



International Association of Consultants, Valuators and Analysts

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30 September 2013

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

Ladies and Gentlemen,

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

As a worldwide organization, we are extremely concerned with the development of guidance and standards related to valuation. We appreciate the opportunity to comment on the Exposure Draft for the Technical Information Paper (TIP) "*The Valuation of Equity Derivatives*". Our responses to the indicated questions are as follows:

1. Under the heading of "Equity Derivative Products" (para 11-22), the main types of equity derivative are listed. Do you believe there are any material omissions? If so, please indicate what they are.

We think that paragraphs 11 to 22 are a good start but that:

- a) Forwards and Futures should be separated as they have significantly different characteristics especially with respect to standardize features, collateral (margin) and for non-financial futures seasonality.
- b) Paragraph 14 should be expanded to discuss total return swaps.
- c) Paragraph 17 should include the definition of barrier options from Paragraph 18 together with illustrative examples.
- d) Paragraph 18 should include illustrative examples of each type.
- e) The order of paragraphs 17 and 18 should be reversed.

2. Do you believe the descriptions provided for each of the listed products are sufficiently detailed?

Again, we consider that the included descriptions are a good start but all should be enhanced by illustrative examples. In addition, some of them, such as of barrier options, need expanding to show how they are constructed.

3. Do you think more complicated derivatives and strategies should be included? For example, where products are combined, such as in straddles and strangles?

We believe that all derivatives, no matter how complicated, should be listed, including at least for options:

- Straddles: buying (long) or selling (short) both a put and a call with the same strike price and expiry
 - Strangles: buying (long) or selling (short) both an out-of-the-money (OTM) call and an OTM put with the same expiry
 - Vertical spreads, buying or selling and sale of a call or a put with different strike prices but the same expiry
 - Butterflies: buying (short) or selling (long), two calls at a current strike price (the body) and buying (long) or selling (short) one call at a higher and one call at a lower stake price (the wings)
 - LEAPS (Long-term Equity Anticipation Securities)
4. The discussion on forwards (para 23 to -27) includes a number of formulae. Do you find the inclusion of formulae to be helpful in understanding the principles or would you prefer a purely descriptive narrative?

We believe that formulae with illustrative examples are helpful in understanding valuation principles but should be only supplemental to a complete written description. Therefore, paragraphs 23 to 27 are incomplete.

5. Would you prefer to see greater use being made of formulae to illustrate principles in other parts of the TIP?

As set out in the answer to Questions 2 and 4, we believe that formulae and illustrative examples should support all descriptions.

6. The discussion of various models types includes the key assumptions and other inputs required. The objective is not to provide detailed instruction on the use of the model, but do you think the information on these inputs is sufficiently detailed to provide an understanding of the principals involved by someone relying on the valuation?

The description of Option Pricing Models (OPMs) (paragraphs 31 to 38), is unsatisfactory as it does not deal with the problem of “fat tails” due to many situations where the real world not having a “normal” distribution, nor the need to consider credit and operational in addition to market risks for any portfolio of Equity Derivatives as each risk has a different profile. The sections on Jump (paragraphs 62 to 71) and alternate diffusion models (paragraphs 72 to 83) are inadequate as they do not explain what inputs are used and how.

7. Do you believe the model section of this paper should discuss each model's relative applications and when it is appropriate to use one rather than another, for example, by mapping each model to a list of products?

We strongly believe that the model section should be substantially expanded and that all generally accepted models be described in detail including their common applications and those other situations when one is appropriate to be used. There should also be cross-references between the types of options listed in paragraphs 17 and 18 and any suitable OPMs.

8. "The Greeks" are summarised with brief descriptions in this paper- Do you believe it would be helpful if there were a more detailed discussion of sensitivities?

As sensitivities are a key factor in assessing the reliability of any model's conclusion, a full discussion is desirable.

9. Please list the departments within your organisation that you believe would find this document useful, e.g. Executive Management, Treasury, Risk, Financial Reporting, Product Control etc.

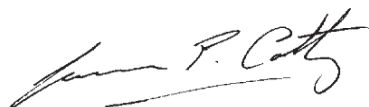
IACVA, a member of IVSC, is a knowledge transfer and credentialing organization devoted to business valuation and fraud deterrence. Our objective is "Best Practices Worldwide". The final version of the Technical Information Paper (TIP) will be of interest to all our 10,000 members.

10. Do you consider that the overall level scope and level of detail in this proposed TIP is sufficient to meet its objective of reducing diversity of practice and raising awareness of the principle methods used for valuing equity instruments among the wider financial community, and in particular investors?

Regretfully we find the level of detail in the proposed TIP is entirely insufficient to meet its objectives as a TIP.

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

Respectfully submitted on behalf of IACVA
Per



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

Appendix

IACVA List of Countries

Americas

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

Africa

Ghana
Kenya
Nigeria
South Africa
Uganda

Europe

Austria
Germany
Netherlands
Switzerland
Romania
Ireland
United Kingdom

Asia/Pacifica

China
Taiwan
Japan
South Korea
Hong Kong
Singapore

Malaysia
Thailand
Australia
India

Middle East

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

Commonwealth of Independent States

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