International Valuation Professional Board
41 Moorgate
London
EC2R 6PP

4 May 2011

Dear Sirs


We are responding to your invitation to comment on the above Exposure Draft 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 Exposure Draft.

Scope and Purpose of Technical Information Paper

We understand that the aim of the proposed new International Valuation Standards is to provide a framework around the subject of valuation and, as stated in the note to respondents, Technical Information Papers are designed to promote consistency of practice and support the application of principles in the IVS. We believe that this Technical Information Paper ("TIP") in its current form is too general and thus we believe there is a substantial risk that it will not achieve the objective of promoting consistency in practice. Given that the valuation standards are intended to provide a general framework, we believe it is important that TIPs offer more guidance to advance the debate on key matters.

We are unsure as to why the application of the paper is restricted and the scope limited to valuations of real property and businesses. If the intention is to keep the paper general then we believe it would be better to reflect general principles and also not to restrict the paper to only certain types of assets (real property and businesses). An alternative which we believe would be more helpful and more likely to promote consistency would be for the paper to address other types of assets (e.g. intangible assets) and address or provide additional guidance for other issues. Some examples of these areas include:

- Other bases of valuation;
- Methods of forecasting cash flows;
The different types of risk and how they can be reflected appropriately in a DCF analysis; when making these sometimes subjective adjustments, guidance on when it is more appropriate to reflect them in the cash flows (i.e. adjustment of the cash flows), or in the discount rate (e.g. application of an 'alpha' factor);

- Approaches to discounting such as when it is appropriate to use a single discount rate and when if the risk profile of the cash flows changes it might be appropriate to use multiple discount rates;

- Terminal value methodologies selection and implementation; and

- Treatment of cash, operating cash vs. excess cash and inclusion of operating cash in working capital

We have outlined in Appendix A to this letter our responses to the Board’s specific questions and some additional comments on the paper in Appendix B. Our comments note some example areas where further guidance or clarification might be helpful.

We believe that the IVSC needs to provide greater clarity regarding its intentions with respect to its vision for valuation standards and how it intends to address the gap between general guidance and how that guidance is applied by practitioners. We would welcome the opportunity to participate in that debate.

If you have any questions on the content of this letter and the attached appendices, please do not hesitate to contact Andreas Mackenstedt, PwC Global Valuations Leader (+49 69 9585 5704), Peter Clokey, UK Valuations partner (+44 20 7804 5557) or John Glynn, US Valuations partner (+1 646 471 8420).

Yours faithfully,

PricewaterhouseCoopers LLP
Appendix A – Questions for Respondents

GENERAL QUESTIONS

1. This Exposure Draft states that the DCF method should not be judged on the basis of whether or not the explicit cash flow assumptions are ultimately realized but rather on the degree of market support for the assumptions at the time they were made.

   Do you agree that the DCF method, if properly applied, can be used as a method to arrive at market value?

We agree that if a DCF is based on market assumptions, the DCF method can be utilised to arrive at market value.

2. The IVPB has concluded that although there may be distinct terms and types of analyses that apply respectively to real property valuations and business valuations, the underlying DCF method is identical in each case.

   Do you agree that the underlying DCF method described in this paper applies equally to the valuation of real property and businesses? If not, please explain the differences that you believe exist?

The paper provides general information about using the DCF method to value a business and to value real property. We do not take exception to the general statements outlined within the paper. We would note though that a business value reflects the interrelationships between several assets and liabilities and thus is conceptually different from a single asset valuation (e.g. real property).

Given the general nature of the information currently included within the paper, we believe the Board needs to consider whether the paper should remain general and simply provide an overview of the DCF method, or the paper should seek to address the other types of assets and groups of assets for which the DCF method would also equally apply.

Depending on the valuation purpose there might be further differences that warrant discussion in the TIP, e.g. that a business value may be prepared as an ‘equity’ or ‘entity’ value whereas a real property valuation is typically prepared as an ‘entity’ value.

3. This Exposure Draft states that the discount rate should be determined based on the risk associated with the cash flows (para 10), whether the DCF model is being used to determine a market value or investment value.

   Do you agree, or do you consider that other matters should be taken into account in determining the appropriate discount rate?

We agree that the basis for the discount rate should be consistent with the derivation of an appropriate set of cash flows (i.e. equivalence principle). Along with considering risk factors, the same principle would also apply to other factors such as currency etc.

4. A number of different methods are identified which can be applied to the calculation of the terminal value at the end of the cash flow period (growth, fading growth, net asset value, salvage value, etc). For long-life real property assets or going concern businesses the Board believes a constant growth model is the most commonly used method, coupled with a cross check for the reasonableness of the figure, e.g by reference to the implied exit multiple.

   Do you agree that the most commonly adopted terminal value calculation at the end of the explicit forecast period is the ‘constant growth’ model, cross-checked for sensibility to an implied capitalisation rate or exit multiple? If not please identify what other method you most commonly use?
We agree that the constant growth model is the most commonly used in practice, but based on the specific circumstances an alternative method may be more appropriate. Additionally, we agree that cross checks are typically an important procedure, particularly when deriving a market value estimate.

5. The Exposure Draft explains that cash flows can be developed on the basis of alternative financial assumptions, eg inclusive or exclusive of anticipated inflation, inclusive or exclusive of tax etc. Providing the discount rate used is consistent with the financial assumptions in the cash flows the valuation result should not be affected by the alternative used. **Do you agree that providing a discount rate is used that is consistent with the financial assumptions made in calculating the cash flows that the choice of using explicit or implicit financial assumptions in the cash flows should not affect the valuation result?**

We agree that using real or nominal cash flows should result in a consistent conclusion of value if the discount rate is consistently developed, all other assumptions remaining constant. However, we note that in practice forecasting real cash flows (i.e. exclusive of anticipated inflation) is complex and would recommend commentary is added to the TIP in respect of this matter.

6. This Exposure Draft is intended to identify best practice in the creation and application of discounted cash flow models. The Board has made the decision not to explain in detail the types of inputs that may be used in different situations or the investigations that may be appropriate. Neither are illustrative examples provided. The preliminary view of the Board is that detailed discussion of inputs or a limited range of examples is inappropriate because it could be misleading if it led readers to believe that these models were endorsed by IVSC or conversely, variations of these models in different situations were not appropriate. There are many industry specific sources for those who require training in the development and use of relevant DCF models. **Do you agree that more detailed discussion and examples of the valuation inputs into a discounted cash flow model are inappropriate? If not how much additional information do you think should be included in best practice guidance?**

We believe more guidance and additional information would be helpful in this Technical Information Paper in order to help promote better understanding and consistency. It is not clear to us why the Board is concerned in this regard. We believe that the role of a standard setter is to set guidance and indicate best practices and inappropriate practices where applicable. To the extent examples are provided that fulfill this objective then a clear description of the basis for the Board’s thinking should alleviate any concerns about misleading readers.

For example, areas where further guidance might be helpful are methods and alternatives for forecasting cash flows. Paragraph 8 states that “Cash flows for future periods are constructed using actual or projected income...” It might be helpful to have some differentiation between the concepts of ‘risk-adjusted’ cash flows and ‘certainty-equivalent’ cash flows.
Appendix B – Additional comments

- It is not clear why the Technical Information Paper only relates to ‘market value’ and ‘investment value’. We believe reference could usefully be made to other valuation bases as well.

Definitions (Paragraph 5)

- We acknowledge the differentiation between ‘market value’ and ‘investment value’. We would note that the definition of ‘Discount Rate’ (Paragraph 5) is defined as a market rate of return although depending on the reason for assessing investment value, a hurdle rate or opportunity cost may sometimes be considered (e.g. fair market value for tax purposes etc).

- The definition of discounted cash flow is not necessarily the most intuitive or commonly seen definition.

- We are unsure why the definition of free cash flow refers to ‘an annual basis’ and would suggest the term ‘period to period basis’. We would also suggest making reference to cash inflows and cash outflows rather than income and expenses. Finally, we would note that the definition of free cash flow makes reference to certain elements of free cash flow so, for completeness, it may be helpful to make reference to tax and financing.

DCF Method - Overview

- Paragraph 8 makes reference to constructing cash flows for future periods using ‘actual’ or ‘projected’ income and, as noted earlier, we would suggest this should be clarified as it is not often that ‘actual’ cash flows would be discounted.

- Paragraph 9 makes reference to ‘appropriate’ and ‘suitable’ assumptions. It might be helpful to clarify what the Board means by these terms and what is the difference between them.

- Paragraph 11 makes reference to a ‘risk-free’ asset such as AAA rated bond. Valuers will typically consider certain government bonds to derive a risk-free rate but corporate bonds could also be AAA rated but would not typically be used as a proxy for a risk-free rate. Additionally no reference is made to the cost of debt, although paragraph 11 is the only paragraph that talks about the discount rate.

DCF Method – General

- We would recommend using more common expressions for reflecting or not reflecting inflation, ‘nominal’ or ‘real’, rather than ‘growth explicit’ and ‘growth implicit’ as stated in paragraph 21.