Hong Kong Business Valuation Quality Mark

Consultation Paper

Comments due by 15 November 2019

www.ivsc.org

Hong Kong
Business Valuation Quality initiative

Draft Consultation Paper
Proposed Standards and Professionalism Framework for Business Valuation in the Hong Kong market
July 2019

(Comments due by 15 November 2019)

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About the IVSC

The International Valuation Standards Council (IVSC) is an independent, not-for-profit, standards setting organisation which works in the public interest.

The IVSC is responsible for developing the International Valuation Standards (IVS) and associated technical guidance for valuations on which investors and others rely. It does this by bringing together experts in valuation from across the world to write standards, and by putting these out for public consultation. To protect the public interest effectively, it also engages with world leaders active in the regulation of the financial markets, as well as other global standards setters, to ensure that valuation issues are properly understood and reflected.

The IVSC is overseen by an independent Board of Trustees which include high profile individuals with unique skills and experience such as the former IASB Chair, a World Bank Leader, a former Finance Minister, a senator and an ex-SEC Commissioner amongst others.

The IVSC works cooperatively with valuation professional organisations, users and preparers of valuations, governments, regulators and academic bodies to enhance the quality of valuations. For additional information about the IVSC, please refer to www.ivsc.org.

Request for Comments

Notice to recipients of this Draft Consultation Paper

The IVSC along with representatives from the organisations listed on the title page invites feedback on all matters in this Draft Consultation Paper (Paper).

To help elevate standards and professionalism, the Hong Kong Business Valuation Quality Initiative Task Force was set up to develop a framework for the Hong Kong market as described in this Paper. Specifically, the 'task force' is interested in your responses to the questions throughout the document.

The members of the task force encourage your colleagues, clients, peer and other professionals to submit their comments. Please compile and submit your responses to the 14 questions contained in this document and any other comments with regard to this Paper, preferably in a Word document, by emailing to comments@ivsc.org **by Friday, November 15, 2019**.

Executive Summary

A proposed standards and professionalism framework to support improved business valuation practice in Hong Kong has been created by leaders from the accounting, valuation, audit and business advisory sector, together with stakeholders such as regulators, professional bodies, and business chambers, following discussion at a number of roundtables and meetings. For the purposes of this Paper, business valuation is defined as valuations of businesses, business interests and the intangible assets of for-profit entities.

This Paper documents the proposed framework and asks key questions on which we welcome your feedback. Your views and input are being solicited as part of an open public consultation, in order to ensure the proposed approach is fit for purpose.

Issue Identification

Globally, the increasing volume and complexity of business valuations, particularly in the area of intangibles, has left the sector with a shortfall of qualified valuers and a gap in service standards among certain segments of the market, largely the lower end of the valuation sector. The increasing demand is led by increases in corporate transactions, including mergers and acquisitions as well as divestitures, compounded with the rise in fair-value measurements used in financial reporting. Hong Kong is a key financial centre, and it is important that there is confidence in business valuations for both listed companies as well as private companies.

There is a lack of accepted technical and professional standards in the Hong Kong market which has meant that not all valuation work is appropriate for the valuation purpose, and there is a wide spectrum in terms of the quality of output. This has been the case for 15-plus years, and previous efforts to create a professional body for business valuation in Hong Kong have failed because the interests of some of those involved were too narrow and lacked a broad public interest remit.

The business governance and social culture of Hong Kong pride themselves on expediency at a bargain price, with business services often obtained through existing relationships and with deference to hierarchical structures. This climate can discourage due diligence, thoroughness of reporting, and the critically important independence of valuers and other professionals who have a role in the life-cycle of these transactions.

Valuation clients are frequently enterprises owned by Hong Kong or People's Republic of China families, particularly start-ups; their leaders can be more speculative and overly optimistic in their entrepreneurial outlook, and sometimes lack experience of the due diligence that would ensure quality reporting, independence and robust risk-advisory services. This presents a risk to shareholders at large, and especially minority shareholders.

Mixed performance by business valuers therefore requires duplication of efforts by company directors, financial advisors, auditors and regulators to screen a questionable work product, spreading the costs and responsibilities for businesses across a variety of individuals, each struggling to take adequate responsibility for their own performance. Auditors in particular are relied on heavily to identify issues, yet they lack the proper valuation training to employ effective professional scepticism.

Among the circulars published by Hong Kong listed companies from 1 Jan 2017 to 30 Jun 2019, 135 circulars contained or quoted a business valuation report to which the listed companies

referenced their proposed corporate transactions.[1] Thus, emphasis on the importance of quality business valuations and the need for better corporate governance of Hong Kong listed companies cannot be underestimated.

Some company directors still lack proper understanding of their duties, and do not possess an informed approach to valuation, particularly in the area of intangibles, to effectively question reports. In addition, directors do not perform adequate due diligence on prospective financial information before providing such forecasts to valuers, who rely on information provided by directors and generally assume prospective information will materialise. Lack of consequences for poor performance across all responsible parties, including limited regulation and a non-litigious environment, fails to foster high performance. This can create a false sense of assurance in the minds of valuers that their performance is satisfactory even when this is not the case.

In contrast, competing countries in the region such as Singapore have established business valuation standards and a profession with regulatory backing. Other major countries in the region have also either taken or begun to take action in relation to business valuation to provide confidence for investors and they are in many cases looking to attract inward investment.

[1] Source: JLL. Please note that in cases in which the circulars quoted a business valuation report (without including the full report in the circulars) are also included in the above figure.

Key Issues in the Valuation Profession

The specific points highlighted by stakeholders in a roundtable in November 2018 include the following.

1. Just as there is a need for the audit profession, there is a need for a valuation profession.
2. Too many valuers lack sufficient business valuation training, experience, and knowledge of the businesses they are valuing.
3. Valuations are not required for certain corporate transactions but are still provided as window dressing to support flawed assumptions and deal structures.
4. Lack of professional scepticism by some company directors, financial advisors, auditors and valuers themselves leads to a lack of independence and fosters an image of the "valuer for hire".
5. Inexperienced valuers are sometimes insufficiently supervised by experienced valuers.
6. Financial reporting is a low priority for quality reporting.
7. There are no entry requirements, and no requirement for a consistent level of education, for the valuation profession, and no continuing professional development is necessary to stay in practice.
8. The lack of common technical and performance standards against which valuers, company directors, auditors and regulators can measure valuations create an uneven playing field for high-performing valuers.
9. Company directors are knowledgeable when it comes to tangible property, but often know little about business and intangible asset valuations.
10. The lack of an independent investigation process that covers all valuers and has enforcement powers where valuers provide low quality valuations.
11. All parties in the transaction are failing to take responsibility or actively seek ways to limit their liability.

Project Approach

In early 2019, collaboration among numerous groups resulted in the formation of a task force, which includes two working groups focusing on relevant aspects of this issue. This paper outlines the approaches and the conclusions developed by each working group.

The two working groups are as follows.

- **Professionalism Working Group**: this is concerned with professional, ethical, entry, and continuing professional development standards, as well as a quality assurance programme, following an independently led self-regulatory model.

- **Technical Working Group:** this focuses on using best-in-class technical standards as well as developing performance standards to be used as best practice, i.e. requirements that will govern the quality of work needed to support valuation conclusions and opinions.

These working groups are described in further detail on subsequent pages.

The task force determined that our preferred way to solve the issues raised is that a business valuer should be appropriately qualified, and that any business valuation qualification needs to contain the following key elements as a minimum:

- ethical approach
- competencies to be demonstrated
- continued professional development
- technical standards
- performance framework
- investigations and complaints mechanisms.

How does this help the Hong Kong market?
This project will first define what professionalism in business valuation looks like in Hong Kong, so that professional bodies will be able to apply this in their qualifications. The aim is that only appropriately qualified professionals should be able to perform business valuations in Hong Kong for listed and for private companies.

The SFC has previously issued a Guidance note on directors' duties in the context of valuations in corporate transactions and outlined director responsibilities in having effective Business Valuations. Directors should ensure that the professional valuer engaged: (a) is independent of and has no conflict of interest; (b) is suitably qualified and of sufficient reputation for the

particular assignment such that its opinion will withstand challenge; and (c) has the relevant expertise and adequate resources to perform its role properly.

The proper identification of appropriately qualified valuers using the same valuation standards will help promote professionalism and consistency in the valuation industry. Directors cannot leave their duties to be performed by others and are under a duty to supervise the functions they delegate. Delegation does not absolve a director's responsibility or liability. The same applies if directors engage professional valuers or other advisers to assist in a transaction: directors are nevertheless required to exercise independent judgment and bring their mind to bear on the issues having regard to the advice and opinions of professionals and other experts.

Ethics

Consistent ethical principles underpin public confidence in the professions. They codify the fundamental expectations that a professional will act with integrity and understand and operate within the boundaries of their competence, balancing the interests of their clients with the need to act in the public interest and provide objective independent valuations.

Recommendations

It is proposed that in order to become qualified in the Hong Kong market, a business valuer must agree to abide by the core principles set out below as a minimum, usually through membership of a professional body whose code of conduct requires such compliance.

These principles are extracted from the International Ethics Standards (IES), an ethical framework for the global property market, agreed by the IES Coalition. While all the IES principles should be followed by professionals, we have extracted those which we believe would have the most immediate impact on the quality and trustworthiness of business valuations.

Ethical principles

- **Accountability:** practitioners shall take full responsibility for the services they provide; shall recognise and respect client, third-party and stakeholder rights and interests; and shall give due attention to social and environmental considerations throughout.

> The principle that valuers should take responsibility for services does not prevent firms or valuers from limiting their legal liability for work by contract, neither does it replace the responsibilities and duties placed on users of the valuation by regulators or their own professional bodies (although it may help users to meet those responsibilities). It ensures that valuers take account of the interests of all stakeholders to produce high-quality valuations.

- **Confidentiality:** practitioners shall not disclose any confidential or proprietary information without prior permission, unless such disclosure is required by applicable laws or regulations.
- **Conflict of interest:** practitioners shall make any and all appropriate disclosures in a timely manner before and during the performance of a service. If, after disclosure, a conflict cannot be removed or mitigated, the practitioner shall withdraw from the matter unless the parties affected mutually agree that the practitioner should properly continue.
- **Integrity:** practitioners shall act with honesty and fairness and shall base their professional advice on relevant, valid and objective evidence.
- **Standard of service:** practitioners shall only provide services which they are competent and qualified to undertake; shall ensure that any employees or associates assisting in the provision of services have the necessary competence to do so; and shall provide reliable professional leadership for their colleagues or teams.

- **Transparency:** practitioners shall be open and accessible; shall not mislead or attempt to mislead; shall not misinform or withhold information as regards products or terms of service; and shall present relevant documentary or other material in plain and intelligible language.
- **Trust:** practitioners shall uphold their responsibility to promote the reputation of their profession and shall recognise that their practice and conduct bears on the maintenance of public trust and confidence in the professional organisations and the professions they represent.

Questions

1) Do you agree with the proposed ethical principles? If not, what would you change?

2) Are there any additional ethical principles that are necessary to ensure confidence in business valuation professionals in Hong Kong?

Competencies and Local Body of Knowledge

It is important that a business valuer demonstrates relevant competencies and is familiar with the local body of knowledge before qualifying as a professional. Competencies and body of knowledge can both be assessed by methods such as formal examinations, case studies and expert interviews, or a combination of the different approaches.

Recommendations

It is proposed that the competencies a business valuer should need to demonstrate before becoming qualified for the Hong Kong market are those detailed in the tables in Appendix A, plus the local body of knowledge (or local standards and technical guidance) in Appendix B.

The competencies are extracted from IVSC's Professional Membership Obligations, which were created by a global board to guide professional bodies on the different aspects of professionalism. These are split between common competencies, business and business interests' competencies, and intangible assets competencies, and colour-coded according to whether they represent basic, intermediate or advanced skill sets, as per the first table in the appendix.

Questions

3) Do you agree with the specified competencies as well as the local body of knowledge? If not, what would you change?

4) Are there any additional competencies and elements of a local body of knowledge (such as standards and technical guidance) not covered in Appendices A and B that would be relevant for business valuation in Hong Kong?

Continued Professional Development

Continuing professional competence relies on a professional reflecting on their own performance, remaining aware of changes to the law, professional practice and the market, and undertaking appropriate continued professional development to maintain the standard of their skills and knowledge.

Recommendations

It is proposed that, in order to qualify as a business valuer in Hong Kong, a professional must demonstrate sufficient continued professional development to maintain their competence. Continuing education activities should be relevant and appropriate to their work.

Professional bodies usually require this to be demonstrated either through an input method, for example recording at least 20 hours of relevant continuing professional development activities each year; or through an output method, for example by maintaining a record demonstrating that each year the professional has reflected on their practice in order to identify skills and knowledge gaps, and has identified and undertaken appropriate continuing professional development and then reflected on whether the activity has adequately addressed the gaps identified.

We propose that, in order to build a culture of continuing professional development in the Hong Kong business valuation profession, an input method should be used, requiring business valuers to record at least 20 hours of relevant and appropriate continuing professional development activities each year. At least 50 per cent of the activities should be directly related to the business valuation competencies, and at least 50 per cent should be verifiable (for example through an attendance certificate for a training event).

Questions

5) Do you agree that an input method of required continuing professional development is appropriate? If so, do you agree that 20 hours per year is a suitable expectation? If not, what would you prefer?

6) Do you agree with the proposal that at least 50 per cent of continuing professional development activities must relate to business valuation?

Technical Standards

Hong Kong Financial Reporting Standards (HKFRS), International Financial Reporting Standards (IFRS) and US Generally Accepted Accounting Principles (GAAP) all require assets and liabilities to be measured at market value; however, financial reporting standards do not prescribe in detail the fundamental valuation requirements, which is the role of the International Valuation Standards (IVS). IVS also require valuers to understand the objective of the valuation engagement and be familiar with the reporting framework with which the client must comply.

The IVSC regularly meets and liaises with senior representatives of both the International Accounting Standards Board (which issues IFRS) and the Financial Accounting Standards Board (which issues US GAAP) to get input and exchange views on financial reporting and valuation matters.

The IVS cover all assets, and comprise a general section applying to all valuations, and an asset-specific section including business valuation and related topics. IVS are created by bringing together experts from around the world into boards that write them, with ongoing public consultation. The IVSC is a not-for-profit body overseen by independent trustees and recognised by many of the most influential organisations in the world, including regulators, the private sector and global bodies such as the World Bank, IMF and UN.

IVSC has a specialist Business Valuation board and the standards have very recently been updated to cover new issue areas and define best practice.

IVS are the most prevalent standards around the world. No other organisation brings together international experts or is overseen by an independent board of trustees. IVSC has members from many countries Asia Pacific across the region including for example the China Appraisal Society which advocates IVS internationally and is therefore relevant to Chinese companies listed in Hong Kong.

Recommendations

It is proposed that the IVS are used to help ensure the quality and consistency of valuations for the Hong Kong market, as these standards help provide confidence for both domestic and international investors.

Questions

7) Do you agree that IVS should be used for the Hong Kong market?

8) If not, what alternative standards should be used, and what would the benefits be?

9) Is there any additional guidance needed for the Hong Kong market over and above IVS? If so, please specify with as much detail as possible.

Performance Framework

The Performance Framework covers how much work should be done in order to prepare a "professional" work product. The framework addresses the scope of work, level of rigour, extent of analysis, consideration of contrary evidence, and documentation needed in both the report and the working papers.

The Mandatory Performance Framework (MPF)[2] and Application of the MPF (Application) were originally developed for valuation professionals performing valuations of businesses, business interests, intangible assets, certain liabilities, and inventories used for management assertions in financial statements issued for financial reporting purposes, specifically for US Securities and Exchange Commission (SEC) registrants and privately held entities that issue financial statements in accordance with US GAAP. The MPF FAQs document gives further information.

We believe the MPF will eventually be adopted and applied in practice to entities required to submit registration statements or filings to the SEC as well as privately held entities that issue financial statements in accordance with US GAAP in 2019 or shortly thereafter. This will result in a dialogue which will continue internationally for the MPF which, given its potential unintended spillover, would be likely considered as 'best practice' internationally including major capital markets like Hong Kong as well as for purposes other than financial reporting.

Recommendations

The Technical Working Group believes, as best practice, the following MPF concepts are applicable for business valuations and intangible assets in Hong Kong:

1. Subcontractors (MPF 2.14)
2. Professional Skepticism (MPF 2.16 - 2.18)
3. Comprehensive Valuation Report or Abbreviated Valuation Report (MPF 2.20.1 - 2.20.2)
4. Management Interviews (MPF 2.23)
5. Selection of Valuation Approaches and Methods (Application A1.3)
6. Prospective Financial Information (Application A1.4)
7. Discount Rate Derivation (Application A2.2)
8. Estimation of Growth Rates (Application A2.3)
9. Selection of Terminal Value Multiple Methods and Models (Application A2.4)
10. Selection of, and Adjustments to, Valuation Multiples (Application A2.5)

[2] It is mandatory for valuation professionals who have earned the CEIV credential to adhere to the MPF and Application documents but should be considered **best practice** by valuation professionals who do *not* have the CEIV credential.

11. Selection of Guideline Public Companies or Guideline Company Transactions (Application A2.6)
12. Discounts and Premiums (Application A2.7)
13. Life for Projection Period (Application A3.4)
14. Customer-Related Intangible Assets (Application A3.5)
15. Selection of Royalty Rates (Application A3.6).

Questions

10) Could a valuation practitioner apply all or most of the MPF concepts in their valuation in Hong Kong, and for which valuation purposes? Please provide sufficient explanation as to why, if some or all of the concepts cannot be applied.

11) Under the assumption that all or most of the MPF concepts are applicable for valuations in Hong Kong, as best practice, how do we encourage practitioners to apply the MPF concepts in their valuations?

12) In cases when the MPF concepts are not applicable, should we require practitioners to state clearly that the MPF was not applied in their analysis?

Investigations and Complaints Mechanism

Professional ethics and standards only provide assurance to the market when there is enforcement action where a professional is falling short or failing to observe the standards required. Such professional assurance and oversight can be reactive or proactive.

Reactive assurance and oversight requires a professional body to have a clear process for receiving and investigating complaints from clients, other professionals, and the public. This normally needs the public to be made aware that the professional is a member of the professional body (for example through publication on a website or a statement on business stationery) so that a complainant is aware they can make a complaint. The professional body must then have an enforcement process, usually involving independent laypeople, that decides whether a complaint is supported by evidence, and to impose sanctions if the complaint is upheld. The sanctions should include the ability to remove the professional's accreditation or expel them from the body. Sanctions should also be published to protect the public and ensure confidence in the profession. However, the extent to which this method provides assurance is limited by whether clients or other stakeholders are likely to make complaints, and issues about access to confidential files can also arise when considering complaints that do not come from clients.

Proactive assurance and oversight includes all the elements of a reactive regime but also involves inspection of work product, auditing this against the standards set. Many professional bodies and regulators use this method to assure high-risk areas of practice. However, this is resource-intensive for both the professional body and the registered professional, involving higher costs for both. There can also be challenges for firms in providing information from confidential files to allow work to be audited. Nevertheless, this method provides more assurance through random sampling of the work, and the prospect of files being inspected will tend to encourage better-quality record-keeping and adherence to standards.

Whether reactive or proactive, any oversight regime should include enforcement action if continuing professional development requirements are not met.

There are different examples of existing assurance processes for business valuation worldwide. For example, the Institute of Valuers and Appraisers of Singapore use a reactive regime, while the CBV Institute in Canada uses a proactive approach.

Recommendations

We do not currently make a recommendation about whether a proactive or reactive assurance and regulation regime would be necessary to assure and improve the quality of business valuation in Hong Kong. We are seeking the views of respondents on the appropriate model to apply, and we are open to suggestions about other assurance and regulation regimes.

Questions

13) Do you believe that a reactive or proactive assurance and oversight regime or another assurance and regulation model is necessary for business valuation professionals in Hong Kong?

14) What elements do you think an assurance and oversight regime for business valuation professionals in Hong Kong should include?

Appendix A: Competencies

Colour-coded proficiency-level table to apply to subsequent competencies tables.

Level of Proficiency	**Description**
Basic	Learning outcomes at the basic level relate to work situations that are characterised by low levels of ambiguity, complexity and uncertainty.
	• Defining, explaining, summarising and interpreting the underlying principles and theories of relevant areas of technical knowledge to complete tasks while working under appropriate supervision. • Performing assigned tasks by using the appropriate professional skills. • Recognising the importance of professional skills and ethics in performing assigned tasks. • Solving simple problems and referring complex tasks or problems to supervisors or those with specialised expertise. • Providing information and explaining ideas in a clear manner, using oral and written communication skills.
Intermediate	Learning outcomes at the intermediate level relate to work situations that are characterised by moderate levels of ambiguity, complexity and uncertainty.
	• Independently applying, comparing and analysing underlying principles and theories from relevant areas of technical knowledge to complete work assignments and make decisions. • Combining technical knowledge and professional skills and ethics to complete work assignments. • Applying professional skills and ethics to work assignments. • Presenting information and explaining ideas in a clear manner, using oral and written communications to valuation and non-valuation stakeholders.
Advanced	Learning outcomes at the advanced level relate to work situations that are characterised by high levels of ambiguity, complexity and uncertainty.
	• Selecting and integrating principles and theories from different areas of technical knowledge to manage and lead projects and work assignments and to make recommendations appropriate to stakeholder needs. • Integrating technical knowledge and professional skills to manage and lead work projects. • Making judgements on appropriate courses of action, drawing on professional skills and ethics. • Assessing, researching and resolving complex problems with limited supervision. • Anticipating and consulting appropriately and developing solutions to complex problems and issues. • Consistently presenting and explaining relevant information in a persuasive manner to a wide range of stakeholders.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Economic theory, principles and concepts	Describes the fundamental principles of microeconomics and macroeconomics and how they may have an impact on the subject of valuation.
	Explains the different types of market structures: • Pure competition • Oligopoly • Monopoly.
	Describes the role of the geopolitical and cross-border considerations in a valuation assignment.
	Identifies the impact of government policies on the economy, including: • Monetary policy • Fiscal policy • Wages policy • Macro-economic reform.
Financial markets	Compares the various sources of capital available to an entity.
	Explains the financial system and the operation of financial and securities markets, including: • Foreign exchange market • Short-term money market • Long-term debt market • Share market • Derivatives market.
	Describes the main linkages within the economy, the role of economic indicators, political developments and market sentiments in driving markets (e.g. increase in interest rates and/or taxes will influence the exchange rate, share prices and, more generally, the value of various financial assets).
Finance theory	Explains how finance theory integrates with valuation theory, including: • Time value of money • Risk–return trade-off • Cost of capital component • Capital budgeting.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Accounting theory	Explains the basic accounting theory of recording and reporting financial information, including: • Debits and credits • General ledger • Components of financial statements.
Legal framework	Explains the various forms of ownership of an asset.
	Identifies the laws and regulations that govern the different forms of legal entities and the sources of obtaining information.
	Explains the court system and alternative dispute resolution mechanisms that apply to the subject matter of the valuation.
	Explains the effect of regulatory requirements on valuation in assessing general industry conditions.
	Identifies the legal considerations when evaluating a transaction or when performing a valuation.
	Explains the laws and regulations applicable to the environment in which valuers operate.
	Explains the concept of professional liability.
	Identifies situations in which consultation with legal counsel is required.
Tax framework	Identifies the tax system applicable to the subject of the valuation.
	Identifies the tax considerations when evaluating a transaction or when performing a valuation.
Valuation theory, principles and concepts	Describes the basic valuation concepts.
	Demonstrates knowledge of valuation theory.
	Applies valuation principles consistent with the purpose of the valuation.
Valuation definitions	Identifies the various sources of valuation definitions, including: • International Valuation Standards • International Glossary of Business Valuation Terms • Other authoritative sources, in accordance with established requirements.
	Applies the appropriate valuation definitions consistent with the purpose of the valuation.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Subject asset/ liability characteristics	Describes the characteristics of the subject matter through which value is created.
Purpose of the valuation	Identifies the purpose of the valuation, including: • Transaction • Financial reporting • Tax compliance • Litigation • Lending • Statutory • Solvency opinion • Insurance • Portfolio valuation/asset valuation • Lease or rental determination • Management planning • Other.
Valuation process	Describes the valuation process in the conduct of a valuation assignment.
	Determines the scope of work in accordance with International Valuation Standards and other applicable standards and requirements.
	Defines and describes the intended user of the valuation.
	Defines the qualitative and quantitative information requirements.
	Assesses, objectively, the qualitative and quantitative information, consistent with the purpose of the valuation.
	Utilises information provided by client while keeping an objective and impartial perspective.
	Describes the purpose of the engagement.
	Describes the purpose of representation letters.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Premise of value	Describes the premise of value, including: • Going concern • Liquidation • Value in continued use • Value in exchange.
	Differentiates between the various premises of value and the implications for the valuation inputs and valuation conclusions.
	Applies the appropriate premise of value consistent with the purpose of the valuation.
	Describes the relationships between the basis of value and the premise of value.
Basis of value	Describes the various bases of value, including: • Market value • Investment value • Other.
	Differentiates between the various bases of value and the implications for valuation premise, valuation inputs and valuation conclusions.
	Applies the appropriate basis of value consistent with the purpose of the valuation.
Highest and best use	Explains the concept of highest and best use.
	Evaluates the concept of highest and best use in the context of a group of assets or a business.
	Applies the concept of highest and best use and assumptions consistent with such use.
Technical standards/ guidelines	Identifies the relevant valuation-related standards and guidelines.
	Applies the relevant valuation-related standards and guidelines consistent with the subject matter and the purpose of the valuation, including: • Financial reporting standards • Private equity and venture capital guidelines • Tax-related standards • Other standards and guidelines in accordance with established requirements.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Valuation approaches	Describes the principal valuation approaches: • Market • Income • Cost.
	Evaluates the applicability of alternative valuation approaches based on the nature of the subject matter, the premise of value and the purpose of the valuation.
	Applies different valuation approaches to analyse and determine the value of the subject of valuation, consistent with the basis of value, premise of value and purpose of the valuation.
Valuation methods	Explains the valuation methods that can apply in the valuation of the subject matter.
	Describes the advantages and disadvantages of each valuation method.
	Differentiates between the various valuation methods that fall under each of the three valuation approaches.
	Applies different valuation methods to analyse, reconcile and conclude on the value of the subject of valuation, consistent with the basis of value, premise of value and purpose of the valuation.
Information technology	Applies information technology skills in data analysis, valuation modelling, report writing and presentation of results.
Financial modelling	Describes the analysis and modelling of the subject of the valuation from a financial perspective.
	Applies spreadsheet or bespoke programmes that are flexible to accommodate modification of major assumptions, as needed.
Valuations for speciality areas, specific industries or markets	Recognises general circumstances in which a specialist or a subject matter expert should be involved.
	Identifies speciality areas and/or industries, including: • Valuation of real-estate holding company • Resource company • Derivatives.
	Describes the key considerations around the availability, transparency and reliability of data and information to perform valuations in emerging markets.

COMMON COMPETENCIES	
Competence Area	**Learning Outcomes**
Reporting of valuation	Applies report writing and/or other communication skills to convey the valuation conclusion.
	Identifies the type of report used and its definition.
	Applies and documents compliance with all applicable valuer standards, including certification etc.
Valuation quality (quality of information, sources and assumptions, integrity of analysis, and robustness of conclusions)	Evaluates information and assumptions provided by management in light of past company performance and industry expectations.
	Evaluates the reasonableness of the prospective financial information in light of industry benchmarks, historical performance and industry expectations, for various items including: • Revenues • Profit margins • Taxes • Working capital • Capital expenditures • Growth rates • Other.
	Assesses the nature of the projected cash flows (expected vs conditional).
	Distinguishes between entity-specific assumptions and expectations and market participant assumptions and expectations.
	Adjusts forecasts and assumptions as appropriate.
	Adjusts methods and assumptions used according to the type and quality of data available.
	Evaluates the valuation conclusion in light of the value creation process at the entity.
	Evaluates and reconciles on a qualitative basis, and explains, any divergent value indications from the application of the various approaches.
	Evaluates internal consistency of data, assumptions and methods applied to the subject asset (or liability), including in the context of other assets (or liabilities) being valued.
	Evaluates, on a high level, relevant historical valuation analyses for the asset or valuations of comparable assets (if available) and explains and rationalises significant changes in the assumptions and methods used.
	Synthesises key discussions, assumptions, decisions, and significant issues arising in the course of the valuation analysis and the manner in which they were addressed.

BUSINESS AND BUSINESS INTERESTS	
Competence Area	**Learning Outcome**
Business and organisational environment	Describes the environment in which an entity operates, including: • Economic • Legal • Political • Social • Technological • International • Cultural.
	Analyses the economic environment and its impact on the profitability, risk and/or growth of the entity.
	Analyses the entity's business strategy.
	Identifies and describes the industry risks.
	Identifies and describes the key risks and opportunities specific to the business.
	Explains shareholder rights and the implication of those rights in a valuation.
Financial theory, principles and concepts	Applies finance theory and concepts relevant to business valuation, including: • Risk–return trade-off • Time value of money • Capital structure • Cost of capital determination.

BUSINESS AND BUSINESS INTERESTS	
Competence Area	**Learning Outcome**
Financial theory, principles and concepts	Evaluates the entity's financial condition as a stand-alone entity, including: • Comparison of current and projected information with historical results • Comparison to company peers/guideline companies • Industry benchmarking • Life-cycle analysis.
Premise of value	Explains the appropriate premise in the valuation of the business: • Going concern • Liquidation premise.
	Applies the appropriate premise of value consistent with the purpose of the valuation.
	Explains the effect of asset obsolescence and impact on the premise of value used for the business valuation.
	Explains the need for general consistency between the premise of value used in valuing the assets of the business and the overall business operation.
Valuation approaches and methods	Compares and contrasts the various valuation methods under the principal valuation approaches, as follows: 1. Income approach a. Main value drivers i. Benefit streams and profitability • Relationship between value and profitability • Cash flow measures vs accounting measures • Invested capital measures vs equity measures ii. Risk • Relationship between value and risk • External sources of risk • Internal sources of risk iii. Growth • Relationship between value and growth • Economic, competitive, capacity, capital and management limitations • Near-term growth • Long-term stabilised growth b. Subject entity analysis i. Qualitative

BUSINESS AND BUSINESS INTERESTS	
Competence Area	**Learning Outcome**
	• Strengths, weaknesses, opportunities and threats ii. Quantitative • Financial statement adjustments • Financial ratio analysis trending and benchmark/peer group comparisons
Valuation approaches and methods	c. Income-based methods: i. Capitalisation of earnings or cash flow, including: • Normalisation adjustments ○ Accounting convention consistency ○ Non-recurring/extraordinary income and expenses ○ Control/owner's discretion ○ Non-operating assets/liabilities and associated income and expense • Determination of sustainable earnings/cash flow • Multiple/capitalisation rate determination: ○ Business life-cycle ○ Relationship between risk and return ○ Cost of equity adjusted for risk: build-up method vs capital asset pricing model, risk free rate, equity/market risk premium, country risk, industry risk premium/beta, size risk and unsystematic risk ○ Cost of debt adjusted for risk ○ Weighted average cost of capital (WACC), cost of debt and equity adjusted for risk, and capital structure considerations ○ WACC (invested capital) vs cost of equity (equity) ○ Matching of WACC or cost of equity to the adjusted benefit stream ○ Growth considerations ○ WACC vs capitalisation rate ○ Comparable transactions ○ Other methods • Redundant net assets: non-operating assets • Non-equity claims • Tax calculations, including tax shield ii. Discounted cash flow, including: • Normalisation adjustments • Discount rate(s) determination • Determination of sustainable earnings/cash flow • Discrete time period until stabilisation • Assessment of management forecasts • Methods of calculating terminal value

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Competence Area	**Learning Outcome**
	iii. Other methods: • capitalisation of earnings before interest and taxes • dual capitalisation • other
Valuation approaches and methods	2. Market approach a. Previous transactions of subject company shares i. assessment of arm's-length indicators ii. difference in size of block iii. difference in economy, industry and competitive environment iv. difference in company-specific factors: qualitative and financial b. guideline publicly traded company method i. selecting guideline companies ii. comparative analyses between guideline companies and subject entity: profitability, risk and growth iii. selection of valuation multiples: invested capital vs equity multiples, and cash flow vs accounting benefits multiples iv. adjustment of valuation multiples for differences in: profitability, risk, growth and other factors c. guideline precedent transaction method i. selecting guideline companies ii. comparative analyses between guideline companies and subject entity: profitability, risk, growth and other factors iii. selection of valuation multiples: invested capital vs equity multiples, and cash flow vs. accounting benefits multiples iv. adjustment of valuation multiples for differences in profitability, risk, growth and other factors d. reconciliation of value indications among different multiples
	3. Asset-based valuation methods, both as a primary valuation method and a risk assessment tool, as follows: a. Adjusted book value or net asset value i. premise of value: in exchange or use ii. valuation of the assets and liabilities, including methods for valuing intangible assets (recorded or not) iii. tax implications and adjustments: tax shield, taxes on disposition and distribution, refundable taxes and relevance thereof b. Liquidation value i. orderly vs forced ii. liquidation costs and expenses iii. tax implications and adjustments: taxes on disposition and distribution, refundable taxes and relevance thereof iv. time value of money
	4. Other methods: a. capitalisation of earnings before interest and taxes b. dual capitalisation c. other.

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Competence Area	**Learning Outcome**
	Applies different valuation methods to calculate, analyse and support a plausible range of values.
	Evaluates the reasonableness of the valuation conclusion and documents the rationale.
Financial statement analysis	Describes the use of financial statements for the purpose of business valuation.
	Explains the differences in financial statements and tax reporting for various entities, including: • Partnership • Sole proprietorship • Private or public company • Joint venture.
	Evaluates completeness of financial statements in the context of setting the proper scope for the valuation, i.e. the extent of the investigation and the normalisation adjustments required.
	Explains the differences in the way differing accounting conventions have an impact on financial statements.
	Evaluates the effect of accounting policies used to prepare financial statements, including: • Cash vs accrual basis • Capitalisation vs expensing of expenditures.
	Describes the use of financial statements for the purpose of business valuation, including: • Historical results vs prospective results • Level of tangible assets • Capital structure. •
Financial forecasting	Identifies inputs and supporting information from internal and external sources and identifies gaps and anomalies.
	Evaluates inputs and supporting information for reliability.
	Applies forecasting methods for the subject of valuation based on rational and reasonable assumptions.
	Describes assumptions, data, inputs and results in a manner to be understood by third parties not involved in the forecast model design.

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Competence Area	**Learning Outcome**
Valuation of equity interests	Explains the relevance of legal agreements in the valuation of equity interests, including: • By-laws • Articles of incorporation • Shareholder agreements • Partnership agreements • Voting trusts.
	Identifies the relevant considerations in the valuation of equity interests.
	Identifies the appropriate premise in the valuation of debt, when debt is deducted from enterprise value in arriving at equity value as a residual.
	Identifies any non-equity claims that are deducted from enterprise value in arriving at equity value as a residual.
	Assesses the valuation issues in allocating value between the classes of shares, including: • Voting • Non-voting • Preferred • Restricted.
	Identifies the issues relating to the valuation of securities of public companies.
	Determines the level of value and its attributes resulting from the application of the valuation approaches and methods, including: • Control • Non-controlling • Marketable • Non-marketable • Liquid • Illiquid.
Discounts and premiums in the	Considers the factors in valuing minority interests, factors affecting value, and legal remedies available.
	Explains the concept of minority discounts.

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Competence Area	**Learning Outcome**
valuation of equity interests	Explains the considerations in valuing controlling interests, including conceptual issues relating to terms such as “premium for control”.
	Explains the concept of blockage discounts.
	Applies the appropriate magnitude of discount or premium consistent with the level of value and the specific facts and circumstances.
Asset attributes	Describes the concept of intangible assets.
	Identifies the asset by reference to its type and describes its attributes: • Marketing-related • Technology related • Customer- or supplier-related • Artistic-related.
	Describes the legal right or interest in the asset.
	Explains how the asset arises (e.g. contractual right) and whether the asset is separately identifiable or not (e.g. goodwill), consistent with the purpose of the valuation.
	Describes the specific characteristics of the intangible assets, including: • Specifications • Function • Market position • Image • Value proposition.
Premise of value	Identifies the premise of value that is consistent with the purpose of the valuation and basis of value.
	Explains whether the selected premise assumes a going concern or liquidation.
	Describes the concept of functional, technological and economic obsolescence in the context of the valuation and the effect on the valuation premise.
	Evaluates the potential impact of functional and economic obsolescence on the intangible asset(s).

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Competence Area	**Learning Outcome**
Valuation approaches and methods	Compares and contrasts the conceptual similarities and differences of the three valuation approaches (income, market, cost) when applied to intangible assets and discusses the strengths and weaknesses of each.
	Evaluates how the characteristics of the intangible asset affect the valuation approach(es) and method(s) applied in the valuation of the asset.
Income approach	Explains the concept of the income approach.
	Outlines the types of assets and circumstances suited to the application of the income approach.
	Compares and contrasts the conceptual similarities and differences of the various methods under the income approach and discusses the strengths and weaknesses of each.
Income approach: relief from royalty method	Explains the concept of a relief from royalty method and its strengths and weaknesses.
	Selects a hypothetical royalty rate by applying one or more methods, for example: 1. Evaluates observed royalty rates and makes adjustments as appropriate to estimate a hypothetical royalty rate 2. Estimates a royalty rate via a: a. Profit split method b. Return on assets c. Return on investment method d. Comparable profits method.
	Evaluates whether the royalty observed or derived is gross or net of maintenance expenses for the subject intangible.
	Applies the relief from royalty method over the projected economic life of the asset.
Income approach: premium profits method (with-or-without method)	Explains the concept of the premium profits (with-or-without) method and its strengths and weaknesses.
	Assesses the differential in profits due to the employment of the subject intangible asset over its economic life.
	Estimates the period over which benefits from the subject asset are received.
	Applies the premium profits method over the life of the benefit.

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Competence Area	**Learning Outcome**
Income approach: multi-period excess earnings method	Explains the concept of the multi-period excess earnings method and its strengths and weaknesses.
	Outlines the types of assets and circumstances suited to the application of the multi-period excess earnings method.
	Calculates the revenues and expenses related to the operating group containing the subject intangible asset and evaluates the projected financial information.
	Describes the contributory assets in the operating group that the subject intangible asset is part of.
	Computes and applies contributory asset charges, and makes other adjustments to the projections, including discounting.
	Estimates the period of time over which to apply the multi-period excess earnings method.
	Evaluates impact of economic obsolescence on the value indications of the multi-period excess earnings method.
Income approach: disaggregated (distributor) method	Explains the concept of the disaggregated (distributor) method and its strengths and weaknesses.
	Outlines the types of assets and circumstances suited to the application of the disaggregated (distributor) method.
	Identifies the various functions of the enterprise to which the distributor method could be applied and identifies the assets required to perform such business functions.
	Estimates the period of time over which to apply the disaggregated (distributor) method.
	Applies the disaggregated (distributor) method.

INTANGIBLE ASSETS	
Competence Area	**Learning Outcomes**
Income approach: greenfield method	Explains the concept of the greenfield method and its strengths and weaknesses.
	Outlines the types of assets and circumstances suited to the application of the greenfield method.
	Estimates the period of time required to establish the business (ramp-up period) under current market conditions.
	Estimates the normalised level of operation of the business at the end of the ramp-up period.
	Estimates costs and investments during the ramp-up period.
	Applies the greenfield method.
Income approach: cost savings method	Explains the concept of the cost savings method and its strengths and weaknesses.
	Outlines the types of assets and circumstances suited to the application of the cost savings method.
	Estimates the period of time over which the costs savings related to the subject intangible would continue.
	Applies the cost savings approach.
Market approach	Explains the concept of the market approach and discusses its strengths and weaknesses when applied to intangible assets.
	Outlines the types of assets and circumstances suited to the application of the market approach.
	Evaluates and interprets observable market evidence related to transactions for identical or similar intangible assets.
	Adjusts observed prices and multiples as appropriate.
	Evaluates and interprets observable market multiples related to similar intangible assets.
	Adjusts, if necessary, the metric of the subject intangible asset that a market multiple would be applied to.
	Applies the market approach.

INTANGIBLE ASSETS	
Competence Area	**Learning Outcomes**
Cost approach	Explains the concept of the cost approach and discusses its strengths and weaknesses when applied to intangible assets.
	Outlines the types of assets and circumstances suited to the application of the cost approach.
	Estimates current replacement cost by purchase and modification of a similar asset.
	Estimates current replacement cost by construction of a similar asset.
	Evaluates and applies a developer's profit.
	Evaluates and applies an opportunity-cost adjustment.
	Applies adjustments for functional, technological, and economic obsolescence, as appropriate.
Obsolescence	Explains the interaction between premise of value and economic obsolescence.
	Assesses the effect of technological, functional and economic obsolescence on asset value.
	Estimates and applies any technological, functional and economic obsolescence adjustments to the indicated value of the subject intangible.
Economic life	Explains the impact of contractual, legal, regulatory, technological factors on the economic life of an intangible asset.
	Explains the effects of obsolescence, demand, competition and other economic factors on the economic life of an intangible asset.
	Explains the effect of another asset or a group of assets that the subject intangible is used with.
	Describes and critiques various methods for estimating the economic life of a subject asset, including: • Methods based on historical customer revenue data • Historical customer count data • Statistical methods • Industry and third-party data sources • Management estimates.

INTANGIBLE ASSETS	
Competence Area	**Learning Outcomes**
Economic life	Evaluates the best method(s) to use based on the circumstances, including the type and quality of data available.
	Estimates the economic life of the intangible asset for the purpose of applying valuation approaches and methods: 1. Marketing-related intangibles lifing: a. Assesses the longevity of the marketing-related intangible in conjunction with contractual, legal, regulatory, technological (related to the associated product or service) factors on the economic life of the subject intangible asset b. Evaluates the impact of planned marketing spending on the life of the subject intangible 2. Technology-related intangibles lifing: a. Assesses the life-cycle of the technology-related intangible in conjunction with contractual, legal, regulatory, technological factors on the economic life of the subject intangible asset b. Evaluates the impact of planned technology development spending on the life of the subject intangible 3. Customer and supplier-related intangibles attrition estimation: c. Evaluates whether the characteristics of the customer population in terms of size, profitability, and other attributes warrant dividing the population into subsets with comparable attributes for analysis purposes d. Analyses historical customer count data for the entire population or a subset e. Assesses historical customer revenue data for the entire population or a subset f. Assesses comparable customer population revenue or count g. Assesses customer attrition estimates from third-party data sources h. Assesses partial period adjustments in the attrition computation, where applicable. i. Applies statistical methods: I. Computes historical retirement rates for individual customer vintages using a time series analysis and constructs observed survivor curve II. Compares and extends observed survivor curves to Iowa or Weibull survivor curve models j. Evaluates, critiques and adjusts educated estimates by management k. Interprets and adjusts irregular attrition patterns l. Assesses the indications of various lifing methods and documents the conclusion reached.
	4. Artistic-related intangibles lifing: a. Assesses the longevity of the artistic-related intangible in conjunction with contractual, legal, regulatory, factors on the economic life of the subject intangible asset.
	Evaluates the impact of planned spending on the life of the subject intangible.
	Determines the length of the projection period for the income approach in light of the economic life estimation.

	Assesses comparability to other intangibles when applying the market approach in light of the economic life estimation.

INTANGIBLE ASSETS	
Competence Area	**Learning Outcomes**
Tax amortisation benefit	Describes the concept of the tax amortisation benefit (TAB) and the effect of the tax laws of a jurisdiction on the ability to apply a TAB.
	Applies TAB to the present value of the asset.
	Evaluates the conclusion and documents the rationale.
Discount rate	Describes the concepts of discount rate, internal rate of return (IRR) and weighted average return on assets (WARA).
	Explains the relationship between the discount rate, the IRR and WARA.
	Evaluates the characteristics of the cash flows and the impact on the range of selected discount rates, including in the case of: • Expected cash flows • Conditional cash flows.
	Evaluates the risk of the subject intangible in the context of its ability to be financed with debt and/or equity.
	Evaluates the risk of the subject intangible in the context of the risk of other assets within the group or business, and the risk of the overall business.
	Evaluates the risk of the subject intangible in the context of the IRR based on the purchase price of the group of assets or business (when the subject intangible asset is an element of a business combination).
	Analyses the stratified rates of return in a WARA framework.
Reconciliation of concluded intangible values	Reconciles and qualitatively weights the value indications of the income, market and cost approaches and concludes on a value range or a single point value estimate, as needed.
	Assesses the reasonableness of the valuation conclusion for the subject intangible in light of the valuation conclusions for any other assets in the group (or business) and in the context of WARA, recent transactions, industry and economic trends.

Appendix B: Local Body of Knowledge

Accounting Standards

Domestic companies whose securities trade on the Stock Exchange of Hong Kong are required to use Hong Kong Financial Reporting Standards (HKFRS). A company that is domiciled in but incorporated outside Hong Kong is permitted to use either HKFRS or International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board. HKFRS have been fully aligned with IFRS for annual reporting periods commencing since 1 January 2005.

An SME (as defined in the IFRS for SMEs) in Hong Kong also has the option to adopt the HKFRS for Private Entities, which is identical to the IFRS for SMEs. Additionally, by law, some Hong Kong-incorporated companies are given an option to use the Hong Kong Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (SME-FRF & SME-FRS).

HKFRS, IFRS, HKFRS for Private Entities and SME-FRF & SME-FRS contain fair-value measurement requirements and might affect the nature, timing, and scope of a valuation professional's work.