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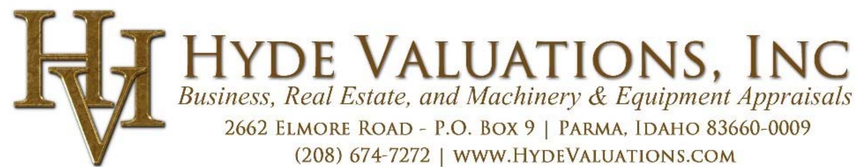

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Subsequent Events

The effect of a subsequent event(s) on the value of a company or other asset is difficult issue. In valuation engagements, the key regarding how to treat subsequent events is related to known or knowable. In other words, only information that was known or knowable as of the effective date of the valuation should be considered.

Facts – not suppositions, but valid information
Available – known or reasonably knowable

Appraisals must be based on information known or reasonably knowable as of the valuation date.

Information that becomes available after the valuation date can be divided into two types:

1. Information that indicates but does not affect value.
2. Information that affects value.

An example of the first type would be a subsequent sale of the business, assuming that there had been no material change in its environment, business, or financial position in the intervening period. Such information could reasonably be interpreted to indicate but not affect value, and could be relevant to a previous valuation date. Several court cases have affirmed this general principle, which makes sense as well.

Examples of the second type abound. In some instances, this information was not known or reasonably knowable as of the valuation date and was thus not relevant to the appraisal. For completeness, however, the appraiser should indicate his or her awareness of it and state why it was given no weight.

Although RR 59-60 3.03 applies strictly to tax appraisals, its relevance to compliance (e.g. financial reporting and ESOP) and litigation engagements is also obvious. In litigation, however (particularly divorce), there is sometimes controversy about the valuation date. If this is not clarified promptly in advance of beginning work, this can create major headaches for all concerned.

An Example:

A business owner died on June 5, 2017. We are valuing a business for estate tax purposes. It is now August of 2017. The valuation date will be June 5, 2017 and the report date will be sometime in September 2017.

1. The company prepares quarterly financials and cannot furnish a June 5 (or May 31) statement. Should we use March 31 or June 30 results?

We would look at both the March and June statements and see if there were material differences. If not, the choice is moot. We would personally lean toward the June statement because it was closer to date of death, even though it is technically after it. If there were major changes between the statements, we might

interpolate an estimated date-of-death statement with management's help. Alternatively, we could work the problem as of both dates and determine the significance of the difference.

2. On October 1, 2017 well after the owner died, the executor received a totally unsolicited offer to buy the business, which had not been put on the market. How should this be addressed in the appraisal?

We would disclose this in our report and not assign it any weight as it was not known or reasonably knowable as of the valuation date. We might use it as a weak test of reasonability. (If the buyer was strategic, this might not be a fair market value indication.)

3. As of the date of death, the company had just become aware of a major new potential customer, but had not done any research, prepared proposals, or contacted any of the customer's representatives. How should this be reflected in the appraisal?

Same as (2); we have no facts with which to quantify the impact or probability of getting the new customer. We are appraisers, not fortune tellers (unfortunately we were not issued a crystal ball with our appraisal designations).

4. Same as (3), but the company had presented a proposal and knew what the revenue, profit and cash flow impact of its acceptance (or rejection) would be. What should be done in the report?

We would try to estimate the chances of getting (or losing) the business and prepare a probability-weighted analysis. We would not talk to the customer, since they would obviously not make this disclosure to a potential supplier in the normal course of business.

5. Same as (3) and (4), but the proposal was accepted (and a contract was signed).

If the offer was reasonable it should be similar to the concluded value in the appraisal report. However, sometimes a buyer will have some reason to pay considerably more than the fair market value for a business. Usually, this is because of expected synergies expected upon combination with an existing enterprise. Accordingly, such an occurrence may not make a change to the value conclusion as of the effective date. Regardless, the payment of a much higher price than expected or the acceptance of a much lower price should be disclosed and explained. When such things occur, it makes an appraiser's life more interesting – especially later on when a matter goes to court and the appraiser is cross examined on the stand as to why the value was so much lower than the eventual sales price.

In summary, if an appraiser is aware of subsequent information, it should be disclosed in the report and a description made of why it was or was not relevant.

Valuations play a part in all strategic transactions, tax, and many litigation matters. For additional information or advice on a current situation, please do not hesitate to call. **We value real estate, businesses, and personal property including livestock and machinery & equipment.**

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