31 March 2013

International Valuation Standards Council
41 Moorgate
London EC2R 6PP
United Kingdom
By email: CommentLetters@ivsc.org

Ladies and Gentlemen,

This letter of comment is submitted on behalf of the International Association of Consultants, Valuators and Analysts (IACVA), a member of your organization as well as of the World Association of Valuation Organizations (WAVO). We are a knowledge transfer and credentialing organization with Charters covering 55 countries, listed in the Appendix, serving about 10,000 members who are mainly involved in business valuation and fraud deterrence.

As a worldwide organization, we are extremely concerned with the development of guidance and standards related to valuation. Therefore, we appreciate the opportunity to comment on the Exposure Draft “Illustrative Examples Chapter 1 – Bases of Value”. Our responses to the indicated questions are set out below.

In particular, our members, who adhere to the IVS, must use a large number of different definitions of value even though the term may be the same or similar in various jurisdictions. For example, the phrase “fair market value”, which is used in both US and Canadian tax legislation, has a separate meaning in each country even though the economies are closely integrated.

Consequently, we believe the proposed illustrative examples would be of much greater usefulness to practitioners if they were expanded to cover not only international standards but also the often overlooked but extensively used local standards.

1. Do you consider the differences among the IVS bases of value have been adequately illustrated? If not, what additional illustrations might be helpful?

We find the descriptions of the differences between the various bases of value to be insufficient as they omit the most commonly used one in the world which is Fair Market Value as adopted in the United States of America (USA); that in Canada is not the same.
The International Glossary of Business Valuation Terms defines Fair Market Value as:

“the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts. NOTE: In Canada, the term “price” should be replaced with the term ‘highest price’.”

With respect to Fair Value in the USA, there are a number of uses. Accounting Fair Value, given by Accounting Standards Codification (ASC) 820, is the same as that in IFRS 13.

“the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.”

This is an exit price, whose definition emphasises that it a market-based measurement rather than an entity-specific measurement. In measuring fair value, an entity must use the assumptions that market participants would adopt to price the asset or liability under current market conditions, including those about risk. As a result, any intention to hold an asset or to settle or otherwise fulfil a liability is not relevant when measuring fair value.

Legal Fair Value according to the American Institute of Certified Public Accountants (AICPA) “Statement on Standards for Valuation Services No.1” is a concept used in state laws referring to shareholder and partnership matters; the term is also referred to in divorce laws. Defined differently in various states and countries (Canada) it generally refers to an equitable, just and reasonable value for property, determined without reference to a simulated or real market transaction since the owner usually has no interest in entering the market at all.

Finally there is the IVS definition of Fair Value:

“The estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties.”

In our view all of those definitions, as well as Market Value, Synergistic Value and Investment Value need to be illustrated.

2. Do you perceive any issues or unintended consequences arising from any of the illustrations? If you do, please explain what these are.

Our detailed comments to the illustrations are set out below by Paragraph indicating those that need amendment or strengthening.
Paragraph 4

In our view, for the IVS to be inclusive and international in their Framework as well as the illustrative examples, both must include the definitions used in all the major economies – USA, Europe, China, Japan and India. The exposure draft appears very Eurocentric in paragraph 4; we realize that it is impossible for the IVSC to identify, much less include, all bases that may be required in the 60 plus countries that, in some form, adopt the IVS but to include USA and China as well as Europe would be easy.

Paragraph 6

The illustrations only deal with the value of a single asset or entity and not the various ownership interests involved. There is need for discussion of discounts (Lack of Marketability- DLOM and Absence of Control - DOAC) as well as premiums for factors other than the much-discussed results of synergies.

Paragraph 8

The information on the three bases of value set out in the IVS Framework should be included with the examples which are demonstrating them. Otherwise, the illustrative examples are hanging in the air and may be misleading. In particular, the IVS Market Value is not the same as USA Fair Market Value as the IVS assumes highest and best use, as does IFRS Fair Value, while Fair Market Value is “as is, where is”.

Paragraph 9

The definitions of Fair Value in ASC 820 and IFRS 13 are identical. We believe that this definition of the term should be adopted by the IVS Framework as it is in common usage nearly everywhere. The IVS usage of Fair Value should be replaced with another phrase such as Sale Price because it is not necessarily an estimate but may be the result of an actual transaction.

Paragraph 11

This paragraph, in Figure 1, mentions a Specific Buyer while paragraph 20 discusses “Special Purchasers”. In our view, there may be more than one of the latter. The term usually refers to a class, such as significant suppliers or major customers, rather than to an individual entity. For example, a steel fabricator has two large users with 50% and 40% of sales; each would be a Special Purchaser but each has a different criteria as a Specific Buyer.

Paragraph 13

The layout of Figure 3 is misleading as it suggests that the Investment Value to the buyer is much greater than that value to the seller. This depends on the relative rates of return they require. For example, the several owner-managers of a fifth generation family business may be willing to accept a rate of return of a small amount above what a bank would pay as there are jobs involved. A buyer would need to replace those individuals
and, based on the principle of substitution, obtain a market return “even if the net cash flows are improved by significant synergies”.

Paragraph 28

There are considerable differences between Fair Market Value (which we consider to be more frequently used than the rather similar Market Value) and IFRS Fair Value. The latter is always an exit price but Fair Market Value and Market Value can also be entrance prices; they both refer to willing sellers while IFRS Fair Value only deals with buyers (Market Participant).

Paragraph 30

The input hierarchy of IFRS Fair Value is extremely important with its strong preference for market based (observable data). Level 2 results using the Market Approach may give significantly different conclusions for many assets than comparable Level 3 results using the Income Approach and expectations of market participants, especially for derivative instruments.

This hierarchy is an integral part of IFRS Fair Value. In our view, with its emphasis on market transactions, it readily gives different results from those that valuers would estimate for Fair Market Values or Market Values, as they would tend to put more emphasis on actual results and managements’ forecasts rather than market participants’ expectations.

Paragraph 31

A full discussion of Value in Use and its differences from IFRS Fair Value and Fair Market or Market Value is essential. The differences are often substantial especially for specialized assets such as a fish hatchery which generate substantial benefits to its owner but are not necessarily saleable. In our view, Value in Use is much closer to Investment Value to Owner than it is to either Fair Market Value or Market Value.

Paragraph 32, Example 1

This example needs quantification and probably should be divided into two, separating the sale of the hotel from the beach transactions. The value of the hotel might be very different, as a family owned unit or if purchased by investors and managed by an international chain (most of those are operators rather than proprietors). The beach transaction might have considerable synergies for joint ownership; this should be another example, again with numbers.

Example 2

The numbers are just not plausible. They are out by at least a factor of 1,000.
There are at least six types of value to be considered:

IRS Fair Market Value – US and many other countries taxes
IVS Market Value – mainly Europe
IFRS Fair Value – US and IFRS countries, 85% of the world
IVS Fair Value – mainly Europe
Value in Use – IFRS countries 35% of the world
Investment Value to Owner – everywhere
Synergistic Value – applies everywhere, in addition, needs to be explained.
Examples are needed for each of them

This is misleading as nearly every synergy has some front end costs; for those listed, they are:

<table>
<thead>
<tr>
<th>Saving</th>
<th>Front end cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>G&amp;A</td>
<td>Implement &amp; lease termination</td>
</tr>
<tr>
<td>Transportation</td>
<td>Material handling equipment</td>
</tr>
<tr>
<td>Channel leverage</td>
<td>Marketing expenditures</td>
</tr>
<tr>
<td>New products line</td>
<td>Launch costs</td>
</tr>
<tr>
<td>Waste reduction</td>
<td>Capex</td>
</tr>
</tbody>
</table>

This needs formatted as set out below:

<table>
<thead>
<tr>
<th>Savings Opportunity</th>
<th>Target</th>
<th>Enabler</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Market Participant</td>
<td>Special Purchaser</td>
</tr>
<tr>
<td>G&amp;A</td>
<td>+</td>
<td>++</td>
</tr>
<tr>
<td>Transportation</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Channel Leverage</td>
<td>0</td>
<td>+</td>
</tr>
<tr>
<td>New Product Line</td>
<td>+</td>
<td>0</td>
</tr>
<tr>
<td>Waste Reduction</td>
<td>+</td>
<td>0</td>
</tr>
</tbody>
</table>

Market Participant – any financial or trade buyer interested in industry
Special Purchaser – competitors, suppliers, customers
Specific Buyers – particular entity

Both Market Value and Fair Market Value, as well as IFRS Fair Value, include the Synergistic Value that could be added by a Market Participant. This needs explanation as it is not implicit in the definition of Market Value:
“the estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm’s length transaction after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.”

Example 4

In a comparison of Market Value with IVS Fair Value, a reference to IFRS Fair Value is misleading.

3. Do you consider that there are any other differences between Market Value and IFRS 13 Fair Value that should be discussed and illustrated?

There are many differences between Market Value and IFRS Fair Value that are not suitably addressed, see our comment on various paragraphs.

4. Does the term “arm’s length” in the Market Value definition need explanation?

The term “arm’s length” indeed needs explanation as the concept is not common outside common law jurisdictions.

Wikipedia defines the arm’s length principle (ALP) as the condition or the fact that the parties to a transaction are independent and, on an equal footing; a deal known as an "arm’s-length transaction". The term is used specifically in contract law to arrange an equitable agreement that will stand up to legal scrutiny, even though the parties may have shared interests (employer-employee) or are too closely related to be seen as completely independent (familial ties).

The Organisation for Economic Co-operation and Development (OECD) has adopted the ALP in Article 9 of the OECD Model Tax Convention, to ensure that transfer prices between companies of multinational enterprises are established on a market value basis. In this context, the principle means that prices should be the same as they would have been had the parties to the transaction not been related. This is often seen as being aimed at preventing profits being systematically deviated to lower tax nations, although most countries are also concerned about prices that fail to meet the arm’s length test due to inattention rather than by design, and that shift profits to any other regimes (whether it has low or high tax rates). The convention provides the legal framework for governments to have their fair share of taxes and for enterprises to avoid double taxation on their profits.

5. Do you find the graphics in the document helpful in understanding the relationships between the bases of value and other pertinent concepts?

The graphics are helpful and more could be added especially with respect to the effect of discounts and premiums on levels of value.
6. Below are examples of other topics within the scope of the Illustrative Examples project which the Board is planning to cover in future chapters:

- Market Participants
- Market
- Proper Marketing
- Forced Sales
- Assumptions and Special Assumptions
- Aggregation and Unit of Account
- Highest and Best Use
- Transaction Costs
- Valuation Date

Please indicate the perceived priorities from this list and if there are any additional concepts or issues within the IVS Framework that you believe it would be helpful to address.

Many of the other topics proposed to be covered should be integrated into this document. In particular, Market Participants, Markets, Proper Marketing, Forced Sales and Highest & Best Use are integral parts of the determination of appropriate guidance relating to the definitions of Fair Market Value, Market Value, IFRS Fair Value, IVS Fair Value and Value in Use.

Our priorities for the other items are:

- Aggregation and Unit of Account
- Assumptions and Special Assumptions
- Transaction Costs
- Valuation Date

In addition, we recommend that the IVSC framework be revised to include IFRS Fair Value and Value in Use, as well as renaming IVS Fair Value.

Should a Board or staff member wish to discuss this matter further, they may contact me during normal business hours (Eastern Time) at 416-865-9766.

Respectfully submitted on behalf of IACVA
Per

James P. Catty, MA, CA•CBV, CPA/ABV, ICVS, CFA, CGMA, CFE
Chair
Appendix

IACVA List of Countries

**Americas**
Bahamas
Canada
Grenadine Islands
Guatemala
United States
Mexico
Puerto Rico
Argentina
Brazil

**Africa**
Ghana
Kenya
Nigeria
South Africa
Uganda

**Europe**
Austria
Germany
Netherlands
Switzerland
Romania
Ireland
United Kingdom

**Asia/Pacifica**
China
Taiwan
Japan
South Korea
Hong Kong
Singapore

**Middle East**
Lebanon
Egypt
Syria
Jordan
Kuwait
United Arab Emirates
Saudi Arabia
Israel
Bahrain

**Commonwealth of Independent States**
Armenia
Azerbaijan
The Republic of Belarus
Kazakhstan
Kyrgyzstan
Moldova
Russia
Tajikistan
Turkmenistan
Ukrain
Uzbekistan
Georgia
Estonia
Latvia
Lithuania