held businesses that do not like to reveal their parameter values. However, on the Internet a

lot can be learned about the activity of a business from the industry rating that is created for every business on the Internet.

One of the advantages of accomplishing the valuations more often is that data will become more available from the business. What is true of all processes that are regularly measured is that those processes tend to improve. Furthermore, the data to support those improvements tends to be available.

Valuation Limitations

All valuations have subjective elements and therefore have limitations. Knowing the limitations is an important part of the valuation and the interpretation of that valuation. The limitations come from the:

1. Selection of the right parameters
2. Accuracy of the values for those parameters
3. Data (value) latency of the parameter values
4. Selection of algorithms
5. Availability of internal comparison data
6. Availability of external comparison data
7. Time to accomplish the valuation

Limitations are all right. There can never be a perfect valuation because there are always arbitrary parameters. Most arbitrary parameters are traced back to the desire to measure human responses. Measuring human responses to marketing has never been an exact science. Therefore, there will always be limitations, but these limitations just need to be known by the reader.

Valuation Background

The report needs to address the background of this particular valuation being accomplished. The background addresses the source of information, how that information is acquired and how that information is relevant to the present valuation.

There needs to be the background of the Internet business. When did it start? What is the stated mission of the business? What is the market niche of interest to this company? Why would this business be a good business and what is the potential in terms of the rest of the niche market?

National/Global Economic Review

All boats are on the same sea. Some are in a part of the sea that is more turbulent than others. The national and global economic status can have enormous impact on the valuation of a business. If the total economy is in a depression or deep recession then individual management of a business may not be able to accomplish company growth no matter what is tried.

There are other times when no matter how bad the product or the management of the business, the company will grow and prosper. Yet sooner or later that economic bubble will burst and the company will need to survive by having better products and better management.

Therefore, the valuation report needs to address the state of the economy as it relates to the Internet business being evaluated. Without this understanding the value of the company may be out of step with the economic times.

Valuation of Industry Overview

The niche market industry also needs to be valued. It may be that all the companies in the market niche are having a difficult time. The economy today is so broad and complex that the economy as a whole may be doing well, but the individual niche markets are not.

Therefore, there not only needs to be national and global economic state but the individual industry that is applicable to the Internet business being evaluated. With the industry data in the report it is easier to establish the values for the individual company. There is difficulty is generating this kind of data. The reason for this is that the Internet is young enough that there is not a lot of historical data.

Furthermore, the right parameters and ratios to rate the industry have not been established and agreed upon by these emerging industries. Time will solve this problem and will account for making it easier to establish this data. As more and more Internet businesses have buyers and sellers agreeing to a sales price, the valuation process will become more robust.

Estimated Financial Valuation

Valuations are about using the historical data to create an image of the future. All future are just estimations. There are no projected values that are absolute. All values in the future are arbitrary. Arbitrary here means subjective. A subjective number is all that valuation can have if it is a price that a hypothetical buyer would pay.

The only valuation that is not subjective is a negotiated value established by a willing buyer and a willing seller. The value will be made from subjective data but the final value is now absolute. These absolute values are like way point updates in a navigation system. Companies are navigating the business world as it evolves. The value of that company at any given point needs to be determined by comparison to other businesses being bought and sold periodically in the marketplace. Hopefully the marketplace for the buyer and seller is free trading and one of the parties in the deal is not under duress. Having one of the parties under duress does not result in a true way point update to the navigation system of the valuation process.

The Elements of the Report

The elements of the report do not need to be the same for every report or for every business, but generally the following elements should be in a valuation report:

1. Title page
2. Letter report (What the valuation task is)
3. Executive Summary
4. Table of Contents
5. Body of Report (details of the valuation)
6. Purpose and Approach to Valuation
7. Limiting Conditions of Valuation
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Chapter 15: The Internet Business Valuation System

Overview
Twenty years from now will be like an eternity for Internet business valuators. We will look back at the simplicity of this valuation process and wonder how we got any good information out of it. Still, it is the system today and we are building the fundamental concepts and applying these concepts in new ways to customer interfaces that are changing rapidly.

The fundamentals of a valuation system is that there are parameters to measure, there are algorithms that take that information and put that information into manageable quantities and there are ratings that place that information in context of the niche industry and Internet business industry.

Once this information is collected and analyzed it needs to be substantiated. Substantiation is accomplished by verifying what is happening today in the marketplace. How are similar businesses being bought and sold? How much are these businesses being bought for in the marketplace today? The associated question with the value of a business is how liquid is the value. The liquidity of the value is also an important aspect of a valuation process. If the business is valued at a million dollars and there are no buyers then the value has only a value to the present owner.

The financial community will still look at the financial numbers first before moving forward. The financial numbers need to be in place. The need to accomplish the accounting aspects of the valuation is still necessary. That is one element that has not changed from the days of traditional business valuations.

In the future there will be more business management interaction because the more detailed numbers will look familiar to the management or prospective management if the company is for sale. Therefore, it is important that the valuation of an Internet business not only address the needs of the financial investment community, but also the more detailed parameter values that will be important to Internet business management professionals.

Valuation Parameters
Full and very exhaustive valuations can have hundreds of parameters. Most valuations are limited valuations that only take a few days to accomplish. But not all valuations should be limited. Once in a while the business should look at all the parameters and determine what subtitles are there that do not meet the eye with a very quick look.

We have looked at many parameters in this book. There is a list of some of these parameters in the glossary. Looking at parameters without having them categorized makes it difficult to understand which parameters are more significant than others. That is the reason for this book: to put those parameters in perspective as the parameters relate to the valuation process.

There are absolute parameters and there are arbitrary parameters. The absolute parameters are those that can be measured precisely. The arbitrary ones are those parameters that have some range of values and are more ”fuzzy” to our way of thinking. These “fuzzy” numbers are the opposite of the absolute parameters that can be measured and known exactly. However, what we are dealing with here are humans as customers and humans, by their very nature, are somewhat unpredictable and therefore some of the most important information is not the exact information on the income statement or the expense statement of an Internet business.

Valuation Algorithms

The algorithms take the parameter information and convert that information into more meaningful numbers. The minds of most people just cannot discern the patterns that are the most important by looking at the raw parameter data. When you are looking at extremes the mind soon asks for averages. Just look at the weather data. Most often it is the averages that are published in books. It has only been since the advent of the Internet that the extremes of the data have been made available to the general public.

A parameter all by itself may tell a business story but it is the combination of parameter values, both absolute and arbitrary, that brings the story together in a meaningful way that the investment community can understand.

Valuation Value Ratings

The ratings go back to the niche market ratings. How many customers do my competitors have visiting their web site? This can be very helpful in understanding the value of the business. On the Internet some businesses have millions of visitors per day. These are the mega-businesses that are addressing certain general needs. There are only so many of these large businesses and they will fill those needs of the general Internet customer base. There will be competition in those niche markets just like there is competition in your niche market.

It is instructive to see the big visitor number but it also can be numbing to think about how your business can get to those kinds of visitor rates. Nevertheless, that is not as important as it is that you have a return on your effort. It does not take very many customers to have a comfortable business. Just take a look at the local traditional businesses. These businesses do not have millions of visitors. The store is just not big enough to accommodate that many visitors.

Valuation Substantiation

Whatever the value stated in the valuation, there needs to be a substantiation process. That is accomplished here by reviewing the businesses that are being bought and sold in the marketplace today. That is why the www.buysellwebsite.com was created. The first reasons was to create a place for business owners to advertise their businesses and the second was to begin to develop the substantiation data needed to create valuations.

Investment Community Interaction
If the business is to borrow money or have investments then there is a need to have an interaction with the investment community. The investment community is a broad vision of that community here. You could go to your local banker and borrow money. You could go to a set of friends and have them invest in your business. You could go to the venture capitalists and have them invest in your business. Or you could go public and sell stock in your company.

All of these methods require that you tell the world about your Internet business. Furthermore, the entire financial community is looking for independent verification that the numbers you are touting are, in fact, believable numbers.

Business Management Interaction
Since business management is the number one reason why startup companies fail then there must be an interaction of the valuation with people who know and understand the management aspect of the Internet business. Therefore, the final reports need to address the needs of this community also.

Business management is imperative if the business is to survive in the fast-paced world of the Internet. Therefore, the valuation and the report of the valuation also need to address these concerns. This is a departure from traditional business valuations. There is a mention of management but the focus has been on the financial numbers.

Recent large corporation business failures have shown that it is very important to look at the management structure, capability and oversight.

Chapter 16: Valuation System Used Today

Overview
This book has been about the value of the Internet Business System that is accomplishing business on the Internet. This type of system is a new form of wealth for the economy.

The Internet Business System consists of all the business and financial elements of an Internet Business. An Internet Business is a business that has the majority of the transactions over the Internet. Companies that have at least fifty percent of their business from a traditional business are hybrid Internet Businesses.

It is easy to measure and determine the expenses and the income of Internet businesses. It is not as easy is to determine the value of such businesses. There are a lot of reasons to want to know the value of the assets of an Internet business. Some of those assets are not measurable with absolute certainty. In some respects Internet businesses have some of the same characteristics as art. The beauty of the art is in the eye of the beholder. So is some of the beauty of an Internet business – it is in the eye of the customer.

Reasons for Valuation
There are many reasons to want to know the value of Internet businesses. The primary goal for now concerns obtaining financing. The purpose of obtaining financing is either to continue to grow the business or to sell the business to an investor or investors.

Valuation for Internet business, in the long run, will probably also turn into a business management tool that will allow the management of the Internet business to accomplish at least a portion of the valuation on a frequent periodic basis to monitor the progress of the company. Because if you do not know the value of the company then how do you know for sure whether the business is producing any wealth?

In the final analysis of this valuation process, we need to ask some fundamental questions as to what we are going to accomplish with the information once we have it. The two fundamental questions are:

- Who is going to use the valuation report?
- What are they going to accomplish by using the valuation report?

In any process there are always a lot of factors taken into consideration. However, the value of any specific company comes down to just a few things that are very important and a lot of things that are not very important. There are also a great number of parameters we monitor that generally do not have much impact. The valuation process is

used to help identify these elements of the Internet business that are very important and important to the value of the Internet business.

You are investing in the Internet business future--not the past. As we are trying to predict the future, all values generated by a valuation process will have uncertainty and investment risk associated with that uncertainty.

In evaluating a company you must also evaluate a market niche of the future. The company may have done very well in the past but would not go forward because the niche market has already been sold to once and the product of the company is something that is only purchased once by a customer.

The Valuation Process

Internet business valuations have absolute parameters and arbitrary parameters. Absolute parameters are hard numbers in a valuation process. Hard numbers may also be misleading as to the value of a company. Absolute parameters have to be tailored by arbitrary numbers where the emotion of the business is dominant.

What is needed is a way to capture the uniqueness of the business and how that uniqueness, in the marketplace, gives the company value. Not all of the uniqueness of a company may be transferable to others. This is because some of the uniqueness may be involved in the characteristics of the present owner and not transferable to someone else if ownership and management of the business are being transferred. This is especially true in small Internet businesses where the creators and owners of the business have not written the business processes down for others to follow.

Therefore, you must also use the arbitrary parameters in order to obtain a better indication of the worth of a company. There is also the emotional aspect of every business that has uniqueness in the marketplace. The emotions of the business can make the value higher or lower than the absolute parameters would indicate.

There are two fundamental kinds of data that need to be involved in an Internet business valuation. The first has to do with financial data. The second has to do with the business data. The business data also includes the marketing data that drives the existence of the company. These parameters are used together in an analysis that in the end have some subjective ratings to the variability of the value of a business.

Customer Impact

Customers drive all businesses. Customers are only customers if they are reachable. So what is a reachable customer on the Internet? There are millions of people connected to the Internet, but connection to the Internet does not make those people a customer of any company.

So we need to go back to the fundamentals of the customer acquisition process. Can we count the potential numbers of customers that can be reached? If the answer to that question is yes, then the next question is what it will take to get these potential customers

to respond. Once you get the potential customer to be a visitor on your web site then there are a series of other qualifying questions that convert the visitor into a customer. For example, do they have sufficient disposable income to purchase your product?

Internet Business Creators

Entrepreneurs start most small Internet businesses. Entrepreneurs are very good at some things and not so good in general at other things in business. Most entrepreneurs are not necessarily good as business managers when the company gets larger. Entrepreneurs are accustomed to having hands on every aspect of the business, whether they are capable of efficiently handling that aspect or not. Therefore, it is important for most entrepreneurs of companies to set up the company for sale if it is going to get very large. Yet some business owners do not want to grow the business outside a certain boundary. Therefore if you do not ever plan on selling the company, then valuations may not serve any purpose. If you also never plan on asking for investment money from some third party, then you may not need a valuation.

So if you are not going to sell the company, and you do not plan on ever borrowing money to expand the company, then what reason would there be to evaluate your company? Well, if you were to die and leave the company to someone who does not want to run the company, they would have a range of what the company is worth as a starting point to sell the business. There are certain parameters that go into valuations that only the business owner knows. Therefore, those parameter values need to be captured at least once in one valuation. Then someone coming later will know to go find the updated numbers for a new valuation.

Substantiating the Numbers

One of the concerns is substantiating the numbers that go into a valuation. If you have real estate to sell then the appraisal is built on similar properties that have sold recently. There is some uncertainty in the appraisal because there is the emotion that a property affects in the buyer. It is the emotion that is so hard to capture in an appraisal. Why would someone pay extra because of the emotion of an item or property?

The valuation process for Internet businesses will become more quantified. This occurs as more and more Internet businesses are valued and the company changing owners at that price validates those valuations. After a time the Internet business will begin to be placed in categories and these categories of Internet Property will have businesses that have been valued and sold. This will establish some historical data that will begin to limit the uncertainty of the valuation process to establish the value of an Internet business.

The present owner furnishes a lot of the numbers that go into a valuation. So how do you verify these numbers independently? Well, there are analysis accomplished by independent reviews on the Internet. You can verify the ranking of the web site by using third party data. This is one element that is radically different from traditional businesses.

So valuations are not just about numbers – they are also about verifiable numbers. If the numbers are not verifiable then the valuation is not of much value. Therefore, the company accomplishing the valuation needs to have some process that finds a way to reduce the risk of having bad numbers. Accounting practices have used a variety of processes to insure integrity of the numbers – so it is also true of valuation numbers – they must be verifiable.

Time will establish what a business is worth as unique parameters are established. Until then the process has greater uncertainty and risks to the potential investor. A number one ranking in a market niche is always worth more than some other lower ranking. Therefore, if you are going to set your business apart then you need to start to attain the highest ranking in your marketplace.

Yet just like location is important in real estate markets, location on the Internet is also important. Location on the Internet is by the domain name and the recognition in the marketplace.

Regular customer traffic to your site is a must. Repeat traffic is absolutely necessary because most customers will not leave you money on the first visit. Back-end sales are always more profitable than the first sale to a customer. Therefore, you must have a marketing strategy that includes back-end sales. If every sale has to be a unique customer sale then it is hard to build an Internet business. Internet businesses are built because your customers get to know who you are and they trust and know your work.

Getting to the Value

Financial data is the easiest of all the data to obtain. But because it is a set of numbers it is also the set of numbers that can be used to mislead people about what is really occurring with the company. Because it is a set of numbers it is the one piece of data you think you can believe. However, there is plenty of evidence in financial markets to indicate that there are those who want to and will alter the numbers in unique fraudulent ways.

Now you have an industry where there is no history of which numbers even matter or how to count or how to analyze. So people with even the best of intentions could be adding up the wrong numbers. Time and experience will remedy this issue. This book is one step on the path of that higher plateau where we know what financial numbers to go after and what to do with the numbers once we have them.

Business data is more difficult to put numbers on these parameters. However in the case of this kind of data it is apparent to all that these numbers are not absolute and therefore each person's discounts them experience in the market place.

This category also includes the business processes that are necessary to run the business. One of these elements in the process is people. Take people out of the equation and you have nothing happening.

Now there are elements of the business that have been automated but these elements are as good as the last update to the automation process being implemented.

Included in this category is the emotion of a business that needs to be characterized. Does anyone really care about the products of this business? Is this just a temporary product? Is it a fad? Can this product be updated?

It is the future that you are investing in and the future has always been uncertain. Nevertheless, the future is where the return on investment is. The past will not acquire you a return on the investment.

The analysis is taking the number and creating a new number. This new number is a composite of all the other numbers that says today this company, if it stays on the present course it is worth between this and this number.

This number by itself should not be the only number or rating used as an investor or business owner as to where they want to be.

Analysis is just analysis. It is no better and no worse than the raw data that went into the analysis and the algorithm used to convert that raw data into another set of evaluated numbers. Analysis can be educational or misleading depending on our understanding of the valuation process.

What this exercise is all about is getting to the investment value of a business that is an Internet business. Business owners need this information on a periodic basis so that they know what their progress is in developing the Internet business.

If the business owner seeks financing, then the lending institution needs something. Lending institutions need some basis to justify why they loaned the money.

There are the standard financial data. But that is not enough. The market on the Internet is hard to characterize. Hard to characterize the competitions, hard to characterize the core technologies that make the Internet work in a marketing sense and how all of this together impacts the worth of a company.

It is the worth that we wish to develop or a process to characterize that evaluates an Internet business until more and more of the uncertainty is removed in the valuation process and go back into normal business uncertainty ranges.

Chapter 17: The Future of Valuations

Overview
Business valuations are an important tool. This is especially true if the subjectivity of the valuation is reduced to a level where the uncertainty range of the final value is close to what a business will sell for in the marketplace. Valuations can be more than just tools for the financial community, if developed and used appropriately.

Standards have been developed over the decades by which valuations need to be accomplished. In the generic sense these standards are still applicable to a business valuation process. What has happened here is that we do not just have a new business category doing business in a storefront like what we are accustomed to. We have a new technology core that has fundamentally changed the way we do business.

On account of this fundamental change in the core of business the language of that business is not adequate to even carry on a conversation about the business. Therefore a whole new language must be developed in order to allow the discussion to occur. That has been what this book is about. Formalizing the language that can be used to have a repeatable method to accomplish the valuation process when evaluating an Internet business.

As a Financial Tool
Because the final number of valuations are a financial number the tool has been viewed as a financial tool. The financial tool was created to acknowledge the value of a business without having to sell the business to discover the worth of the company.

This is why the valuation wants to give an unambiguous answer to what the Internet business is worth. This unambiguous answer has historically been in a single number or a range of numbers that says the business is at least worth this minimum amount but it may be worth as much as some maximum amount.

This element of an unambiguous value will probably not change in the future. This is because when the business is sold there is a single number that is agreed to, for the final offer to sell a business. There are not two numbers or a range of numbers at that point. For example, a real estate property when sold as a single value. Even though the valuation predicts a range of values that the Internet business can be sold for there will be a single value when the business is sold.

The valuation of the future will still need to consider all relevant information. The thing that will change as the Internet changes is what is considered relevant information. The issue here is can we predict how this list of relevant information will change as the Internet evolves?

The answer is that it will be difficult to predict – except that there will be laws created that will restrict what you may or may not do with information from your customers. This legislation will certainly change the parameters used and the algorithms that use the data from measuring those parameters.

There will be other technologies invented that will also change the way we communicate. The communications will become more "wireless." People are mobile and the communication will become mobile. How this mobility will change the parameters that we will need to measure is not clear at this point. The difficulty with "wireless" is that the information is not about locations anymore. It relates to classes of people who respond.

In the case of traditional businesses where location is everything, the Internet will shift that paradigm to where it is the person no matter what the physical location. Phone numbers do not keep changing because of physical location changes but stay the same because that is easier then trying to keep track of where people are located.

There is a requirement that after the valuator has identified all relevant information, that the information be gathered and analyzed. There will be changes in the way we gather information. The core technologies of the Internet will continue to change. The core technologies are driven by the computations and communications capabilities. These technologies have been growing at a constant rate for decades and there does not seem to be an end in sight. Each improvement will change the way we do business and as those changes occur there will be changes in the valuation process for Internet businesses.

The computational power will continue to increase also. This increase in computational power will allow algorithms of considerably more power to be implemented. The use of fuzzy logic and neural network technology will be commonplace in the valuation industry. Today it is difficult to use these technologies extensively because the fundamentals of the Internet business parameters are not established.

The concepts will probably become more and more driven by the information technologies so that the method of valuation will tend toward marketing. This will be in contrast to the industrial revolution where the trend was to use capital and labor as the driving valuation methods.

Since the Internet lends the possibility of automation of some of the processes of the valuation then there will be a trend toward limited valuations. Limited valuations means that only a portion of the valuation will be used. This will become increasing obvious because certain portions of the business will not change very much while other portions will change a lot as technology changes. It is expected that the customer interface will be

the one element of the valuation that will be under constant change for a long time to come.

The valuation in the future will still contain:

a. The information about the fundamental characteristics of the Internet business.
b. The nature, history and outlook of the Internet business.
c. The historical relevant financial data of the business such as past valuations and how the company has performed against those valuations.
d. The assets and liabilities of the Internet business, which will require new definitions of what assets are and what liabilities are in this world.
e. The comparison to relevant industries and how this business rates in relationship to those other companies in the industry.
f. The various economic factors that will play a part in the valuation, such as the major general economic factors that affect all business and especially those businesses in a given niche market.
g. Major recent transactions of the business that will change the value of the business.
h. Also any other information that is relevant to the valuation and the relevancy for Internet businesses will continue to change over time.

What will change are the parameters and analysis to generate the information above. Ignore the changes and the valuations will not have much meaning in the buy and sell marketplace where there is an exchange of businesses.

As a Management Tool

The greatest change from a valuation viewpoint will be the use of the fundamental valuation technology and processes to accomplish management of the Internet business. The primary reason why businesses fail is poor business management. The valuation will not stop managers from making bad decisions. What it will do is give the manager more data on which to base decisions.

The area of the business that it will impact the most is the customer interface. It is the customer interface that is so difficult with traditional businesses. It is hard to record individual customer events or actions. What it will not get is the thought process unless you invent ways to measure the performance of the business in the eyes of the customer.

Very short surveys can be enlightening about the company. These simple questionnaires can ask for two pieces of information:

a. What is the thing you like the most about the company.
b. What is the thing you like the worst.

A very good image of the company can be built just on the answers to these two questions. These types of customer questionnaires will be developed to accomplish a comprehensive valuation. If a company has had several thousand customers in the email

database a simple survey like this with just a few respondents will have an impact on the future value of the company.

The minute-by-minute data about customer activity on the web site is a powerful indicator of the capability of the web site. The web site design and the products and services that it provides is a composite story for the customer. If that story is not correct then there will be a decrease in customer activity. Very bad web sites that are not customer friendly will push people away. However, what will happen in the future is that the web site that is customer friendly will change as the technology changes and as the competition finds ways to attract customers.

The marketing parameters identified in this book will become daily management tools as businesses find ways to automatically record and display this information to management decision-makers. The disadvantage of this information is that it needs to periodically be compared to normal values in other companies within your marketing niche. Just because the values look good to you does not insure that they are excellent values when compared with your competitors.

The Internet has introduced a core technology and will continue to change. There is a standard curve that has been used to follow the development of technology and that is an S-curve. The curve looks like a lazy S. At the end of the S the technology has reached maturity. The investment is low and the return is high. This is contrasted to the lower end of the S-curve where the investment is high and the return is low.

The Soviet government made a decision to watch the S-curve development of the computer industry and to steal the technology when the technology reached the end of the S-curve. This was to be accomplished instead of developing the technology within the Soviet Union. What happened was that the technology continued to develop at the same rate for decades until it was too late for the Soviet Union to recover from the technology deficit.

The computer and communications industries are still improving at the same rate as decades ago when the Soviet Union made a decision not to invest. Internet businesses are driven by that technology development. If you choose not to invest in the technology and just wait and steal it from your competitors it may be way too late for you to recover.

Valuation parameters today will become management tools tomorrow and there will be a new set of valuation parameters needed. The algorithms used today will become the management valuation algorithms of tomorrow and there will be new analysis technologies that will allow more and quicker insights into the marketplace and how your business should respond to the changes.

Appendix A

Questions for Valuation of Internet Businesses

Creating a valuation of any Internet Business requires an understanding of the issues that relate to that business and how it is evaluated. There are a number of ways to get at that understanding, but one of the most efficient is to ask questions. This appendix is added to the book to help the reader understand the types of questions one must ask and eventually answer if there is to be a successful valuation of an Internet Business.

No matter what the subject, the method of asking questions, prioritizing questions and answering questions can be a very effective tool to arrive at an understanding of the subject. We learned how to ask questions early in life. (Have you ever been around a five-year-old?) Along the way we stopped asking lots of questions. Yet questions are an excellent method to gain insight into a subject and should be considered as a primary means of becoming knowledgeable of the Internet Business valuation process. Therefore, this appendix has been added to give you a suggestion of the kinds of questions that you may want to ask and answer as you proceed to evaluate and place a value on your own Internet Business.

The categories and questions are not in any sequence of importance. Each business will have their own priorities that will drive the sequence of answering the questions.

I. Categories

1. Systems - Internet Business
2. Valuation Process - Internet Business
3. Valuation Process - Traditional Business
4. Valuation Process Differences Between Internet and Traditional Valuation Processes
5. Parameters - Absolute
6. Parameters - Arbitrary
7. Analysis of Absolute Parameters
8. Analysis of Arbitrary Parameters
9. Analysis of Dominant Absolute Parameters and Some Arbitrary Parameters
10. Analysis of Dominant Arbitrary Parameters and Some Absolute Parameters
11. Conversion Process of Absolute Parameter to Internet Business Ratings
12. Conversion Process of Arbitrary Parameters to Internet Business Ratings
13. Conversion Process of Absolute/Arbitrary Parameters to Internet Business Ratings
14. Conversion Process of Arbitrary/Absolute Parameter to Internet Business Ratings
15. Web Site Design
16. Web Site Design - Internet Links
17. Web Site Design - Language Issues
18. Web Site Design - Valuation Elements
19. Stability Factors - Internet Business
20. Customers, Customer Traffic – Internet Business
21. Advertising - Internet Business
22. Expenses - Internet Business
23. Income - Internet Business
24. Investment – Internet Business
25. Financial Data– Internet Business
26. Business Data – Internet Business
27. Search Engine, Keyword Impact - Internet Business
28. Manufacturing Capability – Internet Business
29. Marketing – Internet Business
30. Intellectual Property - Internet Business
31. Support Structure – Internet Business
32. Product – Internet Business
33. Service – Internet Business
34. Visitor – Internet Business
35. History of Property Appraisal
36. Periodicity of Valuations for Internet Businesses
37. Measurement Methods for Absolute Parameters
38. Measurement Methods for Arbitrary Parameters
39. Financial Markets and Internet Businesses
40. Customer Financing for Internet Businesses

Questions by Category

1. Systems - Internet Business

The questions in this section have to do with the definition and identification of Internet Business systems. Trying to identify the types and kinds of businesses that will constitute Internet Businesses. These questions are to develop the insight into web-based business systems as an integral unit and how they are different and also the same as traditional business systems.

1. What is an Internet Business system?
2. What are the characteristics of an Internet Business system?
3. What percentage of the income of a business needs to be accomplished on the Internet before a company is considered an Internet Business system?
4. What are the marketing parameters used in an Internet Business system that make it a different system then traditional business systems?
5. How are businesses characterized that have half their business from the Internet and the other half from a traditional business?
6. What are the financial parameters used in an Internet Business systems?
7. What are the business parameters used in an Internet Business system?
8. What are the marketing parameters used in an Internet Business system?
9. How do you recognize and categorize into types for valuation purposes an Internet Business system?
10. How is an Internet Business system different then Traditional Businesses system?
11. What constitutes a successful Internet Business system?
12. What constitutes a failed Internet Business system?
13. What is the average length of time for an Internet business system to become profitable?
14. What are the stability requirements for Internet Business systems?
15. How are the stability parameters measured and evaluated for an Internet Business system?

2. Valuation Process - Internet Business

The questions in this category address the overview of how an Internet Business is evaluated and appraised. These are the parameters and processes that have been used in the past and are evolving in the future. Some of these parameters and processes can be borrowed from traditional business valuation and valuation processes.

1. What is considered to be an Internet business where this valuation process would apply?
2. What are the business parameters needed to accomplish an Internet business valuation?
3. What are the financial parameters needed to accomplish an Internet business valuation?
4. What are the marketing parameters needed to accomplish an Internet business valuation?

5. What requirements are driving the Internet business to accomplish an valuation?
6. How often must an Internet business have a valuation?
7. What valuation parameters will have the most impact on the value of the Internet business?
8. What analysis processes are used to evaluate an Internet business?
9. What conversion processes are used to convert the parameter analysis to Internet business values and ratings?
10. What elements of the valuation have low risk and high certainty?
11. What elements of the valuation have high risk and high uncertainty?
12. How does the valuation process account for businesses that have a substantial traditional business component to the business?
13. If the business has a substantial traditional business component is the business appraised as two separate businesses?

3. Valuation Process - Traditional Business

The questions in this category address the overview of how a traditional business is evaluated and appraised. These are parameters and processes that have been in place for a long time. Many of those parameters and processes are applicable to Internet Business systems.

1. What is considered a traditional business that is being evaluated and appraised?
2. What are the financial data parameters used in the traditional business valuation?
3. What are the market valuation parameters used in the traditional business valuation?
4. What are the marketing data parameters used in a traditional business valuation?
5. What are the business data parameters used in a traditional business?
6. What are the valuation requirements for a traditional business valuation process?
7. What are the business design requirements for a traditional business that will impact the valuation process?
8. How often does an valuation need to be accomplished for a traditional business?
9. What parameters does the business owner change to have a significant impact on the valuation process and value of the business?
10. How do these valuation parameters change from industry to industry types in a traditional business?
11. Can traditional valuation processes be used to evaluate any portions of an Internet Business system?
12. What are the analysis processes used in the valuation process for traditional business parameters.

13. What is the conversion process of the parameter analysis to business value and ratings for traditional businesses?
14. What part of the valuation process is considered well established and without uncertainty when evaluating traditional businesses?
15. What part of the valuation process is considered arbitrary and with uncertainty when evaluating traditional businesses?

4. Valuation Process Differences Between Internet and Traditional Valuation Processes

The questions in this category address the overview of the differences between traditional businesses and Internet Businesses. It is to address how business characteristics are different and how those differences can complement a traditional business if so desired.

1. What are the characteristics differences in an Internet businesses from traditional valuation processes?
2. What are the valuation parameter differences between an Internet businesses and traditional businesses?
3. Do Internet businesses all have the same industry category from an valuation viewpoint?
4. Do Internet businesses need different industry valuation criteria depending on what products or services are being sold?
5. Can valuation parameters used in the traditional business valuation processes be modified to use for portions of an Internet business valuation?
6. What valuation parameters are used in Internet business valuations that are not used in the traditional business valuations?
7. How quickly are unique, Internet business, parameters changing as the Internet is changing?
8. How quickly are traditional parameters that can be used to evaluate an Internet business being modified because of the changing Internet environment?
9. How fast do the marketing trends occur in an Internet business that makes it unique from a traditional business?
10. What are the differences in customers between traditional businesses and Internet businesses?
11. What are the differences in customer loyalty between traditional businesses and Internet businesses?
12. Is there a difference in the rate of acquiring the parameter information between the traditional process and the Internet business systems?
13. What is the difference in cost of understanding the valuation parameters with a traditional business versus an Internet business?
14. Are brick and mortar traditional businesses easier to evaluate and appraise then Internet businesses?
15. What elements of the valuation and valuation process for Internet businesses are much easier to accomplish then a traditional business?

5. Parameters - Absolute

The questions in this category address the parameters that can be measured with a great deal of certainty. These parameters are those that have very definable and very measurable processes that have repeatable results. These parameters are not sufficient to evaluate an Internet-based business but are a foundation upon which to begin to evaluate and to appraise. If these parameters are not within certain limits then other less exact (arbitrary) parameters are very difficult to evaluate.

1. How many different absolute parameters can be measured by using the Internet business communications technology?
2. What are the names of these absolute parameters?
3. What does having a visitor mean in an Internet business?
4. What does it mean to have a customer in an Internet business?
5. What does it mean to have a repeat customer in an Internet business?
6. How does one measure having a visitor in an Internet business?
7. What does having a unique visitor mean in an Internet business?
8. How does one measure having a unique visitor in an Internet business?
9. What does it mean to have web site link popularity?
10. How does one measure web site link popularity?
11. How are these absolute parameters measured in general for an Internet business?
12. Is measuring customer and visitor absolute parameters an invasion of customer privacy?
13. Which of these absolute parameters may not be available in the future because of legislation restrictions?
14. What are the periods of time that these parameters must be measured in order to be meaningful to the valuation process?
15. What are the limits of each of these absolute parameters in creating meaningful information?

6. Parameters - Arbitrary

The questions in this category address the parameters that can only be measured with some degree of uncertainty as to the value and the meaning of that value. Ultimately Internet businesses, like traditional businesses, are dealing with people and what we are attempting to measure is the response of people to the business to determine the business value. Measuring people's responses is always a bit arbitrary.

1. What are the arbitrary parameters that need to be measured for an Internet business?
2. How many different arbitrary parameters can be measured by using the Internet business communications technology?
3. What are the names of these arbitrary parameters?
4. How are these arbitrary parameters measured?
5. Is measuring customer and visitor arbitrary parameters an invasion of privacy?

6. Which of these arbitrary parameters may not be available in the future because of legislation restrictions?
7. What are the periods of time that these arbitrary parameters must be measured in order to have meaningful information?
8. What are the limits of each of these arbitrary parameters in creating meaningful information?
9. What does having a professional designed web site mean as an arbitrary parameter?
10. How does one measure the value of a professional designed web site?
11. What does it mean to have a unique marketing advantage on the web?
12. How does one measure having a unique marketing advantage on the web?
13. What is a domain name?
14. How does the domain name increase or decrease the value of an Internet business?
15. How does one measure the increase or decrease in the value of an Internet business created by the domain name?
16. How does one take a arbitrary parameter and create data valuation analysis and conversion processes that are more like the absolute parameters without so much uncertainty?

7. Analysis of Absolute Parameters

The questions in this category address the analysis of the absolute parameters. Because these parameters are definable and measurable then computer based tools can be used to help the analysis and conversion processes of these parameters to meaningful business values and ratings..

1. What is an analysis and conversion process of absolute parameters for an Internet business?
2. What are the algorithms that can be used to accomplish the absolute parameter analysis?
3. How are these absolute parameter analysis algorithms changing with the development of the Internet business systems?
4. What are the substantiation data, which will be used for these absolute parameter algorithms, which will validate the valuation?
5. How are the algorithms of the analysis of absolute parameters changing from product category to product category of Internet businesses?
6. Where are the uncertainties in the analysis process of absolute parameters?
7. Do the absolute parameter algorithms create a distorted view of the business value and what is that distortion?
8. What is the income monthly average gross over three months parameter, how is it measured and why is it important to an Internet business?
9. What is the income monthly average net over three-month parameter, how is it measured and why is it important to an Internet business?
10. What is the income multiplier net over nine-month parameter, how is it measured and why is it important to an Internet business?

11. What is the income multiplier net over twelve-month parameter, how is it measured and why is it important to an Internet business?
12. What is the maximum/minimum income ratio, how is it measured and why is it important to an Internet business?
13. How long does it take to acquire the parameter values needed for the valuation?
14. How long does it take to accomplish the analysis of the absolute parameters?
15. How much of the parameter value acquisition and parameter analysis can be automated?

8. Analysis of Arbitrary Parameters

The questions in this category address the analysis of the arbitrary parameters. These parameters are much more difficult to use in an analysis because of the subjective nature of the parameters. Human valuation processes are much better at accomplishing this. The difficulty with using humans to accomplish this analysis is that the process is not necessarily repeatable. Two different people can arrive at two very different answers, while looking at the same set of data as inputs to an analysis.

1. What is an analysis of arbitrary parameters?
2. What are the algorithms that can be used to accomplish the arbitrary parameter analysis?
3. How are these arbitrary parameter analysis algorithms changing with the development of the Internet business systems?
4. What are the substantiation data, which will be used for these arbitrary parameter algorithms, which will validate the valuation?
5. How are the algorithms of the analysis of arbitrary parameters changing from product category to product category in Internet businesses?
6. Where are the uncertainties in the arbitrary parameter analysis process?
7. Does the arbitrary parameter algorithm create a distorted view of the business value and what is that distortion?
8. How does the valuation process reduce the uncertainty between two different people accomplishing the valuation for arbitrary parameters?
9. How does the valuation process reduce the uncertainty between two different valuations of the same business separated by at least one year between valuations?
10. Can customer surveys be used to help in the valuation of these arbitrary parameters?

9. Analysis of Dominant Absolute Parameters and Some Arbitrary Parameters

The questions in this category address the use of mostly absolute parameters with some arbitrary parameters to develop valuation value ratings of Internet businesses. This analysis improves the absolute parameters by injecting some of the emotion of the business into the valuation value ratings.

1. What is an analysis of dominant absolute and some arbitrary parameters?
2. Why is it important to have both kinds of parameters in the analysis of an Internet business?
3. What are the algorithms that can be used to accomplish the absolute/arbitrary parameter analysis?
4. How are these absolute/arbitrary parameter analysis algorithms changing with the development of the Internet business systems?
5. If the parameters and analysis are changing with time how does a business owner correlate two different valuations that were accomplished one or two years apart?
6. What is the substantiation data that these absolute/arbitrary parameter algorithms are valid for this kind of valuation?
7. How are the algorithms of the analysis of absolute/arbitrary parameters changing from product category to product category in Internet businesses?
8. Where are the uncertainties in the absolute/arbitrary parameter analysis process?
9. How much risk is in the uncertainty of the analysis?
10. Is the uncertainty of the analysis less then the uncertainty of the future of business on the Internet?
11. Does the absolute/arbitrary parameter algorithm create a distorted view of the business value and what is that distortion?
12. If the view is distorted by some amount, how is that distortion quantified?

10. Analysis of Dominant Arbitrary Parameters and Some Absolute Parameters

The questions in this category address the use of mostly arbitrary parameters with some absolute parameters to develop valuation value ratings of an Internet business. This analysis improves the arbitrary parameters by injecting some of the absolute numbers into the valuation value ratings.

1. What is an analysis of dominant arbitrary and some absolute parameters?
2. Why is it important to have both kinds, arbitrary and absolute, parameters in the analysis of an Internet business?
3. What are the algorithms that can be used to accomplish the arbitrary/absolute parameter analysis?
4. How are these arbitrary/absolute parameter analysis algorithms changing with the development of the Internet business systems?
5. What is the substantiation data that these arbitrary/absolute parameter algorithms are valid for this kind of valuation?
6. How are the algorithms of the analysis of arbitrary/absolute parameters changing from product category to product category in Internet businesses?
7. Where are the uncertainties in the arbitrary/absolute parameter analysis process?
8. How are the uncertainties of the analysis quantified?
9. How are the uncertainties turned into to recognizable business risks?

10. Does the arbitrary/absolute parameter algorithm create a distorted view of the business value and what is that distortion?

11. Conversion Process of Absolute Parameters to Internet Business Ratings

The questions in this category address the issue of integrating together into meaningful ratings the absolute parameter analysis. The analysis gives numbers but the conversion process converts those numbers into absolute valuation rating and what those absolute valuation ratings mean to business owners and investors.

1. What are the valuation ratings for the absolute parameters that were measured?
2. What are valuation ratings for absolute parameters?
3. What are the emotions of valuation ratings for absolute parameters?
4. How does one take most of the emotion out of the valuation process for absolute parameters?
5. Where are the uncertainties in the absolute parameter analysis process?
6. How are the valuation ratings interpreted for absolute parameters?
7. What is the conversion process of taking absolute parameter analysis and turning that data into valuation information that can be evaluated for business value and business ratings?
8. What format is used for the valuation rating of the absolute parameter?
9. Does this format of the business value information change between different categories of Internet businesses?
10. How is the historical data of different categories of Internet businesses put into the valuation process?
11. How is the current buying and selling of Internet businesses injected into the valuation process?
12. How is the absolute parameter information understandable by business owners and business investors?
13. How many different people that receive the valuation information need to have the viewpoint of that data depending on their expertise?

12. Conversion Process of Arbitrary Parameters to Internet Business Ratings

The questions in this category address the issue of integrating together into meaningful ratings the arbitrary parameter analysis. The analysis gives the numbers but the conversion process converts those numbers into the valuation values and ratings and what those valuation ratings mean to business owners and investors.

1. What is the conversion process of taking analysis and deriving valuation information for arbitrary parameters?
2. Why isn't the raw parameter data used for business valuation ratings?
3. What does converted analysis tell the business owner that the raw data does not?

4. Where does the appraiser derive the industry average norms information to understand how this business is doing compared to competing businesses?
5. What are the valuation ratings for the arbitrary parameters that were measured?
6. What is the meaning of the valuation ratings for arbitrary parameters?
7. What are the emotions of valuation ratings of arbitrary parameters?
8. How does one take most of the emotion out of the valuation process of arbitrary parameters to get to consistent repeatable results?
9. How are the valuation ratings interpreted for arbitrary parameters?
10. What is the conversion process of taking arbitrary parameter analysis and turning that data into valuation information that can be evaluated?
11. What format is used for the valuation rating of the arbitrary parameter?
12. In what form is the arbitrary parameter information understandable by business owners and business investors?
13. Do different readers of the valuation need different formats of the valuation results in order to be understandable in their terms of analysis of arbitrary parameters?
14. If different readers need different presentations of the information, how many different formats are needed and what are those formats for the valuation results of the arbitrary parameters?

13. Conversion Process of Absolute/Arbitrary Parameters to Internet Business Ratings

The questions in this category address the issue of integrating together into meaningful ratings the absolute/arbitrary parameter analysis. The analysis gives the numbers but the conversion process converts those numbers into the absolute/arbitrary valuation ratings and what those absolute/arbitrary valuation ratings mean to business owners and investors.

1. What is the conversion process of taking analysis and deriving valuation information for absolute/arbitrary parameters?
2. What are the valuation ratings for the absolute/arbitrary parameters that were measured?
3. What is the meaning of the valuation ratings for absolute/arbitrary parameters?
4. What are the emotions of valuation ratings of absolute/arbitrary parameters?
5. How does one take most of the emotion out of the valuation process of absolute/arbitrary parameters?
6. How are the valuation ratings interpreted for absolute/arbitrary parameters?
7. What is the conversion process of taking absolute/arbitrary parameter analysis and turning that data into valuation information that can be evaluated?
8. What format is used for the valuation rating of the absolute/arbitrary parameter?
9. In what form is the absolute/arbitrary parameter information understandable by business owners and business investors?

10. What format is used for the valuation rating of the absolute/arbitrary parameter?
11. In what form is the absolute/arbitrary parameter information understandable by business owners and business investors?
12. Do different readers of the valuation need different formats of the valuation results in order to be understandable in their terms for the absolute/arbitrary parameter analysis?
13. If different readers need different presentations of the information, how many different formats are needed and what are those formats for the valuation results of the absolute/arbitrary parameter analysis?

14. Conversion Process of Arbitrary/Absolute Parameter to Internet Business Ratings

The questions in this category address the issue of integrating together into meaningful ratings the arbitrary/absolute parameter analysis. The analysis gives the numbers but the conversion process converts those numbers into the arbitrary/absolute valuation ratings and what those arbitrary/absolute valuation ratings mean to business owners and investors.

1. What is the conversion process of taking analysis and deriving valuation information for arbitrary/absolute parameters?
2. What are the valuation ratings for the arbitrary/absolute parameters that were measured?
3. What is the meaning of the valuation ratings for arbitrary/absolute parameters?
4. What are the emotions of valuation ratings of arbitrary/absolute parameters?
5. How does one take most of the emotion out of the valuation process of arbitrary/absolute parameters?
6. How are the valuation ratings interpreted for arbitrary/absolute parameters?
7. What is the conversion process of taking arbitrary/absolute parameter analysis and turning that data into valuation information that can be evaluated?
8. What format is used for the valuation rating of the arbitrary/absolute conversion parameter information?
9. How is the arbitrary/absolute conversion parameter information understandable by business owners and business investors?
10. What format is used for the valuation rating of the arbitrary/absolute conversion parameter information?
11. In what form is the arbitrary/absolute conversion parameter information understandable by business owners and business investors?
12. Do different readers of the valuation need different formats of the valuation results in order for it to be understandable in their terms of the arbitrary/absolute conversion parameter information?
13. If different readers need different presentations of the information, how many different formats are needed and what are those formats for the valuation

results for the analysis of the arbitrary/absolute conversion parameter information?

15. Web Site Design

This category addresses the valuation issues that have to do with the design of the web site. There are many issues associated with the design of the web site that will cause a significant change to the Internet business value.

1. What is the own domain name parameter and how is it measured?
2. Why does the business owner care that the business has it's own domain name?
3. What is a professionally designed site and how is it measured?
4. What is the site uniqueness parameter and how is it measured?
5. Why is the site uniqueness parameter so important?
6. What is a unique domain name parameter and how is it measured?
7. Why is a unique domain name parameter so important?
8. What is browser compatibility and how is it measured?
9. Why is browser compatibility important?
10. What is the load time parameter and how is it measured?
11. Why is the load time parameter so important?
12. What is the spelling parameter and how is it measured?
13. Why is the spelling parameter so important?
14. What is the grammar parameter and how is it measured?
15. Why is the grammar parameter important?
16. What is the HTML design parameter and how is it measured?
17. What is the Meta Tags parameter and how is it measured?
18. What is the web site description parameter and how is it measured?
19. Why is the web site description parameter important?
20. What is the Images per Page parameter and how is it measured?
21. What is the Image File Size parameter and how is it measured?
22. What is the Page file size parameter and how is it measured?
23. Why is the Page file size parameter important?
24. What is the File Transfer Rate parameter and how is it measured?
25. What is the Server Space parameter and how is it measured?
26. Why is the Server Space parameter important?

16. Web Site Design - Internet Links

This category addresses the valuation issues that have to do with the design of the web site links to other URLs on the Internet. There are many issues associated with the design of the web site links that will cause a significant change to the Internet business value.

1. What is the audience (potential customer) created by a link?
2. How is the audience link, that is created, important to the valuation process?

3. What makes the link content be relevant to the valuation process?
4. Why is the link content relevance so important to an Internet business?
5. How do you measure the link content relevance?
6. What is the link friendly parameter?
7. How is the link friendly parameter measured?
8. Why is the link friendly parameter important to an Internet business?
9. What is the non-competing link parameter?
10. How is the non-competing link parameter measured?
11. Why is the non-competing link parameter important to an Internet business?
12. What is the link page rank parameter by Google?
13. How is the link page rank parameter measured?
14. Why is the link page rank parameter important to an Internet business?
15. What is the link popularity parameter?
16. How is the link popularity parameter measured?
17. Why is the link popularity parameter important to an Internet business?
18. What is the link promotion parameter?
19. How is the link promotion parameter measured?
20. Why is the link promotion parameter important to an Internet business?
21. What is the link ranking parameter?
22. How is the link ranking parameter measured?
23. Why is the link ranking parameter important to an Internet business?
24. What is the quality site link parameter?
25. How is the quality site link parameter measured?
26. Why is the quality site link parameter important to an Internet business?
27. What is direct traffic parameter?
28. How is the direct traffic parameter measured?
29. Why is the direct traffic parameter important to an Internet business?
30. What is the individual page value parameter?
31. How is the individual page value parameter measured?
32. Why is the individual page value important to an Internet business?
33. What is the dead/failed link parameter?
34. How is the dead/failed link parameter measured?
35. Why is the dead/failed link parameter important to an Internet business?
36. What is the re-directs parameter?
37. How is the re-directs parameter measured?
38. Why is the re-directs parameter important to an Internet business?
39. What is the re-register parameter?
40. How is the re-register measured?
41. Why is the re-register parameter important to an Internet business

17. Web Site Design - Language Issues

This category addresses the valuation issues that have to do with the language and language usage in the design of the web site. There are many issues associated with the language and language usage in the design of a web site that will cause a change to the Internet business value.

1. What is the relationship between proper grammar on a web site and the ranking of the web site in the marketplace?
2. What is the relationship between proper language phrasing on a web site and the ranking of the web site in the marketplace?
3. What is the relationship between misspelled words on a web site and the ranking of the web site in the marketplace?
4. What are the numbers of different languages that will be used on a web site in order to interface with different language visitors?
5. How does an Internet business handles on the web site the need for different languages because the customers are from different countries?
6. How does the valuation process account for the different effects of using different languages to serve different customer bases?
7. What other barriers than language would keep visitors from other countries from using your Internet business products or services?
8. How does the handling of specialized vocabulary to a given industry handled by the valuation analysis?
9. What impact does the use of acronyms have on the valuation process?
10. What impact does the use of slang language have on the valuation process?
11. How does the valuation account for language that is not standard for Internet business but is appropriate for a specialized niche market?

18. Web Site Design - Valuation Elements

This category addresses the valuation elements within the design of the web site. There are valuation parameters that can be placed in the web site to help monitor the performance of the Internet business.

1. How does compatibility with the top three browsers impact the Internet business ranking in the niche market?
2. How does owning a domain name for the Internet business impact the performance of the business?
3. What is a unique domain name?
4. How does owning a unique domain name for the web site impact the Internet business valuation results?
5. How does the web site design compatibility of the HTML code to different standards impact the Internet business valuation results?
6. How does the image file size that needs to be transferred over the Internet impact the Internet business valuation results?
7. How does the use of Meta tags to allow search engines to find and catalog the web site impact the Internet business valuation results?
8. How does the page file size that needs to be transferred over the Internet impact the Internet business valuation results?
9. How does the professional nature of the web site design impact the Internet business valuation results?

10. How does the amount of server space required for the web site impact the Internet business valuation results?
11. How will the uniqueness of the site and the products of the web site impact the Internet business valuation results?
12. How does the transfer rate of all files impact the web site valuation results?
13. How does the time required for all files to transfer impact the web site valuation results?

19. Stability Factors - Internet Business

This category addresses the valuation issues that have to do with the stability of the Internet business. Because it is so easy to establish an Internet business it is also easy to stop an Internet business. There is no brick and mortar here that needs to be torn down or disposed of in a liquidation process.

1. What is the time in business parameter, how is it measured and why is it important to an Internet business?
2. What is the customer satisfaction parameter, how is it measured and why is it important to an Internet business?
3. How is the customer satisfaction parameter related to the business stability?
4. What is the maximum/minimum income ratio parameter, how is it measured and why is it important to an Internet business?
5. How is the maximum/minimum income ratio related to the stability of an Internet business?
6. How does the business organization structure impact the stability of the business?
7. Is there any relationship between the number of employees and the stability of the company?
8. How does the financial resources of the company impact the stability of the Internet business?
9. Does the nature of the financial resources have an impact on the stability of the Internet business?
10. How does the hours of operation of the business impact the stability of the company?

20. Customers, Customer Traffic – Internet Business

This category addresses the valuation issues that have to do with customers in general and customer traffic in specific. There are many issues associated with the customers that will cause a significant change to the Internet business value.

1. How does the number of visitors impact the Internet business?
2. What is the threshold of visitors before a company can be ranked as an Internet business?
3. What is the threshold of customers before a company can be ranked as an Internet business?

4. How do you determine when all you have is repeat visitors without every buying?
5. How do you determine which visitors will have a high probability of becoming customers?
6. How do you determine how many visitors are directed by search engines?
7. How do you determine how many visitors are directed by other web sties?
8. How do you determine how many visitors are directed by other advertising?
9. How do you determine the value of each customer to your business?
10. How do you determine the value of the unique visitors that come to your web site?
11. How do you determine how long the visitors spend at your web site on the average and how is that important?
12. How do you determine for your Internet business what you need to pay a search engine for directing visitors to your web site and how does this impact the valuation value?

21. Advertising - Internet Business

This category addresses the valuation issues that have to do with advertising on the Internet and other locations to promote the Internet business. There are many issues associated with the advertising that will cause a significant change to the Internet business value. No advertising normally results in no business which results in zero value for the Internet business.

1. Is it apparent that there is an advertising campaign to attract new visitors and customers?
2. What are the resources that are being placed into the advertising campaign.
3. What is the effectiveness of the advertising campaign?
4. How is the effectiveness of the advertising campaign?
5. How is the advertising campaign related to the valuation value?
6. Has the past advertising campaign exhausted all the potential customers from that market sector?
7. Does the advertising campaign have a multi-facetted strategy to have multi ways to attract customers?
8. Is the advertising campaign robust enough to be considered a long-term consistent impact on the business?
9. How does the advertising campaign account for the changes in the Internet core technologies?
10. How does the advertising campaign account for the changes in Internet customer habits and characteristics?
11. In an advertising campaign, how many visits does it take by a customer before there is a high probability that they will become customers?
12. How many companies can be advertising on your web site as banner advertising before the site becomes to cluttered with other company messages?

13. How does a business owner discover that there are competitor companies that are two or three links removed from paid advertising on their web site?
14. When is a friendly web site that shares mutual reciprocal advertising turn into a not friendly web site because of leading your customers to other competitors?

22. Expenses - Internet Business

This category addresses the valuation issues that have to do with the Internet business expenses. There are many issues associated with the expenses that will impact the valuation value of the Internet business.

1. What is included in business expenses for valuation purposes?
2. What is included in monthly operating expenses?
3. What is included in yearly operating expenses?
4. Does this Internet business have a lot of capital requirements and how are those being expensed?
5. How is the debt of the Internet business handled?
6. What is the amount of debt of the Internet business?
7. How does the debt impact the valuation value of the business?
8. What are the recurring fixed expenses of the Internet business?
9. How does the recurring fixed expenses impact the valuation value of the Internet business?
10. What are the large one-time expenses of the Internet business?
11. What financial reserves does the Internet business have in order to cover unexpected expenses?
12. What are the likely unexpected expenses of a given Internet business?

23. Income - Internet Business

This category addresses the valuation issues that have to do with the Internet business income.

1. What are the numbers of different methods that the Internet business has established to allow your customers to pay you?
2. How does the Internet business handle credit card payments?
3. Does the Internet business have a credit card merchant account?
4. What is the fee rate for the credit card merchant account?
5. How does what the Internet business pays for collecting receivables impact the valuation process?
6. What is the level of account receivables?
7. How old are the account receivables?
8. What impact does account receivables have on the valuation process?
9. How does the Internet business use third party collection companies to collect the account receivables?

10. What fees is the Internet business needing to pay for the third party collection process?
11. How many different third party collection companies can the Internet business use?
12. How do you use PayPal to get paid?
13. Do you ever use postal payment methods in an Internet business?
14. What fees are appropriate to pay for having a third party accomplish the collection process?

24. Investment – Internet Business

This category addresses the valuation issues that have to do with the Internet business investment. There are many issues associated with the investment that will impact the valuation value of the Internet business.

1. When does an Internet business seek outside investment?
2. What are the Internet business parameters that are the most important to venture capitalists?
3. What is the relationship between venture capitalists and Internet business entrepreneurs?
4. At what point do you know that you want to grow the business faster then you have personal resource capital to expand?
5. How do you sort out the desire of venture capitalists to want to manage your business when you know best?
6. At what stages of the development of an Internet business when it is just not appropriate to have outside financing?
7. What autonomy will the owner of an Internet business give up when third party financial resources are accepted?
8. How do you identify the right kinds of resources for your Internet business?
9. Will local banks loan money to Internet businesses?
10. Are there special companies that only deal with Internet businesses and understand how to finance these kinds of businesses?

25. Financial Data– Internet Business

This category addresses the valuation issues that have to do with the Internet business financial data. There are many issues associated with the financial data that will impact the valuation value of the Internet business.

1. What are the financial parameters of an Internet business that are relevant to the valuation process?
2. How many of the financial parameters are absolute parameters?
3. How many of the financial parameters are arbitrary parameters?
4. How many of the financial parameters for Internet businesses the same as traditional businesses?
5. What analysis is accomplished on financial parameter data?
6. Can any of the financial parameter value be taken as is?

7. How many of the financial parameter values need further analysis and conversion before the numbers will mean something to the readers of an valuation?
8. Can accountants develop all of the financial parameters needed for the valuation?
9. How much emotion is associated with financial data parameter values?
10. Can financial data values be misleading with not viewed in context with business data values?

26. Business Data – Internet Business

This category addresses the valuation issues that have to do with the Internet business data. There are many issues associated with the business data that will impact the valuation value of the Internet business.

1. What are the business data parameters of an Internet business that are relevant to the valuation process?
2. How many of the business data parameters are absolute parameters?
3. How many of the business data parameters are arbitrary parameters?
4. How many of the business data parameters for Internet businesses are the same as traditional businesses?
5. What analysis is accomplished on business data parameters?
6. Can any of the business data parameter values be taken as is?
7. How many of the business parameter values need further analysis and conversion before the numbers will mean something to the readers of an valuation?
8. Can accountants develop all of the business parameters needed for the valuation?
9. How much emotion is associated with business data parameter values?
10. Can business data values be misleading when not viewed in context with business data values?

27. Search Engine, Keyword Impact -Internet Business

This category addresses the valuation issues that have to do with the Internet business interaction with search engines and the keywords used by the search engines.

1. What are the numbers of keywords that can be used to search to find this web site?
2. What are the unique keywords that if used will have a high probability of bringing a visitor to this web site?
3. What are the numbers of different keywords that buying customers are using to find the products or service presented on this web site?
4. What is the latency between when a modification is made on the web site and that web site is re-registered with the search engines?
5. What is the ranking of your web site by the search engines?
6. How do you change the ranking by the search engines?

7. How do you measure the number of visitors directed to your web site by the search engines?
8. How do you measure the quality of the visitors that are directed by search engines?
9. How do you create products that match keyword searches that do not have much competition for the keyword as on yet?
10. How do you correlate the keywords on your web site so that too many keywords will cause the search engines to bypass your web site?

28. Manufacturing Capability – Internet Business

This category addresses the valuation issues that have to do with the Internet business manufacturing capability to create the products that are sold by this business.

1. How do you measure the capacity of the manufacturing element of the Internet business?
2. What are the time constraints for the manufacturing element to respond to the customer demand after an order is placed?
3. How is the quality of the manufacturing element measured for an Internet business?
4. Can the products you plan to sell on the Internet be manufactured by third parties?
5. Is it cost effective to accomplish internal manufacturing or external manufacturing?
6. What are the skills needed to accomplish manufacturing for your products?
7. Are the skills needed to accomplish the manufacturing in sort supply in your area?
8. Are special machines required to manufacture your products?
9. Are there long lead times for the delivery of these kinds of machines?
10. How much floor space will be needed to accomplish the manufacturing?

29. Marketing – Internet Business

This category addresses the valuation issues that have to do with the Internet business marketing strategy and how that strategy is carried out.

1. What is the market potential parameter, how is it measured and why is it important for an Internet business?
2. What is the search engine ranking parameter, how is it measured and why is it important for an Internet business?
3. What is the web site appeal parameter, how is it measured and why is it important for an Internet business?
4. What is the web site ease of use parameter, how is it measured and why is it important for an Internet business?
5. What is the advertising versus numbers of visit parameter, how is it measured and why is it important for an Internet business?

6. What is the page abandonment before completing the shopping cart activity parameter, how is it measured and why is it important for an Internet business?
7. What is the best selling product parameter, how is it measured and why is it important for an Internet business?
8. What is the keyword uniqueness parameter, how is it measured and why is it important for an Internet business?
9. What is the numbers of competitor parameter, how is it measured and why is it important for an Internet business?
10. What is the customer benefits parameter, how is it measured and why is it important for an Internet business?
11. What is the keyword space parameter, how is it measured and why is it important for an Internet business?
12. What is the keyword rank parameter, how is it measured and why is it important for an Internet business?
13. What is the phrase rank parameter, how is it measured and why is it important for an Internet business?
14. How do you determine the number of direct competitors on the Internet in your marketing niche?
15. How do you determine how well you rank with the keywords you are using?
16. How do you go about picking keywords that are being used that do not cost so much to reserve?

30. Intellectual Property - Internet Business

This category addresses the valuation issues that have to do with the Internet business intellectual property and how well that intellectual property is protected and can that property value be turned into an Internet business value.

1. What are the numbers of patents held by the company that are relevant to the products being sold?
2. How does an appraiser determine if a patent is relevant to the value of the Internet business?
3. When will the patents expire?
4. How do the patents give the Internet business uniqueness in the marketplace?
5. What is the uniqueness of the products in the niche market that the Internet business is operating?
6. Does the Internet business have unique software that is either sold stand-alone or is used in the processes of the business to give an advantage?
7. Does the Internet business have a unique service that is protected with some intellectual property for the marketing niche in which the business is operating?
8. Can the Internet business use authorship of books to increase the intellectual value of the business?
9. What copyrighted materials that the company has can be of some valuation value to the company?

10. Can additional copyrighted materials be created to help increase the value of the Internet business?

31. Support Structure – Internet Business

This category addresses the valuation issues that have to do with the Internet business support structure what will allow the company to function.

1. What are the real estate property resources that will be used?
2. What personal property resources will be used?
3. How will the shipping of the business products to customers be handled?
4. How will the financial department be set up?
5. How will the account receivable be handled?
6. How many different ways will the company be able to receive payment?
7. Will the company answer the phone?
8. How many hours a day will the phones be manned?
9. What are the business processes that will be used?
10. Will there be business policies and procedures set up in order to handle most routine tasks in the company?

32. Product – Internet Business

This category addresses the valuation issues that have to do with the Internet business products that are being offered by the company to customers on the Internet.

1. How do you determine the best selling products on your web site?
2. How do you select products if you do not create your own products?
3. What are the numbers of ways that you can deliver your products to your customer?
4. What is the relationship between the product placement and the web site and how that product is selling?
5. How do you determine what the customer wants in the form of a product?
6. What kinds of long term commitment must be made in order to have the authority to sell someone else's product?
7. How do you control the costs of products to sell when you do not control those products?
8. How do you protect the marketplace from long term competitors with the same product or similar products?
9. What will be the evolutionary path for the products that you have selected?
10. How do you handle defective products?

33. Service – Internet Business

This category addresses the valuation issues that have to do with the Internet business services that are being offered by the company to customers on the Internet.

1. What services does the Internet business offer?
2. Which of these services are unique in the niche marketplace?
3. How do you differentiate a service item from the competition?
4. How do you display the service on the web site to obtain the maximum customer response?
5. How do you receive payment for the service that you are offering?
6. How does the service impact the valuation value of the Internet business?
7. What is the process of accomplishing an valuation on an Internet business that only has a service and no product to offer to their customers?
8. Can services be offered in conjunction with products to increase the valuation value of the business?
9. What are the expenses of an Internet business that only offers a service to the customer?
10. What are the total income levels that can be expected with different types of services offered to your customers?

34. Visitor – Internet Business

This category addresses the valuation issues that have to do with the Internet business visitors to the web site by potential customers on the Internet.

1. What is the direct traffic parameter, how is it measured and why is it important to an Internet business?
2. What is the traffic to the web site parameter, how is it measured and why is it important to an Internet business?
3. What is the return visit number prior to purchase parameter, how is it measured and why is it important to an Internet business?
4. What is the targeted traffic parameter, how is it measured and why is it important to an Internet business?
5. What is the search engine directed parameter, how is it measured and why is it important to an Internet business?
6. How do you determine the number of times the visitor abandoned a page before becoming a customer?
7. How do you determine the number of times any given visitor visited your web site before purchasing?
8. How many different levels of visitors can be distinguished from one another, which visit your web site?
9. What level of visitor traffic must be obtained before there can even be a consideration of turning a single visitor into a customer?
10. How do you get visitors to your web site without using the search resources of the Internet?

35. History of Property Appraisal

This category addresses the appraisal issues for property valuations from an historic perspective.

1. How long has there been a history of business appraisals?
2. How can appraisals such as real estate appraisals be used as a model for Internet business appraisals?
3. How will the Internet modify the appraisal history?
4. How will electronic auctions impact the appraisal process?
5. How can customers who have historically been in close proximity to the appraised objects be assured with Internet business appraisal process?
6. How will the languages of appraisals change because of the Internet?
7. How will the auctions of the Internet impact the appraisal process in real time?
8. Will appraisals eventually arrive at the point where they will be in real time and the company value will be displayed on the web site along with other company data?
9. Which of the property appraisal processes available are the most similar to that which is needed for the Internet business?
10. Can the Internet business even be considered a property that can be bought and sold as normal property?

36. Periodicity of Valuations for Internet Businesses

This category addresses the time sensitivity for valuations of an Internet business.

1. What are the parameters that will decide when an Internet business will have a valuation the first time?
2. Which of these parameters are the most driving parameters as to why a business owner would consider a valuation?
3. Would a business owner consider a valuation as a management tool?
4. Would a business owner consider a valuation as an incentive to employees that would get a bonus once the company arrives at a given value?
5. What kind of valuation would a business owner consider using in seeking financial resources?
6. How often would a financial resource want to have an update to the valuation?
7. What financial implications to borrow resources would occur when the value of the company fell below certain level?
8. When will the valuation process occur too often to be considered relevant for an Internet business?
9. What impact does the valuation have on taxation by local governments?
10. What impact does the valuation have on the estate of an owner who passes away?

37. Measurement Methods for Absolute Parameters

This category addresses the measurement methods for valuations that are available for measuring absolute parameters in an Internet business.

1. What are the absolute parameters that must be measured?

2. How many of these absolute parameters are measured in the normal course of everyday business?
3. Does the Internet allow the business owner increased frequency of measurement of these absolute parameters?
4. Can any of these absolute parameters be accomplished in real time on an Internet business?
5. Can special software be developed that will allow turning valuation absolute parameters into business management parameters that can be used often?
6. Can measurement of absolute parameters lead to a better understanding of the performance of an Internet business?
7. Can any of the analysis of absolute parameters be converted to automated software programs that will give not only the parameters but also the analysis on the parameters?
8. Can the analysis of absolute parameters be converted to business decision data automatically?

38. Measurement Methods for Arbitrary Parameters

This category addresses the measurement methods for valuations that are available for measuring arbitrary parameters in an Internet business.

1. What are the arbitrary parameters that must be measured?
2. How many of these arbitrary parameters are measured in the normal course of everyday business?
3. Does the Internet allow the business owner increased frequency of measurement of these arbitrary parameters?
4. Can any of these arbitrary parameters be accomplished in real time on an Internet business?
5. Can special software be developed that will allow turning valuation arbitrary parameters into business management parameters that can be used often?
6. Can measurement of arbitrary parameters lead to a better understanding of the performance of an Internet business?
7. Can any of the analysis of arbitrary parameters be converted to automated software programs that will give not only the parameters but also the analysis on the parameters?
8. Can the analysis of arbitrary parameters be converted to business decision data automatically?

39. Financial Markets and Internet Businesses

This category addresses the financial market view of Internet businesses. It also addresses the management concerns that financial resources desire in an Internet business.

1. How does the financial markets view the Internet business?
2. How did the dot com failures of the early 2000s change the way the financial markets view the Internet business?
3. What financial parameters are the most important to the financial markets?

4. What business parameters are the most important to the financial markets?
5. Why would an entrepreneur ever care about financial markets view of his business?
6. How does a business owner organize his Internet business to have the best opportunity to sell the business in the financial markets?
7. How can an valuation help the prospective investor understand this Internet business?
8. What educational materials must be given to the financial market to educate the market people about your specific Internet business?
9. How does a business owner keep financial market people from wanting to run his business their way?

40. Customer Financing for Internet Businesses

This category addresses how customer financing might work to grow an Internet business.

1. What is customer finance of an Internet business?
2. How have customers already financed other Internet businesses?
3. Why would customers be interested in financing an Internet business?
4. What are the services that would cause a customer to finance an Internet business?
5. What are the products that would cause a customer to finance an Internet business?
6. What are the advantages of having your customers finance your Internet business?
7. What are the disadvantages of having your customers finance your Internet business?

Appendix B

Refund Procedure

If you have decided this information isn't what you expected and would like a refund please send mail to:

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Please include a piece of paper with your name, email, the date you purchased the book and the price purchased for.

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I truly apologize the information was not up to your expectations and wish you the best of luck with whatever endeavor you have chosen.

Most Sincerely,

Nelson Bates
BuySellWebsite.com Publishing
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Appendix C

Feedback is an important component to the book and I frequently update it by what you suggest. You'll have the opportunity to download the book in the future and it could have the answers to your questions or comments you send me. Please feel free to send me an email and let me know what you think about the book. Positive or negative comments are welcome. And I truly make it a point to address your concerns and pay attention to what you send me. Email to support@BuySellWebsite.com.

Keep in mind the following questions.

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2. What was missing that you thought should be included?
3. Areas that could use more explanation?

Also let me know why you bought the book.

1. Was it a gift?
2. Was it to start a new business?
3. Was it to build on an existing business?

Appendix D

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www.BuySellWebsite.com

Appendix E: Resources

Analysis Tools and Web Site Tools

1. www.webtrends.com
2. www.linkpopularity.com
3. www.websitegarage.com
4. www.marketleap.com
5. www.webposition.com
6. www.alltheweb.com
7. www.altavista.com
8. search.aol.com
9. www.google.com
10. www.hotbot.com
11. search.msn.com
12. www.alexa.com

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Glossary

Word	Definition
Absolute Parameter	A valuation parameter that has a value that will not change from valuator to valuator.
Advertising Campaign	The implementation effort of the Marketing Strategy that includes all forms of advertising to create business value.
Advertising versus Visits	Number of visits by a visitor before they become a customer.
Advertising: Competitors from Links	Number of competitors that will show up on links that are two sites removed from your web site. The first link takes the visitor to a friendly site and the link from there takes the visitor to a competitor.
Advertising: Individual Page Value	Valuation value of a web site page that is created by analysis of number of visits and the products that are sold from that page.
Advertising: Others on Your Site	How many other companies are advertising on your web site in the form of banner advertising or links to their web sties.
Analysis Value Methodology	The method of analyzing the Internet business. There are many different algorithms that can be used to analyze the value of a business. The one most often selected for Internet businesses today is the income method.
Appraisal	Sometimes appraisal and valuation are used interchangeably but generally appraisal has to do with physical objects value.
Arbitrary Parameter	A valuation parameter that has a value that will change from valuator to valuator.
Best Selling Products	Best selling products on your web site.
Browser Compatibility	Compatibility to top three browsers.
Business Data	Information about the business being evaluated. This normally has two elements: the business structure data and the marketing data. Sometimes the marketing data is separated into a separate category.
Company Organization	How the company is organized to do business;
Company Size	The number of employees of the company.
Competitors: Number of	Number of competitors on the Internet.
Conversion Process	This is the process of taking the parameter data and converting that raw data into finished, decision-making information.

Customer Benefits	Number of benefits the potential customer will derive from your product or service as outlined on your web site.
Customer Benefits Value	Customer perception of the value of the benefits that the web site is offering as computed by the number of visits to the site and the length of time the visitors stays on the web site.
Customer Financing	If a business is successful then the customers always finance the business. The question here is if the customer will participate as an investor.
Customer Satisfaction	Determined by the response to customer surveys about your site.
Different Methods for Customer to Contact	The number of ways the customer can contact the company to discuss products, services and/or issues.
Different Methods for Delivering Product	Number of ways that your product can be delivered to the customer.
Different Methods to Process Payment	Number of different ways the customer can purchase the product and/or service.
Domain Name: Uniqueness	Uniqueness of the domain name and ease of remembering.
Domain: Own Domain Name	Own the domain name of the web site.
dot coms	Companies that only accomplish their business on the Internet.
Expenses: Monthly	Business monthly expenses: this includes operation and debt expenses.
Expenses: Yearly	Business yearly expenses that includes operation and debt expenses.
Financial Data	This data is what accounting is all about.
Financial Markets	These markets are the investment capital markets that are needed for a business to have resources.
Financial Resources	The financial resources of the company.
Hours of Operation	The hours of operation as compared to the number of potential hours the visitors need assistance.
HTML	The software code language of the Internet. It is the code that converts information to the displays that customers see.
HTML Design	Compatibility of the HTML design to different HTML standards.
Image File Size	Image file size that needs to be transferred.
Income: Maximum monthly in a year	Maximum monthly income during a year. Used in the max/min ratio analysis.
Income: Minimum monthly in a year	Minimum monthly income during a year. Used in the max/min ratio analysis.
Income: Monthly Average Gross	A parameter used in the valuation algorithm that is derived from the business gross monthly income.

Income: Monthly Average Net	A parameter used in the valuation algorithm that is derived from the business net monthly income.
Income: Monthly Gross	Monthly gross income from the web site business.
Income: Monthly Net	Monthly net income from the web site business.
Income: Multiplier Net	
Income: Yearly Gross	Yearly gross income from the web site business.
Income: Yearly Net	Yearly net income from the web site business.
Intellectual Property	Patents are the most often category of intellectual property that people think about. Copyrights are in this category also.
Internet Business	A business that only accomplishes business on the Internet.
Internet Business Rating	How one Internet business rates as compared to others. There is not a lot of data yet to have excellent ratings. The Internet is too young.
Internet Customer	A customer that deals with your company only through the use of the Internet.
Internet Investor	A financial community member that invests in Internet businesses.
Internet Language	The Internet has a language all of it's own. This book has identified many of those words that are unique to the Internet business world.
Internet Links	The Internet allows links to other sites. With a click that customer is at your site or someone else's site.
Internet Property	It is not yet certain what is meant by Internet Property. It is not yet clear how much of the Internet property is tangible and how much is intangible.
Internet Visitor	A visitor is someone who visits your web site and is not yet a customer.
Keyword	The Internet is driven by words. Keywords are the language of finding information in the sea of words.
Keyword Rank	How well your keywords rank when used in the search engines.
Keyword Space	Number of keywords that can be used to search to find this web site.
Keyword Uniqueness	Unique keywords that if used will have a high probability of bringing a visitor to this web site.
Keyword: Customer Use of	Number of keywords that buying customers are using to find this web site.
Language: Grammar	Ranking as to how well proper grammar is used on the web site.
Language: Number of Languages on Site	Number of different languages that are used on the web site to interface with different language visitors.
Language: Phrase Rank	Ranking as to how well proper phrasing is used on the web site.

Language: Spelling	Ranking as to how many missed spelled words are found on the web site. Used as a way to measure the professional level of the site.
Link Audience	Determines the audience of the links from your web site when the visitor clicks on a link - what is that customer like?
Link Page Rank by Goggle	Goggle has an algorithm that ranks web site pages.
Link: Content Relevant	Ranks the relevance of the web site content to the potential audience.
Link: Failed	Links on your web sites that are no longer valid.
Link: Friendly	Links on your web site that takes you customer to other sites that are compatible with your web site from a marketing viewpoint.
Link: Non Competing	Number of links from your web site that do not for sure compete with your web site.
Link: Popularity	Ranking of links to your web site from other web sites.
Link: Promotion	Ranking of the use of links as a method of advertising.
Link: Quality of Site	Ranking of the quality of web site that your web site links to.
Link: Ranking	Ranking of the web sites that link to your web site.
Manufacturing	The support structure that allows for building the products that your business is selling.
Manufacturing Capability	Measure of the capacity of the manufacturing element of the company to respond to the market demands.
Manufacturing Quality	Measure of the quality of the manufacturing element.
Market Potential	Analysis of the potential in the market place of this particular product. (Need to develop the parameters that go into this analysis parameter.)
Marketing Data	This data has to do with the interface to the customer and all the elements that go into that part of the business. This includes the advertising that is necessary to carry out the marketing strategy.
Maximum/Minimum Income Ratio	Taking the maximum and the minimum monthly income from the web site business creates the ratio. This is an indicator of the yearly variation in the business.
Meta tags	A hidden portion of the web site that allows search engines to identify and categorize your web site.
Niche Market	Most businesses are addressing only niche markets. Not everyone in the world can be his or her customer.
Page Abandonment before Shopping Cart	Number of times the visitor abandoned a page before coming a customer.
Page File Size	Page file size that needs to be transferred.
Page: Images per Page	Number of images per web site page that will need to be transferred uniquely.

Patent Value	Marketing analysis to determine the valuation value of the patents to the market place through this web site.
Patents	A protection method that allows exclusive use of certain ideas and concepts for a limited time.
PayPal	The most used way on the Internet to make and collect payments.
Product Uniqueness	Marketing analysis of the uniqueness of the product in the Internet advertising space.
Professional Design Site	Valuation as to the professional nature of the web site.
Proprietary Software	Unique software owned by the company either as an item to sell or marketing data that is unique to the company.
Redirects	Number of redirects on your web site once someone has linked to your web site.
Re-register	Latency between when a modification is made in a web site and when that web site is re-registered with the search engines.
Return Visits: Number Prior to Purchase	Number of times a given visitor visited the web site before purchasing.
Search Engine	The method used by the Internet to find keywords on the web sites of the Internet.
Search Engine: Ranking	The ranking of your web site by the search engines.
Search Engine: Visitor Directed	Number of visitors directed to your web site by the search engines.
Server Space	How much server space the web site needs.
Service Uniqueness	Marketing analysis of the uniqueness of the service in the Internet advertising space.
Site Ease of Use	Rating on how intuitive the site is to use by the visitor.
Site: Content Value of Site	A percentage multiple determined by the valuator's opinion.
Site: Description	The description and use as adverting that is used by search engines.
Site: Marketing Appeal	Visitor appeal of the web site as an analysis of number of visitors and length of time the visitors spend on the web site.
Site: Uniqueness	Valuation as to the uniqueness of the web site.
Time in Business	Number of years the company has been in business.
Traditional Business	A business that interfaces with the customer by having a location where the customer can visit establishment.
Traffic - to Web Site	Number of visitors to web site.

Traffic Value	Analysis of the value of each visitor.
Traffic: Direct Traffic	Visitors that are directed to your web site by search engines.
Traffic: Targeted	Number of visitors that have a high probability of becoming customers.
Traffic: Targeted Value	The value of the customers that are visiting.
Traffic: Unique Traffic	The number of visitors that are unique because of the web site design or products.
Traffic: Unique Traffic Value	The value of the unique visitors that come to your web site.
Traffic: Visit Time	How long the visitors spend at your web site on the average.
Transfer Rate	The rate at which the Internet system allows information to travel from the location of the server where the web sites resides to the customer.
Transfer: File Transfer Rates	Rate at which files are transferred.
Transfer: Load Time	Amount of time required loading the web site on the visitor's computer.
Web Sites	The place of business of an Internet business is the web site of that business.

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Back Cover

- **A valuation of your Internet Business periodically can give you enormous insights into the performance of your business.**
- **Valuation will lay the groundwork for additional capital to grow the business.**
- **Valuation will give potential investors a measure of your business value.**

The Internet has radically changed the way we accomplish our work as Businesses. In 1995 it was not appropriate to be on the Internet marketing your company. By the year 2002 you needed to be on Internet if you were to be taken seriously as a company.

Lots of businesses have been created in the intervening years since 1995. Most of these companies are not traded on a stock exchange. Therefore how does a potential investor know how to evaluate the worth of these businesses?

A method to evaluate the worth of an Internet Business is needed. There have been limited attempts at creating a system to determine the worth of an Internet Business. However it is difficult to establish measurable parameters for the Internet businesses unless you understand this marketplace and take into account numerous parameters.

What you will learn is:

4. How to place a systematic value on your Internet Company
5. Most Internet Businesses are really niche market businesses.
6. How niche markets are 200,000 to 700,000 potential reachable customers.
7. How the numbers of visitors to your web site impacts the value of your business.
8. There are two types of parameters needed to measure the worth.
9. There are absolute parameters like unique visitors and net income.
10. There are arbitrary parameters like web site design and programming that you will need specialized knowledge to know the values.
11. That the arbitrary parameters are very important to the analysis process.
12. How these two types of parameters are consolidated into a powerful business worth valuation.
13. How to pull the data together into an understandable analysis that has meaning to investors.
14. You will be able to evaluate most small Internet businesses in a short period of time when you know what parameters to use and have developed Internet experience.

The Internet is now old enough that Internet Business owners will be trying to sell their Internet property. There will be good deals and bad deals just like buying and selling in any other marketplace. What you need is a systematic process that will allow you to take advantage of either selling your property or if you are a buyer or investor to invest in these kinds of exciting and potentially lucrative businesses**.**

If this system had been in place before the dot com busts, a lot of investors would have saved millions.