

January 15, 2021
comments@ivsc.org

Mark Zyla, Chair, IVSC Standards Review Board
4 Lombard Street
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Dear Mark:
re: IVS Agenda Consultation 2020

Thank you for the opportunity to provide our views on the IVSC's Agenda Consultation 2020, laying out potential future topics for consideration within IVS.

We thank the IVSC's Standards Review Board (SRB) for its continued efforts on enhancing International Valuation Standards in order to achieve international consistency and a robust set of standards.

On behalf of CBV Institute our comments are as follows.

IVS Gap Analysis

Question 1.1: Do you agree with the current categorisation and timings of the topics contained in the IVS Gap Analysis and if not why?

Largely, yes. We agree with the timing proposed for all of the topics. The only 3 exceptions where we wish to make alternative suggestions are:

1. AVMs' – while we agree this should be a short term project, we believe AVMs do not necessarily need an IVS standard, but rather are best addressed by a Perspectives Paper at this stage. This is because we do not view AVMs to be valuations in and of themselves, but rather a tool (like any other) used in a valuation, and because we don't think there is sufficient consensus among users or valuers as to this topic. While technological disruption is a major trend, and we do agree that many users of AVMs may take these "valuations" at face value without always fully understanding the purpose, workings or limitations of the models

being used, all that is presently required as part of IVS is clarification that the outputs of AVMs are “calculations” that may not be compliant with IVS and that AVMs are a tool, rather than a “valuation”. To go any further and attempt to make AVMs IVS-compliant is potentially a slippery slope.

We do agree that IVS should contain an overarching valuation standard on valuation modelling requirements (or best practices) within IVS 105 *Valuation Approaches and Methods*. We agree that IVS should add language in IVS 105 to clarify that when a valuation model is used, the valuer must take responsibility for the output of the valuation model and keep appropriate records to suppose the selection of the model. We also believe the valuer should take responsibility for the appropriateness of the inputs and assumptions into the model. We also agree that more valuation modelling guidance (i.e. using the word “may” or “should”) can be included in specific sections of IVS (IVS 200 for business valuations, IVS 400 for tangible assets and IVS 500 for FI).

We want to draw to the SRB’s attention the question of whether the IVS is about providing standards for valuation conclusions, or whether the long-term view is that IVS should be broader – providing standards for valuation services? This should be made clear. We would suggest that a focus on valuation conclusions would be more appropriate, and that any related issues can and should be dealt with via Perspectives Papers.

2. Governance – we note that the topic of Governance (separate and apart from the ESG topic), is proposed to be addressed via a standard in the short term. While we are unsure what exactly is meant by “governance” and what is contemplated, we would be of the view that such a broad topic, with applicability well beyond the world of valuations, might best be dealt with via a Perspectives Paper (rather than a standard) at least initially, and perhaps in collaboration with other governance associations/bodies.
3. Internally generated intangibles – we note that this topic is proposed to be addressed via a standard in the short term. While we do agree that there is a market need for guidance on the criteria and types of internally generated intangibles that could be valued with sufficient confidence to enable an organization to disclose such amounts, due to the controversial nature of this topic, we believe it would be more prudent to “test the waters” and international reaction to this topic via a Perspectives Paper prior to developing a standard.

Question 1.2: Are there any other topics which you believe should be included or deleted from the IVS Gap Analysis and if so why? (Please state the relevant specialism, categorisation and timing for any proposed additional topics).

Nothing further to add. The list of topics in the Revised Gap Analysis is comprehensive.

Automated Valuation Models (AVMs)

Question 2.1: Do you consider AVMs to be a growing area and therefore something IVS needs to address? Please provide your reasoning for your answer as this will help the Board with their deliberations.

Yes, we do agree that AVMs are a growing area that should be addressed, however we believe it should be addressed by the IVSC's Tangible Assets Board via a Perspectives Paper initially. In our view, the issue of utmost importance to stakeholders is understanding what AVMs are or are not, and how/when they differ from a "valuation", such that stakeholders can determine when each is appropriate for their use. The objective of the Perspectives Paper would be to educate/inform, and share the research and findings of the IVSC's working group, including the differences between AVMs and other forms of valuation models. Such Perspectives Paper should:

- acknowledge the ways in which AVMs are presently being used (in tangible asset valuations, FI valuations and increasingly BVs);
- the issues regarding the use of AVMs
- examples of fully automated AVMs
- discussion of why valuer judgement remains important, and what types of judgements are appropriate for each of a AVM's main uses

We do not believe that the IVSC should rush to incorporate AVMs into the standards at this stage. Following the publication of a Perspectives Paper on the topic, a forum for discussion between relevant stakeholders could be organized (including valuation firms, banks, VPOs, etc), and a further assessment could then be made regarding whether there is sufficient stakeholder agreement to develop a standard.

Question 2.2: Should AVMs be included/addressed within IVS? If you think AVMs should be outside IVS how should they be considered and what clarity will valuers require?

We believe that AVMs should be mentioned within IVS, and some high level principles outlined in IVS 105 to distinguish them from value conclusions, and some additional guidance provided within the tangible assets sections of the standards and the FI standards.

Question 2.3: Do you agree with the definition of AVM shown below. If no, please provide a suggested alternative definition together with a source for this definition.

Automated Valuation Model (AVM) A system that provides an indication of value of a specified Asset at a specified date, using calculation techniques in an automated manner. An AVM may not be a Model as defined in this glossary.

We appreciate the difficulties in defining AVMs across a range of specialisms. We fear that by using the word “indication of value” within the definition, it will create confusion with other elements of IVS which tend to refer to valuation as an estimate, such as:

- “Valuation Model” (IVS 105 par 90.1), which “refers collectively to the quantitative methods, systems, techniques, and qualitative judgements used to estimate (emphasis added) and document value.”
- “Valuation” – “the act or process of determining an estimate of value (emphasis added) of an asset or liability by applying IVS”

CBV Institute faces similar challenges within its own existing standards in distinguishing between different levels of valuations - a calculation valuation, an estimate valuation and a comprehensive valuation. We are concerned that introducing the term “indication of value”, which is already used within IVS in the context of “weighting” different indications of value obtained using various methods/approaches, will be confusing.

We also believe the last sentence in the definition “An AVM may not be a Model as defined in this Glossary” is also confusing – is it a model or not? One might think that because Automated Valuation Model contains the word “model”, it would be a type of Model.

A possible alternative definition for AVM is:

A system that uses mathematical or statistical or other calculation techniques and various data in an automated manner to generate a value. AVMs are not Valuations in that ___ (explain how they differ). AVMs are often used to calculate values for residential properties based guideline/comparable properties, for financial instruments, and increasingly used to provide a value of a businesses.

The above definition is our own.

Question 2.4: Do you agree with the definition of Model shown below. If no, please provide a suggested alternative definition together with a source for this definition.

Model: A Model is a formalised system relating several variables, assumptions, judgements and equations to calculate the Value of an Asset under a given Basis of Value.

We are in favour of using the word “calculation” as part of the definition of model, as a way to distinguish a model from a valuation. That said, we believe IVS should be crisp and clear on what a valuation is, and what it is not.

We suggest the following alternative definition for Model:

A model is a tool/system using inputs (variables, assumptions) and formulaic or pre-determined rules/procedures that has been designed to calculate an output for a specific purpose. A model may be used by a valuer as part of a Valuation.

Or

A model is a process that might be used in a determination of value.

The above definition is our own.

Question 2.5: Should IVS consider Hybrid Valuations as illustrated in the diagram Key Categories of Valuation Methods. Please provide your reasoning together with any examples of Hybrid Valuations currently used in your market.

We have no comment (not applicable to business valuations).

Environmental, Social and Governance

Question 3.1: What role do you see IVS having in measuring the value of ESG? Please provide details and reasoning with your response.

We believe that ESG is one of the many relevant considerations for business valuers (and indeed all types of valuers) in arriving at a conclusion of value. That said, given the increasing discourse on ESG and the lack of consistent global measurement frameworks for ESG, we do believe that this is an area where the IVSC’s role is, for the moment, one of education. The IVSC can work collaboratively with other standard-setters to educate valuers about how to give more fulsome consideration to these factors in valuations.

We support the IVSC’s efforts to create a working group and conduct research. We look forward to the findings of that research. We believe the IVSC should monitor and work alongside the IASB, IOSCO and others in their efforts on sustainability reporting (to avoid duplication of efforts, and leverage off existing research in this area). The IVSC can encourage its members to collaborate and share information, perhaps via a member survey, on how ESG data is used in practice. While this would be a substantial undertaking, it would be valuable to understand how certain key stakeholders in the capital markets consider ESG factors and use ESG data in decision-making:

- Credit rating agencies
- Pension and institutional investors
- Underwriters and bankers

Question 3.2: How do you consider ESG within your valuation process? Please provide details of your country, specialism and as detailed an example as possible together with any data sources used, if applicable.

It is difficult to answer this question on behalf of all members/practitioners in the Canadian marketplace. CBV Institute has been a contributor (along with A4S and CPA Canada, as well as other international organizations) to a soon to be released A4S Essential Guide to Valuations and Climate Change.

Question 3.3: What definitions and or framework do you currently use when considering ESG in your valuation work? Please provide the definition, framework and source.

It is difficult to answer this question on behalf of all members/practitioners in the Canadian marketplace. This topic can have an entire discussion paper to itself, and be focussed on specific users.

IVSC could take a leadership role in this area by, for example, endorsing the Financial Stability Board's TCFD recommendations, or by offering to work alongside the organizations who have recently announced their collaboration on building a set of metrics on global non-financial reporting: Sustainability Accounting Standards Board (SASB), the Global Reporting Initiative (GRI), the Climate Disclosure Standards Board (CDSB) and the Climate Disclosure Project (CDP).

Question 3.4: What are the demands from valuation stakeholders when considering ESG? Please provide details.

From a VPO perspective, we perceive that the greatest demand is for a consistently applied global sustainability-reporting standards (firstly), and guidance on how to conduct climate-related scenario analyses (secondly).

Question 3.5: As outlined above ESG can be subdivided into a number of issues. Can you separately account for any of these issues within the valuation process and if so please provide further details?

The issues comprising ESG are issues whose impacts should be considered together at a macro level when determining the value of a business. Many of

them will also have individual, more micro or specific, impacts. For example, executive remuneration and carbon emissions will directly impact the cash flows of an asset or business; customer satisfaction metrics may directly be related to customer retention rates used in the valuation of customer relationships. It is impossible to enumerate all of the ways in which different ESG issues impact a valuation, only that they must all be considered as part of a business valuation and assessed for relevance.

Long -term Value

Question 4.1: Have you faced pressure from banks or other institutions to provide a prudential valuation? If so, in which market and in which specialism do you operate?

No comment, N/A.

Question 4.2: Do you agree that Market Value already incorporates the concept of a prudential valuation within its definition? If not, please provide your reasons.

We believe that all properly supported valuation conclusions should be defensible at a particular point in time. Since the definition of Market Value is based on arm's length parties acting prudently, it should notionally incorporate the concept of a prudential, or at least prudent, value. However, this is just an assumption, as in reality rarely do these conditions exist perfectly. In other words, the definition of Market Value is an "ideal".

30. IVS-Defined Basis of Value – Market Value

30.1. **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.

As it has been described, the concept of "sustainable long term value" and "sustainable value" appears to allude to the use of conservative (or more conservative) inputs and assumptions than the current market would suggest. Indeed, we acknowledge that the current environment is indeed more complex, and that stock market values are increasingly disconnected from notional/intrinsic valuations. The concept of sustainable/long term value appears to be more relevant to in-house valuers performing valuations for lending or investment purposes.

If we as valuers believe the premise that financial markets are rational (which is a fundamental premise/assumption of valuers who rely on observable market data

to support their valuation conclusions and a fundamental premise underlying IVS, which gives precedence to market-based inputs) then to suggest that a new and more conservative Basis of Value for “financial stability purposes” appears to be at odds with that.

We find the concept of a “sustainable” value interesting as it appears to capture an “enduring” or “floor” value that can be maintained over some period of time/cycle. The challenge with such a measure of value is in the determination of the length of that period/cycle and the appropriate long term value index – challenges which are significant. Getting consensus in this area will be difficult, and ensuring consistent application between valuation professionals, even more so. The concept is very different than Market Value.

Mandating such a type of long-term/prudential/sustainable form of value, including a long term value index, should be driven by prudential and/or banking regulators, not the IVSC. The protection of lending institutions from the cyclicity of market fluctuations is indeed a complex area, made difficult by the fact that any form of “smoothing” has the risk of being arbitrary, and would have to meet the particular risk profile of that financial institution or user. A long term value index would be a “how to” and if developed or endorsed by the IVSC, would move the IVSC from a principles-based standard setter into a different role. We believe IVS already captures this and other alternate Bases of Value via its statement on “Compliance with other standards” in the IVS Framework and IVS 102.

Question 4.3: Do you feel that the research in relation to a European Long - Term Value Index would be helpful or not? Please provide the reasoning for our response.

This research could be helpful to a certain subset of IVSC members (tangible assets, in Europe), but we suggest it should not be a project led by the IVSC, but rather by the relevant European banking organizations. The IVSC could share such research globally to further increase global awareness of this concept, and how it could be applied in practice.

Question 4.4: Should Long -Term Value be a separate basis of value or a concept to be included in a basis of value?

It would be equally difficult to incorporate this concept within an existing basis of value. We believe that IVS could list this new separate basis of value within IVS 104 (if and when consensus on a definition was arrived at by prudential regulators or banking authorities).

We believe it would be beneficial for the IVSC to share additional research or thought leadership in this area with its members before undertaking any further review of the standards. What is the intended meaning of “long term”? Who determines the term? How and when would such a basis of value be used? Once additional information for available, the question of how to best make reference to Long-Term Value could then be revisited.

Question 4.5: The current research for a Long -Term Value Index is currently restricted to European Markets. Do you feel that this research should be extended to your market, and if so, in which market do you operate?

Yes, it would be beneficial to obtain the views of various markets across the globe in relation to this concept. CBV Institute operates primarily in the Canadian marketplace, and would be willing to suggest this as an area of future sponsored research by our VPO.

Social Value

Question 5.1: Do you agree with the proposed definition for Social Value outlined below? If not please provide your reasoning and proposed revisions to the above definition or an alternative definition, together with the source, if applicable.

Social Value

Social Value includes the social benefits that flow to asset users (social investment) and the wider financial and non -financial impacts including the wellbeing of individuals and communities, social capital and the environment, that flow to non -asset users.

We support this definition. The IVSC’s perspectives paper on Social Value was very well done. We are sharing this paper within our marketplace.

Question 5.2: Are you currently required to address Social Value within your valuations, and if so, what is your specialism and in which country are you located?

While it is difficult to answer this question on behalf of all members/practitioners in the Canadian marketplace, we do not believe that Social Value is currently required to be addressed.

Question 5.3: How do you address Social Value within your valuation process? Please provide as detailed an example as possible together with any data sources used, if applicable.

No comments.

Uncertainty and Risk

Question 6.1: Do you feel that IVS should include a section on Uncertainty and Risk? Please provide the reasoning for your response.

Yes, we believe it would be beneficial for IVS to include a section on Uncertainty and Risk as this concept should be made clear and transparent to users of valuation services, and distinguished from market risk (or other types of risk which can be quantified).

Question 6.2: Do you feel that it would be possible to provide an overarching section on Uncertainty and Risk which applies to all specialisms? If not, please indicate where you think it does not apply and provide your rationale.

Yes, we believe it could apply to all valuation specialisms, but that this type of disclosure and whether it should/needs to be included is a matter of professional judgement.

Question 6.3: Do you feel that the text provided above in relation to the difference between valuation Uncertainty and Risk is sufficiently detailed for inclusion within IVS? If not, please provide details of the other elements you would like to be included and your rationale for including these elements

The text provided appears to be appropriate.

Data Management

Question 7.1: Do you feel that IVS should include an overarching standard in relation to data management within IVS 105 Valuation Approaches and Methods? If no, please provide your reasoning.

Yes, we believe that IVS should include a standard governing the valuer's responsibilities vis-à-vis the data that they use and rely upon, such that the valuer has taken reasonable steps to consider the source of the data, and assess that it is unbiased, reliable, appropriate, and free from significant material risks or limitations (or rely upon an expert to do so), or disclose that he/she was unable to do so via a limitation in the valuation report. The valuer should have latitude to decide the extent of procedures/investigation performed that are suitable for purpose.

Question 7.2: How detailed should IVS be in relation to data management, and are there any elements that you feel should be included or excluded from this standard?

We suggest that this standard should be fairly high level, and outline principles, avoiding a “how to” approach.

Question 7.3: How should market uncertainty and risk impact the exercise of professional judgement when market data is not observable?

At a high level, the valuer should approach the valuation with an increased level of professional skepticism when relevant market data is unavailable to help corroborate or support management representations/assertions underpinning key inputs to the valuation. The valuer would not rely on market approaches if market data was not observable, increasing the importance of the valuer’s professional judgment when assessing and evaluating the appropriateness of inputs to the valuation.

Thank you and best regards,

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