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Regulation in Business Valuation: The Case of the International Valuation Standards Council

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Abstract
This paper calls attention to the theme of standardization in business valuation which is still a neglected area of research in the scientific community, differently from what happens with regard to the standardization of financial reporting. The issue, in truth, deserves attention because high quality best practices applied by the global valuation profession has effects on the efficiency of the entire economic system, in other words on the public interest. The aim of the paper is to analyse the state of the art of International Valuation Standards (IVS) issued by the International Valuation Standards Council (IVSC), an independent international institution that has the purpose of setting international standards and also of promoting and developing quality professional practices.The study is conducted in the light of an interpretative model that identifies three critical variables: the regulated matter, the regulation strategy, and the regulation system. From the analysis emerges that the International Valuation Standards" (IVS) are by no means comparable to national or international accounting standards (IAS/IFRS and US GAAP) either by extent or by depth of regulation. In particular IVS devote greater attention towards procedural and formal issues rather than towards content issues. They represent only a set of minimum requirements that experts are required to respect, so the subjective nature of business valuation is of particular relevance.
Keywords: business valuation, business valuation regulation, business valuation standards.

1. Introduction

The professional field of business valuation, which already grew significantly in the second half of the twentieth century, is still having an unceasing development in the new century[1]. This is largely due to the increasing demand of valuation services over time. The valuation of businesses, equity interests or assets are activities that are increasingly required for many purposes: mergers and acquisitions, IPOs, insolvency proceedings, divorces, division of family and inherited property, tax assessments, employee stock ownership plans (or ESOPs), buy-sell agreements[2], financial reporting[3], insurance claims, and more. The growing demand of valuation services caused a significant growth in the number of professionals in this sector[4]. This led to a professionalization process that created a veritable professional category of experts in business valuation. Over time, these professionals felt the need to create their own professional associations in order to have their requirements better defined and met, as well as to regulate their activities by issuing specific standards.

The technical-professional and public organisations whose institutional purposes include the issuing of valuation standards are professional associations, such as the Institute of Business Appraisers (IBA) (About its standards see: IBA 2011), the National Association of Certified Valuators and Analysts (NACVA) (About its standards see: NACVA 2011), the Canadian Institute of Certified Business Valuators (CICBV), the Royal Institution of Chartered Surveyors (RICS) (About its standards see: RICS 2013), the American Institute of

1 In 2016, the U.S. magazine "Accounting Today" published the Top 100 Firms in Accounting, highlighting that over eighty per cent of them reported increased business in the business valuation area (Accounting Today, 2016). The results of this research are consistent with the conclusions of another study conducted by the American Institute of Certified Public Accountants (AICPA) in the same year, which states that 54% of interviewed professionals expected growing business in this specific sector with percentages ranging from 10% to 50% over a span of two to five years (AICPA, 2014, p. 2)

2 These are legally binding agreements between the co-owners of a business that establish how corporate assets will be managed in the future if, for example, one or more of them dies, becomes permanently disabled or withdraws from the partnership.

3 It is useful to remember that business valuation has implications also on financial reporting, for example regarding the fair value measurement.

4 Actually, a full range of professional figures is included under this category. In fact, business estimates are determined not only by certified public accountants (CPAs), business and investment banks, auditing companies, and, last but not least, the well-known 'Big Four', and business brokers, but also, especially in North-American, business valuation firms which exclusively provide valuation services to meet the different requirements of their customers.

Certified Public Accountants (AICPA) (About its standards see: American Institute of Certified Public Accountants [AICPA] 2007), the Institut Der Wirtschaftsprüfer (IDW) (About its standards see: Institut Der Wirtschaftsprüfer [IDW] 2009); and government agencies[1] such as the Internal Revenue Service (IRS) (About its guidelines see: Internal Revenue Service [IRS] 2006) and the Direction Générale des Finances Publiques (DGFiP); and independent institutions such as the International Valuation Standards Council and the Appraisal Foundation.

The purpose of this paper is to analyse the state of the art of international standards issued by the International Valuation Standards Council (IVSC) in the light of the harmonisation efforts made with other national and international standards. By using the term 'valuation standard', we specifically refer to the whole set of documents issued with the purpose of regulating the activity of business valuation specialists[2]. For a better understanding of the spirit of the subject matter at issue, we deemed it appropriate to first briefly analyse the structural features and organisational model of the Institute. The approach adopted to analyse the regulations set forth by IVSC identifies certain critical variables that help understanding the distinguishing features of the regulation, namely the regulated matter, the regulation strategy, and the regulation system.

While there is a clear need to define the content of the regulated matter in order to specify the operating range of the Institute, the other two variables pertain to the researchers' intuition and tacit scientific understandings[3] and are based on literature already developed in different but related scientific fields.

As regards the regulation strategy, the scientific community recognised its significance and proposed a bureaucratic, a delegate and a self-regulatory model. Even though they have been defined by making reference to regulation experiences that differ from those examined here, they seem to be perfectly suitable to qualify business valuation regulations, and therefore, we adopted that classification for our paper.

As regards the regulation system, again the scientific community proposed a compatible subdivision that seems to be appropriate for our analysis, so we will constantly refer to the distinction of regulation systems into "principles-based", "rules-based", and "mixed".

The structure of this paper is described below. The second section presents the governance, mission and business model of the International Valuation Standards Council (IVSC). The subsequent section outlines the state of the art of the principles issued by the organisation (International Valuation Standards) by analysing, in particular, its regulated matter, strategy and regulation system. Then the theme of the harmonisation of valuations at local and international level is raised before drawing conclusions.

2. IVSC: Constitutive Features

2.1 The Foundation and Governance of IVSC

The International Valuation Standards Council, briefly IVSC, is an independent not-for-profit organisation acting in the public interest that was incorporated on April 1, 2004 as an Illinois Not-for-Profit Corporation, but with operational headquarters in London.

Actually, the institution was incorporated much earlier – precisely in 1981, in Melbourne, under the name of International Valuation Standards Committee[4], upon the initiative of about twenty professional organisations that felt the need to create a private independent organisation to be entrusted with the task of setting standards for the valuation of businesses and individual assets and liabilities that could be used at supranational level. The globalization of financial markets was already going into that direction at that time. IVSC is a multidisciplinary entity that deals with several valuation areas, not only the valuation of businesses. IVSC issued its first standards in 1985[5].

Today, as we read in its website, it "... consists of nearly 100 member organisations from around the world and is supported by numerous sponsors who are leaders in the valuation field. These include the world's leading accountancy and valuation firms, professional bodies and other important global organisations". In detail, its

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1 Government agencies felt the need to provide indications on the valuation of businesses, equity interests and individual asset within the framework of their specific operating area - taxation.

2 In the case of IVSC, this is a set of different documents, which also includes a framework.

3 "... if a researcher would approach things without a preconceived opinion, how would he be able to pick the facts from the tremendous richness of the most complicated experiences that are simple enough to reveal their connections through laws?" (Einstein 1919, 108).

4 The initial name was *International Assets Valuation Standards Committee* (IAVSC), then amended in 1994 to become the present name.

5 The first standard-setting experiences in the field of business valuation date back to the seventies of last century, with the Royal Institution of Chartered Surveyors, which issued its first principles in 1976. Since then, there has been a succession of new issued standards, particularly in the eighties and nineties, even if other standards were also issued more recently, in the first years of the third millennium. Just think of the American Institute of Certified Public Accountants (AICPA), whose standards were published in 2007, and the Conseil Supérieur de l'Order des Experts-Comptables (CSOEC), which issued standards in 2012.

members are represented by 56 Professional valuation organisations; 25 Institutional members; 5 Corporate members; 4 Academic members. In addition to that, its members come from almost 50 different countries.

The progressive increase of members with such a varied geographical origin is a proof of the importance the organisation has gained in an international perspective and of the effort of cooperating with other organisations operating in the same field. This is the perspective that should also be used to read the memorandum of understanding signed in 2014 with the International Financial Reporting Standards Foundation, to promote improvements in the valuation practices used in the preparation of financial reports.

The IVSC Bylaws grant important prerogatives to its members, some to be exercised periodically and others continuously (International Valuation Standards Council [IVSC] 2013c). As to the former, during the annual meeting the members elect Trustees to the Board of Trustees, receive reports of the IVSC Boards, admit new members, formalise appointments of persons to IVSC Boards and receive the financial statements of the Corporation (International Valuation Standards Council (IVSC) 2017d).

In parallel, there is a more ongoing duty, which consists in taking part in the Valuation Professional Organisations Advisory Forum, whose role is to support and promote IVSC activities.

The IVSC includes three main Boards, each with a term of office of three years, but with the possibility to be renewed.

At the top of the structure there is an independent global Board of Trustees, elected by the IVSC's members, whose tasks regard basic governance policies, strategic direction, and funding, up to the control of technical boards (exercised by the IVSC Standards Board and the IVSC Professional Board). But the board also plays another essential role, that of ambassador - "to achieve buy-in and recognition of International Valuation Standards" (International Valuation Standards Council [IVSC] 2017a).

The two core activities, i.e. setting international standards, promoting and developing quality professional practices, and consequently professional valuers, are supervised by the IVSC Standards Board (IVSB) and by the IVSC Professional Board (IVPB), whose members are appointed by the Board of Trustee.

The IVSC Standards Board plays the most critical and important function of setting forth international valuation standards, for which purpose it also liaises with other standard setters operating in various countries worldwide, and defining the methods and procedures used to accomplish that task, because standards are approved only after completing a complex process consisting in the preparation of many intermediate documents, i.e. consultation papers and exposure drafts, which are supervised by "experts, parties interested in valuation standards and the public at large" for their opinions (International Valuation Standards Council [IVSC] 2013c, art. V, 46. B; International Valuation Standards Council [IVSC] 2014b, 7). The IVSC Professional Board has the task of promoting the dissemination of high quality professional practices also by defining International Professional Standards (IPSs)" (IVSC Annual report 2015-16, 6). The IVSC Professional Board includes the following sub-boards: the Tangible Assets Standards Board, the Business and Intangible Asset Standards Board and the more recent Financial Instruments Standards Board.

Continuous cooperation with external parties is also institutionalized through the creation and management of bodies entrusted with the task of connecting the IVSC with the operating environment. One example is the Valuation Professional Organisations Advisory Forum, which includes the Valuation Professional Organisations (VPO) in membership of the IVSC.

The purpose of the forum is to spur internal dialogue in the VPO and "to provide advice and counsel to the IVSC Boards" (International Valuation Standards Council [IVSC] 2017b).

IVSC's Mission and Business Model

As is well known, the Mission defines the identity of an organisation by specifying its primary purposes[1], and necessarily affects its operating models and scope of action. Since the IVSC is an independent institution, its mission can be clearly inferred from the IVSC Sixth Amended and Restated Bylaws, which states that the institute "is organized and shall be operated exclusively in pursuit of establishing and maintaining a rigorous high quality set of international valuation standards (the "International Valuation Standards" or the "IVS") and to contribute to the development of the worldwide valuation profession thereby serving the public interest" (International Valuation Standard Council [IVSC] 2013, Article 1. 2; About the relationship between accounting and public interest see: Baker, 2005; Cooper, 2005; Gaffikin, 2005; Graham & Neu, 2005; Davenport & Dellaportas S, 2009; Lehman C.R., 2005; Sawabe, 2005. See also: IFAC, 2012a, 2012b).

Consistently with its nature of independent institution, the IVSC identifies a first institutional purpose in playing the role of standard setter on an international scale (International Valuation Standard Council [IVSC] 2014a). This having been said, issuing standards or principles necessarily implies another important function: to harmonise valuation practices globally.

The other institutional purpose is to operate for the development of the profession in the field of valuation,

[1] "The mission statement spells out the underlying motivations for being in business in the first place – the contribution to society that the firm aspires to make" (Collis & Rukstad 2008, 85).

always on an international scale, by favouring the dissemination of the appropriate practices and ethical principles to protect the quality of the professional services rendered and increase confidence in the task of valuation. This function is also carried out through the preparation and la publication of International Professional Standards (IPSs). However, we should point out that the IVSC is a non-member organisation, which means that it may not become a trainer and an accreditation body. This nature of non-member organisation is simultaneously a strength and a weakness: the former because this feature favours the independence of the institute, the latter because the institute has no sanctioning power on valuation experts. Ethical rules and valuation standards, whose aim is to require correct behaviours from a deontological and technical perspective, respectively, tend to lose effectiveness because they cannot leverage the sanctioning power of the organisation[1].

Both institutional purposes foster a climate of confidence in business valuation with the different stakeholders and serve public interest, which becomes the very rationale of the organisation and a distinguishing feature of its operations.

3. The Regulation of IVSC in the Business Valuation Area: State of Art

The standards issued by IVSC can be analysed by adopting different perspectives. As we have advanced earlier, we chose the three following observation profiles: the matter regulated by standard setters, the regulation strategy, and the type of regulation system selected.

3. 1 The Regulated Matter

The IVS regulate different valuation service areas, the main being business valuation. They have been updated many times, but this paper will only consider the last version approved by the IVSC Standards Board on 15 December 2016, effective from 1 July 2017. The matter is regulated according to a hierarchical order; therefore, after a short introduction and a small glossary, the framework is presented to indicate that it "... serves as a preamble to the IVS" (Introduction, 2) and highlights the need to comply with certain priority standards, which include the objectivity and competence of the valuer's professional judgement. These are followed by General Principles, which identify basic assumptions and requirements to be complied with in the valuation of all sorts of assets, for any purpose. The last part regards the IVS Asset Standards, which regulate the valuation of specifics assets.

For completeness of information, we provide the following table summarising the subdivision of International Valuation Standards:

- Introduction
- Glossary
- IVS Framework
- General Standards
  - IVS 101 Scope of Work
  - IVS 102 Investigations and Compliance
  - IVS 103 Reporting
  - IVS 104 Bases of Value
  - IVS 105 Valuation Approaches and Methods
- Asset Standards
  - IVS 200 Business and Business Interests
  - IVS 210 Intangible Assets
  - IVS 300 Plant and Equipment
  - IVS 400 Real Property Interests
  - IVS 410 Development Property
  - IVS 500 Financial Instruments

The following parts of this paper will exclusively analyse the Framework and General Standards in view of their universal applicability[2].

3.2 The Regulation Strategy

There are several different ways to issue standard, which determine different regulation strategies. Part of the scientific community distinguishes between a "bureaucratic model", a "delegate model" and a "self-regulation

[1] See hereinafter § 11.3.2.

[2] We should point out that this paper will only analyse the regulatory system originating from the IVS, and will neither take into account Technical Information Papers (TIPs), i.e. specific technical guidelines, nor International Professional Standards (IPSs), which, as we can read in IVSC's website, "are standards that govern the competency of valuation professionals, through codes and benchmarks for their conduct, capability and competency" (International Valuation Standards Council [IVSC] 2017c).

model" (Di Pietra, McLeay & Riccaboni 2001, 920-923). While in the "bureaucratic model" regulation is the result of a direct intervention by the State (by the Parliament or Government), in the "delegate model" regulatory functions are assigned by the State to an Authority and in the "self-regulation model" the regulatory process stems from actions of the same users of the standards, through their own representative organisations.

Based on these facts, we may observe that, in business valuation, regulation stems from the– direct or mediated – initiative of professional associations, and only in the specific case of valuations for tax purposes they stem from government agencies, which take care of collecting taxes and ensuring a correct application of tax laws.

In the case of the IVSC, and, more generally, of independent institutions, regulation is the result of the corporatist spirit of professionals operating in the field of business valuation; therefore, we have an example of self-regulation, because the users of the standards are those who take care to define them through the activity of their own representative bodies[1].

This is proved by the fact that:

- IVSC was created by associations of professional categories;
- The revision of the standards issued by the Institute is based on an involvement and consultation process that is generally used precisely by said associations, which periodically receive Consultation Papers or Exposure Drafts to solicit comment letters;
- Valuation professionals are also members of the Standards Board of the Institute, the organisation entrusted with developing, monitoring, reviewing and amending standards, sometimes representing their own associations.

The self-regulation model enjoys the benefits of the flexibility of standards, which makes it easier to develop and amend, but is simultaneously affected by a weaker cogent force, which limits compliance with the standards. In addition to this, the IVSC has no sanctioning power on expert valuers, as we said before, because they are non-members.

At the moment, its principles are adopted by valuation professionals on a strictly voluntary basis. In a report published in 2007 by the IVSC entitled *Review of the International Valuation Standards*, we read that *"… the role of standard setters is to set standards, not to enforce them. The international valuation standards can only be enforced by others, such as national institutes, regulators, and auditors"* (International Valuation Standards Council [IVSC] 2007, 11). The only exception are the rare cases where professional associations adopted the same standards and made them compulsory for their members. In this regard, we point out that the RICS requires its members to also adopt the International Valuation Standards of the IVSC (RICS 2013, 1).

Undoubtedly, the effectiveness of the regulation, and consequently the quality of valuation processes and estimates, greatly depend on the enforcement of the standards issued, that is on the actions implemented by the various parties, whether public or private, to ensure compliance and restrain violations. In the opinion of the authors of this paper, this is an essential element for the future of domestic and international valuation criteria. Nobody can deny that, at the moment, there is virtually no sanctioning system to punish the infringement of IVS international standards, except for the sole case of RICS members, because standard are adopted on a purely voluntary basis.

3.3 The Regulation System

Standards may be developed according to different approaches based on their degree of flexibility. Let us now briefly summarise the main characteristics of the three regulation models described, which can be principles-based, rules-based or mixed (Alexander 1999, 240-241; Alexander & Jermakowicz 2006, 137-139; Burgemeestre, Hulstijn & Tan 2009, 38-41; Nelson 2003, 91-93; Wüstemann & Wüstemann 2010, 14-16).

The *principles-based model* is based on a set of guiding principles that can inspire the solution of several problems (Benston, Bromwich & Wagenhofer 2006, 165-168; Schipper 2003). Being ample guidelines rather than detailed rules, having a professional judgement is of paramount importance (Sin, Moroney & Strydom 2015, 283). Even if some rules cannot be avoided, guidelines or preset rules are not meant to be used for each situation. The problem subject to regulation must be resolved, in the case at issue, according to the underlying rationale of the standard. We may say that, in such an approach, substance prevails over form (Psaros, Trotman 2004, 78).

Conversely, the *rules-based system* consists of a body of strict rules created to accurately define the specific features of the matter examined. In this case, formal compliance with the rules set by the standards prevails over the professional judgement. The rules must be applied almost mechanically. Therefore, it is not wrong to say that, in such a system, form prevails over substance.

[1] Although it is true that, in this case, independent institutions actually operate as *super partes* third parties, delegated by the professional associations of valuers, it does not seem logical to classify this case under the "delegation model", because the mandate is usually of a legislative nature, in this case.

The two regulatory approaches just described represent extreme limits within which intermediate solutions are possible. That is the case of the so-called *mixed systems*, where general basic principles may exist together with detailed rules (AAA Financial Accounting Standards Committee 2003, 74).

A question can be raised at this point: are IVS more informed to a *principles-based*, a *rules-based* or a *mixed* approach?

According to our investigation, the regulation system adopted seems to lean towards the *principles-based* model, as can be inferred from various, more or less explicit, symptomatic elements (Tweedie 2007).

The hierarchical structure assigned to the regulated matter already leans towards this interpretation. As we have seen in the previous paragraph 11.3.1, after the introduction and the glossary, the principles start with the Framework, followed by the General Principles, to be only subsequently followed by the IVS Asset Standards referred to the valuation of specific assets.

A further aspect that reveals the largely *principles-based* nature of the *standard*s examined in our investigation seems to be found in the fundamental role extensively recognised in the different documents to the *professional judgement* of the expert within the framework of the the valuation process. It is appropriate to quote the opening of the IVS Framework of the IVSC: *"applying the principles in these standards to specific situations will require the exercise of judgment"* (International Valuation Standards Council [IVSC] 2013a, 12). The large use of professional judgement, in the opinion of the authors of this paper, constitutes further evidence that this is a *principles-based* regulation system more based on guidelines than on detailed rules, which means that a greater discretionary power is left to the valuation expert[1]. In many points the standards refer to the discretionary power of the valuer, who is entrusted with many choices concerning, for example, the bases of value (IVS 104, 20.2), the valuation approach and the method(s) (IVS 105, 10.4), the level of detail of the investigations to be conducted for the estimate (IVS 102, 20).

But there is even another feature that seems to confirm the adoption of a principles-based approach to a certain extent: the text mentions certain 'minimum requirements' the expert is required to meet concerning, for instance, the content of the report (IVS 103, 30.1). In other words, the know-how codified in the principles at issue is a rather limited portion of the knowledge required for the expert to carry out his valuation activity with due professional diligence. This is very clearly reflected in the simple comparison between the short documents published, which only in rare cases exceed one hundred pages, and the more known business valuation treaties, which sometimes even exceed one thousand pages[2].

Now, if this is true, it is then rather evident that the knowledge required to render valuation services is more extensive than the inherent knowledge of the standards themselves and that, consequently, the latter are informed to a more *principles-based* than *rules-based* approach[3].

Another aspect that drives us towards a *principles-based* nature of the standards examined may be their *low degree of differentiation*. The documents propose univocal solutions for the regulation of actually different situations, therefore they are general in nature. This feature is also found in the Asset Standards, which concern a more specific and restricted content than General Principles (IVS 200, 20.10; IVS 210, 20.10; IVS 300, 20.12; IVS 400, 20.8; IVS 410, 20.2; IVC 500, 20.2).

Conversely, experience teaches that the processing of estimates and valuation reporting are often characterised by extremely different features as a function of the varying parameters used, such as, *inter alia*, the *expert's task* (e.g. valuation, fairness opinion, opinion on the work done by other experts, etc.), the *activities carried out as a basis for the valuation task* (e.g. special finance operations, such as assignments, contributions, mergers, demergers, transformations, listing in stock exchanges; insolvency proceedings, employee stock purchase plans, divorces, divisions of inherited assets, buy-sell agreements, payment of due taxes, etc.), the *valuation scope* (e.g. business, business branch, equity interests of various kinds or intangible assets), the *type of business* (e.g. manufacturing, commercial or services companies, old or new economy companies, financial or non-financial companies, divided or undivided companies, family or non-family run businesses, asset management companies – financial or real estate holdings – or operating companies, etc.), the *valuation perspective* (e.g. neutral or party valuations).

Finally, we may observe that the analysis of the contents of the various documents at issue clearly showed their prevalent *general* and *abstract* nature, which is exactly the typical nature of documents written with a

1 In this regard, it has been appropriately observed that *"the more discretion a provision reposes the more it is principle-like and the less discretion reposed the more it is rule-like"* (Cunningham 2007, 10). And again: *"… principles are typically described as broad guidelines that, instead of providing detailed implementation guidance, require preparers to exercise judgment in applying the principles to specific transactions and events"* (Wüstemann, Wüstemann 2010, 14-15). On the same subject, also see: Tweedie, 2007, 7; Psaros, 2007, 528; Agoglia *et al.* 2009, 750-751.

2 In the literature in English, Hitchner (2011), Pratt & Niculita (2007), Trugman (2012), *inter alia*, exceed 1,000 pages.

3 Note that *"applying rules requires relatively little knowledge. Knowledge of the rule itself and the instantiation of the concepts involved, suffices. Applying principles requires more knowledge, such as knowledge of the context and of all other relevant principles"* (Burgemeestre, Hulstijn, Tan, 2009, p. 39).

principles-based approach[1].

3.4 Framework and General Principles

The Framework, which serves as an introduction to the subsequent General Principles and Asset Standards, begins by clarifying some deontological issues, i.e. the need for the valuer to be professionally qualified and possess the necessary skills and specific knowledge required to perform the task in each market sector and for each purpose and scope of valuation[2]. In addition, the valuer is required to apply the principle of objectivity, because valuation is certainly a judgement – which does not exclude elements of subjectivity in itself –, but a judgement that must be impartial and based on reliable inputs and assumptions. Subjectivity should be as limited as possible throughout the entire valuation process "... to avoid biased analyses, opinions and conclusions" (Framework, 40.1)[3].

General Principles

IVS 101 Scope of Work: this is the principle that informs the minimum content of the scope of work, where the terms that qualify a valuation engagement are outlined. Defining the purpose of the valuation and the responsibilities of the various parties involved in the task is essential.

Apart from some common constitutive elements that are found in every contractual relationship (e.g. the identification of the valuer, the identification of the client, the date of valuation), the valuation must necessarily include a definition of its purpose ("the valuation purpose"), required to identify the specific type of valuation to be conducted among the possible variants and a specification of the Asset(s) to be estimated. This will imply the selection of the basis or bases of value to be used[4], as well as the nature, extension and limitation of the valuer's task. In fact, the purpose affects the whole content of the valuation, i.e. the valuer's qualification, the nature and sources of information- all points to be defined.

In addition, the principle requires the specification of the assumptions of the valuation process, the type of report agreed between the parties, as well as any restrictions on the use and disclosure of the report.

The Scope of Work shall then be preferably completed in writing, before or during the conduction of the task, but in any case before its conclusion. The valuer shall also declare that the valuation "... will be prepared in compliance with IVS and that the *valuer* will assess the appropriateness of all *significant* inputs", and specify any departure from these standards (Framework 60.1. – 60.4.)

IVS 102 Investigations and Compliance

The principle states how the task shall be performed. First of all, it recalls the need to conduct a preliminary investigation in compliance with the valuation purpose and with the basis(es) of value. Limits to the investigation can be agreed between the parties, provided that they do not affect the reliability of the valuation and, in any case, that they are indicated in the Scope of Work. Furthermore, if, during the investigation, the information collected is deemed to be inadequate for the purpose of the valuation or, in the event that they have been supplied by third parties, it is deemed to be insufficient or non-reliable, the Scope of Work shall be reviewed, otherwise the valuation assignment will not comply with the IVS.

Then the information processed shall be archived and preserved for a reasonable period of time, obviously keeping any legal obligations in due consideration.

IVS 103 Reporting

The valuation process is concluded with a Report that will be prepared and delivered to the parties involved, who will generally use that document only to learn the outcome of the valuation and understand the criteria that led to the value shown. For this purpose, the Report shall contain extremely clear and unbiased information to allow the reader to trace back all the logical steps of the process that led to the specific result starting from the "... scope of the assignment, its *purpose* and intended use (including any limitations on that use) and disclosure of any assumptions, special assumptions (IVS 104 Bases of Value, para 200.4), *significant* uncertainty of limiting conditions that directly affect the valuation" (IVC 103, 10.2). Depending on the purpose, complexity of the assets to be valued and user's requirements, the valuer will define the most appropriate level of detail.

The format of the report is not predefined; however, it should be appropriate for its communication purpose. Then the principle details the minimum content required for the report both if the task includes the valuation of

1 *"A… classification views rules and principles in terms of designated attributes such as their relative generality versus specificity, abstractness versus concreteness and universality versus particularity. Provisions characterized by generality, abstractness or universality are principles while those being specific, concrete and particular are rules"* (Cunningham 2007, 10).

2 "*Valuer* has been defined as an individual, a group of individuals, or a firm possessing the necessary qualifications, ability and experience to undertake a valuation in an objective, unbiased and competent manner" (Framework, 30.1.), and later "Valuations *must* be prepared by an individual or firm having the appropriate technical skills, experience and knowledge of the subject of valuation, the market(s) in which it trades and the *purpose of the valuation*" (Framework, 50.1.)

3 The Framework also contains departures from the IVS that can be deemed acceptable.

4 IVS 104 is devoted to the base of value.

one or more assets and if it is the result of a valuation review.

IVS 104 Bases of Value

The last version of the general principle introduced IVS 104 to extend the description of the bases of value previously briefly outlined in the Framework.

The general principle plays a prominent role in valuation, as the bases of value summarise the fundamentals of the estimate as regards, for example, the parties to the transaction and their identification – hypothetical, known or specific parties, members of an identified/described group of potential parties, etc. (IVS 104, 10.6). These preconditions, as we have seen earlier, must be consistent with the purpose of the valuation and may, in their turn, affect the choice of the valuation method adopted and the nature of the transaction – hypothetical transaction, actual transaction, a purchase (or entry) transaction, a sale (or exit) transaction, a transaction in a particular or hypothetical market with specified characteristics (IVS 104, 10.4).

The cases of value defined by the IVS are not exhaustive; in fact, the same principle recalls others, not contemplated therein. Those described in the principle are:

- Market Value
- Market Rent
- Equitable Value
- Investment Value/Worth
- Synergistic Value
- Liquidation Value

The Market Value is defined as "... 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" (IVS 104, 30.1.)[1]. Such a value configuration requires the existence of an active and competitive market where participants can act freely and where a negotiated price is formed. Therefore, it is precisely from the market that the input for the valuation must be taken.

The principle specifies that the Market Value of an asset reflects "... its highest and best use", or the use "... that maximises its potential and that is possible, legally permissible and financially feasible"[2] (IVS 104, 30.4.).

Instead, the Market rent is nothing but "... the estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion" (IVS 104, 30.1).

Close to the Market Value configuration we find the Equitable Value configuration, which is always referred to an estimated transfer price for an asset or liability between two well-identified contracting parties, keeping into account the respective advantages and disadvantages, unlike the first value configuration. In this case, the value is eventually devoid of the requirement of neutrality.

The Investment Value/Worth is the value assigned to an asset by assuming the perspective of the current owner or a future buyer. It must take into account the benefits the asset brings to its present or future owner, whether for operating purposes or for investment. It is therefore an entity-specific basis of value, which means that it is a value estimated regardless of an assumed exchange, but rather determined by the peculiar circumstances and objectives of the entity for which the valuation is performed.

The Synergistic Value is a party value and not a neutral one, because it includes the synergies that can be produced to the benefit of a specific buyer as a result of the combination of two or more assets or interests[3] - this is its difference from the Market Value.

The Liquidation Value is the value that can be realized when an asset or a group of assets is sold in an atomistic manner, also considering the costs to be incurred to prepare the asset(s) for sale and the cost of the related liquidation[4].

Then, in the subsequent sections, the principle examines the peculiarity of each base of value. Briefly, we simply point out how the principle includes a rather long definition section with the purpose of avoiding any

1 The principle then accurately analyses the meaning to be attributed to each term of the sentence.

2 The principle specifies that "The highest and best use may be for continuation of an asset's existing use or for some alternative use. This is determined by the use that a market *participant* would have in mind for the asset when formulating the price that it would be willing to bid" (IVS 104, 30.4.).

3 In par. 190 the principle makes a digression concerning the notion of Synergies.

4 The principle specifies that the liquidation can be an orderly transaction or a forced transaction. While the former refers to the value that can be realized with an atomistic sale performed over an adequate period of available time to find one or more buyers, with the seller being compelled to sell on an as-is, where is basis, in the latter case the value is estimated by considering that the owner is induced to sell by force majeure, and consequently cannot manage the liquidation stage in the times and with the methods required to ensure the best possible gain. The two types of liquidation value are detailed in paragraphs 160 and 170 of IVS 104.

ambiguity and uncertainty on the meaning of the technical terms used, which is undoubtedly a benefit for the consistency of the language and practices.

IVS 105 Valuation Approaches and Methods

This principle outlines the most common approaches adopted in the valuation practice and the respective applicable methods. Like the previous, this principle was also introduced with the last revision of the standards.

The principle repeats that it is the valuer's task and responsibility to choose the most appropriate approach and method by taking into account the purpose of the valuation, and therefore the basis(es) of value and the premise(s) of value[1], the nature of the asset, as well as the availability and reliability of the information required for the method(s) selected. The valuer may also consider it appropriate to use multiple approaches or methods, to then reconcile the different values in a conclusive value, by adopting – for this purpose – a logical process duly described in the report.

The different approaches and methods require various kinds of information to be collected from a variety of different sources; however, the valuer should appreciate and prefer, where possible, information sourced from active markets, because one should never forget that "... price information from an active market is generally considered to be the strongest evidence of value" (IVS 105, 10.8).

The approaches described are well known in the literature and in professional practice; they are the Market Approach, the Income Approach, and the Cost Approach. For each of them the valuer shall analyse the application assumptions and the most common methods. For the latter, their main features must be described by summarising their key steps and formula parameters wherever the method so requires. All this will help the valuer to make his main choices in the application of the approaches and most common methods[2], as well as any element to be considered to make his best efforts in performing the task.

4. The Harmonisation of Valuations at International and Local Level

The role played by the IVSC is particularly complex due to the delicate balance that must be reached, on the one hand, with an authoritative organisation, 'The Appraisal Foundation', and, on the other hand, with the domestic organisations operating in the various countries where it exercises its influence.

As to the former, we should remember that The Appraisal Foundation (TAF) is a non-profit organisation founded in 1987 by nine main valuation professional organisations operating in the United States and Canada[3] with the purpose of establishing reliable and shared valuation practices not only as far as a business, a business ownership interest, a security, or an intangible asset, but also for real and personal property.

The principles issued by TAF, known as Uniform Standards of Professional Appraisal Practice (USPAP), are commonly adopted in the United States because they are applied no only by valuers who are members of TAF-affiliated professional organisations, but also by professionals charged with the task of providing valuations in federal related transactions. In this regard, we should point out that, in the United States, the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) recognised the USPAP of The Appraisal Foundation in 1989 as generally accepted principles and required valuation experts to comply with them for transactions taking place in the federal territories, this actually attributing TAF a role of non-governmental standard-setter[4]. In addition to this, several U.S. government agencies require the adoption of USPAP in valuations performed for them.

It is therefore natural for IVSC and TAF to cooperate, as they have been doing for several years now, in the standard-setting activities in order to reach a single set of global principles. In a first Memorandum of Understanding signed by the two organisations in 2006, known as Madison Agreement, we can read, *inter alia*,

[1] In the choice of the approach and the method the valuer shall also consider the "... approaches or methods used by participants in the relevant market" [IVS 105, 10.3. (c)].

[2] For example, concerning the Income Approach, the principle lingers on the Discounted Cash Flow (DCF) Method to briefly recall the most significant choices the valuer will be required to make to apply the method and the considerations that will inform his choice; to this purpose, the text refers to the Type of Cash Flow, to the choice of the Explicit Forecast Period, and to the preparation of Cash Flow Forecasts, an estimate of the Terminal Value and of the Discount Rate (IVS 105, 50).

[3] The nine professional organisations are: The Appraisal Institute of Canada, the American Institute of Real Estate Appraisers (AIREA), the American Society of Appraisers, the American Society of Farm Managers and Rural Appraisers, the International Association of Assessing Officers, the International Right of Way Association, the National Association of Independent Fee Appraisers, the National Society of Real Estate Appraisers, and the Society of Real Estate Appraisers. Remember that, in 1991, AIREA and the Society of Real Estate Appraisers merged under the new name of 'Appraisal Institute'.

[4] "*The Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) of 1989 makes compliance with USPAP mandatory for all federally related real estate transactions. Although not mandatory for federally related transactions involving personal property and business appraisals, USPAP has been adopted by major appraisal organizations in North America and has become widely recognized as the generally accepted standards of appraisal practice*" (Pratt & Niculita 2007, 4-5).

that *"the International Valuation Standards Committee (IVSC) and The Appraisal Foundation (TAF) share the common vision of a valuation profession with a single set of high quality understandable and enforceable global valuation standards"* (International Valuation Standards Committee [IVSC] and The Appraisal Foundation [TAF] 2006, 1). In October 2014, the two organisations signed a second memorandum of understanding with the purpose of harmonising, over a span of three years, all the remaining differences between the two sets of standards (International Valuation Standards Council [IVSC] and The Appraisal Foundation [TAF] 2014b). More recently, on June 29, 2016, a guide called "A Bridge from USPAP to IVS. A guide to producing IVS-compliant appraisals" was published "... to assist appraisers familiar with USPAP to produce a valuation that is also compliant with the IVS" (The Appraisal Foundation [TAF] 2016, 2).

As regards the relationship between professional associations and the IVSC, we should point out that these two organisations have a sort of biunivocal relation with each other – see Figure 1.

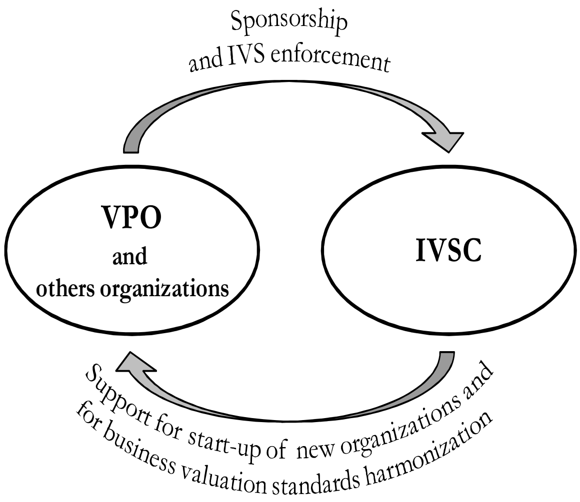

Figure 1. — Relationship between professional associations and IVSC
Source: graph processed by the authors.

Professional associations, acting as sponsors of IVSC, promoted its creation; since then, they support and fund its activity with annual support, but in some cases they also enforce IVS by stating the mandatory nature of its adoption for their members. IVSC, in its turn, provides support in terms of expertise and knowledge for the creation of new professional associations or the development of existing ones[1], but most of all plays the role of harmoniser by issuing its own standards with an international application. In fact, this is a "bipolar system", which raises a number of issues about the institutional relationships between domestic professional associations and the IVSC, and concerning the applicability of the valuation principles issued by both organisations.

The existence of these bodies, with overlapping scopes, clearly requires harmonisation.

A first attempt at harmonising the principles of a professional association and the international principles of IVSC has been the basic approach of the standards issued by the Royal Institution of Chartered Surveyors (RICS), whose 'Red Book', new 2014 edition, collected the principles issued by the RICS. This publication not only recognised and adopted IVS by requiring its members to adopt them, but even supplemented them with a set of detailed guidelines and specific assumptions to be used in their implementation (Royal Institution of Chartered Surveyors [RICS] 2013, 1). This clear intention of the RICS to align its own standards with those of the IVSC is also confirmed by the fact that the Red Book, as outlined in its own subtitle, includes the IVS principles in the final part of the document itself. This is a clear example of an enforcement of the IVS by a professional association.

In France, the attempt at harmonising the different standards in force in the national territory with those of the IVSC is being promoted by the Fédération Française des Experts en Evaluation (FFEE), an organisation that gathers fourteen French professional associations, including the Conseil Supérieur de l'Ordre des Experts Comptables (CSOEC) (For further details see: Conseil Supérieur De l'Ordre des experts-Comptables [CSOEC] 2012) and the Compagnie Nationale des Commissaires aux Comptes (CNCC), whose members are expert

[1] In this regard, we remind readers that the IVSC, in 2013, published a guide entitled *Establishing and Developing a Valuation Professional Organisation* (International Valuation Standards Committee [IVSC] 2013b) as a first initiative to provide "*… practical assistance to the developing profession to support current and prospective member bodies in their efforts to become fully effective valuation organisations, contributing to economic growth and stability worldwide"* (p. 1).

valuers operating in different valuation areas (For further details see: Compagnie Nationale des Commissaires aux Comptes [CNCC] 2011). The most interesting feature for our study is that the FFEE institutional purposes, inferred from its Mission, are precisely *"… la promotion des normes édictées par l'IVSC et… l'application de celles-ci par ses membres*" (Fédération Française des Experts en Evaluation [FFEE] 2013). In this case, the enforcement of IVS is included in the mission of the organisation itself.

The examples described reveal the ongoing process towards a progressive harmonisation of the standards established by the different organisations at local, national and international level. Clearly enough, the existence of a globally shared pattern could uniform the action of the valuation experts operating in different countries – an increasingly important requirement in the present global economic scenario. And this is exactly the role the IVSC intends to play[1] - a role that has even been recognised to the IVSC by the G20, when the President of the Group, in 2011, invited the Council, together with eight private organisations, to take part in a task force charged with the task of analysing and creating recommendations on the convergence of the rules regulating the professions and industries operating in the financial sector[2]. And it is in this direction that the IVSC is operating with increasing intensity. To mention just an example of this, during the IVSC Advisory Forum Working Group (AFWG), held in 2016, Working Group members defined the objective to intensify their relationships with professional organisations that already were members of the IVSC, but also to create new professional organisations, not related to the institute, in order to gain more insight in the regulation of the profession of valuer and as regards the level of use of the IVS, not yet sufficiently widespread in the global business valuation community.

5. Conclusion

This paper highlighted how the request for appropriate valuation services for the complex scenario of the economic scopes to be valued and the globalisation of the markets has called for the development of special professional qualifications that need deontological and technical support tools.

The IVSC plays a prominent role in this process by preparing adequate technical tools for the valuers even beyond national borders. As we have seen, the Council exclusively plays a role of international standard-setter, while it has no standard-enforcement functions, consistently with its nature of non-member organisation. As a consequence, it has no sanctioning power vis-à-vis those who do not adopt its standards. For this reason, in order for this Council to operate effectively in the interest and for the protection of the common welfare, a coordination is required with domestic organisations whose members are required to comply with the valuation standards they promote. Cooperation and coordination between organisations operating in the field of valuation are therefore seen as compulsory steps to achieve the purpose of harmonising valuation standards and valuation practices on a global scale. It is a complex process. In fact, as we pointed out several times, several national and international organisations exist together in the world of valuation services, so much so that we are in a really "bipolar system", consisting of domestic associations, on one hand, and international organisations, such as the IVSC, on the other hand. Therefore, it is logical to believe that the future of the valuation profession will be affected by the dynamics of such a system, and particularly by the role the IVSC will play in the next few years, as well as by the consent it will be able to achieve with national associations. If said system will progressively consolidate – as it is likely to do, and perhaps as it would be desirable – then the tasks of the two parties at stake will have to be clearly defined. The theme, as one can imagine, includes several different issues, including, not less importantly, the significance of national and international valuation principles within each country. In this case there will be more than one question to ask: which will be the role of domestic standards in front of a possible reinforcement of international standards? Will national principles maintain their own independence from international standards or will we have a progressive harmonisation of the former into the latter? Does it make sense to believe that, in a closer or more distant future, international standards will even replace national standards?

Perhaps the best answer to these questions can be given by recalling the vision expressed by the IVSC about the relationship between national and international standardization: starting from the distinction between standard-setting and standard-enforcement, the proposal put forward by the IVSC to the professional associations of the various countries is to give up, at least in part, their role of standard setters, i.e. domestic principles, and adopt the IVS, to make them compulsory for their members by exercising their own power of enforcement. These associations will continue to issue supplementary standard or IVS interpretation guides, when needed, as required to tackle specific local situations linked, for example, to national laws or regulations[3].

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1 We remind readers that the institutional objectives of the IVSC also include the following: "*to build confidence and public trust in valuation by producing standards and securing their universal adoption and implementation for the valuation of assets across the world*"" (IVSC, 2017, p. 1).

2 For more insight on the final report published by the task force, see: http://www.ivsc.org/sites/default/files/20111006_pstf__final_report.pdf

3 We deem it appropriate to report the entire part to which we have referred: "*A valuation professional organisation needs*

But there are two more issues that deserve more attention, which concern the content of the standards.

One first aspect that cannot be missed by an attentive reader is that the standards contained in the document represent a set of minimum requirements, particularly as regards the valuation methods the experts will have to use. This means that the sole compliance with said standards does not ensure, in itself, the quality of valuation processes and estimate reports. Rather, valuers must enframe their analyses and the information to be disclosed in their estimate reports within a wider content, by taking inspiration from the theory and principles of valuation – codified, instead, in the best business valuation manuals –, from the body of laws formed on that matter, as well as from the rules of the applicable legal framework.

A secondo elements to be highlighted is that valuation standards indicate a greater attention towards procedural and formal issues rather than towards content issues. It is useful to add that, as regards the extent and degree of insight in the themes at issue, standards are not at all comparable in themselves, for instance, with U. S. generally accepted accounting principles (GAAP) or International Financial Reporting Standards (IFRS). In order to express a global judgement on the principles of the Statement dedicated to the most valuation-related part, we may observe that, unfortunately, they touch the themes described above, particularly the valuation approaches and methods, as well as value adjustments (premiums and discounts), in a rather hasty manner. For example, the document does not contain indications addressing the choice of approaches, methods and estimate procedures of the different valuation parameters (e.g. flows, cost of capital, growth rate, etc.). In other words, none of the standards provides elements that may inspire a valuer to select one or more specific approaches, one or more particular methods, to choose among the different methods for the appraisal of valuation parameters. The standards pass the decision to the "professional judgement" of the expert, recognised to play an essential role in the valuation process and this is the result of a precise choice of the IVSC. In the opinion of the authors of this paper, IVS is characterised more as a *principles-based* than as a *rules-based* system.

Two closely related questions arise at this point: does the waiver to be a more robust regulator of valuation issues stem from a final choice or is it to be related to an assumed initial stage of the lifecycle of the IVSC standards, that will presumably be followed by action aimed at expanding and increasing its scope by the Institute? And again: may we believe that, in a more or less distant future, there will be a drift of the *regulation* model from the *principles-based* type towards the *rules-based* type? It is not easy to answer these questions. Certainly, at present, an expert who wants to process a valuation cannot rely exclusively on the principles in question. The knowledge and professional competences required for this activity are significantly larger. In fact, we may repeat that while from the point of view of the definition of the task, the collection, analysis and revision of the information, the different stages of the valuation process, the structure and content of the reports, the final certifications – just to mention a few main aspects -, the standards may actually prevent fraudulent behaviour or ambiguous estimate reports, under other profiles they present equally clear criticalities and limits, namely:

- an excessively restricted scope compared with the present development stage of the scientific community and business valuation research;
- a lack of indications on the choice of the different valuation logics, methodologies and procedures and on the main associated application issues;
- an insufficient consideration of the valuation errors the expert may make;
- a sanctioning system, in case of non-conformance with the standards by the valuers, limited only to the penalties imposed by the IVSC.

In the light of all this, it will be interesting to observe the future developments of the principles examined.

It follows from what has been said that the research can be developed according to different directions. In the opinion of the authors, two lines of research seem particularly promising: the first one concerns the relationship between national and international business valuation standards and their harmonization; the other one concerns convergences and divergences between standardization in financial reporting and in business valuation, in terms of both process and content.

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to distinguish between the roles of standard setting and standards enforcement. Setting, or creating, standards is a difficult and time consuming task as not only will they have to be agreed on by the valuation professionals that will use them, but they also need to be accepted by the business community, government regulators and other stakeholders. The IVSC acts as the global standard-setter for valuation but has no role in enforcing their use or ability to sanction individuals who breach the standards. In contrast, valuation professional organisations do have the ability to enforce implementation of the IVSs by their members and to monitor compliance. By adopting the IVSs, a valuation professional organisation not only ensures that its members are following internationally recognised practice, but also avoids spending time and resources on creating standards which, although they may be similar, will not have the same level of recognition as the IVSs. In an increasingly globalised world, the consistency and compatibility of standards across jurisdictions is a particularly important issue. Where necessary, the valuation professional organisation may issue supplemental standards or guidance to reflect local circumstances (e.g. to help its members comply with valuations required under national laws or regulations)" (IVSC, 2013b, p. 33).

One final observation: we believe that the standards issued by the IVSC deserve special attention for several reasons, including:

- the authoritativeness of their source – the IVSC - the larger professional association in the world for number of members, equipped with solid expertise in rule-making and standard-setting activities in different professional areas;
- the recognised status of international principles;
- the general recognition of the IVSC by the various domestic organisations.

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