



DE-RISKING THE DISTRESSED

# Valuations Deep Dive: Asset value implications during economic uncertainty

Tangible assets can contribute significantly to an organisation's value, performance and strategic direction. As we continue to witness COVID-19's economic impacts ripple through the world – with Australia in its first recession in decades – having accurate and reliable asset values, along with the proper disclosure of these, is now more crucial than ever for businesses.

Tangible asset valuations are often utilised to assist organisations with their asset management, strategic, fiscal and legislative requirements, including in times of significant change. Partnering with an experienced and independent valuation provider to help you navigate through significant change is critical.

The economic downturn associated with the pandemic will likely place many companies in financial distress. Each stage of the restructuring and turnaround lifecycle presents unique risks and issues. Valuation can play a key role in every step, including when a company comes out the other side on the road to recovery.



FIG. 1. RESTRUCTURING AND TURNAROUND LIFECYCLE

## Phase 1: Financial Distress

When a company becomes financially distressed or during times of change and uncertainty, it is imperative that the values of tangible assets are correctly identified. Significant change within the business can lead to the requirement for valuations for numerous purposes including legal, accounting, regulatory, financial or transactional requirements.

The following are some examples where valuation plays a critical role in helping companies meet disclosure and reporting requirements, as well as helping management understand the true value of their business at all times, whether they are in financial distress or operating under uncertainty.

### Impairment testing

Many businesses are restructuring their business model or pivoting their products and services to alleviate financial distress and stay afloat, while others unfortunately did not survive the economic impact of the pandemic. Economic downturn and uncertainty can cause a fixed asset's value to diminish.

An asset that loses its value and needs to be written down is referred to as an "impaired asset." An asset can become impaired for a number of reasons including becoming obsolete, failing to meet regulatory standards, being damaged, and changing market conditions. (E.g. A piece of specialised machinery that makes a specific model of infant carseats fails to meet new safety standards.)

Increasing focus and scrutiny on the long term resilience and performance of companies mean that many are reviewing and reassessing their impairment testing processes and assumptions. International Accounting Standard 36 Impairment of Asset requires extensive disclosures on the impairment tests performed and impairments recognised.

These tests are typically done in the form of a tangible assets valuation, as companies are required to provide an explanation of events and transactions that may affect the financial position or performance since the last annual reporting date.

Marsh can assist with fixed asset impairment testing, including consultations and valuations performed for impairment possibility, with results suitable to be disclosed in an organisation's financial statements.

### Financial reporting

There are potential implications for financial reporting arising from the current economic climate including a company's ability to forecast cash flow, financial changes, impairment, currency

fluctuations and any going concern issues as part of their obligations to disclose the financial position and asset values to shareholders and/or stakeholders.

Public entities, as well as some private entities, must conduct periodic valuations (e.g. every 3 to 5 years, or when material changes are anticipated) to determine the fair value of their assets in order to meet accounting standards and requirements. With ongoing economic uncertainty, increased scrutiny from stakeholders over values and disclosures means an increased burden on directors, who are ultimately responsible for the accuracy of financial reporting.

### MATERIALITY

With the relatively unknown impact of COVID-19, auditors are increasingly requiring businesses to perform Materiality Reviews between valuation cycles, even when there is no anticipated change to asset values. Whilst an organisation may have previously undertaken a valuation for financial reporting purposes, it is a requirement to disclose material changes to these values as and when they occur. Marsh can assist clients with Materiality Reviews to help businesses meet disclosure requirements.

### Exchange rate impacts

*A significant proportion of plant and machinery assets in Australia are procured from overseas. As such, the exchange rate can potentially increase/decrease the gross current replacement cost or secondary market value, which may impact the fair value of the assets.*

*This aspect of valuation should not be considered in isolation. For many businesses, economic obsolescence caused by reduced product demand due to the pandemic could mean that the enterprise value of the business has fallen, thereby limiting the proportion of the business value that can be apportioned to plant and machinery, resulting in an impairment issue.*

## Mergers, acquisitions and disposals

### PURCHASE PRICE ALLOCATION

Upon acquisition or merger, there will often be a requirement for the buyer to recognise the tangible asset values as part of the sale in their financial accounts in accordance with accounting standards (e.g. AASB 3 – Business Combinations).

Accounting organisations will often undertake and charge for these services as part of their engagement. The cost of having tangible assets services undertaken by large accounting firms is often substantially higher than engaging with a tangible asset professional.

### TAX CONSOLIDATION

Where a company owns or acquires multiple businesses, there may be taxation benefits in consolidating these into a single entity, such as reducing compliance costs, removing impediments and maximising depreciation. Undertaking a fixed asset valuation during asset consolidation will allow the carrying value to be reset and potentially provide significant tax benefits to the consolidated entity.

The Marsh valuation team remains up to date with the latest Australian Taxation Office (ATO) guidelines regarding valuations for Tax Consolidation. We follow the process of:



FIG. 2. TAX CONSOLIDATION VALUATIONS PROCESS

Whilst a Fixed Asset Register (FAR) provides a good guide, in our experience, there are often gaps and inaccuracies that can impact the results of the valuations. Marsh's comprehensive valuation process involves physical inspection and verification of the assets leading to increased accuracy in the results.

### **Pre-valuation assessment: Do you need a comprehensive valuation?**

*Before an organisation commits to a full valuation exercise for tax consolidation, our comprehensive modelling can help determine the likelihood of significant changes from the current book value to the Fair Value of your assets. This is a quick and cost effective way for organisations to determine whether there is potential financial benefits in undertaking a comprehensive valuation.*

*For example, in a merger or acquisition situation, pre-valuation assessment modelling can provide an indication of the potential additional depreciation a business could achieve from undertaking a valuation for tax purposes. A prediction of significant cost benefits (which is common) will justify the business undertaking a full valuation, or conversely, the modelling can also inform that the cost benefit would be minimal, saving the business from the cost of undertaking a full valuation.*

## Strategic decision-making

While the purchase or sale of a business typically focuses on the financial performance, the tangible assets and their values play a key role in a buyer's due diligence and decision-making process.

Does an organisation's current asset values reflect their true fair value? If an asset is held at book value, fully written down, or has not been recently reviewed and accounted for by its Fair Value, the asset could be over-depreciated and its value understated, potentially inflating the attractiveness of your company and impacting sale negotiations.

Undertaking a valuation of your tangible assets prior to a sale by the vendor/seller acts as a useful marketing and data tool to provide a level of comfort to potential buyers and facilitate strategic decision-making. By doing this, the seller can effectively show the valuation of its tangible assets to potential buyers while reducing the buyer's obligation to carry out a valuation for purchase price allocation.

## Phase 2: During Administration or Receivership

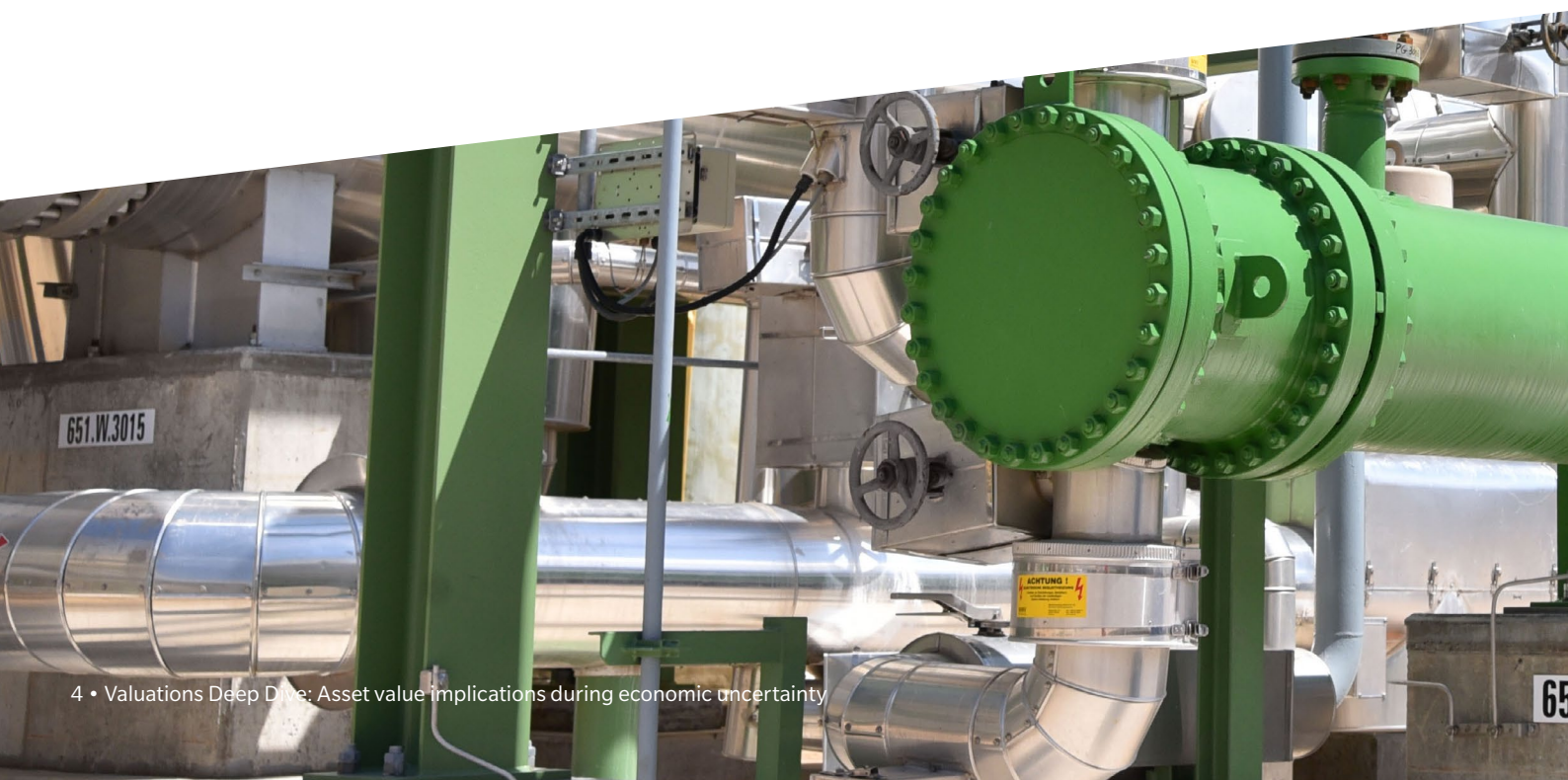
During this phase, a company should not trade while insolvent, and directors must actively monitor the financial position of the company and regularly assess solvency. A properly executed asset valuation is a critical element during the administration, receivership or insolvency process, helping to drive best outcomes in the restructuring process.

Marsh's dedicated valuation specialists can support the insolvency practitioner in a variety of situations including voluntary administrations, creditor's voluntary liquidations, court liquidations and receiverships. We can assist in all facets of the valuations process, whether it be determining liquidation values for distressed assets or providing market values in continued use for going concerns.

Under these scenarios, independence is key. In some instances, the valuation is conducted by the auction company, which can be problematic as the valuer may also have a vested interest in the assets being valued. i.e. the auction company valuing assets for a liquidator is likely also desiring to be engaged to dispose

the assets through their auctions, as the proceeds of an auction often far outweighs the valuation fee. This creates a significant conflict of interest and can often result in artificially inflated valuations in an attempt to entice the company to sell their assets through the same auction house.

On the contrary, Marsh has no interest in selling the assets and thereby can conduct a truly independent valuation. Equipped with a more accurate assessment and idea of a company's worth, administrators and liquidators can be better informed in their decision-making process around the future of the company and its assets.



## Phase 3: Emerging From Distress

During this phase, companies will be realigning and making different business decisions appropriate to their new situation. As a business recovers from financial distress and maps out their strategic direction for the future, Marsh can help provide strategic tangible asset valuation advice on how best to categorise assets and values in order to capture tax benefits or better structure a company's investment portfolio.

### Asset register reconciliations and review

A Fixed Asset Register review ensures all assets are captured, disposed assets are removed and written-off assets are actually no longer in use. This allows a business to make strategic decisions around their assets and the values accounted for. It also assists with asset management and transferring into new accounting software.

### Valuations for insurance purposes

Ensuring that accurate values are declared under a company's Property Damage or Industrial Special Risks (ISR) insurance policy is crucial in determining an adequate total sum insured. Inaccurate or under-valued declarations can lead to underinsurance, whereby insurers could rely on co-insurance clauses within the policies to potentially reduce or deny cover in the event of a loss/claim.

Additionally, in an increasingly hardening insurance market, up-to-date insurance valuations are highly regarded by insurers and will assist your broker in negotiating the best coverage and terms on your behalf.

### Tax depreciation schedule

Having a tax depreciation schedule prepared by an independent expert often uncovers hidden depreciation resulting in substantial tax savings, both immediate and ongoing (up to 40 years) for investment properties. Available depreciation is typically greater than anticipated and is often overlooked.

Conducting an insurance valuation at the same time as collecting data for a tax depreciation schedule will create synergies and save organisations time and cost.



# Why Marsh

## Our Differentiators



### Competitive fees

Our consulting fees are often substantially lower than having tangible assets valued by large accounting firms.



### Deep experience and Pacific-wide presence

Valuing over 10,000 assets across the Pacific region worth over \$60 billion annually, our local team of 30 valuation experts undertake valuations in all locations and industries across the Pacific region. Deep local expertise enables us to deliver valuation solutions to organisations, whilst drawing on Marsh's unrivalled experience and support of valuation specialists and over 35,000 insurance professionals globally.



### Independence

Specialising solely in valuations and not auctions, accounting or tax services ensures Marsh Valuations has no vested interest in the value of the asset and thereby eliminating any potential conflict of interest.



### Mobility and agility

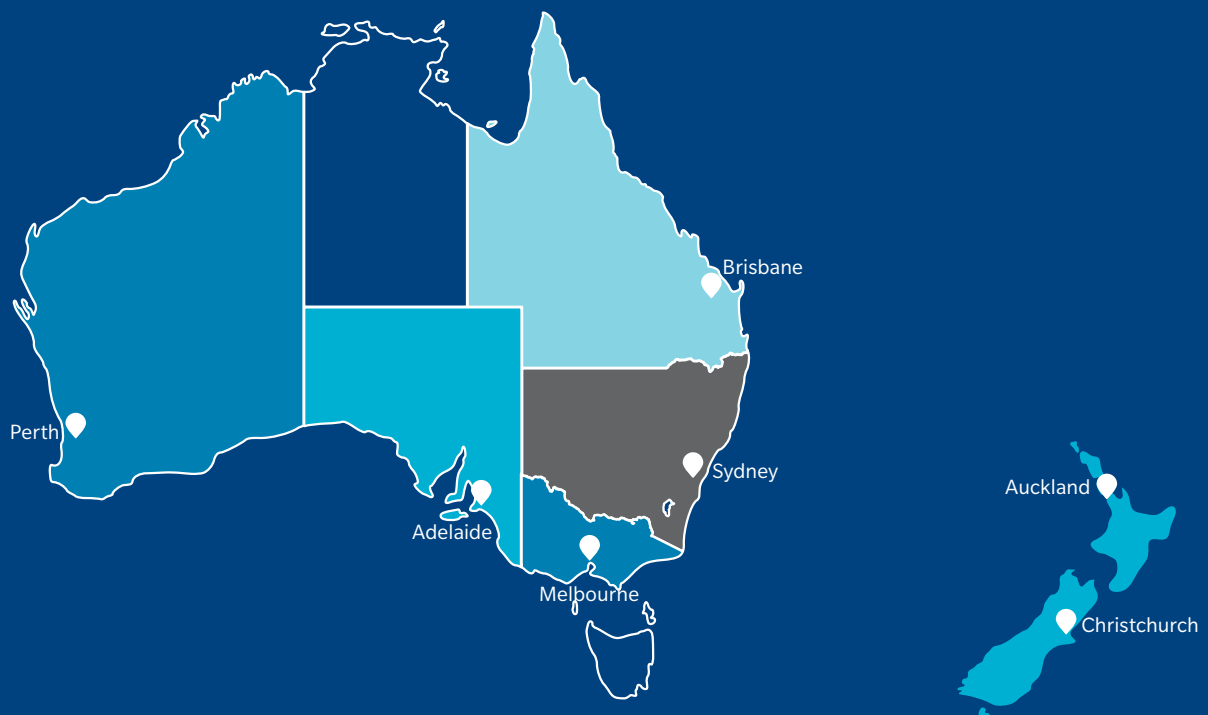
We understand time is of the essence as stakeholders need to know very quickly the total value of assets in order to assess the position of a company. We also understand that liquidators typically only have a short window to be on site, as the landlord is usually owed rent and therefore the company may need to vacate the premises. Our dedicated team are highly mobile and agile. We swiftly respond to requests and conduct valuations in locations across all regions of Australia and New Zealand, often at very short notice.



### Comprehensive and consultative

We look into the issues that can materially affect value rather than relying solely on client provided information such as Fixed Asset Registers. Whilst many valuations are executed as a transactional service, Marsh operates in a consultative and committed approach to ensure businesses not only receive accurate and comprehensive valuation results, but also understand the drivers behind their values.

## Our Presence



## Our Experience

### ASSETS

Our specialists undertake valuations of the following asset types:

- Property – land and buildings
- Infrastructure and long life assets
- Plant and Equipment
- Contents
- Mobile Plant / Yellow Goods

### INDUSTRIES

Our valuations team work across a myriad of industries, including:

- Mining and Earthmoving
- Energy, Oil & Gas
- Manufacturing
- Agriculture
- Hospitality
- Infrastructure
- Construction
- Healthcare and Hospitals
- Printing
- Chemical
- Grain Storage and Processing
- Transport and Logistics
- Retail
- Government

## Has your business been financially impacted by COVID-19?

To learn more about where valuations fit in and how to manage the unique risk and people issues through the various phases of the Restructuring and Turnaround Lifecycle, download a copy of [De-Risking the Distressed: Risk and People Solutions for Distressed Companies](#).

## Contact us

For further information, please contact your local Marsh office or visit our website at [marsh.com/au](https://www.marsh.com/au).

SIMON O'BRIEN  
Head of Valuations – Marsh Advisory  
+61 417 079 204  
[simon.obrien@marsh.com](mailto:simon.obrien@marsh.com)



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