



Mitchell & Taylor
VALUATIONS

"Converting Experience
into Expertise"



Physical Asset Under-Insurance - Causes and Solutions



Physical Asset Valuations
including Plant,
Equipment, Buildings and
Infrastructure



Physical Asset Due
Diligence



Fixed Asset Register
Establishment and
Verification




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Insurance Valuation Review 2021

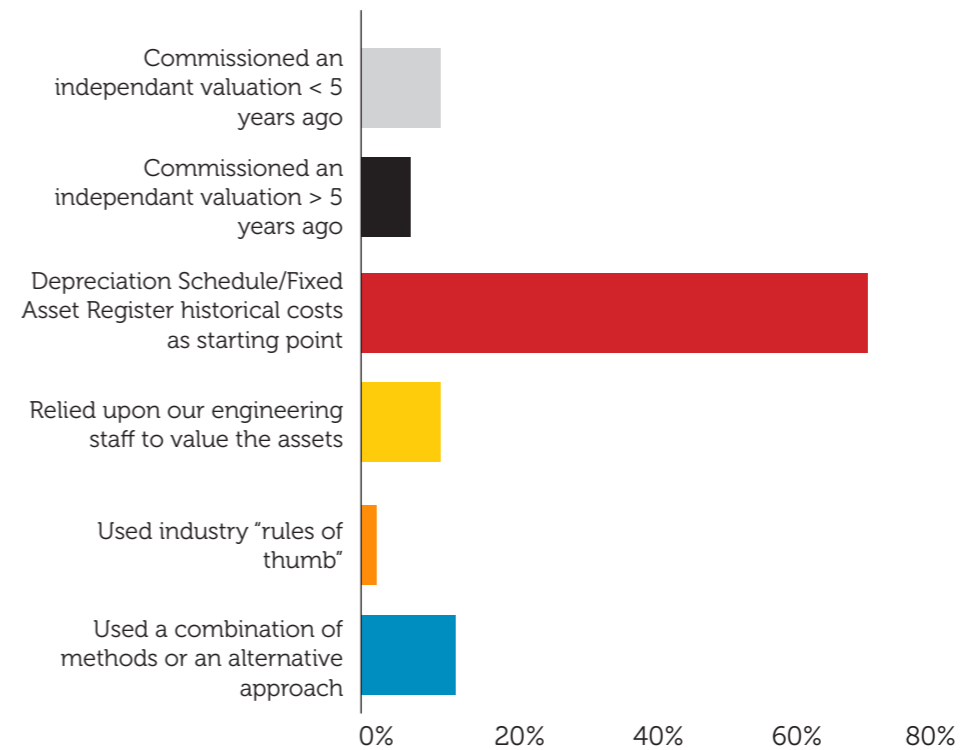
This paper considers why 75% of Australian businesses under-insure their physical assets.

"If Australian businesses are not initially seeking professional valuation advice in determining accurate sums insured for their physical assets there is a very high probability they will have an inaccurate view on asset reinstatement costs and an increased risk of under-insurance"



Assessing Reinstatement Costs - Client Approach

Given the very high incidence of under-insurance in Australian businesses we liaised with our clients to determine their initial approach in calculating reinstatement costs <> sums insured prior to seeking our independent opinion.



The vast majority of clients (68%) indicated they used historical purchase costs capitalised in their accounting fixed asset register/depreciation schedule (FAR) and applied Australian CPI to 100% of these costs, in order to arrive at their asset reinstatement costs.

We tested the plausibility of this approach, based upon:

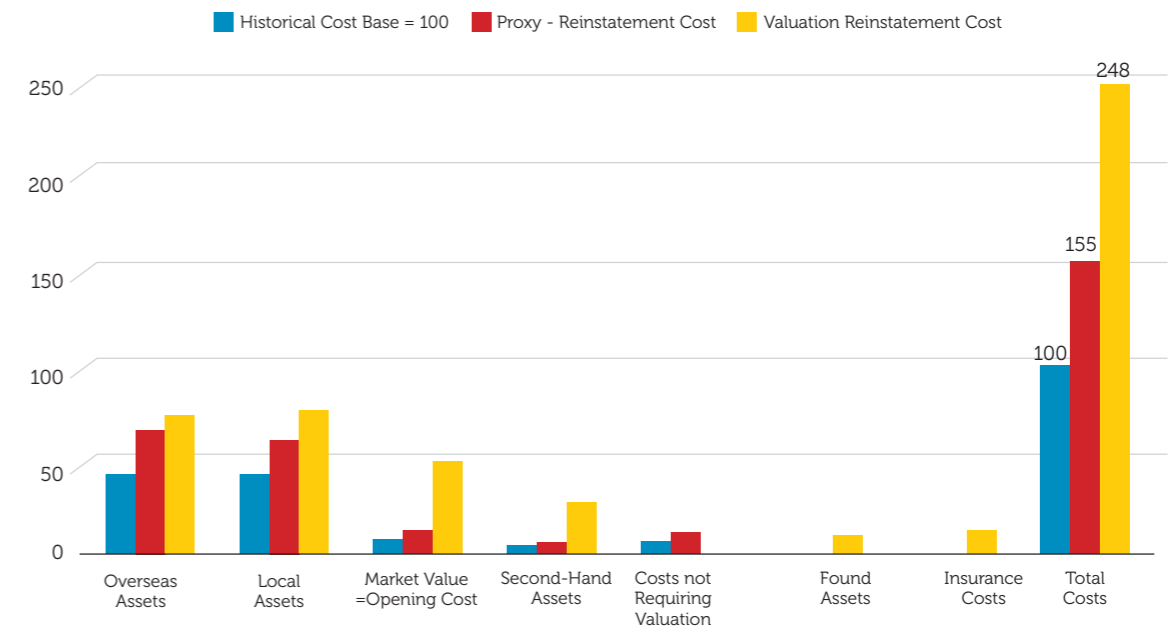
- Does the historical FAR data/costs accurately reflect the physical assets that would be replaced in a loss situation?
- Does Australian CPI inflate historical FAR costs into current and accurate reinstatement costs for insurance purposes?

Historical Cost Approach to Reinstatement Costs v Valuation



To replicate our clients approach we stratified the Historical FAR's for 12 individual businesses which contained a total of 92,000 line items. These FAR's had a total combined historical cost base of >\$2bn (100). We applied Australian CPI to this cost base which resulted in a proxy reinstatement cost of >\$3bn (155).

Our valuers had previously undertaken formal insurance valuations for these 12 businesses resulting in a total reinstatement cost of >\$5bn (248). The resulting shortfall of 60% between the proxy cost and our valuation infers a business will often understate their reinstatement costs using historical FAR data & costs.



In our opinion this understatement occurs for the following key reasons:

- Opening Historical FAR costs are often recognised at Market Value which can be far lower than reinstatement cost for:
 - assets acquired as part of a business transaction
 - assets acquired second hand
 - assets revalued for financial reporting purposes
- Opening Historical FAR costs do not capture nor consider, the following insurable costs:
 - off-balance sheet items on hire, lease or loan
 - physical assets not captured or capitalised on FAR (found assets)
 - movements in costs for commodity based products such as steel
 - installation and commissioning costs undertaken In-house
 - engineering, procurement, construction management (EPCM) costs that would be incurred following a loss
 - demand surge pricing for materials and labour following catastrophes including earthquakes, cyclones, and pandemics
 - optimisation of the existing older assets with modern equivalent assets (excluding betterment)
- Historical FAR data often captures costs that can distort the calculation of reinstatement costs:
 - historical costs often include commercial discounting that would not be available in a loss situation
 - non-insurable costs i.e. prior asset disposals, opex and sustaining capex can lead to an overstatement of the sums insured
 - physical assets that would not be replaced in case of a loss

Impact of overseas inflation & currency on insurance values

Is it plausible to apply Australian CPI to inflate historical purchase costs into reinstatement costs for insurance purposes?

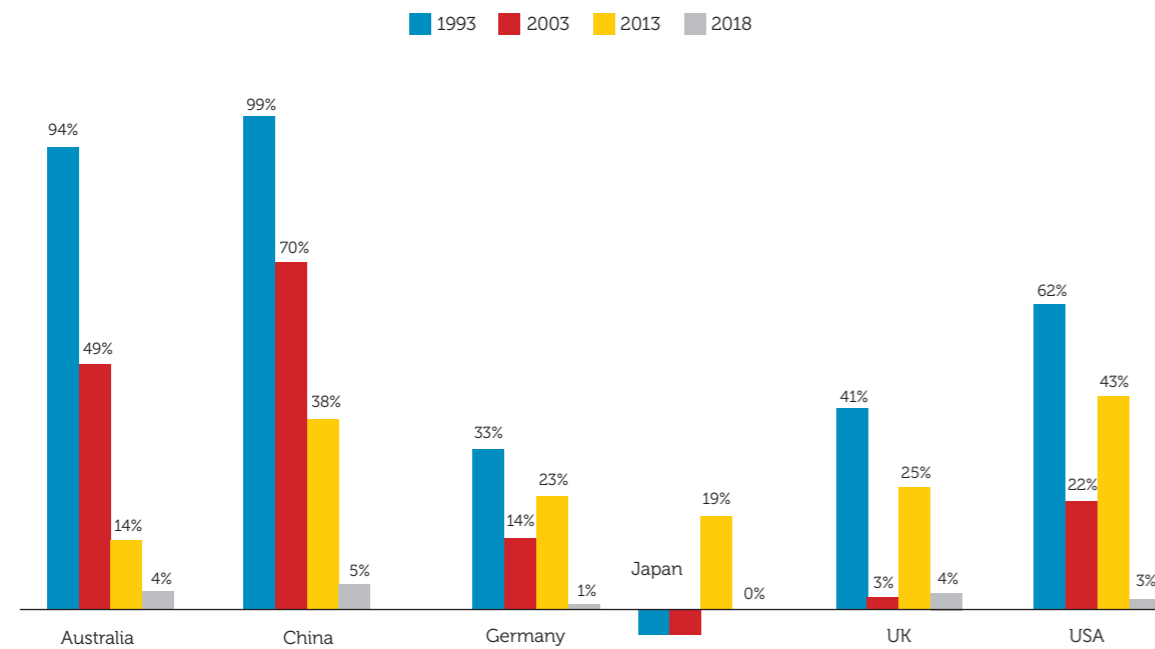
The graph highlights a wide variation in the combined effects of currency and inflation.

A worked example is as follows:

- If an asset imported from the USA in 2013 cost \$1,000 AUD it would have increased by 43% to \$1,430 AUD in 2021. In contrast an Australian made asset costing \$1,000 AUD in 2013 would have increased by 14% to \$1,140 AUD in 2021.

A blanket Australian CPI approach to historical purchase costs will result in the asset reinstatement costs <-> sums insured being inaccurate.

Capital Equipment Currency & Inflation Indices for Australia 2021



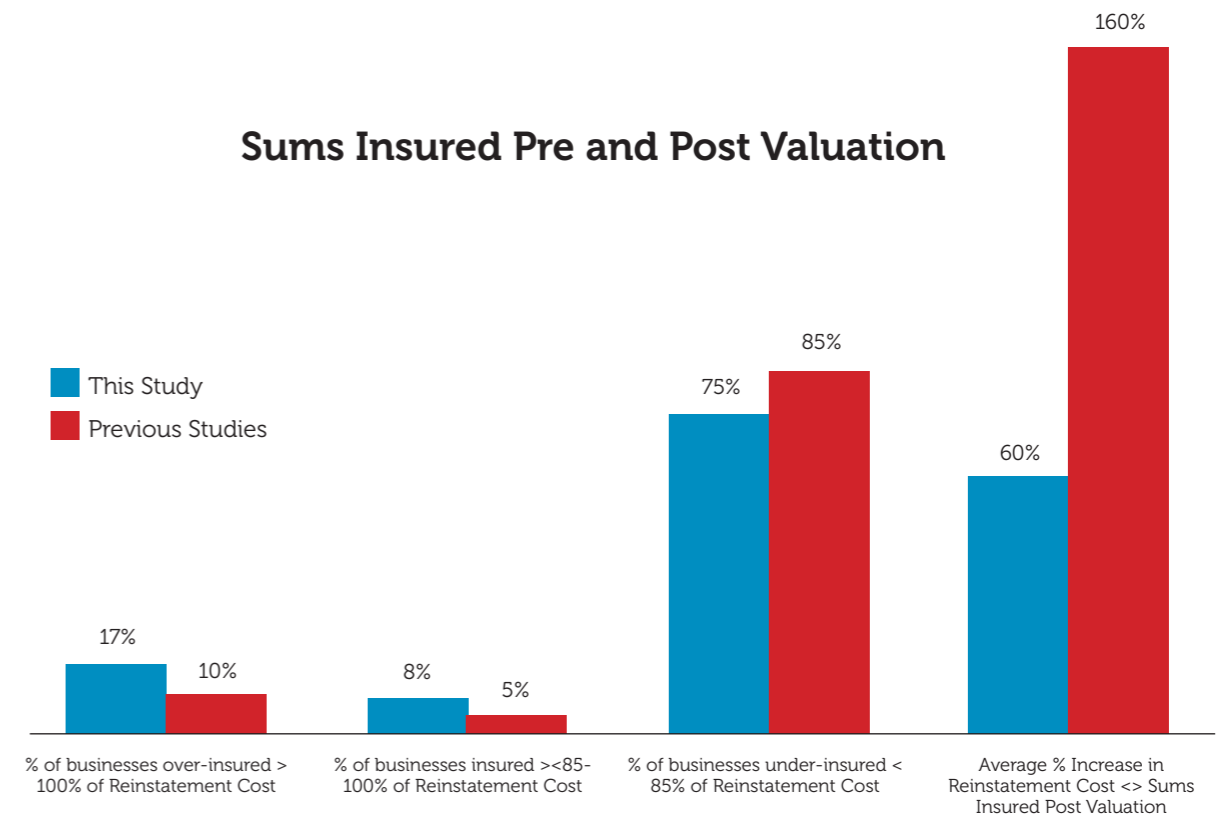
Under - Insurance

The pre and post valuation reinstatement costs from this study were compared to previous studies our valuers undertook of 200+ businesses across many different industries.

As a result, we observed the same recurring statistics despite 15 years between surveys. The pre-valuation reinstatement costs were significantly understated compared to the post-valuation outcomes.

A professional valuation by certified practising valuers will ensure the correct reinstatement costs are declared and the significant risks of under-insurance <-> co-insurance are mitigated.

Sums Insured Pre and Post Valuation



Our KPI's

80	Years of physical asset advisory expertise
1,300+	Valuation, Due Diligence & Data Projects
30+	Countries
15+	Industry Sectors
320+	Specific industries
1,500,000+	Individual assets valued

Our certified practising valuers assess the core requirements of a valuation engagement and provide cost-effective solutions to meet our client's specific needs. Our experience tells us new and existing clients are motivated to obtain physical asset valuation, due diligence and data advice for one or more of the following requirements:

- Insurance & Risk Management
- Transactions, Mergers & Acquisitions
- Accounting, Tax & Duties
- Legal Disputes
- Asset Based Lending
- Restructuring, Insolvency & Disposal
- Physical Asset Due Diligence
- Fixed Asset Data Management

Key Personnel



David Mitchell

David has 40 years experience in plant and machinery valuations. Throughout his career, David has managed plant and machinery valuation teams for some of the world's largest finance, insurance and real estate advisory practices as well as founding his own valuation practices.

David's breadth of experience has resulted in him being able to offer his clients expert valuation advice across all industry groups within Australia and 25 countries worldwide.

David is a Certified Practising Valuer and an examiner with the Australian Property Institute. He has given testimony to Australian courts as an expert valuer.

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Stuart Taylor

Stuart has over 30 years of plant & machinery valuation experience across a range of industries.

Stuart has serviced clients across the Asia Pacific Region and his expertise comprises a broad range of valuation instructions for Australia's top 500 companies including valuations for financial reporting, tax consolidation, purchase price allocation, insurance and mortgage lending purposes.

His industry experience covers many sectors including Agriculture, Food Manufacturing & Processing, Precision Engineering, Oil & Gas, Hotels & Leisure, Timber & Forestry, Mining, Construction, Pharmaceuticals & Infrastructure.

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Brian Parton

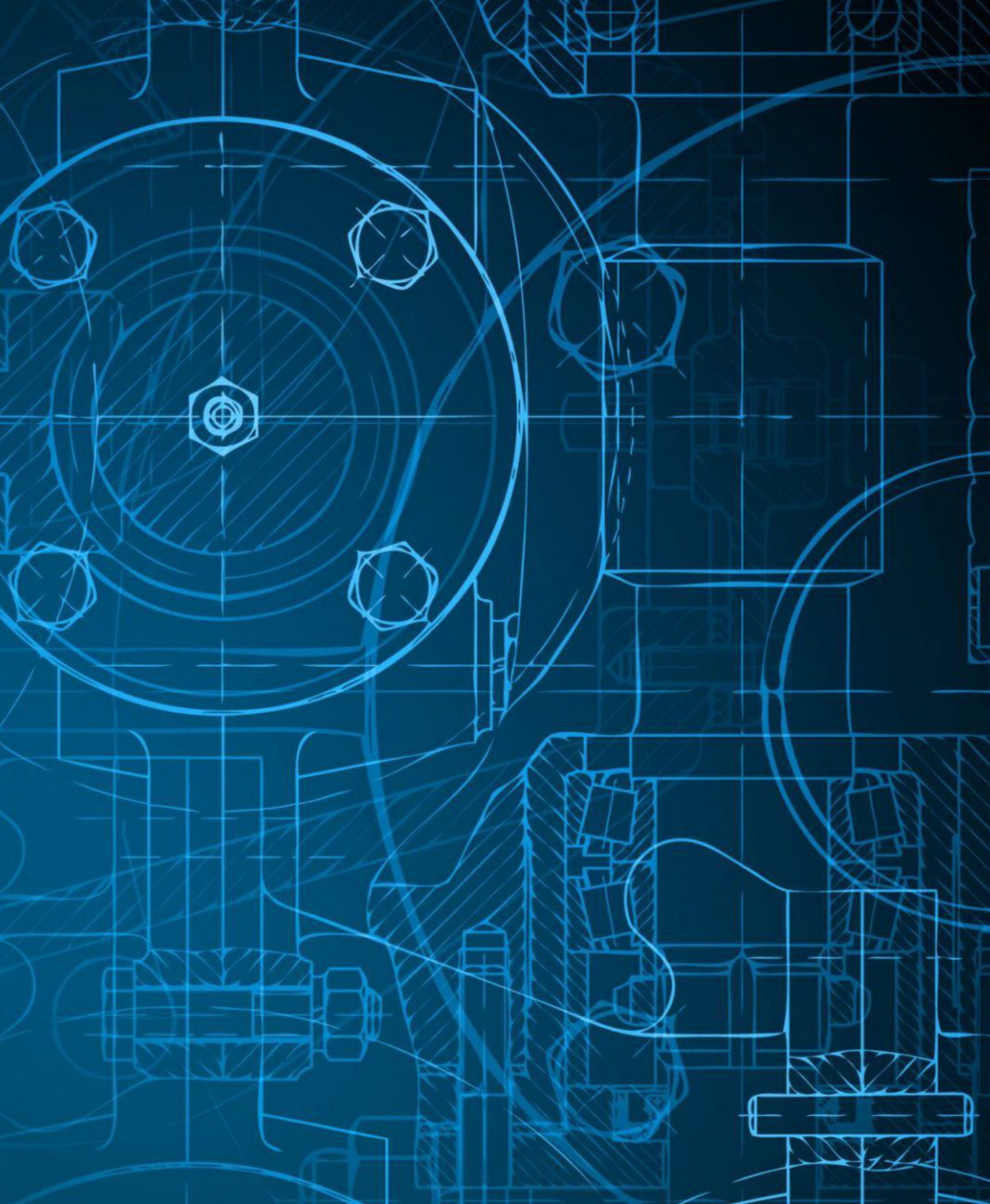
Brian has 35 years investment markets and financial services experience.

Brian co-ordinates the valuation requirements arising from mergers & acquisitions, capital raising and off-balance sheet financing for our private equity, venture capital and investment clients.

Brian's focus is developing and maturing Mitchell & Taylor's client and stakeholder relationships within the financial services sector.

He is currently undertaking a Graduate Diploma-Property (Valuations).

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