

Alert

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The Five Stages of Denial, Valuation Edition

“Impaired? What am I going to tell my CEO?”

The “Five Stages of Denial” may be considered the components of the psychological process by which people deal with unfortunate or unpleasant circumstances. And nowadays, we have seen this process, and the psychological character of our clients, reflected during our valuation engagements.

Mostly we have experienced this in impairment reviews. As Dr. Valuation, we have seen the typical process play out in various ways:

Stage 1, Reality Warping: “Just because my stock price is down 82%, we are not impaired because I met plan.” Or, “My level 3 assets are fine because the only trades happening are not at ‘real prices,’ and are only distressed sales that don’t apply to me.”

Stage 2, Anger: “It’s not fair! I’m outperforming all of my peer group.” And, “Why me? I never levered up my balance sheet/did crazy acquisitions like those guys!”

Stage 3, Bargaining: “If we just suspend mark-to-market accounting, my balance sheet will be fine.” Or, “My stock price is only temporarily depressed – just give me until Q3.”

Stage 4, Depression: “My bank covenants! My bonus pool! My board member who never liked that deal anyway!”

Stage 5, Acceptance: “We’ll bite the bullet.” And “Everyone’s in the same boat, so I’m feeling OK about it.” And most commonly, “That’s all? I was thinking [or hoping] for more of a write-down. While we’re at it...are you sure your discount rate is high enough?”

These impairment studies – whether at the entity or reporting unit level (most often for FAS 142 goodwill impairment reviews) or at the individual asset levels (under FAS 144 and FAS 157) – have definitely seen the shifting tides of time. Two years ago, we wore the hat of “bad cop,” often having to wrestle with our clients about the extent of the impairment. Many CEOs were NOT going to readily take an impairment charge on their pet acquisitions. Now, there has been much less resistance in what would previously have been Stages 1 to 3. (Not quite enough that many now think of us as the “good cop,” but at least there is less contention.)

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The recent run up in most stock prices has definitely been a relief to many, and taken many back from the edge of Stage 4, depression. But for many, their recent reporting of impairment – often driven then by stock prices that were then at what were their multi-year lows – was quite a shock to the system. Not only did they have to present their write-offs to their boards, but they also had to wrestle with their external auditors about them; adding enough insult to injury to depress just about anyone.

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MISERY LOVES COMPANY

There is also certainly a “misery loves company” or safety in numbers sentiment now being experienced in Stage 5. Like a type of collective financial *schadenfreude* - or the emotional upside of another’s misfortune - Stage 5 today might also be described as *paired impairment, or relief in common impairment*.

VRC assists its clients with not only impairment studies, but also as a “support group” for FAS 157 review (including review of one’s own internal models), purchase price allocation, stock-based compensation, fairness opinions and other fair value analyses, as well as in the perhaps ultimate Stage 5 recovery and acceptance phase: fresh start accounting.

For questions or more information, contact one of our valuation “doctors,” Raymond Weisner, at (212) 983-3370 and let him know where it hurts. **VR**



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