

INTERNATIONAL VALUATION STANDARDS BOARD

5 February 2010

AGENDA ITEM 6

PROJECT BRIEF FOR FORESTRY ASSETS

The Board is invited to approve the following outline project brief to form the basis of a call for volunteers to serve on an expert group.

- 1) A paper prepared by the Association of Consulting Foresters of Australia was considered by the Board at the meeting on 5 November in Madrid. This paper outlined a number of principles for the valuation of commercial forestry. In discussion the Board heard that there was possibly diversity of practice in valuation practice around the world. However, the paper did not identify whether the problems were concerned with a lack of agreement as to valuation objectives, or the detail of methods used. The point was additionally made that many of the basic principles and objectives that would apply to valuing forestry would equally apply to other agricultural assets generally.
- 2) The Board agreed that an expert group be convened to examine the issue with sufficient representatives to ensure suitably diverse geographic representation of valuation specialists, forestry companies and users.
- 3) Proposed brief for approval:
 - To review ACFA paper and consider what additional views should be canvassed or topics considered in order achieve consistency of approach.
 - To identify issues concerning either a lack of clarity as to the valuation objective, the appropriate assumptions that should be made in different situations or reporting clarity and which should be addressed in IVS.
 - To identify issues that are concerned with the merits of different valuation methods or their application to forestry and which could be addressed by developing professional guidance.
 - To consider whether the extent to which these issues are common to other agricultural or biological assets.
 - To review the current GN/Standard on Agricultural Property (GN 10 in IVS 2007).
 - To consider whether a separate standard is justified for commercial forestry or whether the issue specific to forestry can be adequately dealt with within a revised GN10.
 - To make recommendations to the Board.

BACKGROUND

Extract from PwC report *Application Review of IAS 41, Agriculture: the Fair Value of Standing Timber* (published 2009)

The application of IAS 41 and the valuation of forest assets are of increasing importance to preparers and investors throughout the world:

- Preparers and investors have expressed interest in the manner in which IAS 41 has been implemented.
- The forthcoming implementation of IFRS in various regions with major commercial forestry activities, such as the United States, Canada and Brazil, also calls for this study.
- Institutional investors are becoming increasingly attracted to forestland as an asset class, seeing such assets as offering an alternative and sustainable long-term investment strategy.
- Forestry is attracting new strategic investor interest as wood-based biomass is seen as a vital renewable energy resource.

The study attempts to shed light on the fair valuation of standing timber for financial reporting purposes, and closely related valuation issues, by reviewing the disclosures in IFRS-based financial reports for forest owners.

Five years have now passed with IAS 41 and use of the standard is now widespread globally, as use of International Financial Reporting Standards (IFRS) has spread. Nevertheless, amongst preparers there are major questions about how the standard is being applied to forest assets. Fair value implies a market based value and whilst there are markets around the world for the harvested products of forest, markets for standing timber are limited in comparison with the total volume of standing forest.

In this short study, which is the first of its kind, we have reviewed how fair value is being applied by forest owning companies using IFRS. It aims to provide insight into the key judgments that are made by preparers from around the world and highlights some of the difficulties as well as similarities and differences. What it doesn't seek to do is pass judgment on how IAS 41 is being applied, but that said, it does aim to provide pointers as to what may be considered as best practices in fair valuing forest assets and the related disclosures.

Our study has highlighted various approaches to the application of the fair value requirements of IAS 41 to standing timber, and in related disclosure practices. Several companies make extensive disclosures which supports transparency to the users of the financial statements. However, often the reasons for the fair valuation approach selected are not explicitly discussed, meaning that users may not appreciate the judgments and related uncertainties that are inherent in the valuation of forest assets.

Our overall conclusion is that there is room for further improvement with regard to the level of the transparency of critical valuation assumptions especially given that the overwhelming majority of standing timber valuations are site specific. Generally, we would welcome an enhanced discussion in the financial reports on price assumptions used in DCF calculations and sensitivity analysis as regards the most significant value driving assumptions.