Financial Accounting Standards Board Norwalk, Connecticut

By email to director@fasb.org

5 March 2007



Dear Sir,

Invitation to Comment: Valuation Guidance for Financial Reporting

File Reference: 1520-100

The IVSC welcomes the opportunity to respond to the Invitation to Comment (ITC): Valuation Guidance for Financial Reporting. We have structured our response in three parts:

- (1) General Comments
- (2) Responses to the specific questions raised in the ITC
- (3) Background on the IVSC and its current restructuring proposals included as an appendix to the letter.

General Comments

The IVSC welcomes the publication of the ITC which it believes will help raise awareness of the critical importance of rigorous valuation standards and guidance to financial reporting. At the IVSC meeting with FASB in March 2006, discussion concentrated on the role of the IVSC and the increased use of fair value measurement in financial reporting worldwide. Both IVSC and FASB agreed that as fair value measurement becomes more prevalent in financial statements, valuations that follow generally accepted valuation principles and valuation practice prepared by qualified valuation professionals would be not only needed, but are essential.

The pressure for global convergence in standards and regulatory systems from users of financial information, regulators and others continues to grow, with many jurisdictions committing to convergence of international standards. In February 2006 the International Accounting Standards Board (IASB) and the FASB published a Memorandum of Understanding reaffirming their commitment to the convergence of US generally accepted accounting principles (GAAP) and the International Financial Reporting Standards (IFRSs) and to their shared objective of developing high quality, common accounting standards for

use in the world's capital markets. The convergence work programme includes a project on fair value measurement.

The FASB has issued Statement of Financial Accounting Standards No. 157 Fair Value Measurements (SFAS 157). SFAS 157 establishes a single set of guidance for all fair value measurements in US GAAP.

In November 2006, the IASB published a discussion paper setting out its preliminary views on providing consistency in the measurement of fair value, when already prescribed under existing IFRSs. Consistent with its commitment to the convergence of IFRSs and US GAAP, the IASB decided to use the US standard as the starting point for its own deliberations.

SFAS 157 does not seek to establish valuation standards nor to provide detailed guidance on 'how to' perform a fair value measurement. Indeed in the exposure draft issued during the development of SFAS 157, the FASB acknowledged that the requirements of the standard should be applied together with application valuation standards and generally accepted valuation practices.

The IASB and the FASB are working towards not just a common set of standards but one set of **consistently applied** global standards for measuring and reporting on companies' financial results.

The IVSC is committed to the development of a single set of global standards and requirements for the valuation of all assets and liabilities. A clear set of internationally recognized and accepted valuation standards, consistent approaches, methodologies and definitions would eliminate the need for constitutents to consider guidance in multiple national standards. The IVSC both invites and urges the international valuation profession to work towards the establishment of international standards that would avoid the need for future 'convergence' of various national standards and professional requirements at a later date.

IVSC RESPONSES TO QUESTIONS POSED IN THE ITC

Question 1 - Is There a Need for Valuation Guidance Specifically for Financial Reporting?

The IVSC supports the need for a set of valuation standards that are accompanied by sufficient interpretative and implementation guidance such that the standard is

understandable, operational, and capable of being applied consistently in similar situations. (see also answer to Q1(a)).

The IVSC does not support the need to set separate valuation standards for financial reporting (as distinct from any application guidance for a specific valuation purpose). The universal concepts, definitions and principles for valuation are the same, although there may be differences in their application and reporting. The navigation through the standards to determine the valuation and reporting bases for a particular purpose — e.g. for financial reporting or for lending purposes — and all matters relevant to it, must be clear and unambiguous.

Although the current IVSC standards include applications for financial reporting and other purposes, e.g. loan security, the principal driver for their creation and development of the valuation standards has always been the development of International Financial Reporting Standards. The IVSC seeks to work collaboratively with accounting standard setters. Recently IVSC has actively engaged with both IASB and FASB in responding to practical measurement issues arising in IAS40 *Investment Property* (and the International Valuation Standards are referenced in the Basis for Conclusions to IAS 40), IAS17 *Leases*, the FASB *Fair Value Measurement* draft and the IASB/FASB Measurement Round-tables. A member of IASB staff is an observer to the IVSC group developing guidance on the valuation of intangible assets.

In a number of countries, including for example the UK, Australia and New Zealand, where revaluation of fixed assets has been a feature of national accounting standards for many years, there has been a long tradition of collaboration between accounting and valuation standard setters. This interaction between the valuation and accounting standard setters helps to ensure a common conceptual understanding and expose any differences in terminology thus assisting in the robust and consistent application of both accounting and valuation standards.

Question 1 (a) – Should valuation guidance include conceptual valuation guidance, detailed implementation guidance, or a combination of both?

Both the IASB and the FASB are working towards the development of principles-based standards. Valuation standards should be developed on the same basis. However, an approach to setting standards that places more emphasis on principles will not eliminate the need to provide interpretative and implementation guidance for applying those standards. Some amount of implementation guidance is needed for entities to apply principles-based standards in a consistent manner. Judgment will be required to decide how much guidance is

needed to achieve those objectives without providing so much guidance that the overall standard together with its implementation guidance becomes a collection of detailed rules.

The IVSC cautions against any suggestion that valuation standards should stipulate the use of specific models or techniques. Standards should focus on fundamental objectives of the valuation and best practice in procurement and reporting valuations in addition to developing the criteria to ensure that valuers are suitably independent, qualified and experienced. Countless valuation models have been developed in different sectors and this is a fruitful area of continuous academic research. The models used by the valuer must reflect the behaviour of market participants. Markets are dynamic and techniques of measurement evolve. Bodies such as IVSC, IASB and FASB may be a catalyst for debate or research on technique, but we would oppose any restriction on a professional valuer's ability to select the most appropriate method or technique to achieve the objective of the standards in any particular situation.

Question 1 (b) – What should be the duration of any valuation guidance setting activities?

The view of the IVSC, borne out of our experience from over 25 years, is that standard setting is a continuing process and not a specific project. The markets and the issues that have to be addressed are constantly evolving.

Question 2 – What level of participation should existing appraisal organisations have in establishing valuation guidance for financial reporting?

The IVSC has recognized, in its Restructuring Proposals (see appendix a), that the functions of a quality valuation standard setter include an independent decision-making structure, adequate due process, and sufficient technical capabilities to develop high-quality standards. The IVSC has concluded that it cannot fulfil all these criteria as a membership-based organization and is recommending that the adoption of a structure for the setting of valuation standards that is similar to that of the IASB and the FASB.

The IVSC considers that membership based appraisal organizations have an important advisory role and should be given extensive opportunities for participation and input into the process of standard setting but should not be the principal standard setters.

Question 3 – What process should be used for issuing valuation guidance for financial reporting?

Valuation is a discipline and specialism with its own experts. The IVSC considers it essential that valuation standards are prepared, endorsed and followed by valuation experts. The necessary guidance should be set out in a separate valuation standards and should be written so that it can be followed by valuation specialists rather than laymen. However the IVSC also recognizes the importance of a due process establishing consultative procedures in order to gain the input and views from all parties interested in the development of high quality valuation standards. Dialogue with representatives of the accountancy profession would be of particular importance to ensure that there is consistency in applying valuation principles in an accounting context.

The IVSC recommends that the process of setting valuation standards and guidance for financial reporting be undertaken at the international level to ensure consistency and reduce the need for future 'convergence' of various national standards and professional requirements at a later date.

It appreciates however that in the interim whilst differences remain between IFRSs and US GAAP any international pronouncements will need to be reviewed for consistency with US requirements and possibly issued as US national standards.

The Appraisal Foundation in the U.S. is an independent standard setter and publishes the Uniform Standards of Professional Appraisal Practice (USPAP). Real estate appraisals used in conjunction with federally related transactions are required to be performed under USPAP. USPAP also contains standards for personal property and business appraisal. The IVSC is aware that at least four other organizations in the U.S. publish or are seeking to publish business valuation standards - the American Institute of Certified Public Accountants, the American Society of Appraisers, the National Association of Certified Valuation Analysts, and the Institute of Business Appraisers). The diversity of the groups that provide valuation guidance coupled with the lack of a 'codified' set of standards creates the potential for confusion and inconsistent application of valuation practices.

The IVSC hopes that the valuation profession in the U.S. can come together to support one widely accepted set of valuation standards and guidance although it appreciates this may take some time and an interim solution may need to be found. In the meantime the IVSC would encourage all valuation groupings within the U.S. to support and participate in the process of setting international standards.

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Question 4 - Should the process of valuation guidance be on an international

or national level?

Financial reporting has seen a period of unprecedented change in the last few years. The

IFRS have become the framework into a basis for financial reporting in more than 90

countries. In February 2006 the IASB and the FASB published a Memorandum of

Understanding reaffirming their commitment to the convergence of US GAAP and IFRSs.

There are easily identifiable advantages to bringing financial reporting rules together around

the world. Yet this process brings with it significant challenges arising from the application and

interpretation of the same standards in different jurisdictions. This requires international

cooperation and co-ordination of a degree never before necessary to ensure consistency of

application across the world.

Against this background it would seem illogical not to develop valuation standards and

guidance for financial reporting on an international level. If the process were to take place on

a national level the danger of the inconsistent valuation and thus reporting of assets and

liabilities would be very real.

The IVSC welcomes the opportunity to respond to this Invitation to Comment and looks

forward to participating in the roundtable to be held in April.

Yours faithfully,

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Background Information

The International Valuation Standards Committee (IVSC)

The IVSC was created in 1981 and published the first set of International Valuation Standards (IVS) in 1985. In serving the public interest, the IVSC aims to develop high quality international valuation standards that are understandable, clear and capable of consistent application, thereby enhancing the quality and uniformity of valuation practice worldwide. From its inception, the IVSC worked towards harmonising national valuation standards by developing standards at an international level that could serve as a model on which national standard setters could base their own standards. These efforts have contributed to raising the level of valuation standards worldwide and reducing the number of differences. However the growing adoption of international standards in other related areas, most notably the International Financial Reporting Standards promulgated by the International Accounting Standards Board, led to the demand for a set of international valuation standards to support the measurement requirements of such other standards. Increasingly, the IVS are seen as a body of standards in their own right rather than as a framework establishing a basis of convergence among national standards.

The IVS are now having a profound impact on the valuation standards of many countries. In some countries IVS have been incorporated into law, in others adopted by national institutes/societies while at the same time international users and providers of valuation services are also demanding adherence to IVS.

For example:

- Countries such as Australia, New Zealand, Romania, Turkey have adopted IVS as their national valuation standards
- National standards are being harmonized to the IVS
 - the Royal Institution of Chartered Surveyors (RICS) in the UK incorporates much of the IVS in the RICS Appraisal and Valuation Standards
 - the Appraisal Institute (AI) incorporates IVS into the AI's Standards of Professional Practice
 - in January 2007, the Board of the American Society of Appraisers endorsed the use of IVS outside of the US by its members
- Companies reporting under the International Financial Reporting Standards (IFRS) are recommended to apply IVS for valuations under IAS 16 and IAS 40 by, among others, the European Public Real Estate Association and in the illustrated model financial statements published by both Ernst & Young and Deloitte.

Although IVSC was founded originally by professional organisations concerned primarily with the valuation of property, it has become clear to IVSC that although real estate has properties that distinguish it from other classes of assets and liabilities, the fundamental principles of valuation, whether they be best practice in procurement and reporting, or in the techniques adopted, are common to most assets and liabilities. Differences in the characteristic of an asset or a market will affect the way in which exchanges take place but do not alter the fundamental economic principles of measurement. The International Financial Reporting Standards (IFRS) around business combinations, intangible assets, employee options and financial instruments highlight the need for more regular valuations of assets and liabilities and the IVSC is broadening its scope to include input from valuers active in other markets. The American Society of Appraisers has been an IVSC member since 1994; the Canadian Institute of Chartered Business Valuators was welcomed into membership in 2006.

The IVSC has put together a team of experts to draft a valuation standard and implementation guidance to address one of the key areas in which the IASB requires fair value guidance – that of measuring the fair value of intangible assets, such as brands, licences, patents, know-how, customer contracts and customer relationships. The IVSC's team is drawn from across the world and includes both valuation and accounting experts. This group is expected to report during second guarter 2007.

Restructuring the IVSC

As greater attention has been focused on IVSC standards, greater pressure has been placed on the IVSC standard-setting structure and process. In January 2007 the IVSC published proposals to restructure the organization seeking to improve the quality of its structure and process to ensure that its future standards are of the highest possible quality.

The restructuring proposals:

- recognize that the functions of a quality international valuation standard setter include an independent decision-making structure, adequate due process, and sufficient technical capabilities to develop high-quality international standards.
- make it possible for all key players to be involved in the process of valuation standard setting through advisory councils. The IVSC will cease to be exclusively an organization of national professional valuation institutes.
- recognise the need to protect the public interest by assisting in the development of high quality practices by the world's valuers and the responsibility to assist the development of the profession in developing countries.

The IVSC restructuring proposals are available to view on the IVSC website - www.ivsc.org

The IVSC hopes to act as a catalyst in initiating an opportunity to lay the blueprint for achieving the ultimate desired structure for an international body serving the whole of the valuation profession. It both invites and urges the valuation profession to demonstrate its commitment to development of a global organization that works to protect the public interest by encouraging high quality practices by the world's valuers. In the area of the setting of international valuation standards, the IVSC believes this proposal is a starting point in a transition over the next 5 years to a worldwide, self-sustaining standard setter founded upon an independent, autonomous decision-making body supported by staff able to address valuation issues pervasive to most nations.

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