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Peter Martin, CA
Director, Accounting Standards
Canadian Accounting Standards Board
277 Wellington Street West
Toronto, Ontario M5V 3H2 Canada

Via email: ed.accounting@cica.ca

Re: Measurement on Initial Recognition

Dear Mr. Martin,

First of all, we wish to commend the Canadian Accounting Standards Board on its important and comprehensive work in discussing the matter of measurement upon initial recognition. This document addresses some of the most important issues that have needed to be resolved relative to making Fair Value a truly supportable, market-based value that provides the relevance, transparency and independence to the benefit of users of financial statements.

The issue of measurement bases is a critical one, especially as convergence between IASB and FASB progresses. As the leading valuation organization in the United States, representing approximately 21,000 real property valuation professionals, the Appraisal Institute is a leader in valuation education and methodology. We continue to support efforts to move toward a market basis for financial reporting and to that end, we hope you will find our comments helpful.

2. **Do you agree with the working terms and definitions, in supporting interpretations of each identified measurement basis (see paragraphs 77-96)? If not, please explain what changes you would make. In particular, do you have any comments on the term "Fair Value" and its definition in the light of the discussion in paragraphs 88-93?**

   We are concerned that the line between Fair Value and Market Value persists in being misunderstood. The Fair Value definition incorporates many of the elements of a Market Value definition, but lacks needed specificity because of the omissions. In fact, many of the measurement bases listed in paragraphs 77-96 could, in various circumstances, be construed as Fair Value, but not Market Value.

   In the United States, under the *Uniform Standards of Professional Appraisal Practice (USPAP),* all real property valuation professionals are required to state whether a market value opinion is developed on a cash basis or upon the basis of specified terms. The differences can be highly significant and should be included in the appropriate value definition and related disclosures.

   There are a number of elements that the definition of Fair Value does not recognize that Market Value definitions generally do, including proper marketing time and payment terms. We would encourage you to look to the International Valuation Standards and its Market Value framework for the clarification of these market value concepts.

To the issue of time for exposure to the market, it is our view that this distinction between requirements for Market Value and Fair Value is an important one. It is our view that this distinction is a necessary addition, at least to the explanations of the final wording of the value definition, because it recognizes that not all assets are optimally sold without adequate exposure on the market. Market understanding and consistent reporting are not promoted if one asset is valued on the basis of immediate liquidation while a similar asset owned by a different entity is valued based on a six-month exposure to the market if that is appropriate. We therefore agree with your proposal that there be research to enable the knowledge condition underlying the concept of a market to be fully defined.

3. **It is proposed that there are two fundamental sources of differences between the identified bases for measuring assets and liabilities on initial recognition: a) market versus entity-specific measurement objectives; and b) differences in defining the value-affecting properties of assets and liabilities. Do you agree that these are the fundamental sources of differences between asset and liability measurement bases on initial recognition?**

We agree that there can be differences between entity-specific and market valuations; however, that is not to say that a market valuation cannot or should not consider entity-specific inputs where applicable. While the market inputs are more relevant as a measurement basis upon initial recognition, if the objectives and performance of the entity being valued are in line with those of most market participants, a valuation based on the entity's actual performance may still be relevant to the assessment of Market Value.

4. **This paper analyzes the Market Value measurement objective and the essential properties of Market Value.**

4.b *Do you agree with the proposed definition of "market" (see paragraphs 55-56 of the condensed version and paragraphs 107-110 of the main discussion paper)? If not, please explain why you disagree, and indicate any changes you would make and any issues that you believe should be given additional consideration.*

We have some concern about the proposed definition of "market," particularly the notion of "sufficiently extensive exchange transactions." To the extent that not all assets and liabilities are capable of valuation under the assumption of efficient frontier pricing, purchase and sale, accommodation must be made for the respective market circumstances if a market standard is to be meaningful. It is our view that the vast majority of valuation situations are capable of market support, even in limited-market situations. Additionally, we would suggest that the concepts of "knowledgeable parties" and "arm's-length transaction" should be left to the definition of the value and do not belong in the definition of market. The size of market and number of transactions are considerations in the analysis process to develop a value opinion, not concepts embedded in the definition of market.

The Dictionary of Real Estate Appraisal (4th edition) defines "market" very simply as follows: "A set of arrangements in which many buyers and sellers are brought together through the price mechanism" or alternatively, "A gathering of people for the buying and selling of things; by extension, the people gathered for this purpose." We believe there is no reason to take the definition further.

5. Do you agree with the definition and discussion of entity-specific measurement objectives (see paragraphs 112-116) and their relationship to management intentions (paragraphs 117-121)?

Again, we agree there is an important distinction between market and entity-specific measurement objectives and that the former is far more relevant as a basis for initial measurement recognition. Market Value is based on property's highest and best use, and current owner/operator's use or objectives regarding the property are irrelevant, although they may indeed correspond with the highest and best use. There are value definitions that look to entity-specific objectives, including Value in Use, defined as "The value a specific property has to a specific person or specific firm as opposed to the value to persons or the market in general" (*The Dictionary of Real Estate Appraisal*). Investment Value, "the specific value of an investment to a particular investor or class of investors based on individual investment requirements," also looks to management intentions and is distinguished from Market Value, which is impersonal and detached.

There is a further distinction between measurement objectives and management intentions where the latter are relevant to the assessment of Market Value. For example, if management regards an asset as surplus and plans on disposing of it, its Market Value may be significantly different than if the particular asset were assessed on the assumption that it would be sold as part of a going concern. FASB recognizes this difference in its Fair Value Measurements draft.

7. It is reasoned that there can only be one Market (Fair) Value for an asset or liability on a measurement date (paragraphs 131-138). Do you agree with this conclusion? If not, please explain why you disagree.

We disagree with the notion that there can only be one Market (Fair) Value for an asset or liability on a measurement date. Under the *Uniform Standards of Professional Appraisal Practice,* any opinion of value—Market Value or otherwise—is based on certain assignment parameters: according to a certain definition, as of a certain date, subject to certain extraordinary assumptions and hypothetical conditions, and according to a certain scope of work. If any one of these parameters changes, the value conclusion could reasonably differ.

12. Do you agree with the proposal that, when more than one measurement basis achieves an acceptable level of reliability, then the most relevant of these bases should be selected?

We agree. Relevance is of key importance, and the basis of valuation adopted for financial reporting should be directed toward that purpose.

18. Do you agree with the proposed hierarchy for the measurement of assets and liabilities on initial recognition, see chapter 8?

The Appraisal Institute is sensitive to the reasons why a Fair Value hierarchy was established, but urges a different approach that combines the rationale for this hierarchy with principles that are more consistent with Generally Accepted Valuation Principles (GAVP).

USPAP requires consideration of all three valuation approaches (sales comparison, cost and income), and recognizes that market circumstances will dictate the evidence that is available, relevant and meaningful. Thus, the appropriateness of valuation approaches is a reflection of the market itself, not a rule that is to be superimposed upon the market. The approaches selected and applied are explained and justified in each valuation report in accordance with these standards.

Our experience indicates that a hierarchy of supportive data, explanation and disclosure emerges as data become less available, relevant and/or meaningful. Our profession believes, in a colloquial sense, that “the last thing the client should be concerned with is the value opinion,” because of the primacy of the ethics, standards, GAVP, available data, competency and professional expertise that must be evidenced in its development.

The notion of a hierarchy also suggests that “value” is (or should be) a precise number -- a notion with which we would disagree for the reasons discussed in Question 8.

If, however, a hierarchy is retained, we would suggest that the most recent hierarchy as proposed by the Financial Accounting Standards Board provides a better distinction between the various levels.

19. Do you have comments on any other issues or proposals, including the proposals for further research?

Though our comments are informed by our experience as real estate valuation professionals, we believe that GAVP applies equally over the other disciplines, including business valuation and machinery and equipment valuation. For that reason, it is of paramount importance that GAVP be better understood and reflected in the accounting of assets and liabilities under a Fair (Market) Value model. We therefore fully endorse your proposal (mentioned in paragraph 275 in the long paper) to pursue a project to understand the International Valuation Standards Committee’s body of knowledge and practice in light of financial accounting measurement objectives. Having been involved with the IVSC since its inception, the Appraisal Institute has expertise in the matter of International Valuation Standards and we would be happy to provide our efforts to the proposed research.

Additionally, we continue to believe that the move toward Market Value in financial reporting is in the best interest of the public, investors, government and business decision makers. We believe your paper helps move the discussion in this direction, but suggest areas for continuing clarification toward this end.

We are pleased at the progress toward a more open dialogue between the accounting and valuation standards-setters and professions. We believe that such a relationship is critical to developing a well-supported framework for financial reporting. We encourage you to include the continuous and robust involvement of the valuation profession in your deliberations and discussion, including members of the International Valuation Standards Committee and The Appraisal Foundation as well as experts from associations such as the Appraisal Institute and other valuation organizations.

Thank you for your consideration of our comments. Should you have any questions, please contact Alison Gerlach, Manager, Special Projects, Appraisal Institute, at 312-335-4116 or agerlach@appraisalinstitute.org.

Best regards,

Richard D. Powers

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Cc: Linda MacDonald, Director, Planning & Support Activities
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