KPMG

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

Our ref: IVSC_Comment Letter_ED
Contact: Patrick Coady, Jim Calvert

7 July 2016

Dear Sir:

Exposure Drafts: IVS 2017: Introduction & Framework, IVS 104: Basis of Value, IVS 105: Valuation Approaches and Methods and IVS 210 Intangible Assets

KPMG's Valuation Services Practice appreciates the opportunity to comment on the Exposure Drafts of IVS 2017: *Introduction & Framework*, IVS 104: *Basis of Value*, IVS 105: *Valuation Approaches and Methods* and IVS 210 *Intangible Assets* (the "ED").

We set out specific responses to the questions raised in the ED in Appendices 1-4 as well as additional commentary. In preparing our comments, we note the Board's objective that all the provisions of the IVS be mandatory with limited explanatory material. We believe that in order to meet the Board's objective to provide much needed clarity and to reduce diversity, it is important that IVSC issue more comprehensive guidance on complex valuation issues. For example, we note that very useful guidance has been issued by the Appraisal Foundation, in particular the Valuation Advisories *Identification of Contributory Assets and Calculation of Economic Rents* and *The Valuation of Customer-Related Assets.* Such guidance could include examples on how standards could be applied to particular facts and circumstances, including potential pitfalls that might be encountered in practice.

Please contact Patrick Coady at +1.613.212.2841 or Jim Calvert at +353.1.410.1001 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

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Appendix 1
Proposed IVS 2017: Introduction and Framework
Response to Specific Questions

(a) In IVS 2013, all substantive portions of the standards were labelled as "commentary" (except for scope and effective date). This label seems to have created some confusion amongst stakeholders as to whether the standards were mandatory. The Board's position is that all aspects of IVS 2017 should be mandatory and this exposure draft has removed the "commentary" label for clarity. Do you agree with the removal of the commentary label?

We believe that "substantive portions" of the IVS, i.e., sections that are intended to be mandatory should not be labelled as commentary to avoid confusion.

(b) Do you agree with the Board's decision to remove the section on Bases of Value from the IVS Framework and produce a single chapter on Bases of Value in order to clarify the mandatory nature of this section and to avoid repeating certain guidance throughout the IVS? If not, why?

We believe that the decision is appropriate to avoid repetition and confirm the mandatory nature of such guidance.

(c) Do you agree with the Board's decision to remove the section on Valuation Approaches from the IVS Framework and produce a single chapter on valuation approaches and methodologies in order to clarify the mandatory nature of this section and to avoid repeating certain guidance throughout the IVS? If not, why?

We believe that the decision is appropriate to avoid repetition and confirm the mandatory nature of such guidance.

(d) Do you agree with the IVS definition of Exceptions and Departures? If not, why?

We agree with the definition of exceptions and departures. However, while a departure from IVS may be required by legislative, regulatory or other authoritative requirement, given that a valuation that includes such a departure can be presented as being in accordance with IVS, a qualitative explanation of the nature and effect of such departures should be provided so that the user of the valuation report can take these into account in their consideration of the valuation.

Additional Commentary

We suggest that paragraph 10.2 be added to circumstances where an exception or departure, as defined has been applied thus requiring that full adopt of IVS has not occurred.

Paragraph 20.1 states that while the standards apply to assets and the guidance is also intended to apply to liabilities. We believe that IFRS 13 provides useful guidance on factors to be considered in applying fair value measurement guidance to liabilities.

Paragraph 30.1 states that the definition of a valuer is "one who possesses the necessary, *qualifications*, ability and experience to execute a valuation". The requirement as stated implies that all three conditions be met, which creates an unrealistic requirement in many countries. Moreover, depending on how this terms is used in the standards, it will not cover a number of skilled, experienced individuals who perform valuations in practice that may have the requisite skills, but lack a specific qualification.

Paragraph 30.1 states that the valuation reviewer must also be a valuer. The concept of a valuation reviewer has not been clearly established, especially given the valuation could have been prepared for a wide range of purposes and users.

Appendix 2
Proposed IVS 104: Bases of Value
Response to Specific Questions

(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?

We believe that it should be acceptable for the valuer to work with the client and other advisers to establishing the basis of value to be applied. For example, in some jurisdictions, the basis of value may have been the subject of extensive case law or regulation for which it may be appropriate for the valuer to consult with the client's or other advisers.

It is unclear why determining the basis of value should be the *sole* responsibility of the valuer especially given the alternative of the valuer working with the client or their advisers to determine the appropriate basis.

(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?***

We believe that special value is similar to investment value and that this intended basis can be covered by other bases of value. However, in our experience, the distinction between market value and special value was useful in explaining and applying the former.

We note that paragraph 30.2(f) references special value in discussing elements of the definition of market value. If special value is removed as a basis of value, this reference should be amended.

(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?

We have previously commented on this confusion and welcome this change.

(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?

We believe that the proposed addition of this basis of value and the related definition are reasonable.

(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?

We agree with the addition of this basis of value.

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

We note that a number of leading VPOs have developed an existing International Glossary of Business Valuation Terms. We would recommend that the IVS adopt these same definitions, including with respect to bases of value, in order to avoid confusion with the industry and to provide consistent guidance to readers of valuation reports.

For example, we note that the definition of Fair Market Value set out below that is referenced in the International Glossary of Business Valuation Terms provides an expansive definition of fair market value which provides a great deal of guidance. It also notes the specific difference as applicable to Canada.

Fair Market Value - 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 arm's 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"}.

Additional Commentary

Paragraph 10.1 could be interpreted as including unit of account as part of consideration of the basis of value. We believe that unit of account determines what is to be measured, after which the basis of value is applied.

In the discussion of market rent, it would be useful to describe whether customary lease incentives such as rent free periods are considered in estimating market rents.

It appears from the discussion in paragraph 70.1 that different synergistic values may exist depending on a specific purchaser. If this is intended, the language should be clarified to indicate this and the difference, if any, with investment value be clarified.

Use of "regardless" in paragraph 150.1 is inappropriate as an alternative highest and best use assumption depends on the change in use being economic. We would suggest the following change to 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 **after considering the economic costs and risks associated with any conversion from its current use**."

In the discussion of a forced sale in paragraph 180.3, it may be useful to reference the lack of time for a buyer to perform the customary due diligence (which causes them to mark down the price they are willing to pay because of the increased risk).

Appendix 3
Proposed IVS 105: Valuation Approaches and Methods
Response to Specific Questions

1) ***Do you agree that when selecting an appropriate valuation approaches and methods a valuer should consider the following?***

   (a) ***the appropriate bases of value, determined by the terms and purpose of the valuation assignment,***

   (b) ***the respective strengths and weaknesses of the possible valuation approaches and methods,***

   (c) ***the appropriateness of each method in view of the nature of the asset, and the approaches or methods used by participants in the relevant market,***

   (d) ***the availability of reliable information needed to apply the method(s), and***

   (e) ***if not, why? What considerations would you add to or remove from this list?***

   We believe that this list is appropriate.

2) ***Under each valuation approach, this exposure draft includes criteria for when the approach should be used. Do you agree with the criteria presented under each approach? If no, what changes would you make? Why?***

   We generally agree with the criteria for when the approaches are used. However, there may be circumstances where the basis of value requires an alternative technique(s), e.g., where investment value, which is also referred to as the value to the owner, is used.

   We note that IFRS prioritises the inputs into valuation techniques rather than the valuation techniques themselves whereas paragraph 20.1 appears to prioritise the market approach in certain circumstances. It would be useful to clarify if the IVSC believes that this could be expected to result in differences in the application of valuation techniques for financial reporting and IVS and, if necessary, add additional clarification as appropriate.

3) ***Are there areas of this chapter that you feel should be expanded upon in future board projects (eg, discount rates, discounts/premiums, etc)?***

   We believe that most valuation techniques are understood at the relatively high level presented in the ED. However, diversity and errors arise in how these techniques are applied in practice. As such, we believe that further guidance across many of the areas in the ED would be useful.

   As an example, paragraph 30.8 references the use of transaction premiums without clarifying that such premiums may relate to synergies between the combining entities rather than the benefits of control. A similar example in 30.18(a) is the reference to the use of option pricing models to quantify marketability discounts without discussing the issues with such an approach.

Additional Commentary

In paragraph 30.3, when evaluating the weight, if any, to be attached to listed prices, another relevant factor is the length of time the asset has been offered at that price without being sold.

Paragraph 30.4 references price/EBITDA as a multiple. In our experience, the relevant multiples is enterprise value/EBITDA.

Paragraph 30.4 refers to yields and interest rate spreads being relevant units of comparison for financial instruments. However, appropriate yields and spreads are determined by the valuer based on units of comparison, e.g., ratings, credit risk.

The issue of premiums and discounts applies under the income and cost approaches and so should be discussed in the context of all valuation techniques.

Paragraph 30.18(b) should be amended to clarify that shareholders in public companies participate in but do not control decision making.

The discussion of the income approach in section 40 includes reference to the reliability of forecasts. While we agree with this in general, we note that in certain sectors, investment decision making relies on highly uncertain forecasts, e.g., pre-approval pharmaceutical or biotechnology companies.

In the discussion of systematic risk in paragraph 40.5, it is stated that the return on a single asset would not be expected to exceed the return on the portfolio. However, the Capital Asset Pricing Model provides that a security with higher beta than the portfolio would have a higher expected return. This could arise as a result of operating or financial risk.

Paragraph 50.4 discusses preparation of cash flow forecasts as a step in the DCF. It also states that the most appropriate type of cash flow depends on the nature of the asset. However, even when an entity's equity is being valued, enterprise cash flows are used. The industry often influences whether enterprise or equity cash flows are used with the latter most common in financial services companies.

Paragraph 50.5 states that an asset's value is independent of how it is financed. We note that the capital structure does influence value, e.g., because of the tax shield associated with interest payments, even if many valuations make an assumption of the optimal capital structure. In this paragraph, change principle to principal.

Paragraph 50.5(d) states that the choice of currency may have an impact on inflation and risk. Inflation and risk are fundamental economic exposures independent of the valuation. This should be amended to refer to the inflation and risk assumptions.

Paragraph 50.7 refers to functional currency. This is a defined term in financial reporting so the ED should clarify how this is to be understood in IVS.

The discussion of expected cash flows in paragraph 50.17 states that all possible outcomes are considered. This is an impossible standard that could not be met except in the most exceptional circumstances. We suggest deleting "all".

As an example of further guidance that could be provided, the discussion of terminal values in section 60 does not clarify that different discount period would be used to discount the terminal value if the mid-year convention was applied depending on whether Gordon Growth or multiples were applied.

Appendix 4
Proposed IVS 210: Intangible Assets
Response to Specific Questions

(a) In IVS 2013, all substantive portions of IVS 210 Intangible Assets were labelled as "commentary" (except for scope and effective date). This label seems to have created some confusion amongst stakeholders as to whether the standard was mandatory. The Board's position is that all aspects of IVS 2017 should be mandatory and this Exposure Draft has removed the "commentary" label for clarity. Do you agree with the removal of the commentary label?

We agree with the removal of commentary label. AS stated elsewhere, we believe that non-binding examples should how the requirement should be and should not be applied would be useful.

(b) Do you agree with the decision to incorporate relevant portions of TIP 3 into IVS 210 and to eliminate TIP 3 as a standalone document? Are there any other elements of TIP 3 that you believe should be incorporated into IVS 210?

We believe that it is useful to apply the guidance from the TIP into IVS.

(c) In addition to the contents of IVS 105, this Exposure Draft includes criteria that should be used by an appraiser in selecting an appropriate valuation approach and method for the valuation of intangible assets. Do you agree with the criteria presented under each approach? If no, what changes would you make? Why?

We believe that the criteria applied are useful.

(d) The Board believes that the standard presented in this Exposure Draft can be applied in the valuation of intangible assets regardless of the purpose of the valuation (financial reporting, tax, transactions, litigation, etc.). Do you agree? If not, for what purpose(s) do you not believe this standard can be applied? Why?

We agree that the proposed approaches can be applied for multiple purposes.