INTERNATIONAL VALUATION STANDARDS COUNCIL

# IVS 104: BASES OF VALUE

## EXPOSURE DRAFT

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Comments on this Exposure Draft are invited before 7 July 2016. All replies may be put on public record unless confidentiality is requested by the respondent. Comments may be sent as email attachments to:

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## Introduction to Exposure Draft

**Why is the International Valuation Standards Board (IVSB) Issuing IVS 104 Bases of Value?**

In October 2015 the IVSC published its *Purpose and Strategy Document* which stated that the priority of the IVSC is to expand the quality and depth of International Valuations Standards (IVS), and ensure they are fit for purpose and provide much needed clarity and market efficiency. Further to discussions with the Standards Board and other stakeholders the Technical writers carried out a preliminary alphabetised gap analysis on IVS 2013 and IVS 104 *Basis of Value* as a priority chapter within IVS 2017.

The IVS Framework chapter in IVS 2013 included a significant amount of foundational information on valuation concepts and approaches. After consultation with stakeholders through direct contact and the IVSC Purpose, Strategy and Structure Document consultation process, the Standards Board (the "Board") have relocated most of the IVS Framework chapter to the IVS General Standards. The Board felt the issue of a new chapter on IVS 104 Bases of Value would assist both established and emerging markets in adopting International Valuation Standards across all valuation specialisms.

The Board acknowledges that one of the IVSC's core strategic objectives is to "Develop high quality international valuation standards which underpin consistency, transparency and confidence in valuations across the world". Consistent with that objective, the Board saw a growing market need to provide consistent international definitions such as the proposed new definitions of *Liquidation Value* and *Replacement Value*.

IVS 104 *Bases of Value* provides the overarching principles applicable to all valuations and form part of the extended General Standards Section within IVS 2017. The Board further noted that there was a significant amount of repetition throughout IVS 2013 related to bases of value and have relocated much of the information in the IVS 2013 Framework chapter into IVS 104 *Bases of Value* in order to eliminate some of the repetition and related confusion.

**What are the Main Provisions?**

IVS 104 *Bases of Value* is based on the key concept that it is a valuer's sole responsibility to choose the relevant basis (or bases) of value according to the terms and purpose of the valuation assignment. The Board further notes that compliance with IVS may in some cases require the valuer to use a basis of value not defined or mentioned in the IVS. This Exposure Draft includes the definitions of bases of value defined by the IVS and other bases of value defined by other organisations. The new structure includes:

- a section on the common elements of many bases of value such as an assumed transaction, an assumed date of the transaction, and the assumed parties to the transaction,
- IVS-defined bases of value included in IVS 2013 such as Market Value, Market Rent, Investment Value/Worth and Equitable Value (previously called Fair Value in IVS 2013),
- two new IVS-defined bases of value to meet market needs (Liquidation Value and Replacement Value/Insurance Value),
- a non-exhaustive list of other non-IVS-defined commonly used bases of value such as Fair Value (International Financial Reporting Standards) and Fair Market Value (Organisation for Economic Co-Operation and Development),

- a new section incorporating valuation concepts that should be considered in conjunction with bases of value, such as premises of value, synergies, assumptions and special assumptions, and transaction costs.

**How do the Proposed Provisions Compare with IVS 2013?**

The majority of the contents of this chapter were previously contained within the *IVS Framework* and the *IVS Asset Standards* of IVS 2013. The Board felt that the basis of value was fundamental to any valuation instruction and to the IVS and therefore merited inclusion as a separate chapter within IVS 2013. Furthermore the Board felt that collating the existing bases of value contents within IVS 2013 into one standalone chapter would provide further clarity to "valuers", end users and other stakeholders regarding the basis/bases chosen during a valuation instruction.

The definitions and commentary contained within this chapter for *Market Value*, *Market Rent, and Investment Value/Worth, Synergistic Value and Fair Value (International Financial Reporting Standards)* are identical to the text contained within IVS 2013. However the commentaries for these bases are no longer labelled as "commentary" and are now more clearly presented as mandatory.

The IVSC definition of *Fair Value* contained in IVS 2013 has had its nomenclature changed to *Equitable Value* to avoid confusion with IFRS 13 and other definitions of "Fair Value" currently used in the market place. However, as with the other definitions previously contained within IVS 2013, the definition and commentary for this is based on and approximately identical to that contained within IVS 2013.

In respect of IVS-defined bases of value, both *Liquidation Value and Replacement Value/Insurance Value* have been added to this chapter as newly defined terms as a result of stakeholder engagement on current market needs.

The chapter also includes (as a non-exhaustive list) other bases of value such as *Fair Value (International Financial Reporting Standards), Fair Market Value (Organisation for Economic Co-Operation and Development), Fair Market Value (United States Internal Revenue Service)* and *Fair Value (Legal/Statutory) in respect of the Model Business Corporation Act and Canadian Case Law.* The incorporation of these other bases of value recognises that "Compliance with IVS may also require the valuer to use a basis of value not defined or mentioned in the IVS". These definitions also place the onus on the "valuer" to "ensure they are using the relevant definition".

Finally the chapter includes a section on *Assumptions* and *Special Assumptions* with identical text to that contained in IVS 2013 and a revised section on premise of value/assumed use, which in addition to "forced sale" also incorporates "highest and best use, "current use/existing use", and "orderly Liquidation."

**Questions for Respondents**

The Board invites individuals and organisations to comment on all matters in this proposed update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

(a) Do you agree that valuers should be responsible for choosing the appropriate basis (or bases) of value according to the terms and purpose of the valuation assignment, and that the basis of value may not be one defined by the IVSC? If not, why?

(b) Prior versions of international valuation standards included Special Value as a separate and distinct basis of value. The Board generally believes that valuers seldom perform valuations using Special Value as a distinct basis of value. Rather, valuations are typically performed using another basis of value predicated on certain hypothetical assumptions ("special assumptions") or a specific purchaser (resulting in synergistic value). Do you agree with the removal of *Special Value* as a separate and distinct basis of value? If not, please describe the circumstances in which you use Special Value as a distinct basis of value?

(c) The IVSC has retitled the previously defined Fair Value as Equitable Value in order to avoid confusion with other definitions of Fair Value. Do you agree with this change, if not why not?

(d) Liquidation Value has been added as an additional basis of value. Do you agree with its inclusion within IVS 2017 and are you in accordance with the definition used? If not, why not?

(e) Replacement Value has been added as an additional basis of value. Do you agree with its inclusion within IVS 2017 and are you in accordance with the definition used? If not, why not?

(f) Are there other bases of value defined by other entities/organisations that should be mentioned in IVS 104? Which ones? Why?

# IVS 104 Bases of Value

**Compliance with this mandatory standard requires a valuer to select the appropriate basis (or bases) of value and follow all applicable requirements associated with that basis of value whether those requirements are included as part of this chapter (for IVS-defined bases of value) or not (for non IVS-defined bases of value).**

**10. Introduction**

10.1 Bases of value (sometimes called standards of value) are statements of the fundamental measurement assumptions of a valuation. They describe the fundamental assumptions on which the reported values will be based (eg, the nature of the hypothetical transaction, the relationship and motivation of the parties, the extent to which the asset is exposed to the market, and the unit of account for the valuation). It is critical for any valuation to be performed using the basis (or bases) of value that is appropriate to the terms and purpose of the valuation assignment, as a basis of value may influence or dictate a valuer's selection of methods, inputs and assumptions, and the ultimate opinion of value.

10.2 A valuer may be required to use bases of value that are defined by statute, regulation, private contract or other document. Such bases have to be interpreted and applied accordingly.

10.3 While there are many different bases of value used in valuations, most have certain common elements: an assumed transaction, an assumed date of the transaction and the assumed parties to the transaction.

10.4 Depending on the basis of value, the assumed transaction could take a number of forms:

(a) a hypothetical transaction,

(b) an actual transaction,

(c) a purchase (or entry) transaction,

(d) a sale (or exit) transaction, and/or

(e) a transaction in a particular or hypothetical market with specified characteristics.

10.5 The assumed date of a transaction will usually influence what information and data a valuer considers in a valuation. Most bases of value prohibit the consideration of information or market sentiment that would not be known or knowable on the measurement/valuation date by typical participants.

10.6 For most bases of value, although there is an assumed date of a transaction, a transaction does not necessarily have to take place.

 

10.7 Most bases of value reflect assumptions concerning the parties to a transaction and provide a certain level of description of the parties. In respect to these parties, they could include one or more actual or assumed characteristics such as:

(a) hypothetical,

(b) known or specific parties,

(c) members of an identified/described group of potential parties,

(d) whether the parties are subject to particular conditions or motivations at the assumed date (eg, duress), and/or

(e) an assumed knowledge level.

**20. Bases of Value**

20.1 In addition to the IVS-defined bases of value listed below, the IVS have also provided a non-exhaustive list of other non-IVS-defined bases of value prescribed by law or international agreement and used by valuers.

(a) IVS-defined bases of value:

(i) Market Value,

(ii) Market Rent,

(iii) Investment Value/Worth,

(iv) Equitable Value,

(v) Synergistic Value,

(vi) Liquidation Value, and

(vii) Replacement Value.

(b) Other bases of value (non-exhaustive list):

(i) Fair Value (International Financial Reporting Standards),

(ii) Fair Market Value (Organisation for Economic Co-Operation and Development),

(iii) Fair Market Value (United States Internal Revenue Service), and

(iv) Fair Value (Legal/Statutory).

a. Model Business Corporation Act, and

b. Canadian Case Law Example.

20.2 It is the valuer's sole responsibility to choose the relevant basis (or bases) of value according to the terms and purpose of the valuation assignment. Compliance with IVS may also require the valuer to use a basis of value not defined or mentioned in the IVS.

20.3 In accordance with IVS 103 *Reporting* the basis of value: "shall be appropriate for the purpose. The source of the definition of any basis of value used shall be cited or the basis explained. Some common valuation bases are defined and discussed in the IVS Framework. This requirement is not applicable to a valuation review where no opinion of value is to be provided or no comment is required on the basis of value used."

20.4 Valuers are responsible for understanding the regulation, case law, and other interpretive guidance related to the basis of value used.

20.5 The other bases of value illustrated in this standard are defined by organisations other than the IVSC and the onus is on the valuer to ensure they are using the relevant definition.

**30. IVS-Defined Basis of Value – Market Value**

30.1. Market Value is 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.

30.2. The definition of Market Value shall be applied in accordance with the following conceptual framework:

(a) "the estimated amount" refers to a price expressed in terms of money payable for the asset in an arm's length market transaction. Market Value is the most probable price reasonably obtainable in the market on the valuation date in keeping with the market value definition. It is the best price reasonably obtainable by the seller and the most advantageous price reasonably obtainable by the buyer. This estimate specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale, or any element of value available only to a specific owner or purchaser,

(b) "an asset or liability should exchange" refers to the fact that the value of an asset or liability is an estimated amount rather than a predetermined amount or actual sale price. It is the price in a transaction that meets all the elements of the Market Value definition at the valuation date,

(c) "on the valuation date" requires that the value is time-specific as of a given date. Because markets and market conditions may change, the estimated value may be incorrect or inappropriate at another time. The valuation amount will reflect the market state and circumstances as at the valuation date, not those at any other date,

 

(d) “between a willing buyer” refers to one who is motivated, but not compelled to buy. This buyer is neither over eager nor determined to buy at any price. This buyer is also one who purchases in accordance with the realities of the current market and with current market expectations, rather than in relation to an imaginary or hypothetical market that cannot be demonstrated or anticipated to exist. The assumed buyer would not pay a higher price than the market requires. The present owner is included among those who constitute “the market”,

(e) “and a willing seller” is neither an overeager nor a forced seller prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in the current market. The willing seller is motivated to sell the asset at market terms for the best price attainable in the open market after proper marketing, whatever that price may be. The factual circumstances of the actual owner are not a part of this consideration because the willing seller is a hypothetical owner,

(f) “in an arm’s length transaction” is one between parties who do not have a particular or special relationship, eg, parent and subsidiary companies or landlord and tenant, that may make the price level uncharacteristic of the market or inflated because of an element of special value. The Market Value transaction is presumed to be between unrelated parties, each acting independently,

(g) “after proper marketing” means that the asset would be exposed to the market in the most appropriate manner to effect its disposal at the best price reasonably obtainable in accordance with the market value definition. The method of sale is deemed to be that most appropriate to obtain the best price in the market to which the seller has access. The length of exposure time is not a fixed period but will vary according to the type of asset and market conditions. The only criterion is that there must have been sufficient time to allow the asset to be brought to the attention of an adequate number of market participants. The exposure period occurs prior to the valuation date,

(h) “where the parties had each acted knowledgeably, prudently” presumes that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the asset, its actual and potential uses, and the state of the market as of the valuation date. Each is further presumed to use that knowledge prudently to seek the price that is most favourable for their respective positions in the transaction. Prudence is assessed by referring to the state of the market at the valuation date, not with the benefit of hindsight at some later date. For example, it is not necessarily imprudent for a seller to sell assets in a market with falling prices at a price that is lower than previous market levels. In such cases, as is true for other exchanges in markets with changing prices, the prudent buyer or seller will act in accordance with the best market information available at the time, and

(i) “and without compulsion” establishes that each party is motivated to undertake the transaction, but neither is forced or unduly coerced to complete it.

30.3. The Market Value of an asset will reflect its highest and best use. The highest and best use is the use of an asset that maximises its potential and that is possible, legally permissible and financially feasible. The highest and best use may be for continuation of an asset's existing use or for some alternative use. This is determined by the use that a market participant would have in mind for the asset when formulating the price that it would be willing to bid.

30.4. Market Value does not reflect attributes of an asset that are of value to a specific owner or purchaser that are not available to other buyers in the market. Such advantages may relate to the physical, geographic, economic or legal characteristics of an asset. Market Value requires the disregard of any such element of value because at any given date it is only assumed that there is a willing buyer, not a particular willing buyer.

## 40. IVS-Defined Basis of Value – Market Rent

40.1. Market rent is the estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.

40.2. Market rent may be used as the basis of value when valuing either a superior interest that is subject to a lease or an interest created by a lease. In such cases, it is necessary to consider the contract rent and, where it is different, the market rent.

40.3. In some instances market rent can be seen as independent basis of value, whereas in other instances market rent is an intermediate step in determining value under other bases of value.

40.4. The commentary on market value shown above can be applied to assist in the interpretation of market rent. In particular, the estimated amount excludes a rent inflated or deflated by special terms, considerations or concessions. The "appropriate lease terms" are terms that would typically be agreed in the market for the type of property on the valuation date between market participants. A valuation of market rent should only be provided in conjunction with an indication of the principal lease terms that have been assumed.

40.5. The contract rent is the rent payable under the terms of an actual lease. It may be fixed for the duration of the lease or variable. The frequency and basis of calculating variations in the rent will be set out in the lease and must be identified and understood in order to establish the total benefits accruing to the lessor and the liability of the lessee.

**50. IVS-Defined Basis of Value – Equitable Value**

50.1 Equitable Value is 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.

50.2 Equitable Value requires the assessment of the price that is fair between two specific, identified parties considering the respective advantages or disadvantages that each will gain from the transaction. In contrast, Market Value requires any advantages that would not be available to market participants generally to be disregarded.

50.3 Equitable Value is a broader concept than market value. Although in many cases the price that is fair between two parties will equate to that obtainable in the market, there will be cases where the assessment of Equitable Value will involve taking into account matters that have to be disregarded in the assessment of market value, such as certain elements of Synergistic Value arising because of the combination of the interests.

50.4 Examples of the use of Equitable Value include:

(a) determination of a price that is equitable for a shareholding in a non-quoted business, where the holdings of two specific parties may mean that the price that is equitable between them is different from the price that might be obtainable in the market, and

(b) determination of a price that would be equitable between a lessor and a lessee for either the permanent transfer of the leased asset or the cancellation of the lease liability.

**60. IVS-Defined Basis of Value – Investment Value/Worth**

60.1 Investment Value is the value of an asset to a particular owner or prospective owner for individual investment or operational objectives.

60.2 This is an entity-specific basis of value. Although the value of an asset to the owner may be the same as the amount that could be realised from its sale to another party, this basis of value reflects the benefits received by an entity from holding the asset and, therefore, does not necessarily involve a presumed exchange. Investment Value reflects the circumstances and financial objectives of the entity for which the valuation is being produced. It is often used for measuring investment performance. Differences between the Investment Value of an asset and its Market Value may provide the motivation for buyers or sellers to enter the marketplace.

**70. IVS-Defined Basis of Value – Synergistic Value**

70.1 Synergistic Value is the result of a combination of two or more assets or interests where the combined value is more than the sum of the separate values. If the synergies are only available to one specific buyer then Synergistic Value will differ from Market Value, as the Synergistic Value will reflect particular attributes of an asset that are only of value to a specific purchaser.

70.2 If the synergies are available to multiple market participants, then the Synergistic Value may be consistent with the Market Value, as the price the asset should exchange on the valuation date between a willing buyer and a willing seller would likely reflect the value of any synergies available to multiple market participants.

**80. IVS-Defined Basis of Value – Liquidation Value**

80.1 Liquidation Value is the amount that would be realised when an asset or group of assets are sold on a piecemeal basis, that is without consideration of benefits (or detriments) associated with a going-concern business. Liquidation value can be either in an orderly transaction with a typical marketing period or in a forced transaction with a shortened marketing period (See sections 170 and 180) and a valuer must disclose whether an orderly or forced transaction is assumed.

**90. IVS-Defined Basis of Value – Replacement Value**

90.1 Replacement Value is the total cost of replacing an asset, generally in its present form and in accordance with appropriate regulations and legal requirements. Replacement Value considers allowances for professional fees and, in the case of tangible assets, considers factors related to construction of a replacement asset (which may include demolition, debris removal and other factors).

90.2 Replacement Value can often be based on the cost of a modern equivalent, for example, a replacement building with the same floor area.

**100. Other Basis of Value – Fair Value (International Financial Reporting Standards)**

100.1 IFRS 13 defines Fair Value as 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.

100.2 For financial reporting purposes, over 130 countries require or permit the use of International Accounting Standards published by the International Accounting Standards Board. In addition, the Financial Accounting Standards Board in the United States uses the same definition of Fair Value in Topic 820.

## 110. Other Basis of Value – Fair Market Value (Organisation for Economic Co-operation and Development – OECD)

110.1 The OECD defines Fair Market Value as the price a willing buyer would pay a willing seller in a transaction on the open market.

110.2 The OECD is made up of 34 member countries and has a mission to promote policies that will improve the economic and social well-being of people around the world. OECD guidance is used in many engagements for international tax purposes.

## 120. Other Basis of Value – Fair Market Value (United States Internal Revenue Service)

120.1 For United States tax purposes, Regulation §20.2031–1 states: "The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts."

120.2 This definition applies to all taxes paid in the United States including citizens, residents, individuals and corporations doing business in/with the United States.

## 130. Basis of Value – Fair Value (Legal/Statutory)

130.1 Many national, state and local agencies use Fair Value as a basis of value in a legal context. The definitions can vary significantly and may be the result of legislative action or established by courts in prior cases.

130.2 Examples of different definitions of Fair Value are:

(a) the Model Business Corporation Act (MBCA) is a model set of law prepared by the Committee on Corporate Laws of the Section of Business Law of the American Bar Association and is followed by 24 states in the United States. The definition of Fair Value from the MBCA is the value of the corporation's shares determined: (i) immediately before the effectuation of the corporate action to which the shareholder objects; (ii) using customary and current valuation concepts and techniques generally employed for similar businesses in the context of the transaction requiring appraisal; and (iii) without discounting for lack of marketability or minority status except, if appropriate, for amendments to the articles pursuant to section 13.02(a)(5), and

(b) in 1986, the Supreme Court of British Columbia in Canada issued a ruling in *Manning v Harris Steel Group Inc.* that stated: "Thus, a 'fair' value is one which is just and equitable. That terminology contains within itself the concept of adequate compensation (indemnity), consistent with the requirements of justice and equity."

**140. Premise of Value/Assumed Use**

140.1 A premise of value or assumed use describes the circumstances of how an asset or liability is used. Different bases of value may require a particular premise of value or allow the consideration of multiple premises of value. Some common premises of value are:

(a) highest and best use,

(b) current use/existing use,

(c) orderly liquidation, and

(d) forced sale.

**150. Premise of Value – Highest and Best Use**

150.1 Highest and best use is the use that would produce the highest value for an asset, liability or a group of assets and/or liabilities, regardless of the actual current use.

150.2 The highest and best use must be physically possible, financially feasible, legally allowed and result in the highest value. If different from the current use, the costs to convert an asset to its highest and best use would impact the value. For example, a piece of property used as a manufacturing facility may be worth $100 million in its current use but it would be worth $120 million if converted to mixed commercial/residential use. The highest and best use of the property would be mixed commercial/residential use only if the cost to convert the property is less than $20 million.

150.3 The highest and best use for an asset may be its current or existing use when it is being used optimally. However, highest and best use may differ from current use or even be an orderly liquidation. For example, the highest and best use for assets employed in a loss-making business may be an orderly liquidation of the assets.

150.4 The highest and best use of an asset valued on a standalone basis may be different from its highest and best use as part of a group, when its contribution to the overall value of the group must be considered.

150.5 The determination of the highest and best use involves consideration of the following:

(a) to establish whether a use is possible, regard will be had to what would be considered reasonable by market participants,

(b) to reflect the requirement to be legally permissible, any legal restrictions on the use of the asset, eg, zoning designations, need to be taken into account as well as the likelihood that these restrictions will change, and

(c) the requirement that the use be financially feasible takes into account whether an alternative use that is physically possible and legally permissible will generate sufficient return to a typical market participant, after taking into account the costs of conversion to that use, over and above the return on the existing use.

150.6 It is generally assumed that knowledgeable buyers and sellers would be aware of the highest and best use and transact at prices reflecting that use. As such, bases of value that assume a market transaction between reasonably knowledgeable market participants generally require the consideration of highest and best use. These bases of value include Market Value (as discussed in paras 30.1 to 30.4) and Fair Value (as discussed in paras 100.1 and 100.2).

**160. Premise of Value – Current Use/Existing Use**

160.1 Current use/existing use is the current way an asset, liability, or group of assets and/or liabilities is used. The current use may be, but is not necessarily, also the highest and best use.

**170. Premise of Value – Orderly Liquidation**

170.1 An orderly liquidation describes the value of a group of assets that could be realised in a liquidation sale, given a reasonable period of time to find a purchaser (or purchasers), with the seller being compelled to sell on an as-is, where-is basis.

170.2 The reasonable period of time to find a purchaser (or purchasers) may vary by asset type. For example, the reasonable period of time to liquidate a portfolio of securities and financial instruments may differ from the reasonable period of time to liquidate a portfolio of real estate.

**180. Premise of Value – Forced Sale**

180.1 The term “forced sale” is often used in circumstances where a seller is under compulsion to sell and that, as consequence, a proper marketing period is not possible. The price that could be obtained in these circumstances will depend upon the nature of the pressure on the seller and the reasons why proper marketing cannot be undertaken. It may also reflect the consequences for the seller of failing to sell within the period available. Unless the nature of and the reason for the constraints on the seller are known, the price obtainable in a forced sale cannot be realistically estimated. The price that a seller will accept in a forced sale will reflect its particular circumstances rather than those of the hypothetical willing seller in the Market Value definition. The price obtainable in a forced sale has only a coincidental relationship to Market Value or any of the other bases defined in this standard. A “forced sale” is a description of the situation under which the exchange takes place, not a distinct basis of value.

180.2 If an indication of the price obtainable under forced sale circumstances is required, it will be necessary to clearly identify the reasons for the constraint on the seller including the consequences of failing to sell in the specified period by setting out appropriate assumptions. If these circumstances do not exist at the valuation date, these must be clearly identified as special assumptions.

180.3 A forced sale typically reflects the most probable price that a specified property is likely to bring under all of the following conditions:

(a) consummation of a sale within a short time period,

(b) the asset is subjected to market conditions prevailing as of the date of valuation or assumed timescale within which the transaction is to be completed,

(c) both the buyer and the seller are acting prudently and knowledgeably,

(d) the seller is under extreme compulsion to sell,

(e) the buyer is typically motivated,

(f) both parties are acting in what they consider their best interests,

(g) a normal marketing effort is not possible due to the brief exposure time,

(h) payment will be made in cash,

(i) the price represents the normal consideration for the property sold, unaffected by special or creative financing concessions granted by anyone associated with the sale.

180.4 Sales in an inactive or falling market are not automatically “forced sales” simply because a seller might hope for a better price if conditions improved. Unless the seller is compelled to sell by a deadline that prevents proper marketing, the seller will be a willing seller within the definition of market value (see paras 30.1 to 30.4).

180.5 While confirmed “forced sale” transactions would generally be excluded from consideration in a valuation, it can be difficult to verify that an arm’s length transaction in a market was a forced sale.

**190. Entity Specific Factors**

190.1 For most bases of value, the factors that are specific to a particular buyer or seller and not available to market participants generally are excluded from the inputs used in a market-based valuation. Examples of entity specific factors that may not be available to market participants include the following:

(a) additional value or reduction in value derived from the creation of a portfolio of similar assets,

(b) unique synergies between the asset and other assets owned by the entity,

(c) legal rights or restrictions applicable only to the entity,

(d) tax benefits or tax burdens unique to the entity, and

(e) an ability to exploit an asset that is unique to that entity.

 

190.2 Whether such factors are specific to the entity or would be available to others in the market generally is determined on a case-by-case basis. For example, an asset may not normally be transacted as a standalone item but as part of a group. Any synergies with related assets would transfer to market participants along with the transfer of the group and therefore are not entity specific.

190.3 If the objective of the basis of value used in a valuation is to determine the value to a specific owner (such as Investment Value/Worth discussed in paras 60.1 and 60.2), entity specific factors are reflected in the valuation of the asset. Situations in which the value to a specific owner may be required include the following examples:

(a) supporting investment decisions, and

(b) reviewing the performance of an asset.

**200.Synergies**

200.1 Synergies refer to the financial benefits associated with combining assets and liabilities. When synergies are present, the value of a group of assets and liabilities is greater than the sum of the values of the individual assets and liabilities. Synergies typically relate to a reduction in costs or an increase in revenue.

200.2 Cost synergies are generated by reducing expenses associated with the combined assets and liabilities, and are often the result of reduced overhead or improved purchasing power.

200.3 Revenue synergies can relate to the ability to sell more products and services, or the ability to charge higher prices for those products and services.

200.4 Whether synergies should be considered in a valuation depends on the basis of value. For most bases of value, only those synergies available to other market participants will be considered (see discussion of Entity Specific Factors in paras 190.1 to 190.3).

200.5 Generally an assessment of whether synergies are available to other market participants is based on the amount of the synergies rather than a specific way to achieve that synergy. For example, if multiple market participants could improve cash flow from a subject asset by 10%, that increase in cash flows would typically be considered a market participant synergy even if the various market participants would achieve that 10% increase in cash flows in different ways (ie, increasing revenue vs lowering expenses).

**210. Assumptions and Special Assumptions**

210.1 In addition to stating the basis of value, it is often necessary to make an assumption or multiple assumptions to clarify either the state of the asset in the hypothetical exchange or the circumstances under which the asset is assumed to be exchanged. Such assumptions can have a significant impact on value.

210.2 These types of assumptions generally fall into one of two categories:

(a) assumed facts that are consistent with, or could be consistent with, those existing at the date of valuation, and

(b) assumed facts that differ from those existing at the date of valuation.

210.3 Assumptions related to facts that are consistent with, or could be consistent with, those existing at the date of valuation may be the result of a limitation on the extent of the investigations or enquiries undertaken by the valuer. Examples of such assumptions include, without limitation:

(a) an assumption that a business is transferred as a complete operational entity,

(b) an assumption that assets employed in a business are transferred without the business, either individually or as a group,

(c) an assumption that an individually valued asset is transferred together with other complementary assets, and

(d) an assumption that a holding of shares is transferred either as a block or individually.

210.4 Where an assumption is made that assumes facts that differ from those existing at the date of valuation, it is referred to as a special assumption. Special assumptions are often used to illustrate the effect of possible changes on the value of an asset. They are designated as "special" so as to highlight to a valuation user that the valuation conclusion is contingent upon a change in the current circumstances or that it reflects a view that would not be taken by market participants generally on the valuation date. Examples of such assumptions include, without limitation:

(a) an assumption that a property is freehold with vacant possession,

(b) an assumption that a that a proposed building had actually been completed on the valuation date,

(c) an assumption that a specific contract was in existence on the valuation date which had not actually been completed, and

(d) an assumption that a financial instrument is valued using a yield curve that is different from that which would be used by a market participant.

210.5 Assumptions and special assumptions must be reasonable and relevant having regard to the purpose for which the valuation is required.

**220. Transaction Costs**

220.1 Most bases of value represent the estimated exchange price of an asset without regard to transactions costs. Value is not generally adjusted to reflect the seller's costs of sale, the buyer's costs of purchase, or any taxes payable by either party as a direct result of the transaction.

 

220.2 However, a valuer may need to consider transaction costs when determining highest and best use, the market for a transaction, and the likely market participants.

 

## IVS 104 Bases of Value: Basis for Conclusions

*The basis for conclusions do not form part of IVS 2017 and will not be included in the finalised document, but have been drafted to provide the reader with the rationale behind certain changes made within this Exposure Draft. The Board feels that the inclusion of this section is a necessary part of the consultative process and is in line with the recommendation contained within the IVSC Purpose and Strategy Document requirement that "standards need sufficient consultation" and that the IVSC should be "operating in an open and transparent way".*

In October 2015 IVSC published their *Purpose and Strategy Document* which stated that the priority of the IVSC is to expand the quality and depth of IVS and ensure they are fit for purpose and provide much needed clarity and market efficiency. Further to discussions with the Board and other stakeholders, the technical writers carried out a preliminary alphabetised gap analysis on IVS 2013 and IVS 104 *Basis of Value* as a priority chapter within IVS 2017.

The IVS Framework chapter in IVS 2013 included a significant amount of foundational information on valuation concepts and approaches. After consultation with stakeholders through direct contact and the IVSC, Purpose, Strategy and Structure Document consultation process, the Board have relocated most of the IVS Framework chapter to the IVS General Standards. The Board felt the issue of a new chapter on IVS 104 *Bases of Value* would assist both established and emerging markets in adopting IVS across all valuation specialisms.

IVS 104 *Bases of Value* provides the overarching principles applicable to all valuations and form part of the extended General Standards Section within IVS 2017. The Board further noted that there was a significant amount of repetition throughout IVS 2013 related to bases of value and have relocated much of the information in the IVS 2013 Framework chapter into IVS 104 *Bases of Value* in order to eliminate some of the repetition and related confusion.

Since the issuance of IVS 2013, the Board received feedback from many stakeholders that the sections on bases of value did not meet current market needs. More specifically, many stakeholders pointed out that valuers are often required to use bases of value that differ from those currently defined by IVS 2013. The Board felt the IVS content on bases of value needed to be structured in a way that allowed valuers performing valuations for a variety of purposes to stay in compliance with IVS, even if the basis of value required for that purpose (such as Fair Market Value) differed from the IVS defined terms.

As a result of the stakeholder feedback and the Board's views on basis of value, the sections on bases of value that were included in the IVS Framework chapter of IVS 2013 have been significantly revised and restructured in this chapter. IVS 104 *Bases of Value* includes the definitions of bases of value, defined by the IVS and other bases of value defined by other organisations. The new structure includes:

- a section on the common elements of many bases of value such as an assumed transaction, an assumed date of the transaction and the assumed parties to the transaction,

- IVS-defined bases of value also included in IVS 2013 such as Market Value, Market Rent, Investment Value/Worth and Equitable Value (previously called Fair Value in IVS 2013),

- two new IVS-defined bases of value to meet market needs (Liquidation Value and Replacement Value)

- a non-exhaustive list of other non IVS defined commonly used bases of value such as Fair Value (International Financial Reporting Standards) and Fair Market Value (Organisation for Economic Co-Operation and Development), and

- a new section incorporating valuation concepts that should be considered in conjunction with bases of value, such as premises of value, synergies, assumptions and special assumptions, and transaction costs.

The Board accepted that most valuation engagements require the use of one or more bases of value and felt that it was not in the remit of the IVS to dictate the circumstances under which a particular basis of value should be used. IVS 104 *Bases of Value* is based on the key concept that it is a valuer's sole responsibility to choose the relevant basis (or bases) of value according to the terms and purpose of the valuation assignment. The Board further accepts that compliance with IVS may in some cases require the valuer to use a basis of value not defined or mentioned in the IVS. Because of this responsibility, a valuer may consider provided instructions regarding bases of value, but must still consider the appropriateness of any instructions to the terms and purpose of the valuation assignment. For example, a valuation performed for financial reporting purposes under IFRS would not be performed in accordance with IVS if it utilised a basis of value other than Fair Value as defined by the IASB, regardless of whether the valuer was instructed to use a different basis of value.

The Board accepts that some bases of value, which may have an identical or similar nomenclature such as Fair Value, can produce significantly different valuations due to variances in interpretation by local jurisdictions and regulatory authorities. In these circumstances there is often additional regulation, case law and interpretive guidance outside IVS and related to bases of value which valuers must be familiar with and follow. One example of such additional interpretive guidance is blockage factors. From a conceptual standpoint, blockage factors may be appropriate when valuing a large number of publicly traded shares (or another publicly traded asset or liability) if the sale of those shares could significantly impact the publicly traded price. However, for financial reporting purposes under IASB and FASB rules, blockage factors are prohibited for assets and liabilities traded in an active market.

The Board has not attempted to summarise such additional guidance, which varies significantly depending on the valuation purpose and jurisdiction in which the valuation is performed and used. The Board does not consider additional guidance on these matters to be part of their remit, though would encourage valuation professional organisations to provide additional guidance on these matters to improve market efficiency when needed. As such, this chapter notes that valuers using any basis of value are responsible for understanding the additional appropriate regulation, case law and other interpretive guidance related to that basis of value.

Since valuers often need to perform valuations using bases of value defined by other organisations, the Board decided that this chapter should include certain commonly used bases of value. However, the Board does not intend to continuously monitor those other organisations to ensure any changes to their definitions are reflected in IVS. As such, a statement was added in this chapter that valuers are responsible for ensuring they are using the correct and up-to-date definition.

In respect of IVS-defined terms the Board said that even though Market Rent is often part of the calculation of Market Value it can also be reported as a separate basis of value and therefore was included in this chapter as a separate basis of value. Market Rent represents a basis of value similar to Market Value so the commentary on Market Rent was moved from chapter IVS 230 *Real Property Interests* to this chapter.

The Board had also received considerable feedback on the existence of two varying definitions of Fair Value within IVS 2013, one of which potentially included additional value from a special purchaser. The Board sought further feedback on these terms from the IVSC Advisory Forum working group and other stakeholders, and it was felt that in order avoid confusion with the commonly used IFRS 13 definition of Fair Value and many other definitions of Fair Value for financial reporting and legal valuations, the nomenclature for the IVS basis of value Fair Value should be changed to Equitable Value. The Board also considered simply removing the IVS-defined Fair Value. However, stakeholder outreach indicated that some constituents do use the IVS definition. Those stakeholders objected to removing the definition of Fair Value altogether, but felt that renaming the term was reasonable.

Further to the stakeholder feedback the IVSC have identified Liquidation Value and Replacement Value as two additional IVS-defined bases of value to be incorporated within IVS 2017 to meet market needs.

The Board felt that as one of the IVSC's core strategic objectives is to "Develop high quality international valuation standards which underpin consistency, transparency and confidence in valuations across the world" there is a growing market need to provide a consistent international definitions such as the new definitions of Liquidation Value and Replacement Value.

This definition of Liquidation Value notes that it can be calculated under either orderly or forced circumstances. The Board considered that "Market Value under the special assumption of a limited marketing period" is consistent with the new definition of Liquidation Value and that valuers may, under appropriate circumstances, continue to use that wording if they so choose.

The Board also understand that it is common market practice for most valuation instructions for secured lending purposes to also request the provision of an Estimated Replacement Cost/Insurance Value for insurance purposes.

Furthermore the Board once again noted that though this was a commonly used term there was no consistent international definition and therefore valuations conducted on this basis are often subject to national and regional variance of definition and interpretation. The Board however recognises that unlike other bases of value, which can be calculated using a range of valuation approaches an Estimated Replacement Cost/Insurance Valuation.

Further to feedback received the Board have also created a new section on Premise of Value/Assumed Use, which describes the circumstances of how an asset or liability is used. This incorporates and extends the previous section within IVS 2013 on "forced sale" and also incorporates "highest and best use, "current use/existing use", and "orderly liquidation" as further premises of value. These are premises that are commonly, but inconsistently used across markets and therefore the Board have provided high level definitions of these terms to improve understanding and increase market consistency.

The Board understands that valuers frequently make assumptions in the course of valuation engagements, but should differentiate between assumptions that may be true and assumptions that are known to be false. In this chapter, the first type are simply called assumptions, while the second type are referred to as "special assumptions".

IVS 2013 included "Special Value" as a separate and distinct basis of value. However the Board's research indicated that valuers seldom perform valuations using Special Value as the basis of value. Rather, valuations are typically performed using another basis of value using certain special assumptions ("hypothetical assumptions") or a specific purchaser with a special interest resulting in Synergistic Value. The Board has included a question for respondents to this Exposure Draft to confirm whether stakeholders believe Special Value should remain a distinct basis of value or whether it is an element that is contained within Synergistic Value.