

PRACTICE STANDARD NO. 120

VALUATION REPORTS

Scope of Work Standards and Recommendations

1. A Valuation Report is defined as **“any written communication containing a conclusion as to the value of shares, assets or an interest in a business, prepared by a Valuator acting independently.”** A Valuation Report does not include work product that is in the process of being completed that is provided to a client or knowledgeable third party in circumstances where each of the following conditions are met: (i) the work product is clearly marked as being in draft form and subject to change; (ii) the work product is issued for the purpose of obtaining comment, instruction, confirmation or other information required to complete the Valuation Report; (iii) the Valuator knows, or reasonably ought to know, that the intended reader(s) does not intend to rely on the work product or distribute the work product to a third party who may in turn rely on such work product; and (iv) the Valuator has a reasonable expectation at the time the work product is provided that a Valuation Report will be completed and issued in due course.
2. At a minimum, for all Valuation Reports the following procedures set out in bold characters must be performed. “Recommendations” are not mandatory, but encouraged. “Explanatory comments” provide additional guidance in applying the specific provisions of the Standard.
3. **General Standards**
The following General Standards apply to all three types of Valuation Reports (i.e. Comprehensive, Estimate and Calculation Valuation Reports):
 - A. **The Valuator shall obtain clear instructions from the person requesting the valuation, including the type of Valuation Report required.** (Recommendation: the Valuator should assess the necessity of obtaining an engagement letter in each circumstance and, if no engagement letter is obtained, consider documenting the nature of the instructions received from the person requesting the valuation, including the type of Valuation Report required.)
 - B. **The work shall be performed by a person or persons having adequate technical training and proficiency in financial analysis and/or business valuation concepts, principles and techniques, with due care and with an objective state of mind.**
 - C. **The work shall be adequately planned and properly executed. If assistants are employed, they shall be properly supervised.**
 - D. **Sufficient evidence shall be gathered by such means as inspection, inquiry, computation and analysis to ensure that the Valuation Report and the conclusion contained therein are properly supported. When determining the**

extent of evidence necessary to support the Valuation Report, Valuators shall exercise professional judgment, considering the nature of the valuation, the type of Valuation Report being provided (i.e. Comprehensive, Estimate or Calculation Valuation Report) and the use to which the Valuation Report will be put. (Explanatory comments: it is expected that the scope of review will be more comprehensive for a Comprehensive Valuation Report and progressively less comprehensive for an Estimate Valuation Report and a Calculation Valuation Report. It is a matter of professional judgment as to the amount of review appropriate for the type of Valuation Report being provided.)

- E. **The Valuator shall perform the work in accordance with the Practice Standards and Code of Ethics of the Canadian Institute of Chartered Business Valuators.**
- F. **When access to essential information is denied by the client or some other party, or is otherwise unavailable to the Valuator, any conclusion expressed by the Valuator in respect of such valuation shall be qualified and the limitation(s) on the scope of work clearly set out in the Valuation Report.**

4. **Specific Standards**

The following Specific Standards apply to Comprehensive and Estimate Valuation Reports: (Recommendation: Valuators should consider applying the Specific Standards to Calculation Valuation Reports.)

- A. **When planning the extent of the scope of work for a particular engagement, the Valuator shall obtain:**
 - I. **Sufficient understanding of the subject of the valuation;** (*Explanatory comment:* depending on the type of Valuation Report being provided, the Valuator should obtain and review material documentation, including agreements, contracts, letters of understanding, letters of intent and correspondence, which bear on the subject of the valuation)
 - II. **Sufficient understanding of the underlying business operations;**
 - III. **Sufficient financial information relating to past results, future prospects and present financial position;** (*Recommendation:* depending on the type of Valuation Report being provided, the information to be obtained and analyzed will include prior years' operating results and cash flows, a current balance sheet, and future oriented financial information such as budgets, forecasts and projections)
 - IV. **Sufficient understanding of the relevant industry(s) in which the underlying business operates;** (*Recommendation:* depending on the nature of the mandate and on the type of Valuation Report being provided, this analysis might consider the following:
 - a. Critical success factors;
 - b. Competitors and their respective market shares;
 - c. Industry regulations;
 - d. New developments;
 - e. Environmental issues;
 - f. Trading volumes and price ranges of publicly traded shares; and

- g. Comparable market transactions)
- V. **Sufficient information relating to the general economic conditions affecting the underlying business operations.** (Explanatory comment: such information might normally consist of selected rates of return, inflation rates and other general economic indicators)
- B. **In performing the business valuation, the Valuator shall determine the appropriate valuation basis and approach to be employed.** (Explanatory comment: the “valuation basis” refers to going concern or liquidation, whereas the “valuation approach” refers to income (earnings or cash flow methods), cost (adjusted net book value method) and market (comparable transactions method).)
- C. **The Valuator shall consider key valuation components and assumptions.** (Explanatory comment: the key valuation components might include the following:
 - a. Normalizing adjustments;
 - b. Capitalization rates;
 - c. Income tax issues;
 - d. Redundancy;
 - e. Minority and other discounts; and
 - f. Special purchasers.)
- D. **The Valuator shall consider the necessity of relying upon the work of a specialist,** for example real estate appraisers, engineers, or equipment appraisers. (Recommendation: if it is deemed appropriate to request the assistance of a specialist, the Valuator should obtain reasonable assurance concerning the specialist's reputation for competence and degree of independence.) (Explanatory comment: the appropriateness and reasonableness of the assumptions and methods used by the specialist are the responsibility of the specialist. Ordinarily, the Valuator may accept the specialist's judgment and work in this regard unless the report of the specialist, the Valuator's communication with the specialist, or the Valuator's knowledge of the business being valued, lead the Valuator to believe that the specialist's assumptions or methods are unreasonable in the circumstances.)
- E. **The Valuator shall determine the necessity of obtaining client representations in writing and, if possible, management representations from management or other representatives of the underlying business.** (Recommendation: such representations may be in letter format, and would normally include a general representation that the client/management:
 - a. Has reviewed a draft copy of the Valuation Report;
 - b. Is satisfied with the valuation concepts and approaches adopted; and
 - c. Does not have any information or knowledge which would reasonably be expected to materially affect the conclusion noted in the Valuation Report.)

October 7, 2010