Business Valuations: Why Is The Valuation Date So Important?

It is common to think about which method the appraiser will use or whether discounts might apply when considering how the value of an asset will be determined. However, the appraisal date is a critical factor that may not immediately come to mind.

What's the Big Deal?

One of the main reasons an appraisal's "as-of" date matters is that appraisers generally can't benefit from hindsight's 20/20 vision. In fact, *IRS Revenue Ruling 59-60* states, "Valuation of securities is, in essence, a prophecy as to the future and must be based on facts available at the required date of appraisal."

The appraisal date serves as a cutoff date for information that can be used to determine the value of a business. As a rule, valuators consider only information that was "known or knowable" on the appraisal date. Why not include subsequent events from valuators' analyses? Because fair market value should be based only on information hypothetical buyers and sellers would have known at the valuation date.

Because subsequent events may be foreseeable and may provide valuation evidence, there are exceptions. In addition, site visits and management interviews may not occur near the valuation date. No steadfast rule applies to all cases. The valuator must evaluate the circumstances and use professional judgment to determine how to treat subsequent events. Selecting the appropriate date often depends on the purpose of the appraisal.

Estate Valuations

For estate tax purposes, assets normally are valued on the date of death. But under certain circumstances, an executor may elect to use the "alternate valuation date," which is six months after the date of death. The later date may be advantageous if the decedent's estate includes securities, real estate or other property that's declined substantially in value since the date of death.

There's a catch, though. The executor can't selectively apply the election to assets whose values have declined sharply. Rather, if the alternate valuation date is selected, it must be used for all assets in the estate (except for those sold between the date of death and the alternate valuation date, which are valued on the sale date).

Divorce Cases

For purposes of divorce, the valuation date is usually prescribed by state law. Typically, it's the date the divorce action commenced, but it could also be the trial date, the date a divorce decree is issued or some other date established by law, agreement of the parties, or attorney preference. In some states, the court may select a valuation date that would be fair to both parties.

Shareholder Oppression

In these cases, applicable law often provides that the presumptive valuation date is immediately before the wrongful act that triggered the litigation. But it's not unusual for parties to argue for an alternate valuation date if they feel that using the presumptive date would be unfair.

Shareholder Oppression (cont)

Circumstances might call for an alternate date, for example, when sufficient market information on the presumptive valuation date is unavailable, or when a contingency or potential liability that wasn't yet resolved on the presumptive date is discovered.

In addition, an aberration that temporarily increased or decreased the stock's value around the time of the corporation's wrongful act might call for an alternate date. Evidence that the corporation's wrongful act was timed to take advantage of a historically high or low stock price might also persuade the court to use an alternate date.

It's All in the Timing

Because the valuation date is so critical, discuss it with your valuator before he or she starts work. Because values ebb and flow over time, this can be a strategic decision that's not to be taken lightly.

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