



INTERNATIONAL VALUATION STANDARDS COUNCIL

Amendments to the International Valuation Standards

EXPOSURE DRAFT

Comments on this Exposure Draft are invited before 30 April 2013. All replies may be put on public record unless confidentiality is requested by the respondent. Comments may be sent as email attachments to:

CommentLetters@ivsc.org

or by post to IVSC, 68 Lombard Street, LONDON EC3V 9LJ, United Kingdom.

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Introduction to Exposure Draft

Following its major review of the International Valuation Standards under the Standards Improvement Project between 2008 and 2011, the IVSC Standards Board approved twelve completely revised standards for publication in July 2011.

A number of minor changes are now required to update the standards to reflect subsequent IVS publications or other changes that impact upon them. Also, work on other IVSC Projects has brought to light a few instances where the existing IVSs could be improved by making minor alterations to remove ambiguity or better illustrate a principle.

In 2012 the Board also commenced two specific projects on Valuation Reviews and the Valuer's Reliance on Information. At its meeting in October 2012 the Board agreed various provisional changes to the existing IVSs to clarify and improve the way these topics are addressed in the IVSs.

This Exposure Draft contains the changes proposed by the Board as a consequence of the above.

Comments are invited on the proposed changes no later than 30 April 2013.

It is proposed that the revised Standards will be published in July 2013, with an effective date of 1 January 2014, although earlier adoption will be encouraged.

Notes for respondents:

In order for us to analyse and give due weight to your comments, please observe the following:

1. Responses should be made in letter format, where appropriate on the organisation's letter heading.
2. It is not necessary to comment on all proposed amendments. However, to enable proper consideration of your comments please clearly indicate the number and title of the proposed amendment, whether you support or oppose the change and if the latter why. If you wish to propose alternative wording please support this with reasons.
3. Comments should not be submitted on an edited version of the Exposure Draft.
4. Unless anonymity is requested, all comments received may be displayed on the IVSC website.
5. Comments letters should be sent as an e mail attachment in either MS Word or an **unlocked** PDF format and no larger than 1mb. All documents will be converted to secured PDF files before being placed on the web site.
6. The email should be sent to commentletters@ivsc.org

1. **Definitions:**

Proposed Change

Valuation Date: The date on which the opinion of value applies. The valuation date shall also include the time on which it applies if the value of the type of asset can be observed as changing materially in the course of a single day.

Reason: In drafting the emerging TIPs on financial instruments it has been pointed out that the concept of the valuation date may be insufficiently precise in this context as instruments can and do have different values on the same day. An alternative would be to introduce “time of valuation” as either a replacement or alternative definition. However, since “valuation date” is widely understood and used within other definitions (eg market value) introducing an alternative could create confusion and some significant redrafting challenges.

2. **Definitions:**

Proposed Change

Valuation Review: The act or process of developing and reporting an opinion about a valuation undertaken by another party.

Reason: The proposed change results from the Board’s project to clarify the applicability of the IVSs to valuation reviews

3. **IVS Framework – 3 and 4.**

Proposed Change:

Independence and Objectivity

~~3 Many states have laws or regulations that only allow certain persons to value particular classes of assets for various purposes. Additionally, many professional bodies and valuation providers have ethical codes that require the identification and disclosure of potential conflicts of interest. The purpose of these standards is to set internationally recognised principles and definitions for the preparation and reporting of valuations. They do not include regulations on the relationship between those commissioning valuations and those undertaking them, as~~

~~4 While specific conduct rules for valuers are outside the scope of these standards, It is nevertheless a fundamental expectation that when applying these standards appropriate controls and procedures are in place to ensure the necessary degree of independence and objectivity in the valuation process so that the results can be seen to be free from bias. The IVSC Code of Ethical Principles for Professional Valuers provides an example of an appropriate framework of conduct rules. Where the purpose of the valuation requires the valuer to have a specific status or disclosures confirming the valuer’s status to be made, the requirements are set out in the appropriate standard. Matters relating to the conduct and ethical behaviour of valuers are for Valuation Professional Organisations or other bodies that have a regulatory role over individual valuers.~~

Reason: Since the standards were published in 2011 the IVSC Professional Board has published the Code of Ethical Principles for Professional Valuers and it is considered appropriate that the IVS Framework should make specific reference to this. Although the

intention of the existing reference to “independence “ was to the need for independence of thought, it is often interpreted as meaning an absence of any connection with the subject, client or user of the valuation (or any combination thereof). The IVSC Code lists “objectivity” as one of the Fundamental Principles of professional conduct and provides guidance on threats to objectivity and safeguards that may be taken to avoid or mitigate such threats, but does not use the word “independence”. The proposed change brings consistency with the Code.

4. IVS Framework – 25

Proposed Change:

Aggregation-Unit of Valuation

24 (no change)

25 Where a valuation is required of assets that are held in conjunction with other complementary or related assets, it is important to clearly define the unit of valuation, ~~whether it is the group or portfolio of assets that is to be valued or each of the assets individually. If the latter.~~ A unit of valuation may consist of a single inseparable asset or a group of complementary assets. Where the unit of valuation is associated with other assets that are excluded from the valuation it is also important to establish whether each asset the unit of valuation is assumed to be valued:

a) ~~as an individual item but~~ assuming that the ~~other associated~~ assets are available to a buyer, or

b) ~~as an individual item but~~ assuming that the ~~other associated~~ assets are not available to a buyer.

Introduce the following definition into the list of IVS Definitions:

Unit of Valuation: The asset or group of associated assets that is the subject of the valuation.

Reason: The concept of “unit of account” is used in IFRS and widely understood. Many valuers try to apply the concept to valuation. An early draft of TIP 2 *The Cost Approach for Tangible Assets* used the term “unit of account” to describe a combination of potentially separable assets that is to be valued as one. However, it was recognised that it would cause confusion to take an accounting term and adapt it to valuations. The concept was renamed “unit of valuation” in the published TIP 2, although no definition as such was provided.

For comparison the IFRS Definition of “unit of account” is:

The level at which an asset or a liability is aggregated or disaggregated in an IFRS for recognition purposes

The relevance of the “unit of account” when undertaking valuations for financial reporting is discussed in IVS 300 para 3. No change is considered necessary to this narrative.

5. **IVS Framework – insert new para 26**

Proposed Change:

26 Where the *unit of valuation* comprises a number of separately identifiable assets or components that are capable of valuation individually, the sum of the individual assets or components is often greater or less than the value of the *unit of valuation*.

(Subsequent paras to be renumbered)

Reason: In consultations on some of the emerging TIPs a number of examples have come to the Board's attention where different components within the unit of valuation, eg land and improvements or assets within a business, are being valued separately, sometimes by different valuers, and then added together in an attempt to value the whole. The proposed new paragraph is intended to make it clear that this will not necessarily provide the true value of the *unit of valuation*.

6. **IVS Framework: 30**

Proposed Change:

30 *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.

Reason: consistency with approved definition. (note: this was a publishing error in the printed version on IVS 2011 only)

7. **IVS Framework: 31 (c)**

Proposed Change:

(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 actual market state and circumstances as of the effective *valuation date*, not as of either a past or future date. ~~The definition also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might otherwise be made;~~

Reason: The references to "exchange" and "completion" are specific to certain countries' systems of contract law and are therefore potentially confusing to readers unfamiliar with these terms. The definition of market value refers to an exchange on the valuation date, meaning that the agreed price is fixed and the asset transferred on that date. Under certain legal systems a contract is said to be "exchanged" when the contract becomes binding and "completed" when the transfer of the asset actually takes place, which may be on a later date. This alternative meaning of "exchange" in the conceptual framework for market value potentially causes confusion. And in any event, the price is fixed when a legally binding contract is entered into (legal exchange), not at any later physical exchange of the assets subject to that contract (legal completion), so the point being made by this sentence is redundant as price does not vary between exchange and completion.

8. IVS Framework: 56

Proposed Change:

56 One or more valuation approaches may be used in order to arrive at the valuation defined by the appropriate *basis of value* (see paras 26 to 29 above). The three approaches described and defined in this Framework are the main approaches used in valuation. They all are based on the economic principles of price equilibrium, anticipation of benefits or substitution. Using more than one valuation approach or method generally provides a cross check on the valuation conclusion and is especially recommended where the inputs to the primary method are limited or inconclusive.

Reason: Recent feedback from various specialist working groups assisting with our projects indicate that there are still problems caused by valuers putting too much weight on a single method, or in other words if the maths used in the model is right then it follows that the valuation must be. This can result in unjustifiable changes in value simply because a different method has been adopted. The method should always be a tool to indicate the result; it should not dictate it. IVS 102 para 7 encourages the use of more than one method where there are insufficient factual or observable inputs for a single method to produce a reliable conclusion, and the proposed addition to the Framework reinforces this.

9. IVS 101 Scope of Work 1

Proposed Change:

1. There are many different types and levels of valuation advice that may be provided. The IVSs are designed to apply to a wide spectrum of valuation assignments including valuation reviews where the reviewer is not required to provide their own opinion of value. A valuation and the work undertaken in its preparation must be appropriate for ~~it's~~ the intended purpose. ~~and~~ It is also important that the recipient of the valuation understands what is to be provided and any limitations on the use of the valuation before the valuation is finalised and reported. ~~A scope of work sets out the agreed purpose of the valuation, the extent of investigation, procedures that will be adopted, assumptions that will be made and the limitations that will apply. The scope of work may be prepared at the outset or during the progress of the valuation assignment but before the valuation and report are finalised.~~

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews and on the requirements on the valuer's reliance on information. The final two sentences of the existing paragraph are a summary of the contents rather than a statement of principle and are therefore redundant, as the provisions are made elsewhere.

10. IVS 101 Scope of Work 2

Proposed Change:

2 A scope of work shall be prepared and confirmed in writing that addresses the matters set out below. For certain asset classes or applications there may be variations from this standard or additional matters to be included or considered in preparing the scope of work.

These are found in the relevant Asset Standard or Valuation Application. References to a valuation or valuation assignment in this standard shall include valuation reviews.

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

11. **IVS 101 Scope of Work 2 (e)**

Proposed Change:

(e) **Bases of Value**

The valuation basis must be appropriate for the purpose. The source of the definition of any *basis of value* used shall be cited or the basis explained. The valuation bases recognised by IVS are defined and discussed in the IVS *Framework*, but other bases may be used. It may also be necessary to clarify the currency in which the valuation will be reported. If a valuation review is being undertaken where the reviewer is not required to provide an opinion of value this shall be confirmed.

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

12. **IVS 101 Scope of Work 2 (h)**

Proposed Change:

2 h) **Nature and source of the information to be relied upon**

The nature and source of any relevant information that is to be relied upon during the valuation process and the extent of any verification that shall be undertaken shall be agreed and recorded.

Reason: The proposed change results from the Board's project to provisions in the IVSs relating to the valuer's reliance on information.

13. **IVS 102 Implementation 1**

Proposed Change:

General Principle

1 Valuation assignments shall be conducted with regard to those principles set out in the IVS Framework that are appropriate for the intended purpose for which the valuation is required. ~~in this standard and the terms and conditions set out in the scope of work~~

Reason: While the assignment should be undertaken in accordance with the Scope of Work, the Scope of Work should also be suitable for the intended purpose, and para 4 of IVS 102 provides that the terms in the Scope of Work should be changed if it transpires that those originally agreed would not provide a credible valuation result. The proposed change removes a potential ambiguity that could suggest that the Scope of Work has to be followed regardless of whether subsequent investigation finds it to be inadequate or inappropriate.

14. **IVS 102 Implementation 2**

Proposed Change:

- 2 Investigations made during the course of a valuation assignment must be adequate having regard to the purpose for which the valuation is required and the *basis of value* to be reported. References to a valuation or valuation assignment in this standard shall include valuation reviews

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

15. **IVS 102 Implementation 4**

Proposed Change:

Insert new para 4:

- 5 When a valuation assignment involves reliance on information supplied by a party other than the valuer, consideration shall be given as to whether the information is credible or that the information may otherwise be relied upon without adversely affecting the credibility of the valuation opinion. In cases where the valuer has doubts as to the credibility or reliability of information, such information shall either not be used or the valuer's concerns highlighted in the report. In considering the credibility and reliability of information provided account shall be taken of matters such as:

- the purpose of the valuation,
- the materiality of the information to the valuation conclusion,
- the expertise of the source in relation to the subject matter,
- whether the source is independent of either the subject or the recipient of the valuation,
- the extent to which the information is in the public domain and
- the limits on the duty to investigate included in the scope of work.

(existing para 4 and all subsequent paras to be renumbered)

Reason: The proposed change results from the Board's review of provisions in the IVSs relating to the valuer's reliance on information. While blind acceptance of all information provided is not acceptable, the Board is also conscious of the need to avoid creating too onerous a duty on the valuer to verify every piece of information relied upon. Also, it must be recognised that many sources can be reasonably trusted without the valuer needing to verify the information, eg information on title from a lawyer, or information from government or public sources. The proposed new paragraph is intended to impose a duty to consider the credibility or reliability of information in the context of the valuation task, and should be read in conjunction with the changes proposed in IVS 101 and IVS 103.

16. **IVS 103 Reporting 1**

Proposed Change

- 1 This standard applies to all valuation reports or reports on the outcome of a valuation review whether printed on paper or transmitted electronically. References to a valuation or valuation assignment in this standard shall include valuation reviews. For certain asset classes or applications there may be variations from this standard or additional requirements to be reported upon. These are found in the relevant Asset or Valuation Application.

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

17. **IVS 103 Reporting 5**

Proposed Change

- 5 All valuation reports shall include reference to the matters listed below. Where the report is of a valuation review items (e), (f) and (m) in this list are not applicable. Items (a) to (k) in this list relate to matters that should be recorded in the scope of work (see IVS 101 *Scope of Work*). It is recommended that the scope of work be referred to in the report.

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

18. **IVS 103 Reporting 5 (h)**

Proposed Change

5 (h) Nature and source of the information relied upon

The nature and source of any relevant information relied upon in the valuation process, and the extent of any steps taken to verify that information ~~without specific verification by the valuer~~ shall be disclosed. In cases where verification was not undertaken a statement should be included reflecting the fact that the valuer had no reason to doubt the credibility or reliability of the information used.

Reason: The proposed change results from the Board's review of provisions in the IVSs relating to the valuer's reliance on information. It represents a corresponding change to that proposed to IVS 101 2(h). It also ties in with the final bullet point in the proposed IVS102 para 4, ie if the terms of the Scope of Work limit the investigations and verification required this should be explicitly disclosed in the report.

19. **IVS 103 Reporting 5 (I)**

Proposed Change

5(I) Valuation approach and reasoning

To understand the valuation figure in context, the report shall make reference to the approach or approaches adopted, the key inputs used and the principal reasons for the conclusions reached.

This requirement does not apply if it has been specifically agreed and recorded in the scope of work that a valuation report shall be provided without reasons or other supporting information.

Where the report is of a valuation review it shall state the reviewer's opinions and conclusions about the work under review, including supporting reasons.

Reason: The proposed change results from the Board's project to clarify the applicability of the IVSs to valuation reviews

20. **IVS 200 Businesses and Business Interests C25**

Proposed Change

~~C25 When the forecasted income or cash flow is expressed in nominal terms, ie current prices, nominal rates which include an inflation component should be used. When the forecasted income or cash flow is expressed in real terms, real rates which do not include an inflation component should be used. If a forecasted cash flow is expressed in nominal terms, a discount rate that takes into account the expectation of future price changes (inflation or deflation) should be used. If a forecasted cash flow is expressed in real terms, a discount rate that takes no account of expected price changes should be used.*~~

* (footnote) *For further information on discounted cash flow techniques see TIP1 Discounted Cash Flow*

Reason: The reference to including an inflation component in the existing wording is potentially ambiguous. If expected inflation is added to cash flows based on current prices it could be understood that inflation is being "included" but if a fixed future periodic cash flow is adjusted downwards to take into account the effect of expected inflation, inflation is "excluded". Both are "adjusting for inflation". Also, the current wording does not consider the possibility of needing to reflect expected deflation. The proposed rewording brings the commentary into line with the wording in TIP 1 Discounted Cash Flow, and a reference is included to this document.

21. **IVS 230 Real Property Interests 3**

Proposed Change

Include the following additional bulleted point to the matters to be considered:

- legal permissions or restrictions on the use of the property and any buildings

Reason: The Board has discussed examples of where there appears to be misunderstanding of legally permitted uses in the context of the highest and best use principle as applied to real property. It has agreed that the standard could probably be improved by adding the legally permitted use to the list of matters that should be considered.

22. IVS 230 Annexe – Historic Property

Proposed Change

Remove the annexe from the IVSs

Reason: The Board does not consider that there are sufficient unique requirements or considerations when valuing historic (real) property that warrant the inclusion of this annexe in the standards. It also provides only guidance, which under current IVSC protocols should be included in a TIP. The guidance provided is similar to that in the proposed TIP on Specialised Public Sector Assets that was issued in late 2012. One proposal is to remove this annexe to this future TIP, or it may be issued as a standalone paper providing information and guidance on some of the valuation criteria to be considered.

23. IVS 233 Investment Property Under Construction C10 and C11

Proposed Change

C10 A valuation of *investment property* under construction may be undertaken using ~~a growth-implicit model, which uses current cost and value inputs, or a growth-explicit model which uses estimated future cost and value inputs~~ either a nominal or a real cash flow model *. In either model, the objective is to estimate the value on the *special assumption* that the property is complete, from which appropriate deductions are then made in order to estimate the value of the property in its present condition. The more appropriate of these alternatives will be the one prevailing in the market for the class of property on the *valuation date*. Inputs from one model should not be used in the other, and the report should make clear which approach is being adopted.

C11 The exact valuation inputs used will vary with the valuation model being used but will normally include those listed in this section. The inputs will also vary depending on whether a ~~growth-implicit or growth-explicit model~~ is nominal or real cash flow inputs are being used, see para C10 above. Typical inputs include:

(a) Completed property

~~If a growth-implicit model is used, this will reflect the value of the *investment property* as if complete, ie~~ The value of the completed property may be based on current values on the *special assumption* its value on the assumption that on the *valuation date* it had already been completed in accordance with the current specification or ~~..If a growth-explicit model is used, this will reflect the projected value of the property upon completion, ie the expected value of the property on the date when it is anticipated to be complete. The choice will depend upon the availability of data to support either current or projected values and should also be consistent with the other cash flows reflected in the model. Care must also be taken to ensure that the discount rate used is commensurate with the valuation of the completed property, ie regardless of whether the completed value is based on current values or projected values the discount rate must also be derived on the same basis.~~

(b) Leasing

If lessees for the property after completion have still to be identified, allowance will need to be taken of the time and costs that it would be realistic to allow for stabilised occupancy to be reached, ie the period required to reach realistic long-term occupancy levels. The costs during this period could include fees, marketing, incentives, maintenance and unrecoverable service charges. ~~The income from anticipated future leases may be based on current market rents if a growth-implicit model is used or anticipated future rents if a growth-explicit model is used.~~ If there are leasing agreements in place that are conditional on the project, or a relevant part, being completed, these should be reflected in the valuation.

(c) Construction costs

The benefit of any work carried out prior to the *valuation date* will be reflected in the current value, but will not determine that value. Similarly, previous payments under the actual building contract prior to the *valuation date* are not relevant to current value. In contrast, the sums remaining to be paid under any binding construction contract in existence at the *valuation date* are often the best evidence of the construction costs required to complete. However, if there is a material risk that the contract may not be fulfilled, eg due to a dispute or insolvency of one of the parties, it may be more appropriate to reflect the cost of engaging a new contractor to complete the outstanding work. If there is no fixed price contract in place ~~and a growth-explicit model is being used, then~~ it may be appropriate to use prospective cost, ie reflecting the reasonable expectation of market participants on the *valuation date* of costs on the dates when they are likely to be incurred.

(f) Buyers profit and risk

(second para)

All significant risks should be identified and evaluated. Typical risks associated with any partially completed construction project will include variations in construction cost, finance costs and the construction programme. Additional risks associated with *investment property* under construction include fluctuations in the value of the completed project between inception and completion, and the time that will be required to secure lessees and a stabilised income. The risks associated with generating income from the property after completion should be identified and evaluated separately from the risks associated with completing construction. ~~If a growth-implicit model is used,~~ the valuation inputs will reflect current values and costs ~~so~~ the risk of these changing between the *valuation date* and the anticipated completion date should be evaluated. ~~If a growth-explicit model has been used~~ the valuation inputs are based on prospective values and costs, the risk of those projections proving to be inaccurate should be evaluated.

* (footnote) *For further information on nominal versus real discounted cash flow techniques see TIP1 Discounted Cash Flow*

Reason: The terms “growth implicit” and growth explicit” were used in the Exposure Draft of TIP 1 on DCF. However, it was clear from the responses to that ED that these terms are not widely understood. Also, the existing text made no reference to “nominal” and “real” DCF models which are discussed in the published TIP1. Some confused the concept of growth explicit and implicit inputs with real and nominal inputs although this is incorrect as growth is not synonymous with inflation. The original consultation on the 2010 Guidance Note upon which IVS 233 is based revealed that in some markets the practice is to use current values and

costs as inputs into the calculation of the value of IPUC and in others projected values and costs are the norm. From a standards' perspective either is acceptable providing there is consistency across all inputs in the model. Given that TIP 1 has now been developed and published the Board believes that there is no need to label different types of input beyond the broadly understood categories of nominal and real and is proposing the changes to bring consistency with the published TIP 1.

It should also be noted that IVS 233 is under review as part of the on-going Investment Property Project. These currently proposed changes deal only with inconsistencies with TIP1.

24. **IVS 300 Valuations for Financial Reporting 10**

Proposed Change

10 The report shall also contain any information that the reporting entity is required to disclose about the valuation by the relevant Financial Reporting Standards. Examples of disclosures required about fair value measurements include methods and significant assumptions used in the measurement and, or whether, the measurement was determined by reference to observable prices or recent market transactions. Some standards also require information about the sensitivity of the measurement to changes in significant inputs.

Reason: To clarify that only valuation disclosures required to be made by the entity need to be included in the valuation report because an entity is required to make disclosures under Financial Reporting Standards in relation to many other matters.

25. **IVS 300 Annexe – Property Plant & Equipment in the Public Sector:**

Proposed Change

25. Remove the annexe from the Standards

Reason: It is considered that the guidance on the requirements of the International Public Sector Accounting Standards (IPSAS) in this annexe is more properly included in the emerging guidance on the valuation of Specialised Public Service Assets. IVS 300 is intended to be applicable regardless of the accounting standards for which the valuation is being prepared and therefore there is no logical reason why the IPSAS should be specifically highlighted rather than any other set of “non IFRS” accounting standards. The Board’s attention has also been drawn to the fact that the current annexe incorrectly implies that the IFRS Fair Value principle is applicable under IPSAS.