Valuology

Comments on IVS published Aug 2021

In early August IVSC released the latest edition of the International Valuation Standards. In line with the latest policy, it does not have a date or edition number as an identifier but is intended to be effective from 31 January 2022.

We set out below a summary of the changes (there are few unless you value inventory) and our comment on each. We also highlight an existing error in the standards which has not been corrected and conclude with some overall comments.

Summary of Main Changes

Core Principles

A list of "Core Principles" for standard setting and for valuation has been added to the Introduction. Much of this is effectively a summary of IVS 101 - 103.

Comment

While these principles might be a useful one minute overview of what the standards are about, from a valuer's perspective they do not introduce anything that was not previously required. If the standards proper had been kept as a concise list of requirements, such a summary would have been unnecessary.

Glossary

The glossary has been extended, although a few of the definitions proposed in the consultation draft have not been included.

Comment

Some of the new definitions (as well as the existing) are simply restating the commonly understood English dictionary meaning. More controversial is the inclusion of definitions taken from other standards or the legislation of a particular country. Such definitions are not within the control of the IVSC (or any valuer) and have no place in the IVS Glossary. On the one hand it gives the impression that the IVS have been designed only for use in the countries referenced; on the other it sets a precedent for hundreds of alternative definitions from every jurisdiction around the world to be included.

Another concern is that stipulating limited meanings for words can obstruct their meaning within the overall context of the clause in which they appear. This can lead to misinterpretation and disputes as to the intended meaning of the clause. While a few key definitions are helpful, too many create problems for presentation and comprehension of the standards overall. It also acts as a barrier to optimal translation of the intended meaning into languages other than English.

Framework

Two clauses are added to explain what is meant by compliance with the standards and when a departure may be made. Other changes are made to indicate that an individual or group of individuals responsible for preparing a valuation must be appropriately qualified, competent, unbiased and act ethically.

Comment

The rule on when a departure may be made is curious given that the IVSC cannot dictate when the IVS apply. The circumstances under which the IVS must be used, including any exceptions, will be for those who choose to adopt them to decide and enforce. Most valuers preparing valuations that comply with the IVS will be members of a professional body, subject to statutory regulation or both and will therefore be subject to requirements on accreditation, competence and behaviour which will override anything in the IVS.

IVS 101 - Scope of Work

Valuers preparing valuations for their own employers are now referred to as "employed valuers". Valuers preparing valuations for a third party client are called "engaged valuers".

Comment

This change is of no immediately obvious purpose or consequence. The focus of the IVS should be on the valuation not the title of the provider.

IVS 102 - Investigations and Compliance

No change – a proposal in the Exposure Draft to remove the final section on compliance because it was duplicating material in the Framework has not been made. Neither has the proposal to include a section on Valuation Governance been carried forward.

Comment

The removal of the compliance section was one proposed alteration that was necessary but has not been actioned. If a statement on compliance is required at all it is certainly misplaced in this standard that is otherwise concerned with the investigations and enquiries that should be made for an IVS valuation.

There is an argument for including a requirement for adequate governance of the valuation process in IVS 102, although the problem is to make this sufficiently generic to be applicable to all potential users of the IVS. Adequate governance by a sole valuer will be very different from that for a large organisation.

IVS103 - Reporting

A proposed change to 10.1 that differentiated between the valuation report and supporting information has not been made.

Comment

This reversal of the proposal is welcome. Given that IVS 103 states that a report should communicate all information necessary for a proper understanding of the valuation, separately categorising "supporting information" from the report would have been counterproductive. Unfortunately, one change that should have been made has not. This is to revert to listing what needs to be included in the report to confirm the outcome of the investigations and other actions outlined in the scope of work instead of simply cross referencing the latter in IVS 101. The scope of work describes what the valuer intends to do; the report confirms what has been done and what was found. Failure to make this distinction clear using appropriate language is a significant shortcoming.

IVS 104 – Bases of Value

A short section on "Allocation" has been added to the end.

Comment

A value may need to be allocated between different elements of a single asset, but this section does not add anything beyond what would be expected from the meaning of "allocate" and generic provisions that apply to all valuations, such as the need to follow any applicable legislation or regulations. Neither is an allocation a distinct Basis of Value so its inclusion in IVS 104 is questionable.

IVS 105 – Valuation Approaches and Methods

A proposal to introduce a fourth valuation approach, the "Hybrid Approach" has not been followed through. Instead wording that used to appear in the introduction making it clear that the market, income and cost approaches are not exclusive and may be used in any combination has been reinstated.

Comment

This change of heart is welcome.

IVS 200 - Businesses and Business Interests
The introduction has been rewritten with the objective of better describing the scope of the standard.

Comment
This helps understanding of what the standard covers but does not make any changes to the scope.

IVS 203 - Inventory
This is a completely new standard. It addresses the valuation of goods which will be used in future production, work in progress, and goods awaiting sale. It excludes real estate and buildings under construction.

Comment
This standard fills a gap in the IVS. It mostly consists of discussion of different methods that may be used to value different types of inventory. Like many other of the standards it should be classified as guidance but is given quasi mandatory status.

Errors Not Corrected in the Latest Edition

"Assumptions" and "Special Assumptions" are distinct concepts in valuation and serve different purposes. This should be clear from the current definitions in the IVS. However, the current IVS provide incorrect examples for each, with examples of an Assumption provided as an example of a Special Assumption. This occurs in IVS 104, IVS 300, IVS 400 and IVS 410. We drew the Board's attention to these errors in our response to the Exposure Draft but they have not been corrected. We believe some of the evident confusion arises from the way in which Assumptions and Special Assumptions are presented as conjoined concepts in IVS 101 and elsewhere. This presentation fails to make the distinct nature and purpose of these terms clear to a reader.

An associated problem is the absence of any comment in IVS 102 on the importance of considering whether any Assumption or Special Assumption set out in the scope of work is reasonable in the light of the investigations and enquiries made. If either an Assumption or Special Assumption is made which is unrealistic or unreasonable on the basis of facts found the resulting valuation will be at best misleading.

Overall Comments

Over recent years the IVS have changed significantly as regards their scope and purpose.

The 2013 version was based on the objective of setting a short set of requirements for the acceptance, undertaking and reporting of valuations, based on consistent concepts and definitions. These were designed to be mandatory for any user of the standards. These requirements were supported by guidance on how they could be applied to different types of asset or for different purposes. This supporting guidance was designated as either a Framework (for the application of the requirements generally), Commentary or Application Guidance. Regardless of the title, this material was clearly designated as advisory and not intended for mandatory application. It was recognised that the approaches needed to achieve the objective of the standards would often vary between different markets and jurisdictions, and therefore could not be realistically mandated by a single global body.

A good example of how rules and guidance need to be split in valuation standards can be seen in the Uniform Standards of Professional Appraisal Practice (USPAP) issued by the Appraisal Foundation in the USA. The standards proper are short concise rules that are generic to most valuation practice. These are accompanied by a much greater volume of "Advisory Opinions" which advise on the application of these rules to different scenarios. These Advisory Opinions are explicitly stated to illustrate the applicability of the rules in USPAP to specific situations but do not establish new standards or interpret existing standards. USPAP are designed to regulate specific types of valuation within a single federal jurisdiction. The need to separate rules from advice and guidance is even more important if designing standards for many valuation purposes across different jurisdictions and cultures.

The major professional valuation bodies supporting the IVSC had always made it clear that they saw it as their role to develop guidance on the application of the IVS core principles that was relevant to their members day to day activity. They also indicated that the IVS needed to better define the boundary between what could be accepted as mandatory and what was provided as illustrative guidance. In 2014 a Memorandum of Understanding was signed by IVSC and more than 20 of the professional bodies in membership. This recognised that the professional bodies need only adopt those parts of the IVS relevant to the work undertaken by their members and that they could issue additional or supplemental standards of their own. To enable implementation of this MoU the Exposure Draft for the proposed 2015 IVS included presentational changes to distinguish even more clearly the core material intended to be mandatory from the optional supporting guidance. However, this edition was never finalised due to a restructuring of the IVSC Boards.

The next edition of the IVS was in 2017 and represented a very significant change in direction involving two key changes. These changes further blurred the respective roles and responsibilities of the IVSC and the professional bodies in membership and reversed the earlier direction of travel for the IVS that had been reinforced by the 2014 MoU.

The first change was to turn the IVSs into a list of instructions for "the valuer" instead of providing the required specification for a valuation in order for it to comply with the IVS. This change from addressing the product to the person who produces it gives the IVS the appearance of a rule book for valuers. Many of the organisations who choose whether and when to adopt the IVS are responsible for setting the rules for the valuers they accredit or regulate, so framing the IVS as a valuer's rule book creates potential for conflicts and a barrier to adoption. Would the International Financial Reporting Standards be mandated or used in nearly 150 countries if they did not set out what should be in an entity's financial reports but instead focussed on who prepared them?

The second change was to make almost all the supporting material previously designated as guidance or illustration either mandatory or "presumptively mandatory". This completely reversed the earlier steps that were taken to make a better distinction between requirements and guidance in response to representations from professional bodies and other users. The word "should" is now narrowly defined as meaning the valuer must comply unless they demonstrate that alternative actions were sufficient to achieve the same result **and that these are documented**. All this achieves is to make the standards much less useable and only applicable to a narrow range of valuation activity. This is yet a further barrier to their wider use and adoption.

This latest edition was only ever billed as a set of technical updates to the previous IVS so it was unrealistic to expect fundamental issues such as those highlighted above to be addressed.   However, a "technical update" suggests a correction of existing errors or clarification of parts where different interpretations have arisen in practice. None of the changes do this – they are simply additions to what was there before and lead the standards into ever narrower areas of applicability.