

Panel: Current Fair Value Publications & Pronouncements

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Agenda

- International Valuation Standards Council
 - Greg Forsythe
- American Institute of Certified Public Accountants
 - Yelena Mishkevich
- The Appraisal Foundation
 - Tony Aaron
- Financial Accounting Standards Board
 - Ben Couch
- After Lunch - Q&A





IVSC Publications and Pronouncements

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IVSC Professional Board Chair
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INTRODUCTION

- Comments from the Regulators
- IFRSs across the G20
- IVSC Standards Board
 - IVS and TIPs/Example Projects
- IVSC Professional Board
 - Valuation Professional Organizations/Advisory Forum
 - Example Projects
- Wrap-up



Regulators Continue to Weigh In: Comments from the SEC Illustrate the Concern (from Dec 2011)

- *“The broadening application of fair value ...and the 2008 financial crisis have cast the spotlight on valuation professionals. At last count, valuation professionals in the US can choose among five business valuation credentials available from four different organizations, each with its own set of criteria for attainment..... Risks created by the differences in valuation credentials that exist today range from the seemingly innocuous concerns of market confusion ...to the more overt concerns of objectivity of the valuator and analytical inconsistency.”*



Comments from the SEC Illustrate the Concern (continued)

- *“One potential solution to consider is whether there should be, similar to other professions, a single set of qualifications with respect to education level and work experience, a continuing education curriculum, standards of practice and ethics, and a code of conduct. One could also contemplate whether a comprehensive inspection program and a fair disciplinary mechanism should be established to encourage proper behavior and enforce the rules of the profession in the public interest.”*



Use of IFRSs for public companies in G-20 countries

IFRSs required

- Argentina (2012)
- Australia (2005)
- Brazil (2010)
- Canada (2011)
- France (2005)
- Germany (2005)
- Italy (2005)
- Korea (2011)
- Mexico (2012)
 - Required for domestic listed companies
- Saudi Arabia
 - Required for certain domestic listed companies
- South Africa (2005)
- Turkey (2005)
- United Kingdom (2005)

IFRSs permitted

- China
 - Permitted for HK listed companies, also convergence of China GAAP with IFRSs
- Japan
 - Permitted in 2010 for certain companies, considering a requirement in 2015 or 2016
- India
 - Permitted in 2011 for domestic listed companies, considering a requirement, date TBD

IFRSs not allowed

- United States (Except foreign private issuers may use IFRSs)
- Indonesia
- Russia

Standards Board Publications

- International Valuation Standards
- TIP 1 – Discounted Cash Flow
- TIP 2 – Cost Approach for Tangible Assets
- TIP 3 – Valuation of Intangible Assets
- Various projects in progress

Standards Board Example Projects I

Project	Reason	Status
Extractive Industries	Diversity of practice, particularly in Asia where regulators have expressed significant concerns	Final deliverable TBD. Discussion paper issued July 2012. Comment period through October 2012
Valuation Uncertainty	G20 identified lack of disclosure of uncertainty as a contributor to financial instability	Discussion Paper issued 2010. Draft guidance anticipated late 2012
Derivative Valuation Methods	Lack of understanding of valuation methods for financial instruments adversely affects investor confidence and market efficiency	TIP in early stage of development
Investment Property	Adoption of IFRS is bringing requirement to value investment property to new markets resulting in diversity	Discussion Paper due November 2012



Standards Board Example Projects II

Project	Reason	Status
Valuation of Liabilities	Increasing need to value non financial liabilities leading to diversity of practice	Project in early stage, developing a Discussion Paper
Valuation Reviews	Consider need for changes to Standards to clarify procedures for valuation reviews	Project in early stage of development
Valuers' Reliance on Information	Need for clarity regarding duties of valuation professional when relying on information provided by client or a third party	Project in early stage of development



IVSC Professional Board

The IVSC Professional Board is responsible for promoting the development of the valuation profession around the world. Working in conjunction with the valuation professional bodies in membership of the IVSC it promotes common professional, education and ethical practices for professional valuers, and seeks to encourage the development of the profession in sectors or markets where there is currently no professional infrastructure.



Valuation Professional Organizations Advisory Forum

The Valuation Professional Organizations (VPOs) in membership of the IVSC are automatically members of the Advisory Forum. The Forum has two objectives:

1. To provide the facility for VPO members of the IVSC to meet and discuss matters of common interest.
2. To give VPO members an opportunity to provide advice and counsel to the IVSC Boards.

The current chairman of the Forum is John Martin of the Australian Property Institute



Valuation Professional Organizations Advisory Forum (cont.)

- There are 50+ VPOs, including these 4 organizations in North America:
 - American Society of Appraisers
 - Canadian Institute of Chartered Business Valuators
 - The Appraisal Institute
 - Appraisal Institute of Canada
- The Forum now has a Leadership Group (including these 4 VPOs) focused on enhancing connectivity between the Professional Board and the VPOs.
- The Appraisal Foundation (TAF) – although not a VPO is a sponsor of the IVSC and active in the Forum & Leadership Group. The IVSC and TAF also have an MoU in place to work closely together.
- This should enable greater awareness of global valuation needs, and the ability to leverage resources.



Professional Board Example Projects

Project	Reason	Status
Code of Ethical Principles for Professional Valuers	Expectations template to assist in developing the profession	Document published December 2011
Professional Valuer Competency Framework 1	To promote awareness of valuation profession and attributes of a professional valuer.	Principles-based framework finalized September 2012
Fairness Opinions	Evidence of diversity in practice in different states and world regions, notwithstanding different regulatory regimes	Guidance paper – Exposure comment letters under review
The Role of the Professional Valuer in the Audit Process	Guidance for professional valuers who may be engaged to provide specialist advice to either an auditor or a reporting entity	Guidance paper exposure issued June 2012. Comment period closed September 15



Professional Board Example Projects

Project	Reason	Status
Professional Valuer Competency Framework 2	Develop sample common curriculum	Project in early stage of development
Illustrative Examples	Need to develop practical illustrations of principles in IVS to different situations to aid understanding and application	Project in early stage of development. It is anticipated that this will be a rolling project

Wrap-up

- Get Involved
- www.ivsc.org
- Subscribe to IVSC E-Newsletter
- Questions?



AICPA Fair Value Publications

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INTRODUCTION

- Accounting and Valuation Guide Series
 - Process Overview
- Accounting and Valuation Guides under development:
 - *Assets Acquired to Be Used in Research and Development Activities*
 - *Valuation of Privately-Held-Company Equity Securities Issued as Compensation*
 - *Testing Goodwill for Impairment*
 - *Business Combinations*
- New Audit Guide under development - *Special Considerations in Auditing Financial Instruments*



Accounting and Valuation Guide Series - Process Overview

- Each project task force consists of:
 - *Valuation specialists*
 - *Auditors*
 - *Preparers*
- Accounting guidance in each guide is reviewed by the Financial Reporting Executive Committee (FinREC), which is the senior technical body of the AICPA authorized to speak for the AICPA in the areas of financial accounting and reporting
- AICPA Forensic and Valuation Services (FVS) committee is actively involved
- Working draft of each guide is released for informal feedback
- Task Forces consider and address feedback received
- Major changes in response to comments are discussed with FinREC
- Guides are issued as final



Assets Acquired to Be Used in Research and Development Activities Guide

- Original practice aid issued in 2001
- Working draft released for feedback in November 2011 (comment period ended May 24, 2012)
- Final guide is expected to be issued in 2013



Assets Acquired to Be Used in Research and Development Activities Guide (cont'd)

Important changes include:

- Eliminated the concept of *core technology*. Introduced new concepts of *enabling technology* and *technology migration*
- Expanded methodological emphasis:
 - Added *Relief From Royalty (RFR)* and *Decision Tree Analysis (DTA)* examples
 - Did not foreclose on the use of *other methods* not demonstrated
- Added discussion and interpretive guidance on the DRAT vs. EPVT1 and EPVT2
- Revised discussion of PFI analysis
- Added a new comprehensive example



Valuation of Privately-Held-Company Equity Securities Issued as Compensation Guide

- Original practice aid issued in 2004
- Working draft released for feedback in March 2011
- In response to comments, developed **new chapter** on “Inferring Value From Transactions in a Private Company’s Securities,” and **new Q&As** which clarify the points where there was most confusion in practice
- New chapter along with the latest version of the guide were released for comment in August 2012 (comment period ended October 1, 2012)
- Final guide is expected to be issued in 2013



Valuation of Privately-Held-Company Equity Securities Issued as Compensation Guide (cont'd)

Important changes include:

- New chapter on private and secondary market transactions, as well as explicit discussion of the "backsolve" method
- New chapter on control and marketability
- New discussion and Q&As on the difference between the fair value of the enterprise, considering an immediate transaction, and the enterprise value used for estimating the fair value of the securities within the enterprise, considering the cash-flows under current ownership and the investors' required rate of return
- New discussion and Q&As on estimating the fair value of debt for purposes of valuing the equity securities within the enterprise
- Introduction of hybrid methodologies, which provide a bridge between OPM and PWERM when one or more exits can be explicitly modeled but others are less certain



Testing Goodwill for Impairment Guide

- Brand new guide which provides accounting and valuation guidance for goodwill impairment testing
- Working draft released for informal feedback in November 2011 (comment period ended May 24, 2012)
- Working draft
 - Addressed practice issues in Step 1
 - Provided an illustration of Step 2
- In response to comments, developed **new chapter** which discusses and illustrates the **optional qualitative assessment**; working draft of new chapter is expected to be released in 2012
- Final guide is expected to be issued in 2013



Testing Goodwill for Impairment Guide (cont'd)

Important provisions include:

- Guidance on Qualitative Assessment
- Examples of the approaches and techniques that are used most often in practice for measuring the fair value of reporting units for Step 1 goodwill impairment test:
 - DCF example
 - Examples of the Market Approach using:
 - Guideline Public Company Method and
 - Guideline Transaction Method
- Guidance on assets that are shared by reporting units
- Guidance on market participant assumptions



Business Combinations Guide

- This project is in a very early stage
 - The task force has been formed
 - Currently deliberating the scope
- Expect to actively start working on this project when other guides are close to final
- The task force will coordinate its efforts with the Appraisal Foundation's project on Contingent Consideration



Special Considerations in Auditing Financial Instruments Audit Guide

- Based on International Auditing Practice Note (IAPN) 1000 by the same title published by the International Federation of Accountants (IFAC) in Dec. 2011
- The purpose is to provide:
 - Background information about financial instruments; and
 - Guidance on audit considerations relating to financial instruments
- Applicable to both financial assets and financial liabilities
- Guidance on valuation - more relevant for financial instruments measured or disclosed at fair value
- Expected to be issued this winter



The Appraisal Foundation's Financial Reporting-related Publications and Pronouncements

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Valuation Principal, Ernst & Young LLP



INTRODUCTION

- The Appraisal Practices Board of The Appraisal Foundation
- The Valuations in Financial Reporting Task Force/Steering Committee (“VFR”)
- The Working Groups
 - Contributory Assets
 - Customer-related Intangible Assets
 - Control Premiums in Financial Reporting
 - Contingent Consideration
- Future Directions



The Appraisal Practices Board of the Appraisal Foundation

- Officially formed by the Appraisal Foundation Board of Trustees on July 1, 2010
- Charged with “the responsibility of identifying and issuing opinions on Recognized Valuation Methods and Techniques, which may apply to all disciplines within the appraisal profession
- Seven Board members, Gary Taylor, Chair, Jay Fishman, Vice-Chair
- VFR Task Force/Steering committee placed under the auspices of the APB
- APB Board member Alok Mahajan (Business Valuation-KPMG) assigned as liaison between APB and VFR TF.
- “Monographs” resulting from Working Group efforts are now being referred to as “Valuation Advisories” from the APB
- The CAC Monograph is “Valuation Advisory #1”



The Valuations in Financial Reporting Task Force/Steering Committee (“VFR”)

- Co-chaired by Jay Fishman (current Vice-Chair of the Appraisal Practices Board) and Carla Glass (former Chair of the Appraisal Standards Board)
- Broad group of members, including Big-4 Firms, major valuation and appraisal Firms, other Appraisal Foundation representatives
- Utilizes topical list developed by a sub-committee of the Appraisal Issues Task Force (“AITF”), a group which serves as a forum for issue identification and discussion, as a basis for Working Group topics (See *“Illustrative Valuation Issues, 2/2/2006, as developed by the Appraisal Issues Task Force (AITF)”* on the Appraisal Foundation Website under the Financial Reporting tab)
- Meets by teleconference periodically to provide updates on Working Group progress, discuss working future group topics, and other valuation matters related to financial reporting valuation (e.g. April 23rd roundtable)



The Working Groups: Contributory Asset Charges

- Working group assembled in late 2006 and concluded its work in 2010
- Most significant takeaways:
 - First publication dedicated to this topic
 - Separately treated identification of contributory assets, calculation of contributory asset charges, and discount rate stratification
 - Reflects input from many commenters
 - Provides a comprehensive example and toolkit
 - Dealt with several controversial issues:
 - Dual or simultaneous application of multi-period excess earnings methods
 - Methodological considerations for various contributory asset categories
 - Introduces “Average Annual Balance” and “Level Payment” methods for fixed asset CACs
 - Special considerations for issues such as practical expedients, cost approach-valued intangibles, elements of goodwill, time effects on CACs, etc.
- Current Status: Complete and regularly utilized in the valuation profession



The Working Groups: Customer-related Intangible Assets

- Working group assembled in late 2008, activities ongoing:
 - Discussion Draft Issued in June 2012
 - Comments were due by August 31, 2012
- Dealing with multiple issues:
 - Sets forth several methods:
 - MPEEM
 - Distributor method
 - “With and without” method
 - Cost approach
 - Provides guidance on controversial issues, such as:
 - Attrition
 - Backlog
 - Deferred Revenue
 - Overlapping customers
 - Pre-existing relationships
- Current Status:
 - Group to reconvene and consider comments
 - Exposure draft and final document to be issued in the future



The Working Groups: Control Premiums in Financial Reporting

- Working group assembled in mid 2009, activities ongoing
- Focused entirely on control premiums in the context of fair value measurement for financial reporting
 - Impairment
 - Investment company holdings
 - Step transactions
- Introduces concept of “Market Participant Acquisition Premium” (“MPAP”) as an alternative to the notion of a traditional control premium
- Quantification focused on:
 - Cash flow impacts, i.e. growth, margins, efficiencies
 - Reduced risk, i.e. increased size, better access to capital, enhanced mix of financing
- Recognizes benefits of observed control premium data, but cautions against sole reliance-consider qualitative factors
- Current Status: Discussion Draft/Exposure Draft to be issued in the future



The Working Groups: Contingent Consideration

- Scope of work document developed by VFR Task Force
- Scope of work document reviewed and approved by the APB
- Scope of work document on Contingent Consideration posted on The Appraisal Foundation website
- Call for Volunteer “Subject Matter Experts” (“SME”) published and extended through September 6, 2012
- Charter will be similar to other working groups:
 - Gather data on current practice
 - Identify types of Contingent Consideration
 - Investigate various valuation methodologies and their strengths/weaknesses
 - Recommend best practices and possible alternatives
 - Develop a document for reference by users
- Group would be expected to commence efforts Fall/Winter 2012



Future Directions

- More Working Groups
- Business Valuation and Personal Property committees
- Additional Forums
- Future added guidance on “Recognized Methods and Techniques” through the Appraisal Practices Board
- Coordination and cooperation with other organizations (e.g. IVSC, ASA, AICPA, RICS, FASB, SEC, PCAOB, and many others)



Recent Publications - FASB

Ben Couch, ASA
Ernst & Young LLP



Developments in Impairment

- ASU 2011-08 *Intangibles—Goodwill and Other, Testing Goodwill for Impairment* was issued in September 2011
- ASU 2012-02 *Intangibles—Goodwill and Other, Testing Indefinite-lived Intangible Assets for Impairment* was issued in July 2012



Developments in Other Financial Reporting

- Proposed ASU, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities* issued in May 2010
- Proposed ASU, *Leases* issued in August 2010. Board recently unanimously agreed to re-expose
- Proposed ASU, *Investment Property Entities* issued in October 2011
- Proposed ASU, *Disclosures about Liquidity Risk and Interest Rate Risk* issued in July 2012
- *Private Company Decision-Making Framework: A Framework for Evaluating Financial Accounting and Reporting Guidance for Private Companies* issued in July 2012



Developments in Other Fair Value-related Financial Reporting

- Project on reducing fair value disclosures related to Level 3 fair value measurements for nonpublic entities
- EITF Issue 12-E, *Accounting for Fair Value Information That Arises after the Measurement Date and Its Inclusion in the Impairment Analysis of Unamortized Film Costs*
- SFAS 141(R) post-implementation review
- IFRS educational material on IFRS 13

