



Consultation questions

Consideration of performance requirements
for machinery and equipment valuations
for financial reporting

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(Comments due by April 30, 2020)



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Notice to recipients of this consultation paper

ASA and RICS, along with representatives from various organizations, invite feedback on all matters in this consultation paper to ensure and enhance quality, consistency and transparency of valuations of machinery and equipment assets.

In addition, we encourage your colleagues, clients and other professionals (e.g. auditors, attorneys, etc.) to submit their comments. Please compile and submit your responses to the questions in this document by filling out the boxes indicated and sending it to John Russell at jrussell@appraisers.org and Steve Choi at schoi@rics.org by April 30, 2020.

1 Introduction

1.1 Objective

The objective of this paper is to obtain market insight to determine whether the development of *Mandatory Performance Framework* and *Application of the Mandatory Performance Framework* documents (collectively the 'MPF') would enhance the quality, consistency and transparency of machinery and equipment valuations in connection with financial reporting obligations. For further information about the MPF, please refer to section 2 of this document.

1.2 Background

Several years ago, the US Securities and Exchange Commission (SEC) criticized individuals performing fair value measurement estimates of entities, intangible assets, financial instruments and tangible assets for financial reporting purposes for SEC-registered US public companies. Public statements by US capital market regulators have called into question whether some of the individuals conducting fair value measurement estimates have the requisite training, qualifications, experience and expertise to perform this type of work. These regulators have also questioned whether individuals conducting these estimates are subject to a consistent set of professional, technical and ethical standards.

In response to these regulatory concerns, ASA and RICS, along with AICPA, non-membership organizations and others, have worked together to focus on the issues facing the valuation profession and how to address them. For further information, see [Certified in Entity and Intangible Valuations \(CEIV\) Credential](#).

2 The MPF

2.1 Mandatory Performance Framework

One of the outcomes of the CEIV initiative mentioned in section 1.2 was the development of performance requirements, or a *Mandatory Performance Framework*, specifically for entity and intangible valuations. The *Mandatory Performance Framework* provides guidance on how much work should be done in order to prepare a professional work product. It addresses, but is not limited to:

- the scope of work
- level of rigor
- extent of analysis
- consideration of contrary evidence and
- documentation needed in the report and the working papers

when designing, implementing and conducting valuations of:

- businesses
- business interests
- intangible assets
- certain liabilities and
- inventory

used for management assertions made in financial statements issued for financial reporting purposes.

Although the issues related to fair value measurements originated with the US generally accepted accounting principles (GAAP), in view of the multi-jurisdictional nature of financial reporting and the convergence of US GAAP and the international financial reporting standards (IFRS) over the past decade, it follows that any initiative regarding cross-border consistency in financial reporting is welcome.

Awareness about the MPF will spread internationally as it continues to be applied in practice for valuations of entities and intangible assets to US GAAP reporting entities and international SEC filers. As a result, it is likely to be considered ‘best practice’ for other asset classes as well, such as machinery and equipment assets.

The *Mandatory Performance Framework* provides valuation professionals with parameters of how much work should be performed and how to effectively and efficiently identify valuation documentation requirements in order to meet the changing needs of clients and other potential stakeholders, mitigate engagement risk and support and document sound decision-making. The *Mandatory Performance Framework* is a set of interrelated and interacting elements that valuation professionals can use in conjunction with relevant valuation standards and technical guidance to promote quality, consistency and auditability. It was not intended to address valuation theory or to be a how-to guide regarding valuation steps.

2.2 Application of the Mandatory Performance Framework

The current *Application of the Mandatory Performance Framework* (a separate document) applies the *Mandatory Performance Framework* to selected areas of professional valuation practice that are misapplied and/or insufficiently supported or documented in valuations of entities and intangible assets prepared for financial reporting purposes, for example:

- selection of valuation approaches and methods
- evaluation of prospective financial information
- discount rate derivation
- selection of, and adjustments to, valuation multiples and
- selection of guideline public companies or guideline company transactions.

In addition, the *Application* document has identified and applied the *Mandatory Performance Framework* to the most common components of an engagement in which the valuation professional provides a conclusion of value of a business or business interest. These sections govern the scope of work and extent of documentation for selected areas associated with the valuation of:

- businesses
- business interests
- intangibles assets
- certain liabilities and
- inventory that are prepared for financial reporting purposes.

Specifically, these sections address matters that need:

- greater consistency in the application of valuation approaches and methods
- support for issues that require the application of professional judgment and

- documentation of inputs.

These sections will continue to evolve and expand to cover a broader spectrum of topics and professional practice trends in the valuation profession.

2.3 Purpose of the MPF

By design, the current MPF does not provide illustrative examples that might otherwise be interpreted as requirements for how to perform a valuation. The purpose of the MPF is to provide valuation professionals with guidance on how much documentation is required when performing valuation services for financial reporting purposes. However, in certain circumstances, the *Application* document may provide some how-to discussion in order to complement the usability and application of the *Mandatory Performance Framework*.

The current MPF can be found online:

- [Mandatory Performance Framework](#)
- [Application of the Mandatory Performance Framework](#).

3 Consultation questions

- 1 As the MPF continues to be applied in practice for valuations of entities and intangible assets to US GAAP reporting entities and international SEC filers, do you believe it would be helpful for ASA and RICS to develop, with input from the broader valuation and user community, an MPF designed for machinery and equipment assets and their valuation for financial reporting purposes? Why or why not?

(Add your comments here)

- 2 If you believe an MPF would be helpful, and given the information provided previously about how an MPF works, which persistent or general financial reporting issues do you feel are most critical to be addressed in an MPF to reduce variations/inconsistencies in auditors' requirements? If you wish to provide examples illustrating why a topic is important, feel free to do so. We would ask that specific recommendations about *how* they should be addressed be left for a formal development process.

(Add your comments here)

- 3 Conversely, are there topics you believe do not need to be addressed by an MPF? This may be for myriad reasons: you may feel they are adequately dealt with currently; they may fall more into a question of standards (e.g. USPAP, IVS or Red Book); they may fall into the area of general knowledge (e.g. something currently taught through ASA's Principles of Valuation courses or promulgated through adherence to the RICS Valuer Registration program).

(Add your comments here)

- 4 How important is it that the proposed machinery and equipment MPF tracks closely to the existing MPF for business valuation and intangible assets? Why or why not?

(Add your comments here)

- 5 While the present consultation deals with the question of an MPF for financial reporting, are there other applications where an MPF could be helpful to practitioners, users or other parties who rely on valuations in specific contexts? If so, please discuss additional possible uses and, if different from above, topics that would and would not be appropriate to address in these additional applications.

(Add your comments here)

- 6 Are there potential unintended consequences – good or bad – from the adoption of an MPF dealing with machinery and equipment for financial reporting purposes? What steps, if any, could be taken to avoid these unintended consequences? Do you believe that any unintended consequence has the potential to undermine the intended effects of an MPF?

(Add your comments here)

- 7 Is there any additional guidance needed for machinery and equipment valuations over and above the existing standards/best practice documents? If so, please specify with as much detail as possible.

(Add your comments here)

- 8 At this time, we are not contemplating a specialist designation like the business valuation CEIV credential for professionals performing valuations of machinery and equipment assets. However, do you think a credential like CEIV in respect of machinery and equipment valuations, which would require certain credential maintenance requirements such as continuing experience and education, would benefit the public (for example, users of valuations, auditors and regulators)?

(Add your comments here)

- 9 We would appreciate, where possible, answers to the following self-reporting questions so we can assess representation by a range of stakeholders in this consultation. We will accept your comments without these responses; however, we wish to ensure feedback across a wide range of participants. Please tell us:
- a your current position, either within the valuation profession, as a user of valuation services or some other related stakeholder group
 - b how long you have served in your current position, and how long you have worked in or around the valuation profession (including as a user of valuation services)
 - c any professional designations you may have, regardless of whether they directly apply to valuation (such as an ASA or MRICS)
 - d the approximate percentage of your machinery and equipment work that relates to the reporting or review of values for financial statements and
 - e the size of your current employer (or if you are self-employed, the number of additional professionals you may contract with or refer to as needed).

(Add your comments here)

10 Development of an MPF, while supported by the ASA and RICS, requires a substantial amount of volunteer support from the practitioner community. Would you be interested in contributing to the development of an MPF? If so, please discuss the specific aspects of an MPF you feel most equipped to contribute to. We would also appreciate input as to other key stakeholders you believe the MPF development team could include or consult with as part of the process (e.g. auditors). (The selection of working group members will be based on the thoughtfulness of the responses received.)

(Add your comments here)

The ASA and RICS are not-for-profit organizations. Each member of the working group members is expected to cover all their travel-related expenses.

4 Other comments

Do you have any other comments about this document that we should take into consideration?

(Add your comments here)