

APES GN 20 Scope and Extent of Work for Valuation Services

Prepared and issued by
Accounting Professional & Ethical Standards Board Limited

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1. Scope and application

- 1.1 Accounting Professional & Ethical Standards Board Limited (APESB) issues APES GN 20 *Scope and Extent of Work for Valuation Services* (the Guidance Note). 1.1 -
- 1.2 APES GN 20 provides guidance to assist Members on the application of APES 225 Valuation Services in determining the scope and extent of review, analysis and evidence that, depending on the particular circumstances, may be appropriate for the three types of Valuation Services defined in section 2 of APES 225. This Guidance Note does not prescribe or create any mandatory requirements. 1.2 1
- 1.3 Members using this Guidance Note should refer to APESB's *Due process and working procedures for the development and review of APESB pronouncements*. - -

2. Definitions

For the purpose of this Guidance Note, all definitions are consistent with APES 225 *Valuation Services*. 2 -

3. Scope and extent of work for Valuation Services

- 3.1 Subject to the terms of the Engagement or Assignment agreed with the Client or Employer, a Member who is planning the scope of work for a Valuation Service should determine the extent to which Valuation Approaches, Valuation Methods and Valuation Procedures are applied to the review and analysis of significant information and of the evidence obtained in respect of the Valuation Service. The extent of work to be performed and the evidence to be obtained is a matter for the professional judgement of the Member and will also depend on the availability of information. To assist the Member to exercise that judgment, a summary table is provided below: 4.4 2

Type of Valuation Service	Extent of Valuation Approaches, Valuation Methods and Valuation Procedures applied in the review and analysis of significant information	Extent of evidence obtained
Valuation Engagement	Limited to extensive use of Valuation Approaches, Valuation Methods and Valuation Procedures applied to the review and analysis of the business and the external environment and all other significant information and factors.	Evidence obtained for significant information and factors.
Limited Scope Valuation Engagement	Minimal to limited use of Valuation Approaches, Valuation Methods and Valuation Procedures applied to the review and analysis of significant information.	Limited evidence obtained for significant information.
Calculation Engagement	None to minimal use of Valuation Approaches, Valuation Methods and Valuation Procedures applied to the review and analysis of significant information.	Little or no evidence obtained for significant information.

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Extent of review and analysis

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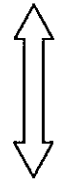
3.2 To assist a Member exercise professional judgement in respect of the extent of review and analysis for the applicable Valuation Service, a Member may find it helpful to consider the following five areas when performing the Valuation Service subject to the terms of the Engagement or Assignment agreed to with the Client or Employer:

- (i) The external environment in which the entity operates;
- (ii) Entity-specific non-financial information (e.g. entity’s operating structure and lifecycle stage);
- (iii) Entity-specific financial information (e.g. historical and future orientated financial statements);
- (iv) Valuation context (e.g. precedent Valuations and transactions for the subject business/interest, comparable transactions, and public market prices of comparable companies); and
- (v) Valuation assessments (e.g. performing Valuation calculations using various Valuation Approaches or Valuation Methods).

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3.3 In determining the extent of review and analysis to be undertaken in each of these five areas, Members should use their expertise and professional judgement. The following table provides guidance to Members on the extent of work that might be undertaken in each of the five areas, depending on the type of Valuation Service, availability of evidence and subject to the terms of the Engagement or Assignment agreed with Client or Employer. The table is only provided to illustrate a typical continuum of scope of work for different types of Valuation Services and is not intended to be prescriptive of the work that needs to be undertaken in any particular Valuation Service. Moreover, there are situations where the work performed for a Limited Scope Valuation Engagement is greater than for a Valuation Engagement or the work performed for a Valuation Engagement is less in one situation than in another due to the unavailability of evidence. Refer examples in Appendix.

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	External	Internal		Valuation Approaches, Valuation Methods & Valuation Procedures
Type of Valuation Service	External environment of the entity	Entity Specific Non- Financial Information	Entity Specific Financial Information	Valuation Context & Valuation Assessments
Valuation Engagement	Limited to extensive	Limited to extensive	Limited to extensive	
Limited Scope Valuation Engagement	Minimal to limited	Minimal to limited	Minimal to limited	
Calculation Engagement	None to minimal	None to minimal	None to minimal	

Extent of evidence obtained

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3.4 Where a Member is performing a Valuation Engagement, the Member should (using appropriate and reasonable efforts), review, analyse and consider information and factors that could have a significant impact on the Conclusion of Value. Further, the Member should obtain sufficient evidence that significant information is appropriate to use for the purpose of forming the Conclusion of Value.

- 3.5 Where a Member is performing a Limited Scope Valuation Engagement, the Member is likely to obtain limited evidence in respect of information and factors used in arriving at the conclusions for that Engagement. The Member should consider disclosing the evidence obtained in order that the users of such Valuation Reports can adequately assess:
- (i) the extent of work performed;
 - (ii) the extent of reliance that may be placed on the Valuation Report; and
 - (iii) the risk of a variation in the conclusions of the Valuation Report, if further evidence was gathered.
- 3.6 Where a Member is performing a Calculation Engagement, the extent of review and analysis, as well as evidence gathered in respect of the external environment and entity-specific information and factors is often very limited or non-existent. In these circumstances, the Member may not be aware of information or factors that could materially affect the Calculated Value, and therefore the Member should disclose the extent of limitations and the impact those limitations have on the reliability of the Calculated Value.

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4. Suitability of a Valuation Service

- 4.1 The Client or Employer is responsible for making the determination as to whether the type of Valuation Service selected is appropriate for the purpose of the Engagement or Assignment. It is possible that the type of Valuation Service selected by the Client or Employer may not ultimately achieve its intended purpose.
- 4.2 Where a Member is providing assistance to a Client or Employer for the Client or Employer to determine the suitability of a particular type of Valuation Service in a particular circumstance, the Member should consider discussing the following matters with the Client or Employer. These considerations are illustrative and are provided only to assist in the discussions with the Client or Employer. These considerations are not intended to be exhaustive or prescriptive of what type of Valuation Service is appropriate in any particular Engagement or Assignment:
- (i) *Extent of reliance* – the extent of reliance on the Conclusion of Value or Calculated Value expressed will vary based on the circumstances. For example, in an open market transaction, the Client may seek only a general indication of value as the market of buyers has been satisfactorily canvassed and the price of a transaction will ultimately be the result of negotiation or auction. In these circumstances a Valuation Service that requires a lesser extent of review, analysis and evidence may be more suitable. In contrast, if an agreement on the price for a transaction or a settlement is being entered into based only on the conclusions expressed in the Valuation Report, the extent of review, analysis and evidence that is appropriate may be greater;
 - (ii) *Significance of the matter to the Client or Employer* – the degree of significance to the Client or Employer may increase the extent of review, analysis and evidence that is required;
 - (iii) *Preliminary nature of the matter* – a Client or Employer may require a Valuation Service that is based on a limited scope of review for the purpose of making a preliminary or interim assessment in the course of an extended matter;
 - (iv) *Number of users of the Valuation Report* – where there is a high number of users, there may be an increase in the need for a greater extent of review, analysis and evidence as the implications of a limited scope of work may not be properly understood by all users;
 - (v) *Public availability* – if the Valuation Report will be disclosed or referred to in a public document, there may be an increase in the need for a greater extent of review, analysis and evidence as the implications of a limited scope of work may not be properly understood by potential users;

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- 15 (vi) *Contentious nature of the matter* – if the matter is (or has the potential for being) contentious, this increases the likelihood that the Valuation Report will be used as evidence and may be the basis for a judgment, which may increase the extent of review, analysis and evidence that is required; and
- 15 (vii) *Regulations or agreements* – regulatory authorities or relevant contracts/ agreements (e.g., a shareholders agreement) may prescribe a certain type of Valuation Report.

Impact of availability of evidence on the type of Valuation Service

- 5.3 17 4.3 A Member should consider the availability of evidence for the type of Valuation Service that is to be performed to base a conclusion. Evidence that the Member might wish to obtain to perform a Valuation Engagement might not be viewed as necessary for a Limited Scope Valuation Engagement or a Calculation Engagement. A lack of particular evidence may lead the Member to determine that it is not possible to perform a Valuation Service of one type but that the Member could still perform a Valuation Service of a different type.
- 5.4 17 4.4 In the circumstances referred to in paragraph 4.3, the Member should consider whether a Valuation Report of a Valuation Service that expresses a conclusion which is qualified by a scope limitation best serves the users of the Valuation Report.
- 5.5 18 4.5 Determining the impact of unavailable or missing evidence on the type of Valuation Report to be issued by a Member is a matter of professional judgement. This judgement should take into account all relevant facts and circumstances including the purpose of the Valuation Service, the scope of work agreed with the Client or Employer, and the importance of that evidence to the conclusion.

Conformity with International Pronouncements

The International Ethics Standard Board for Accountants (IESBA) has not issued a pronouncement equivalent to APES GN 20.

Acknowledgement of the Canadian Institute of Chartered Business Valuators

APESB gratefully acknowledges the publication of the Canadian Institute of Chartered Business Valuators (CICBV) listed below which provided the basis for the development of this Guidance Note. Components of the CICBV publication have been reproduced with the kind permission of the CICBV with variations made to suit the Australian context and APES 225 *Valuation Services*.

Practice Bulletin Number 3: Guidance on Types of Valuation Reports
Canadian Institute of Chartered Business Valuators, September 2012

Appendix: Illustrative Examples

This Appendix contains some examples to assist Members determine the scope and extent of work for a Valuation Service.

Members are cautioned that the determination of the scope of work for a Valuation Service in accordance with APES 225 is a matter to be judged based on the particular facts and circumstances. The examples contained in this Appendix are provided for illustrative purposes only and are not intended to be, and cannot be, all inclusive. The examples are not a substitute for reading the full text of APES 225 and APES GN 20 and applying the pronouncements to the particular circumstances. In all of the examples presented below it is assumed that there are no unmentioned facts which would be relevant to the determination of the scope and extent of work for a Valuation Service.

Example 1: Valuation of a minority interest in equity for capital gains tax without access to the company

Facts: A Member in Public Practice is engaged by a Client who holds a minority interest in the issued share capital of a company to perform a Valuation as at today's date of that minority interest for the purpose of capital gains tax and to provide a written report to the Client. There is no restriction or limitation placed on the Member in choosing the appropriate Valuation Procedures or Valuation Approach to use. Neither the Client nor the Member has access to the management and the books and records of the company. The Member has access to the annual reports, minutes of general meetings, and other documents provided by the company to the Client as a shareholder.

Analysis: If the Member did have access to the company (i.e. to its management and to its books and records) then, depending on the circumstances, the Member might consider:

- holding discussions with management about the nature and history of, and outlook for, the company's business;
- obtaining and reviewing any management accounts and reports and asking for details of any assumptions underlying them and the basis of their preparation;
- obtaining and reviewing any strategic or business plans;
- obtaining and reviewing any forecasts or budgets and asking for details of any assumptions underlying them;
- obtaining details of any revenues, expenses, assets, or liabilities that the Member considers relevant;
- obtaining details of any borrowings;
- obtaining and reviewing any crucial contracts;
- obtaining information on any revenues and expenses reported in the financial statements that management considers to be non-recurring, abnormal, or on non-commercial terms; and
- asking for any other information that the Member considers, in the circumstances, to be relevant to the valuation.

However, in this example this information is not available to the Member because the Member does not have access to the company. The fact that the extent and quality of the information available to the Member is less than would be the case if the Member did have access does not mean that the Engagement is a Limited Scope Valuation Engagement. That is because the Member remains free to employ the Valuation Approaches, Valuation Methods and Valuation Procedures that a reasonable and informed third party would perform taking into consideration all the *specific facts and circumstances* of the Engagement available to the Member at the time – and those specific facts and circumstances include the fact that the Member does not have access to the company.

Conclusion: This is a Valuation Service. The Member has been engaged to perform a Valuation, without any restriction or limitation placed on the Member by the Client, and to provide a Valuation Report, which constitutes a Valuation Engagement.

Example 2: Relationship between Valuation Conclusions in a Limited Scope Valuation Engagement and in a Valuation Engagement

Facts: A Member in Public Practice is approached by a Client who wishes to obtain a Valuation of a portfolio of patents for financial reporting and tax purposes. The Member's report will be provided to the Client's auditors and to the Australian Taxation Office. The Member is not a tax agent or an auditor. The Client wishes to minimise the cost of the Valuation and to that end is willing for the Member to limit the amount of work that the Member would otherwise do and for the Engagement to be a Limited Scope Valuation Engagement instead of a Valuation Engagement. The Member explains to the Client that if the Member were instead to perform a Valuation Engagement then the Valuation Conclusion, which will be in the form of a range of values, might be different. The Client says that it is willing to proceed with a Limited Scope Valuation Engagement because it understands that the range of values that the Member would determine in a Limited Scope Valuation Engagement is simply wider than that which the Member would determine in a Valuation Engagement.

Analysis: The Client understands that the Valuation Conclusion might be different under a Limited Scope Valuation Engagement than under a Valuation Engagement. However, the Client appears to assume that the range of values that would result from a Valuation Engagement would fall within the range of values that would result from a Limited Scope Valuation Engagement. Whether this would be the case will depend on the facts and often it will not be possible to predict without performing the additional work involved in a Valuation Engagement. Hence, while it is possible that the range of values under a Limited Scope Valuation Engagement would fall within the range under a Valuation Engagement, it is also possible that it would not or that there would only be a partial overlap.

Conclusion: In light of the Client's apparent misunderstanding and assuming that the nature of the limitations on scope are such that it is not possible to predict whether the range of values that would result from a Limited Scope Valuation Engagement would fall within the range that would result from a Valuation Engagement, either fully, partially, or at all, the Member should inform the Client of that fact before an Engagement is entered into so that the Client is able to make an informed choice.

Example 3: Choosing between different types of Valuation Engagements

Facts: The facts are the same as for Example 2 except that (a) the Client understands that in the circumstances it is not possible to predict whether the range of values that would result from a Limited Scope Valuation Engagement would fall within the range that would result from a Valuation Engagement, either fully, partially, or at all; and (b) the Client asks the Member whether it should commission a Limited Scope Valuation Engagement or a Valuation Engagement.

Analysis: It is the Client's responsibility, not the Member's, to determine which type of Engagement should be commissioned. Many matters may be relevant to that determination and the Member may be able to assist the Client in understanding some of them. For example, the Member could assist the Client to understand how the two types of Engagement might involve different costs as well as different burdens on the Client from requests for information or access to management. The Member could also assist the Client to understand that because the Valuation Conclusion in a Limited Scope Valuation Engagement might be different from the Valuation Conclusion in a Valuation Engagement, commissioning a Limited Scope Valuation Engagement carries an additional degree of risk. Whether that risk is acceptable to the Client will depend on the circumstances, including the Client's tolerance for risk and how much weight the Client places on the perceived benefits such as lower cost and burdens. In the circumstances of this example, the determination may also depend on the attitude of the Client's auditors and of the Australian

Taxation Office to a Limited Scope Valuation Engagement as well as on any relevant law or regulations.

Conclusion: The Member should inform the Client that it is the Client's responsibility, not the Member's, to determine which type of Engagement (i.e. Valuation Engagement or Limited Scope Valuation Engagement) should be commissioned in the circumstances. The Member could also inform the Client that the Member may assist the Client to understand some of the matters that may be relevant to that determination.

Example 4: Extent of evidence

Facts: A Member in Public Practice is engaged by a Client to perform a Valuation of a business, and provide a Valuation Report, for the purpose of the Client's negotiations with a third party for the sale of the business. The Valuation Report will not be provided to that third party. The Client instructs the Member to use the discounted cash flow method of valuation. But for that instruction, the Member would have used the capitalised earnings method of valuation. The Member will need more information to perform the Valuation using the discounted cash flow method than the Member would have needed to perform the Valuation using the capitalised earnings method. The additional information will include, amongst other things, long-term cash flow forecasts for the business.

Analysis: The Member is not free to use the Valuation Method that the Member believes a reasonable and informed third party would use taking into consideration all the specific facts and circumstances of the Engagement.

Conclusion: The Engagement is a Limited Scope Valuation Engagement, notwithstanding that the Member will do more work than would be required for a Valuation Engagement. It is a Limited Scope Valuation Engagement, due to the restriction placed on the Member on the Valuation Method to be used.

