International Valuation Standards Council
41 Moorgate
London EC2R 6PP
United Kingdom

30 April 2013

Dear Sirs,

Re: Discussion Paper – Valuation of Liabilities

We are responding to your invitation to comment on the above Discussion Paper ("DP") on behalf of PricewaterhouseCoopers.

Following consultation with several members of the PricewaterhouseCoopers network of firms, this response summarises their views. "PricewaterhouseCoopers" refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity. PricewaterhouseCoopers appreciates the International Valuation Professional Board's (IVPB) efforts in this process and welcomes the opportunity to provide comments on the DP.

Scope and Purpose of Discussion Paper

We understand that the aim of the proposed new International Valuation Standards is to determine appropriate valuation practices for liabilities and develop a dedicated standard and supporting technical guidance. As is stated in the note to respondents, IFRS 13 stipulates that specific assumptions are made that may or may not be appropriate when establishing the value of a liability for purposes other than financial reporting. As a result, the DP speaks of the need for guidance "in a wider context" despite the statement later in the DP that financial reporting "is the most common purpose for which liabilities are required to be valued". The DP goes on to propose different bases of value which should expand the context even wider. We believe that this "wider context" will be too general and thus we believe there is a risk that it will not achieve the objective of further promoting consistency in practice. Given that the valuation standards are intended to provide a general framework, we believe it is important that standards generally offer more guidance and specific examples to advance the debate on key matters or at least highlight the issues that are relevant in practice or tend to be the cause of diversity or debate. We question whether the current approach would yield a standard that is so general that it would not address valuation specifics that would be useful to those who would use it as a guide to value liabilities.

We believe that all liabilities, and in particular those valued in the context of financial reporting and that have significant Level 3 inputs, should be in the scope whether they are for example, financial instruments or legal proceedings. We believe such liabilities are subject to the same general valuation principles and issues. Such issues encountered include implied bid/ask spreads between assets and corresponding liabilities and the applicability of the no arbitrage argument for inherently illiquid or non-existent markets.

We have provided responses to each of the questions in the DP. Our comments note some example areas where further guidance or clarification might be helpful.

If you have any questions on the content of this letter and the attached appendices, please do not hesitate to contact John Glynn, US Valuation Leader 646 471 8420) or Romil Radia, UK Valuations partner (+44 20 7804 7899).

Yours faithfully,

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

Appendix A – Questions for Respondents

QUESTIONS

1. *Do you agree with that the IVSC should produce a standard or guidance on the valuation of liabilities as defined above? If not please explain why?*

We agree that guidance on the valuation of liabilities would be helpful as there is significant variability in practice. As most of the valuation guidance has been designed around the valuation of assets, there is uncertainty in the valuation of liabilities with respect to methodologies, discount rates, projections, markets, market participants, etc. While liabilities can sometimes be valued as having an equivalent value to its offsetting asset, there are cases where assets and liabilities would trade in different markets, have different market participants, and be viewed as having different units of account. This raises the question of whether a liability must always have the identical value as its offsetting asset or if a bid/ask spread should be considered. Because of these uncertainty and lack of current guidance, we believe that this guidance should provide details and specific illustrative examples.

2. *Do you agree that the possible definition of a liability given above is both clear and adequate? If not any alternative suggestions would be welcome.*

We do not think that a new definition of a liability is helpful. In cases where liabilities most typically need to be valued (financial reporting and tax), a definition of a liability already exists. We are concerned that a new definition of a liability would be confusing to practitioners. Providing specific guidance and implementation of a definition that is not in wide use is not likely to be helpful. We question whether the attempt to make this standard appropriate to all purposes dilutes its use for specific purposes such as financial reporting and tax.

3. *Do you agree with that liabilities arising under a financial instrument should be excluded from the scope of this project?*

A financial instrument is defined under IAS 32.11 as "Any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity." We believe that liabilities which arise under financial instruments would seem to fit under the same definition as liabilities. The common principles appropriate to the valuation of liabilities are also appropriate to liabilities which arise under financial instruments. Furthermore, excluding liabilities which arise from financial instruments would seem to exclude contingent consideration from the scope of this project. We believe that contingent consideration should be included within the scope of the valuation of liabilities. As contingent consideration is an area where there is diversity in practice, we feel that it should be included within the standard.

4. *Do you agree that other liabilities such as rental payments, pension liabilities, insurance liabilities and deferred tax should also be excluded?*

While IFRS and US GAAP may specifically exclude these liabilities from being measured at fair value (although insurance liabilities can be valued under US GAAP in a business combination if elected), we see no need to exclude these liabilities from the overall scope. If there was a need to value these liabilities, the same principles should apply to the valuation of these liabilities as would exist for other liabilities. However, we believe the primary focus should be liabilities for which a fair value needs to be determined for financial reporting purposes.

5. *Do you consider that contingent liabilities as described above should be included? Please also indicate if there are any other types of contingent liability that should be included.*

Contingent liabilities are among the most challenging liabilities to value. As a result, guidance on the valuation of such liabilities should be included in a paper on the valuation of liabilities. Contingent liabilities would include, but would not be limited to the following: contingent consideration, legal liabilities, guarantees, financial instruments, and asset retirement obligations.

6. *Please indicate whether you believe potential litigation liabilities can or should be valued and whether they should be included in this project.*

We acknowledge the difficulties in valuing potential litigation liabilities due the difficulty in obtaining certain inputs from specialists in the legal profession. We also understand that there could be a significant variance between the fair value estimate and the final resolution of the liability. Still, the valuation methods used to value litigation liabilities would be consistent with methods that would be used to value other liabilities. Implicitly, such liabilities are valued any time there is an acquisition of a company that is involved in a lawsuit. We believe that litigation liabilities can be valued and that they should be included in this project.

7. *For what purpose are you aware of liabilities being valued?*

We are aware of liabilities being valued for financial reporting, tax, and litigation purposes.

8. *What base or bases of value do you normally encounter?*

For financial reporting purposes, the basis of valuation that we generally encounter is fair value as defined by IFRS, US GAAP, or other generally accepted accounting principles. For tax purposes, value is determined as required by applicable tax regulations such as fair market value, as defined by US or other local tax regulations.

9. *Do you agree that the bases that are appropriate objectives for a valuation of liabilities fall within one of the three categories described in the IVS Framework?*

We think that having multiple bases of valuation (Market Value, Investment Value, Special Value, and Fair Value) is likely to lead to confusion as to which base of valuation is being used. Moreover, the Fair Value definition provided speaks to settling the liability with “a specific party” as opposed to the IFRS and US GAAP fair value definition which transfers the liability "between market participants". While we are not sure if there is a functional difference between these definitions of Fair Value, we believe that valuations prepared for financial reporting will need to use the definitions found in the applicable financial reporting standards. Tax valuations will need to use the definitions found in the applicable tax regulations.

10. *Do you agree that it may be necessary to modify some of valuation bases definitions in the Appendix in order for them to be applied to liabilities as opposed to assets? If so it would be helpful to indicate any changes you believe appropriate.*

A liability which is valued for financial reporting purposes must use the definition found in financial reporting standards. A liability which is valued for tax purposes must use the definition that is found in the applicable tax regulations. In our view, this limits the usefulness of other definitions.

11. *If you have experience of using the market approach to value liabilities, please indicate the nature and types of liabilities where this is used.*

Standalone transfers of liabilities are not generally observed. Many liabilities have either transfer clauses, or are transferred with assets. Examples of where this is the case include insurance liabilities and bank deposit liabilities. We are not familiar with liabilities which trade on markets. A possible exception to this is the original issuance of debt. Other trades in the debt markets are transfers of the right to receive payment (an asset).

12. *Please give an example of a type of liability where you have encountered or used a DCF method and indicate the purpose for which the valuation was required.*

We have used DCF methods when valuing debt, warranties, guarantees, insurance contracts, and contingent consideration. In each case, the purpose of the valuation was financial reporting.

13. *For the example given in question 12, please indicate the source of the projected financial information used in the cash flow forecast.*

In our experience, the projected financial information is typically provided by the holder of the liability (i.e. management).

14. *For the example given in question 12, indicate what risk factors you reflected and whether these were reflected by probability weighting the cash flows or the discount rate.*

In debt valuations, it is most common to reflect the risk factors in the discount rate as they can be observed in a public market (in the form of yield to maturity for debt instruments). In certain cases, the risk can be fully reflected in the projections so that a risk free rate can be used. In most discounted cash flow valuations for liabilities, there is a component of risk found in the projections and the discount rate.

15. Do you consider that a "risk free" rate should be used when estimating the current value of a future liability? If not please indicate how you derive the rate and the rationale to support it.

While there are option pricing and DCF approaches that use a risk free rate (which reflect all of the risk in the projections), it is more common to reflect risk in the discount rate as well as in the underlying cash flows. The determination of the discount rate may be performed in a similar manner to the discount rate determination of an asset.

16. Please indicate if you have used or encountered option pricing in estimating the value of liabilities. If so please indicate the nature of the liability and the purpose for which the valuation was required.

We have both used and encountered option pricing in the valuation of convertible debt, debt, contingent consideration and guarantees.

17. Please indicate whether you agree that in calculating the value of a liability based on the cost of fulfillment at a future date a "profit margin" (or risk premium) should be included to reflect the risks to the holder of the cost estimate proving inadequate. If so, please give an example.

It is generally appropriate to consider the inclusion of a "profit margin" for the party that fulfills the liability. It may be appropriate to consider additional compensation for assuming a liability if the range of future outcomes is not symmetrical. See for example IFRS 13 paragraphs IE35 to IE39 as well as ASC 820 paragraphs 820-10-55-66 to 820-10-55-70 which illustrate the application of a profit margin.

18. If you use or are familiar with the Cost Approach, please indicate in your experience how the cost of fulfilling, transferring or settling/cancelling an equivalent liability is determined.

We have not used the Cost Approach to value liabilities. The Cost Approach is founded on the principle of substitution which applies for functional equivalents for assets. We are not sure that the principle of functional equivalents applies to liabilities. As a practical matter, the costs of fulfilling liabilities are often found within the cash flows which are used in a discounted cash flow.

19. Do you agree with the Board's proposed approach?

We support the Board's overall objective to provide guidance on the valuation of liabilities; however our concern is that the approach is too general. Multiple definitions of value are being considered. While we understand that the goal is to have a document that is appropriate to the valuation of all liabilities for all purposes, we are concerned that such an approach would yield a standard/guidance that is so general that it would not address valuation specifics that would be useful to those who would use it as a guide to value liabilities.