Risk management and valuation: a Board issue

As said in the Introduction to the International Rule ISO 31000 *Risk Management – Principles and guidelines, "**All activities of an organization involve risk**"*. In a scenery of political and economic uncertainty, or in contexts with a globalized *supply chain*, risks multiply and time to decide shortens dramatically.

A critical situation

More than in other European countries, the use of the appraisal as a decisional tool is underrated in Italy. The insurance valuation of the fixed assets – when considered – is perceived as a commodity, while the valuation – and the insurance - of the losses deriving from business interruption is a privilege of no more than 5% of the companies, although the business interruption is the first cause of bankruptcy.

In transactions or in financial operations, as well, little attention is paid to the value of the fixed assets and to their capacity of granting a prosecution of the usual production, while the interest is focused on the financial perspective of the companies involved: but how to minimize the effects of an uncertain situation, where the market is instable or, sometimes, nonexistent? How banks can avoid the risk of a non performing loan? Could a private equity eliminate the risk of growing post-acquisition maintenance expenditures?

The lack of a common terminology among the different stakeholders, the unplugged gaps in the local and the international regulations involving the asset management (IAS/IFRS, US GAAP, SOX, etc.) don't facilitate the birth of a real "culture" of the value and of the risk.

To know the impact makes the business less vulnerable

A professional appraisal can represent an essential tool, when:

- Insuring the fixed assets against the material damages;
- Assuring the business continuity;
- Choosing a supplier or a partner;
- Selling shares, assets and businesses;
- Asking for a loan;
- Contributing in a joint venture.

In fact, the choice of using this instrument not only shows a will of transparency and a long-sightedness, but also provides a basis for a fair discussion, and – by means of specific policies – implies a real transfer of responsibility to a third, professional and independent party.

The insurance appraisal

The twin perils of over and under insurance are avoided by an accurate valuation assessment of the sums insured. Over insurance results in excessive premiums. Under insurance, whilst delivering cheaper premiums, can be disastrous, with the failure of insurers to pay out sums sufficient to reinstate the assets of a business, or to compensate for business interruption, frequently resulting in wider business failures. An independent appraisal eliminates the most part of the discussions connected to a loss settlement.

The market valuation

Appraisers are called to carry out a valuation of the assets with a view of determining their fair market value, taking into consideration the following factors:

- Date of purchase;
- Type of asset and extent of use (general purpose or specific);
- Repairs & Maintenance policy of the enterprise;
- Availability of spare parts in the future;
- Future demand for the product manufactured by an asset.

The IAS "fair value" – a theoretic value, for financial use only – has represented a real question mark for the appraisers: the elusive definition and methodology permitted a wide range of interpretations. On January 1st, 2013, the newly adopted IFRS 13 will – finally - provide clear and consistent guidance for measuring it, addressing valuation uncertainty in markets that are no longer active and defining an identical wording for IFRSs and US GAAP to increase transparency in cross-border transactions. For the first time, classes of assets and liabilities will be determined on the basis of their nature, characteristics and ***risks.***

A tool for Corporate decision makers

Born "to serve and serve you well whenever you feel the need of such service." (*Company mission statement, February 1, 1896),* we are focused on appraisal and value since over a century. Our main goal is to create a "culture of value", allowing us to share our experience and methodologies with a competent, well-informed customer.

But it's not only of matter of value: more and more often we are called to detect functional and economic obsolescence of the assets, within M&A operations. In fact, the risks in purchasing a business are often hidden in the maintenance and running costs, not correctly forecasted/measured at the moment of the purchase.

A recent assignment concerning an oil refinery resulted in the decision of not closing the deal when our study - after having considered the size, the complexity, the product range, the age of the assets, the technology and the market - highlighted a reduced productive capacity in comparison with a new plant, an increase of the energetic costs and a huge demand of investment deriving from a previous lack of extraordinary maintenance. In fact, significant technological advances have been made in technology, energy conservation and process configuration over the years which a prudent investor must consider if constructing a refinery today, the use of new technology resulting in higher production yields, increased control, reduced labor requirements and utility costs, reduced chemical and catalyst expense, and greater operating flexibility.