

# 2020 BENCH-BAR CONFERENCE

## CASH-INTENSIVE BUSINESS (A Back-Solve Method)

### Sample

The viewpoint of Thomas Gillmore, CPA/ABV

Moderator, Honorable Donald Myers

**Note: The methods and results of this business valuation sample are provided by the Appraiser for educational and discussion purposes only and do not reflect the opinion of the Judiciary or legal position of an attorney.**

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Dear Conference Attendee:

In this sample, a lifestyle analysis lays the foundation to estimate alimony or business value using a back-solve method, similar to what the IRS uses in similar endeavors.

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Responding to the Attorney's Inquiry

Dear Attorney,

In determining the value of your client's cash-intensive business, we offer the following suggestions and a sample lifestyle analysis that may be useful in your case. Our fee estimate for this analysis is in the range of \$\_\_\_\_\_ for the simplified method and \$\_\_\_\_\_ for the deep dive method. A sample lifestyle analysis is attached to this letter.

#### **Simple Method**

Capitalizing lifestyle expenses will approximate the business fair market value, using Sellers Discretionary Earnings multiple, which can be found on DealStats. The financial affidavits should be enough to get in the ballpark to estimate how much someone would invest to be able to spend that type of money, excluding inheritances and other sources of income.

#### **Expensive Method**

Diving deeper requires analyzing the Z-tape and performing a few IRS audit techniques described in this link, e.g., capitalizing food and liquor purchases at industry mark-up rates and looking at lifestyle expenditures

Specific IRS Technique Guide

- [https://www.irs.gov/pub/irs-utl/cashchapter5\\_210639.pdf](https://www.irs.gov/pub/irs-utl/cashchapter5_210639.pdf)

#### **Example Cash T Method**

The taxpayer stated in the initial interview that all income is deposited to the business bank account, and gross receipts are determined by totaling bank deposits. However, there appear to be significant cash expenditures for business and personal expenses with no method to include the cash paid out in income. The gross profit percentage (GPP) is well below industry averages. At this point, Cash T indicates a cash shortage of approximately \$40,000. A Fully Developed Cash T method will be performed to capture the cash paid out and calculate the correct income.

Or,

**Example -Source and Application of Funds Method**

The cash-intensive business which is the only reported income for this family of four, consistently reports an ordinary income of \$20,000 to \$30,000 in the past six years. During the same period, the taxpayer has accumulated two rental properties whose FMV is more than \$180,000. Both properties report unusually small rents and substantial expenses, resulting in losses. Property improvements are observed, and the taxpayer confirms the improvements are made in the exam year; however, no expenditures can be found for the improvements. A Source and Application of Funds method will calculate the taxpayers' total income from all sources.

Yours truly,

The Appraiser

Enclosure: Sample Lifestyle Analysis

**2020 Bench Bar - Bonus Handout**  
**16 Month Income & Expense Analysis**  
**February 2019 through May 2020**

	<u>Feb '19 - May 20</u>
<b>Ordinary Income/Expense</b>	
<b>Corporate Income</b>	
ATM Deposits to Wells #34	7,311.43
Whistle Stop, LLC - Euro Revenues	247,886.00
Whistle Stop, LLC - US Revenues	85,570.00
Whistle Stop, LTD - Government Re	131,155.00
Mobil Deposits to Wells #34	3,813.00
Fast Properties	44,756.00
<b>Total Income</b>	<u>520,491.43</u>
<b>Corporate Expenses</b>	
Whistle Stop, LLC - 1099	26,243.00
Whistle Stop, LLC - AMEX	52,850.00
Whistle Stop, LLC - Payroll	307,055.00
Whistle Stop, LLC - Wells #36	42,202.00
Whistle Stop, LTD - Expenses	86,373.00
<b>Total Corporate Expenses</b>	<u>514,723.00</u>
<b>Gross Profit from Corporations</b>	<b>\$5,768.43</b>
<b>Living Expenses</b>	
<b>CC's Not Accounted For</b>	
Bank of America	450.00
Commerce Bank	8,544.00
Discover Card	1,799.00
JC Penny	522.00
<b>Total CC's Not Accounted For</b>	<u>11,315.00</u>
<b>Children's Expenses</b>	
Child Support	8,324.00
Daughter	680.00
Extreme Cheer	2,011.00
Gifts to Others	230.00
Healthcare Not Insured	1,224.00
<b>Total Children's Expenses</b>	<u>12,469.00</u>
<b>Healthcare</b>	
Pharmacy	877.00
<b>Total Healthcare</b>	<u>877.00</u>
<b>Household</b>	
Alarm	1,011.00
Cable TV	3,878.00
Cell Phone	3,150.00
Eating Out	13,888.00
Electricity	7,484.00
Groceries and Home Supplies	4,221.00
HOA Fees	1,400.00
Home Insurance	5,456.00

**2020 Bench Bar - Bonus Handout**  
**16 Month Income & Expense Analysis**  
**February 2019 through May 2020**

	<u>Feb '19 - May 20</u>
Home Warranty	45.00
Household Furnishings	6,743.00
Lawn Care	2,369.00
Mortgage - Main	24,291.00
Natural Gas	512.00
Pest	673.00
Pool Maintenance	1,043.00
Property Taxes	7,335.00
Repairs & Maintenance	1,190.00
Water, Sewer, Garbage	1,668.00
<b>Total Household</b>	<b>86,357.00</b>
<b>Insurances</b>	
Life Insurance	16,364.00
<b>Total Insurances</b>	<b>16,364.00</b>
<b>Other Monthly Expenses</b>	
Bank Fees	60.00
Card Renewal	800.00
Clothing Purchases	6,395.00
Dry Cleaning	26.00
Gifts to others	1,500.00
Grooming	81.00
Gym	2,808.00
Legal Fees	27,985.00
Leisure	6,353.00
Lottery Subscription	1,825.00
Pension Contribution Euro	1,175.00
Pet Expenses	2,511.00
Tax Collector	3,081.00
Travel - Personal	4,122.00
<b>Total Other Monthly Expenses</b>	<b>58,722.00</b>
<b>Vehicles</b>	
Audi Lease	16,486.24
Fuel	550.00
Insurance - Auto	12,443.00
Jaguar Orlando	9,109.00
Land Rover	16,000.00
Tolls & Parking	2,197.00
Vehicle Repairs	2,385.00
<b>Total Vehicles</b>	<b>59,170.24</b>
<b>Total Living Expenses</b>	<b>245,274.24</b>
<b>Net Living Expenses - Excess or (Deficit)</b>	<b>(\$239,505.81)</b>
<b>Other Income/Expense</b>	
Personal Savings Account and UBS Loan	

**2020 Bench Bar - Bonus Handout**  
**16 Month Income & Expense Analysis**  
**February 2019 through May 2020**

	<u>Feb '19 - May 20</u>
Capital One #80	104,000.00
Closure of Misc. Company	9,980.00
Sale of Company	22,971.00
RBS Bank #64	86,800.00
UBS Loan	36,000.00
<b>Total Other Income</b>	<b>259,751.00</b>
<b>Other Expense</b>	
Bad Cars - Purchase of Com	73,188.00
<b>Total Other Expense</b>	<b>73,188.00</b>
<b>Net Personal Savings and UBS Loan</b>	<b>186,563.00</b>
<b>Net Excess or (Deficit)</b>	<b><u><u>(\$52,942.81)</u></u></b>