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## **Key Person Discounts**



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# Hard To Replace

- The key person discount measures the economic adjustment of losing one individual.
- That person's skills, relationships, or reputation materially drive earnings and cannot be readily replaced.
- The test is whether a hypothetical buyer would pay less on the valuation date.
- The harm must be durable, not a transition-period inconvenience.
- The adjustment must be identified and supported in a report.

# What It Is Not

- An acknowledgment that the owner works hard.
- A shareholder-level discount like lack of control or marketability.
- A substitute for normalizing owner compensation.
- A percentage borrowed from another engagement.

# Facts Must Stack

- No single factor carries the conclusion, the case strengthens as conditions accumulate.
- Customers and referral sources deal with the individual, and the reputation is fused to the person.
- There is no bench, no successor, and no employment agreement or funded buy-sell.
- Insurance payable to the company, a deep bench, or contracts surviving a change in control cut it back.

# Cash Flow Wins

- The adjustment goes in cash flows, the discount rate, or as a discrete percentage.
- Scenario weighted modeling is most defensible, as every input is testable.
  - A discrete percentage invites the charge that the figure was arbitrary.
- Revenue at risk and replacement cost data quantify the harm.
- Five to fifteen percent is a reasonableness check.

# Entity Level Governs

- The adjustment attaches to the enterprise, not to the percentage being valued.
- It reduces value for every shareholder proportionately, controlling or minority.
- In statutory fair value proceedings, it is not automatically foreclosed.
- Reach the value indication, apply the key person adjustment, then apply control and marketability.

# Count It Once

- One economic fact charged twice is the first thing opposing counsel looks for.
- If compensation was normalized to a market rate, the earnings already carry that cost.
- If the risk premium reflects owner dependence, say which adjustment carries it.
- An exclusion of personal goodwill may have removed the key person economics already.
- Multiples from owner-dependent transactions may already embed the risk.

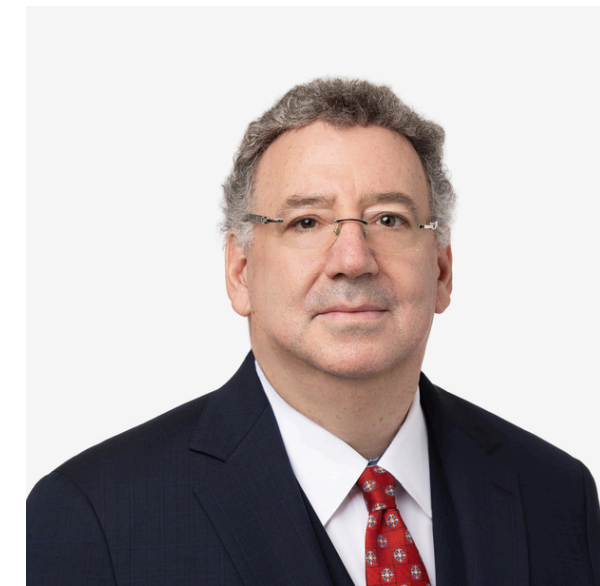
# Questions?

*Have a specific accounting  
or valuation question about  
your case? Call me.*



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