INTERNATIONAL VALUATION STANDARDS COUNCIL

Valuation Experts and Accountants Working Together

Sir David Tweedie

Chairman, International Valuation Standards Council; Past Chairman, International Accounting Standards Board (2001-2011)

Prerequisites of Successful Global Standards

- Acceptance of the need for global standards

- A strong, respected, identifiable profession to implement and enforce the standards

Why Global Standards – the Example of IFRS

The IFRS Foundation and the IASB are dedicated to developing and sustaining a single set of **globally accepted accounting standards:**

- Aimed at **providing high-quality, transparent and comparable information** for investors and other users of financial information
- Providing the world's integrated capital markets with a **common language for financial reporting**
- Promoting capital market stability through the **transparency and integrity of financial reporting**
- Taking appropriate steps with regulators and standard-setters to help promote **consistent application of standards**

Why Global Standards are needed

Accounting and valuation standards evolved nationally because companies borrowed and investors invested only in their home country.

- Globalisation is inconsistent with multiple, national or regional accounting and valuation languages that **hinder comparability**
- Corporations must consolidate global network of operations
- Investors seeking diversification and return increasingly invest outside domestic markets

Status of IFRS Use

- Since 2001: Companies in 138 countries are now required or permitted to use IFRSs
- Recent new joiners: Brazil, Canada, Korea, Mexico, Russia
- Japan: IFRS permitted for international companies; progress toward IFRS adoption continues as more large companies move away from US GAAP
- 2014: After more than ten years, convergence work with FASB winds down with significant new high quality standards for revenue recognition, leasing, impairment, classification & measurement

Valuation at the Core of Economic Stability

- Valuations undertaken in accordance with generally accepted principles are central to financial stability and for financial reporting under IFRS and US GAAP
- Poor valuation practice was identified by the Financial Stability Forum and the G20 as a significant contributor to the 2008 financial crisis with a particular focus on financial instruments, where there was much inconsistency in valuation between financial institutions as well as across national borders
- Reliable and consistent valuation is also of fundamental importance to prudential regulators and market participants in determining the capital adequacy of financial institutions
- Valuation is an integral part of the risk management processes applied by financial institutions and other businesses

International Valuation Standards Council History

- Established in the early 1980s
- Expanded its mandate in 2008 to establish standards applicable for all purposes and all asset and liability categories
- The IVSC has around 100 members and sponsors from around the world
- Global standard setter
- To protect the public interest
- To improve the credibility of and enhance public trust in valuation profession

What do we want to achieve?

1. Develop high quality international valuation standards which underpin consistency, transparency and confidence in valuations across the world;

2. Be seen and referred to as the standard setter for valuation with international valuation standards which are recognised and over time adopted by key stakeholders around the world;

3. In achieving the above add status to IVSC member and sponsor organisations and the valuation profession.

Challenges Facing the Valuation Profession

- Developed as secondary specialization by experts in different types of asset
- Led to fragmentation by asset type
- Unintended consequences of legislation
- Regarded as technique rather than profession
- Who are skilled valuers – accepted qualifications?
- Lack of recognition by regulators, other professions and prospective recruits

What is a Profession?

- A learned and respected body of individuals – exclusivity
- An organised body to create and uphold standards
- Standards based on a conceptual underpinning
- Entry requirements
- Code of Ethics
- Core training leading to qualification
- Work experience
- Assessment of competence
- Continuing Professional Development
- Monitoring and oversight

Professional Membership Obligations

Initial Professional Development

- Entry Requirements to Accreditation Programmes
- Professional Skills and Ethics
- Technical Knowledge
- Practical Experience
- Assessment of Professional Competence

Continuing Professional Development

The Conceptual Framework

- Objectives
- Qualitative Characteristics
- Elements
- Recognition
- Valuation
- Presentation
- The reporting entity

Statement of Protocols IVSC - IASB

Fair Values

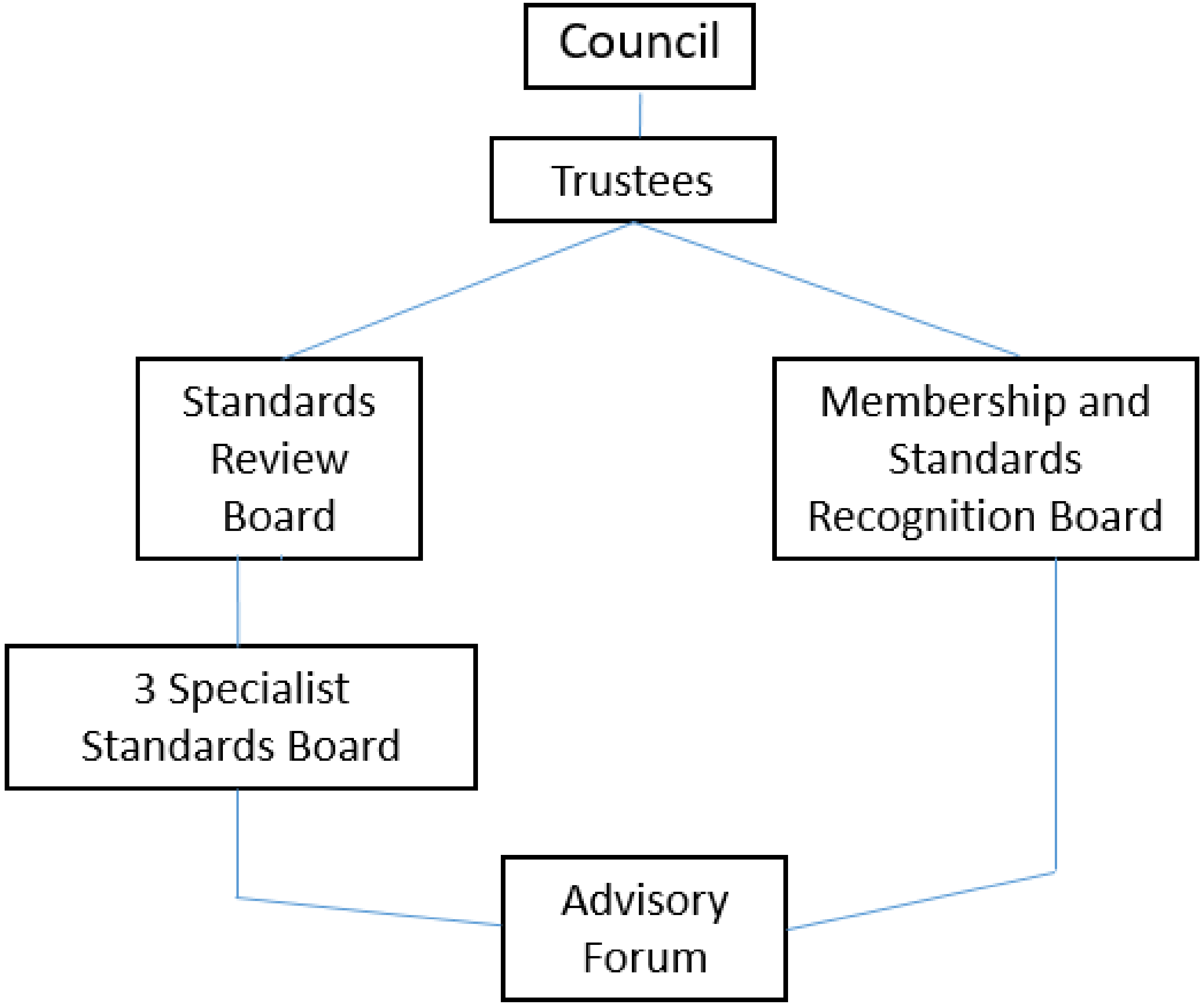
Common interest in ensuring IVS is consistent with IFRS

- Provide input to each other's standards
- Comment on each other's developing standards
- Include staff on the other's projects
- Inform other of diversity in practice in fair value measurements
- Inform other of emerging issues
- Organise joint discussion sessions on relevant issues

Benefits of an effective IVSC

1. Increased confidence and stability across financial markets
2. Easier to do business across the world
3. Valuation Professionals work is relevant globally
4. Increased international business for valuers with local and global relevance
5. Become seen as a high calibre profession

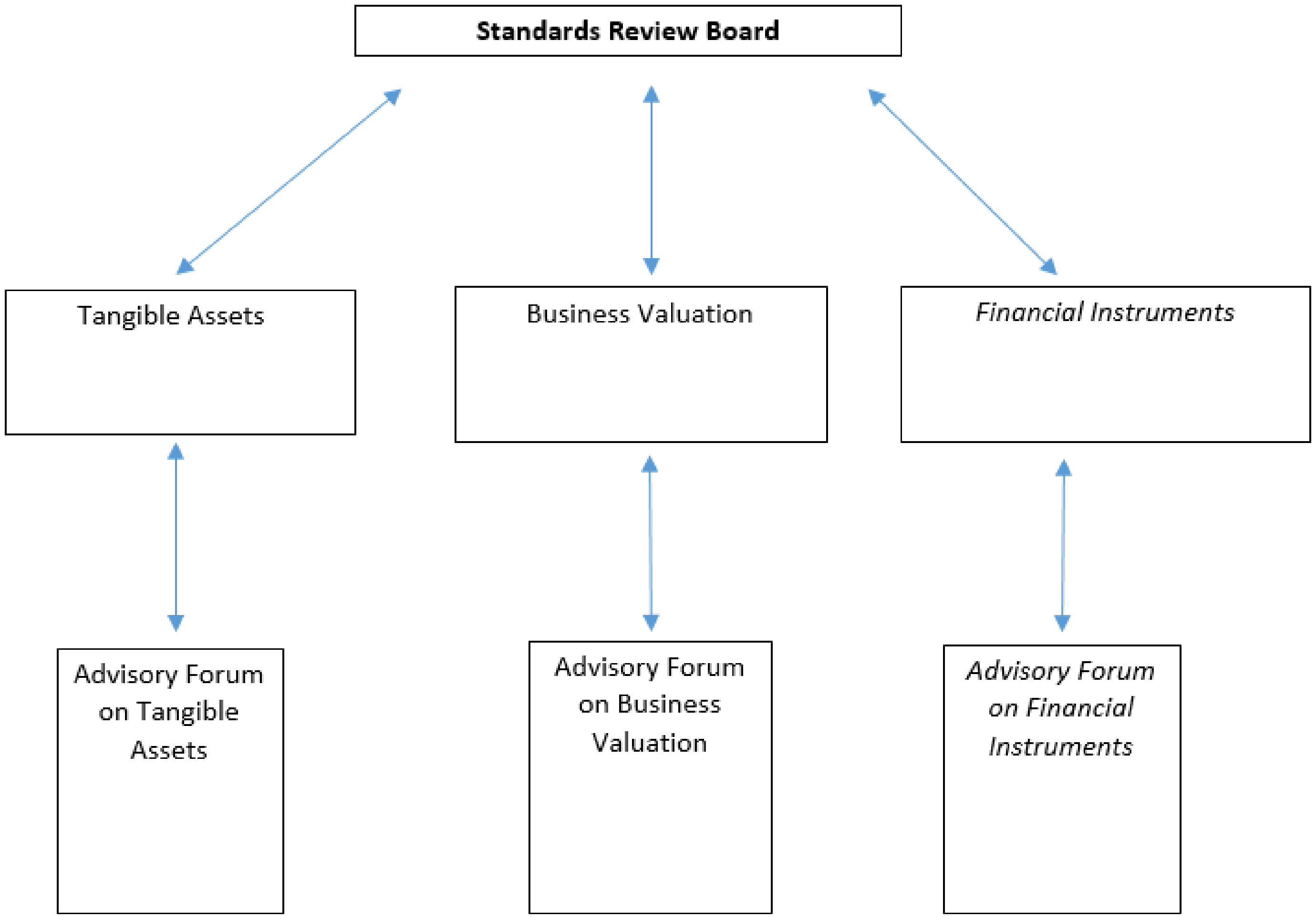
New IVSC Structure



Valuation and Financial Reporting

- Real estate / investment properties
- Intangibles
- Mergers and Acquisitions
- Extractive industries
- Agriculture
- Financial instruments
- Pension schemes
- Liabilities

Increased Focus



Financial Instruments Valuation Issues

- IAS 39 / IFRS 9 / IFRS 13 not very specific on valuation principles hence each issuer makes its own rules. Regulators have observed huge variation in the FI valuation of financial institutions.

- Valuation for financial reporting and transactions versus regulatory reporting

- Conflicting approach between accounting standards and current view of market practitioners (funding adjustments, concentration)

Our response

The FI initiative:
Roundtable in London with regulators (banking and regulators) and GSIFI banks in 2016

- Recognised that there is an issue to be fixed
- Proposal of Task Force involving banks, insurers, asset managers, valuation firms, key users, accounting firms, credit rating agencies and with IOSCO and key central banks as observers
- Focus on valuation of financial reporting and market activities; increased transparency in what valuation includes or excludes; to avoid regulators deliberately increasing capital requirements as a result of doubts about valuations. To deal with the most urgent issues i.e. how to price liquidity
- Aim to enhance governance and internal controls

Outcome of Task Force Meeting

- Creation of 4 working parties
  - Governance
  - Framework of a valuation
  - Data sources and assumptions
  - Purpose of valuation – relationship with accounting standards
- Creation of FI Standards Board

The Simplification of FI Accounting (IAS39 → IFRS9)

- IAS39
- rule based/complex
- multiple impairment models
- IFRS9
- measurement based on
- business model for managing financial assets
- contractual cash flow characteristics of financial asset

Impairment : Incurred Loss → Expected Loss

Incurred Loss

- trigger event needed before recognition of credit loss
- aim to limit ability to create hidden resources to permit earnings management in bad times
- problem in crisis – different type of earnings management – losses postponed. (Note actual default not required before impairment – but often become practice)

Impairment : Expected Loss

- no trigger event needed
- expected credit losses to be recognised at all times (updated at each reporting date to reflect changes in credit risk)
- can look to future expected events rather than past events and current conditions
- based on reasonable and supportable information available without undue cost and effect

The IASB Impairment Model

Stage 1 – portion of lifetime expected credit losses that are possible in 12 months

Stage 2 – if credit risk increases significantly from the time of origination or purchase and resulting credit quality is not considered to be low credit risk, full lifetime expected losses are recognised

Stage 3 – if the credit risk of a financial asset (generally an individual asset) increases to point that it is considered credit impaired lifetime expected credit losses still recognised

FASB Impairment Model

- full lifetime losses recognised immediately
- the net amortised cost of the loan measured at the present value of the cash flows expected to be collected, discounted at the original effective rate

Rationale – simpler and more conservative

Why didn't IASB follow FASB?

Majority of non-US users preferred IASB 3 stage model

Why:

- distorts value of loan book
- depresses book value per share and earnings per share
- incentive to sell loans and run down loan book to release large allowances and book gains
- In bad times, banks incentivised to cut off liquidity by lending less and for shorter durations

The Future of the Profession

- IVSC in partnership with the valuation and accountancy professional institutes
- Global reach
- A place among the international professions
- IVSs required by IFRS and regulators – implemented by internationally accredited valuers

Thank you