ASEAN VALUATION PRACTICE GUIDE

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ASEAN VALUERS ASSOCIATION

ASEAN VALUATION PRACTICE GUIDE

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FOREWORD

In recent years, great changes took place in the accounting, financial, and real estate industries. The Global Financial Crisis in 2007 produced severe impacts and shock which resulted in bank failures, declines in stock indexes and corresponding reductions in the value of equities and commodities and coupled with the US sub-prime mortgage crisis which drastically reduced liquidity in the global credit markets and value of property assets.

Despite the crisis, the most impactful global development in the past decade has been the rapid ascent of Asian including ASEAN economies into prominence. Key markets in ASEAN have seen property prices rising to new heights. In order to cope with the challenges posed by rapid globalisation, growing economy and keen competition, the valuation profession must continue to upgrade and innovate. Increasing globalisation has seen rising cross-border developments and investments. The Global Financial Crisis has caused changes to the way assets, both real property and financial, are being evaluated and assessed. There is a constant demand for consistent standards and practice guidelines on property valuations and those relating to the valuations of financial assets that need to be carried out in compliance with the International Financial Reporting Standards (IFRS).

The ASEAN Valuers Association has considered the need to produce a guide for valuers practising in ASEAN. Reference is made to the specific local requirements and legal framework of the individual ASEAN countries. The objective of this ASEAN Valuation Practice Guide is to encourage the development of best valuation practices that meet international as well as local requirements.

It is hoped that this Guide will prove useful to both the valuation professionals and users of valuation reports in the ASEAN region. This Guide will be constantly revised to take account of changes as well as feedback from the industry.

ASEAN Valuation Practice Guide Committee, May 2016

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GENERAL

1.1 PROFESSIONAL ETHICS

1.1.1 Introduction

1.1.1.1 Valuation is an established and recognised profession. To promote and maintain professionalism in valuation practice, valuers need to observe a proper code of professional ethics. This code of ethics serves as a general framework for the practice of valuation.

1.1.1.2 The ethical standards for valuers when undertaking a valuation assignment serve to inform clients and users of valuation service of the expected ethical behavior of valuers, and hence help promote public confidence in valuation as a valuable means for decision-making.

1.1.2 Details of ethical conduct

1.1.2.1 Integrity

Valuers must not act in a manner that is misleading or fraudulent. Valuers must not knowingly communicate a valuation report that contains false, inaccurate or biased opinion and analysis. Valuers must not knowingly use false, misleading or exaggerated claims to secure assignments. Fees for the assignment must not depend on a predetermined outcome of valuation.

1.1.2.2 Conflict of Interest

Valuers must not act for two or more parties in the same matter unless consent is obtained from the parties concerned. Valuers must ensure there is no conflict of duty. Examples of possible conflicts exist in the following situations:

- Acting for a buyer and seller in the same transaction
- Acting for two or more parties competing for an opportunity.

Valuers must disclose any personal or corporate relationship with the company or client which seeks the assignment that may give rise to potential conflicts of interest. Personal or corporate relationship may occur when the valuers acting either in their personal capacity or representing a company have conflict of interest with the parties they are engaging with in a transaction.

1.1.2.3 Confidentiality

Valuers must deal with a client's affairs with proper discretion and confidentiality. Valuers must not disclose sensitive data obtained from the client or the results of the assignment to anyone other than the client or third parties specifically authorised by the client.

1.1.2.4 Impartiality

Valuers must perform an assignment with independence, objectivity and impartiality. Valuers must not accept an assignment that includes reporting of a predetermined opinion or conclusion. Valuers should not use or rely on unsupported conclusions or information without checking or verification.

1.1.2.5 Competence

Valuers must be suitably qualified, have sufficient knowledge and understanding of the relevant market, skill and experience to complete the valuation assignment. Valuers shall carry out the assignments with due care and diligence at all times.

1.1.2.6 Disclosure

Valuers are to communicate the analysis, opinions and conclusions to users of services through a comprehensive report that provides sufficient information and clear understanding to the user.

1.1.3 Explanation

1.1.3.1 It is important for valuers to conduct themselves according to a proper code of professional ethics in the practice of valuation. A valuer needs to be aware of the relevant code to guide him when considering any particular valuation assignment. Valuation training and ethical codes will provide an environment to cultivate a high level of ethical conduct and raise the level of professionalism.

1.2 PURPOSES OF VALUATION

1.2.1 Introduction

1.2.1.1 A valuation is commissioned for an intended use and the purpose for which a particular valuation is required, is critical to the selection of an appropriate basis and method of valuation. Therefore, the valuer should be clear about the purpose of valuation. This Guide sets out the various situations when a valuation is required.

1.2.2 Details

1.2.2.1 The purpose for which the valuation is undertaken must be clearly stated.

1.2.2.2 The purpose of valuation and the basis of valuation to be adopted must comply with the following unless the client, statutory/regulatory requirements or legal documents (such as agreements or leases) specify otherwise. In such a case, the valuer must explain the reasons why a different basis of valuation is adopted.

a. *Loan Security and Sale by Public Auction*
The basis of valuation for loan security and sale by public auction shall be Market Value. The valuer shall not provide any other basis of valuation such as Forced Sale Value or Auction Sale Price unless specifically requested by the clients. In such instances, the valuer shall provide the assumptions on which the value is based.

b. *Fire Insurance*

The basis of valuation for fire insurance shall be the Reinstatement Cost New or such other basis as is identified in a fire insurance contract or policy. The valuer may provide the valuation on the Indemnity Basis if specifically instructed.

c. *Company Accounts and Financial Statements*

The basis of valuation for company accounts and financial statements shall be as follows :

i. For properties occupied for the purposes of the business, the basis of valuation shall be Market Value for the Existing Use or Existing Use Value. However, if the Market Value for its highest and best use is materially different from the Market Value for the Existing Use or Existing Use Value this shall be discussed with the client as to whether the Market Value is to be reported in addition to the Market Value for the Existing Use.

ii. For investment properties or properties surplus to the requirements of the business, the basis of valuation shall be Market Value.

iii. For all valuations submitted to the State's Regulatory Authority or Stock Exchange for its consideration pursuant to a public listing, the basis of valuation shall be in accordance to the relevant Guidelines or Listing Manual.

d. *Sale and Purchase*

The basis of valuation for sale and purchase shall be Market Value.

e. *Compulsory Acquisition*
The basis of valuation for compulsory acquisition shall be in accordance with the provisions of the relevant legislation.

f. *Property Tax*
The basis of valuation for property tax shall be in accordance with the provisions of the relevant tax legislation.

g. *Other Purposes*
The basis of valuation for other purposes shall be Market Value; if any other basis is used, the valuer shall explain the basis and its rationale.

1.2.3 Explanation

1.2.3.1 The Guide is to ensure that the appropriate basis and method of valuation is adopted in relation to the purpose of valuation for which the valuation is required.

1.2.3.2 In the ordinary course of conducting an asset valuation, the valuer will be instructed by the Directors of the enterprise or by their professional advisors, as to whether the assets are held for purposes of the business or for purposes of investment or surplus to the enterprise's requirements. In the absence of specific instructions, the valuer will be obliged to make a factual determination of the most appropriate classification of each asset based on his experience, knowledge and expertise. In this case, the determination and its basis must be fully disclosed by the valuer.

1.2.4 Specific National Practice

1.2.4.1 Malaysia

For valuations submitted to the Director of Insurance and Takaful Supervision, they must comply strictly with the "Guidelines on Property Valuations of Insurance Companies".

1.2.4.2 Singapore

Specific purposes of valuation in Singapore include development charge and collective sales.

a. *Development Charge*
In situations where the approved development exceeds the existing requirements, development charge will be payable. The basis of valuation for development charge shall be in accordance with the provisions of the relevant planning legislation.

b. *Collective Sales*
In cases where approval is granted to sell an existing development collectively known as enbloc sales, the basis of valuation for collective or enbloc sales shall be in accordance with the provisions of the strata title legislation.

1.3 CONDITIONS OF ENGAGEMENT AND CONFLICT OF INTEREST

1.3.1 Introduction

1.3.1.1 The Valuer must always seek to understand the client's needs and requirements and carry out the client's instructions accordingly. Wherever possible, there should therefore be a written statement or agreement stating the conditions of engagement of a Valuer's services, indicating the scope of work, reporting formats, assumptions to be made, limiting conditions (if any) etc. This is to minimise any misunderstanding between the client and the Valuer so that the client understands the extent of a Valuer's responsibilities, limitations of valuation reports and is satisfied with the valuation service.

1.3.2 Details

1.3.2.1 To ensure the highest standards and expertise to be provided to the client, a Valuer, before he accepts any instructions from a client, must ensure that:-

a. he has the necessary qualifications;
b. he has the relevant experience or expertise;
c. he is an "Independent Valuer";
d. there is or will be no conflict of interest; and
e. he meets any other conditions as imposed or required by the client or their advisors or users of the Valuation Reports or Certificates.

1.3.2.2 Before a valuation is reported, a Valuer must agree or confirm with the client on the following:

a. purpose and intended use of the valuation;
b. the material date of the valuation;

c. the subject matter of valuation i.e. identification of the property and the interest to be valued;
d. the basis of valuation (e.g. market value);
e. assumptions to be used in arriving at the valuation;
f. requirements in relation to supporting documents;
g. basis and responsibility for his fee;
h. timescale for the valuation assignment; and
i. limits or exclusion of liability to other parties other than the client (i.e. "Limiting Conditions").

1.3.3 Explanation

1.3.3.1 The Guide is meant to specify the scope of work of the appointed Valuer and to avoid misunderstanding with the client. Should the Valuer be asked to base his valuation on "additional" or "special" assumptions, he should make a statement to such an effect in the Valuation Report or Certificate.

1.4 LIMITING CONDITIONS

1.4.1 Introduction

1.4.1.1 A Valuer may accept instructions to value a property subject to certain limiting conditions and exclusions as agreed with the client.

1.4.2 Details

1.4.2.1 Neither the whole nor any part of the valuation and report or any reference to it may be included in any published document, circular to statement nor published in any way without the Valuer's prior written approval of the form and context in which it may appear.

1.4.2.2 Where it is stated in the report that information has been supplied to the Valuer by another party, this information is believed to be reliable but the Valuer can accept no responsibility if this should prove not to be so. Where information is given without being attributed directly to another party, this information has been obtained through the Valuer's best efforts from reliable sources in the public domain, including but not limited to Government or other appropriate bodies.

1.4.2.3 The Valuation and Report is confidential to the party to whom it is addressed and to his professional advisors for the specific purpose to which they refer. The Valuer disclaims all responsibility and will accept no liability to any other party.

1.4.2.4 The values assessed in the report for the property and any allocation of values between parts of the property apply only in the terms of and for the purpose of the report. The values assessed should not be used in conjunction with any other assessment as they may prove incorrect if so used.

1.4.2.5 While due care is taken to note building defects in the course of inspection, no structural survey is made and no guarantee is given in respect of rot, termite or pest infestation or other hidden defects.

1.4.2.6 Investigations are not normally carried out on site in order to ascertain the suitability of the ground conditions, and the services, for any new development. Unless otherwise informed, the valuation is on the basis that these aspects are satisfactory and that, where development is proposed, no extraordinary expenses or delays will be incurred during the construction period.

1.4.2.7 Where market values are assessed, they reflect the full contract value and no account is taken of any liability to taxation on sale or of the costs involved in effecting a sale. The property is valued on the assumption that it is free and clear of all mortgages, encumbrances and other outstanding premiums and charges.

1.4.2.8 Any sketch, plan or map in the valuation report is included to assist the reader in visualising the property. No survey of the property and no responsibility in connection with such matters should be assumed.

1.4.2.9 Planning information is obtained from the set of Master Plan and related statements published by the relevant authority. Unless otherwise instructed, requisitions are not normally carried out with the various public authorities to confirm that the property is not adversely affected by any public schemes such as road improvements etc.

1.4.2.10 The valuation is prepared on the basis that the premises and any works thereto comply with all relevant statutory regulations. It is assumed that they have been, or will be issued with a certificate of statutory completion by the relevant authority.

1.4.2.11 The Valuer is not required to give testimony or to appear in the court of law or tribunal by reason of the Valuation Report, with reference to the property in question, unless prior arrangement has been made thereof.

1.4.3 Explanation

1.4.3.1 This Guide is meant as a model list of limiting conditions that a Valuer may append to the engagement letter and valuation report. Valuers are reminded that limitations are only effective if the client is made aware of them in advance of the valuation assignment.

REAL ESTATE VALUATION

2.1 GENERAL VALUATION CONCEPTS AND PRINCIPLES

2.1.1 Introduction

2.1.1.1 This Guide provides an explanation of the general valuation concepts and principles adopted in real estate valuation.

2.1.2 Land, Property and Asset Concepts

2.1.2.1 Land refers to the earth's surface, the space beneath which extends to the centre of the earth, and the space above which extends to the skies. It is often subject to legal and physical constraints.

2.1.2.2 Property is a legal concept, commonly used in general reference to real estate and/or personality. The term may be considered applicable to both the rights of ownership and to the physical item owned.

2.1.2.3 Real property is a non-physical concept and refers to all rights, interests, and benefits related to the ownership of real estate.

2.1.2.4 Personal property is a non-physical concept and refers to all rights, interests, and benefits related to ownership of personality.

2.1.2.5 Personality includes tangible and intangible items which are not real estate.

2.1.2.6 Assets are used in accounting which distinguishes between current assets and fixed assets.

2.1.2.7 Current assets are assets not intended for use on a continuing basis in the activities of the enterprise such as stocks, debtors and cash in bank and in hand. In certain circumstance, real estate, normally treated as a fixed asset may be treated as a current asset. Examples include improved real estate held in inventory for sale by real estate developers.

2.1.2.8 Fixed assets are tangible and intangible assets which fall into two broad categories, namely, property, plant and equipment and other long-term assets.

a. *Property, plant and equipment.* Assets intended for use on a continuing basis in the activities of an enterprise including land and buildings, plant and equipment, and other categories of assets, suitably identified.

b. *Other long-term assets.* Assets not intended for use on a continuing basis in the activities of an enterprise, but expected to be held in long-term ownership including long-term investments, long-term receivables, goodwill, expenditures carried forward, and patents, trademarks, and similar assets.

2.1.3 Price, Cost and Value

2.1.3.1 Price is a term used for the amount asked, offered, or paid for a good or service. It is a historical fact, whether it is publicly disclosed or retained in private. Arising from the financial capabilities, motivations, or special interests of a given buyer and seller, the price paid for goods or services may or may not have any relation to the value which might be ascribed to the goods or services by others. Price is, however, generally an indication of a relative value placed upon the goods or services by the particular buyer and/or seller under particular circumstances.

2.1.3.2 Cost is the price paid for goods or services, or the amount required to create or produce the good or service. When completed, it is a historical fact. The price paid for a good or service becomes its cost to the buyer.

2.1.3.3 Value is an economic concept. It refers to the monetary relationship between goods and services available for purchase and those who buy and sell them. Value is not a fact, but an estimate of the worth of goods and services at a given time in accordance with a particular definition of value. The economic concept of value reflects a market's view of the benefits, which accrue to one who owns the goods or receives the services as at the effective date of valuation.

2.1.4 Highest and Best Use

2.1.4.1 Highest and Best Use is defined as :

a. The most probable use of an asset which is physically possible, appropriately justified, legally permissible, financially feasible, and which results in the highest net value of the asset being valued.

b. A use that is not legally permissible or physically possible cannot be considered a highest and best use. A use that is both legally permissible and physically possible may nevertheless require an explanation by the Valuer justifying why that use is reasonably probable. Once analysis establishes that one or more uses are reasonably probable uses, they are then tested for financial feasibility. That use which results in the highest net value, in keeping with the other tests, is considered the highest and best use.

2.1.4.2 Highest and best use of a property is affected by many factors, including its past and present use, land-use controls, nearby land uses, the availability or absence of utilities and transportation facilities, and recent or anticipated economic growth in the area.

2.1.4.3 In contrast to highest and best use is existing use. Existing use refers to the use of the property as it is on site at the date of valuation. The existing use of a property may or may not be the same as its highest and best use. If the property is under-utilised, its existing use value will be below its highest and best use value. In valuing for the purpose of sale/purchase, the basis should be determined at the highest and best use of the site.

2.1.5 Principles of Valuation

2.1.5.1 Utility refers to the usefulness or satisfaction one receives from a good or service. In valuation, land value is established by evaluating its utility in terms of the legal, physical, functional, economic, and environmental factors which govern its productive capacity.

2.1.5.2 The principles of valuation applied in valuing real estate include the principles of supply and demand, competition, substitution, anticipation or expectation, and contribution.

a. *Substitution*

A prudent buyer will pay no more for the property than the cost of acquiring an equally desirable substitute in the open market. It supports the premise that a buyer will not pay anymore for a home or other real estate than the cost of reproducing the improvement on a similar site.

b. *Anticipation*

The current value of a property depends on the anticipated utility or income that will accrue to the property owner in the future. The present value of a property depends on the expected future benefits of ownership. This principle is often used in the income method.

c. *Contribution*

The value of a component part of a property depends on the amount it contributes to the value of the whole. Certain improvements to a property can actually have a negative effect on value. While a tasteful landscaping may increase the value of a home, extensive plantings of exotic shrubs will not increase the value of the property very much. Even though a property may have an expensive feature or characteristic, the contribution to market value is often less than the cost of feature because the typical buyer in the market does not desire that feature in the property.

2.2 MARKET VALUE BASIS OF VALUATION

2.2.1 Introduction

2.2.1.1 Property is generally transacted at its market value. This is the amount a property would fetch if offered for sale in the open market at the date of valuation under circumstances that meet the requirements of the Market Value definition. To estimate Market Value, a Valuer must first estimate the highest and best use, or most probable use for the property in question. This determination is made from market evidence.

2.2.1.2 This Guide applies to the Market Value of property and other real estate related elements.

2.2.2 Details

2.2.2.1 The Valuer shall use the Market Value basis of valuation for all purposes unless specifically instructed to do otherwise.

a. Market Value is defined as follows:
Market Value is the estimated amount for which an asset or liability should exchange on 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.

b. Further explanations of the definition are given below:

i. *"The estimated amount..."* refers to a price expressed in terms of money payable for the property in an arm's length market transaction. Market Value is measured as the most probable price reasonably obtainable in the market at the date of valuation. It is the best price reasonably obtainable by the buyer. This estimate normally excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale, or any element of Special Value (Guide 2.3.4.6). Where there are special terms and circumstances, these should be specifically stated in the Valuation Report.

ii. *"...a property should exchange..."* refers to the fact that the value of a property is an estimated amount rather than a predetermined or actual sale price. It is the price at which the market expects a transaction that meets all other elements of the Market Value definition should be completed on the date of valuation.

iii. *"...on the date of valuation..."* requires that the estimated Market Value is time-specific as of a given date. As markets and market conditions may change, the estimated value may be incorrect or inappropriate at another time. The valuation amount will reflect the actual state of the market and circumstances as of the effective valuation date, not as of either a past or future date. The definition also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might otherwise be made.

iv. *"...a willing buyer..."* refers to one who is motivated, but not compelled to buy. This buyer is neither over-eager nor determined to buy at any price. This buyer is also one who purchases in accordance with the realities of the current market, and with current market expectations, rather than an imaginary or hypothetical market that cannot be demonstrated or anticipated to exist. The assumed buyer would not pay a higher price than the market requires. The present property owner is included among those who constitute the market.

v. *"...a willing seller..."* is neither an over-eager nor a forced seller, prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in the current market. The willing seller is motivated to sell the property at market terms for the best price attainable in the open market.

vi. *"...an arm's length transaction..."* is one between parties who do not have a particular or special relationship between themselves. The open market transaction is presumed to be between unrelated parties, each acting independently.

vii. *"...proper marketing..."* means that the property would be exposed to the market in the most appropriate manner to effect its disposal. The length of exposure time may vary with the market conditions and the nature of property but must be sufficient to allow the property to be brought to the attention of potential purchasers.

viii. *"...acted knowledgeably, prudently..."* presumes that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the property, its actual and potential uses, and the state of the market as of the date of valuation. Each is further presumed to act for self-interest with that knowledge, and prudently to seek the best price for their respective position in the transaction.

c. Market Value is understood as the value of a real property estimated without regard to the costs of sale or purchase, and without offset for any associated taxes.

d. Market Value is a conceptual framework and not dependent on an actual transaction taking place at the date of valuation. It is an estimate of the price that should be realised in a sale at the valuation date under conditions of the Market Value definition.

2.3 VALUATION BASES OTHER THAN MARKET VALUE

2.3.1 Introduction

2.3.1.1 Although the majority of professional valuations involve Market Value, there are circumstances that call for bases other than Market Value. It is essential that both the Valuer and valuation users clearly understand the distinction between Market Value and non-Market Value based valuations, and the effects (if any) the differences between these concepts may have upon the applicability of the valuation.

2.3.1.2 This Guide is directed to bases of valuation other than Market Value.

2.3.2 Details

2.3.2.1 For certain stated specific purposes of valuation the Valuer may use a basis of valuation other than the Market Value.

2.3.2.2 For those purposes the Valuer shall state the purpose and the basis of valuation clearly in the valuation report.

2.3.2.3 The Valuer shall distinguish that the valuation is not a Market Value estimate if the assignment is on a basis other than Market Value.

2.3.2.4 Specialised properties by virtue of the fact that they are rarely, if ever, sold in the open market are to be valued on the Depreciated Replacement Cost (DRC) basis, subject to adequate potential profitability or service potential.

2.3.3 Explanation

2.3.3.1 Properties may be valued on bases other than Market Value, or may exchange hands at prices, which do not reflect Market Value as defined. Such alternative bases may either be reflections of a non-market perspective of utility, or of unusual and non-market conditions. Examples include Going Concern Value, Special Value, Forced Sale Value etc.

2.3.4 Other Bases of Valuation

2.3.4.1 ***Market Value for the Existing Use or Existing Use Value.*** The Market Value of an asset based on continuation of its existing use, assuming the asset could be sold in the open market for its existing use, and otherwise in keeping with the Market Value definition regardless of whether or not the existing use represents the highest and best use of the asset.

2.3.4.2 ***Value-in-Use.*** The value that a specific property contributes to the enterprise of which it is a part, without regard to the property's highest and best use or the monetary amount that might be realized upon its sale. Value-in-Use is the value a specific property has for a specific use to a specific user and is therefore non-market related. Value-in-Use is therefore a non-market basis of value measured from the perspective of a particular user.

2.3.4.3 ***Depreciated Replacement Cost (DRC).*** DRC is a method of valuation which is based on an estimate of the current Market Value of land for its existing use plus the current gross replacement (or reproduction) costs of improvements less allowances for physical deterioration and all relevant forms of obsolescence. The result, which may be non-Market Value, is referred to as the Depreciated Replacement Cost estimate. This result is subject to the adequate potential profitability or service potential of the enterprise.

The Valuer should qualify every valuation on the DRC basis as being subject to adequate potential profitability of the business having due regard to the value of the total assets employed and the nature of the operation. It is for the Directors or owners of the property to decide on the adequacy of the profit potential or service potential.

2.3.4.4 ***Insurance Value.*** The value of property on the appropriate basis as defined in the insurance contract or policy.

2.3.4.5 ***Forced Sale Value.*** The amount that may reasonably be received from the sale of a property under (forced sale) conditions that do not meet all the criteria of a normal market transaction. Forced sale involves a price which arises from disposition under extraordinary or atypical circumstances, usually reflecting an inadequate marketing period without reasonable publicity, an inappropriate mode of sale and sometimes reflecting an unwilling seller condition, and/or disposal under compulsion or duress. For these reasons, the price associated with a forced or distressed sale, called Forced Sale Value, is not a representation of Market Value. The price paid in a forced or distressed sale is a matter of fact. It is generally not easily predictable by a Valuer because of the nature and extent of subjective and conjectural assumptions that must be made in formulating such an opinion.

Therefore, Valuers shall not provide a Forced Sale Value unless specifically requested by the clients. In all such instances the Valuer shall provide the assumptions on which such value is based.

2.3.4.6 ***Special Value.*** A term relating to an extraordinary element of value over and above the Market Value. Special Value could arise, for example, by the physical, functional or economic association of a property with some other property such as the adjoining property. It is an incremental value, which could be applicable to a particular owner or user, or prospective owner or user, of the properly rather than to the market at large; that is, to a purchaser with a special interest. Special Value could be associated with elements of Going Concern Value. The Valuer must ensure that such criteria are distinguished from Market Value, making clear any assumptions made.

Special Value may accrue to a property by reason of a unique location, a temporary situation under exceptional market conditions, or a premium payable by a purchaser having a special interest. Such elements of Special Value may be reported separately from Market Value established in accordance with the definition of Market Value. Special Value should not be incorporated into a statement of Market Value, as such a procedure would be misleading and, by default, would signify that such incremental element of value is not special (most special assumption valuations would fall into this category).

2.3.4.7 ***Investment Value.*** This refers to the value of a property to a particular investor, or a class of investors, for identified investment objectives. This subjective concept relates a specific property to a specific investor or group of investors with identifiable investment objectives and/or criteria. The term Investment Value should not be confused with the Market Value of an investment property.

2.3.4.8 ***Going Concern Value.*** This is the value of a business as a whole. The concept involves the valuation of a continuing enterprise from which allocations or apportionment of overall Going Concern Value may be made to constituent parts as they contribute to the whole, but none of the components in themselves constitute Market Value.

Going Concern Value expresses the value ascribed to an established business, not to any of its constituent parts. The value allocated or apportioned to individual assets making up a part of the going concern is based upon their contribution to the whole, commonly referred to as their Value-in-Use when related to a specific business and its owner. It is not market related and is not to be confused with Market Value for the Existing Use.

2.3.4.9 ***Fair Value.*** The usual definition of fair value is the estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties. There is now greater similarity in the definition of fair value with market value.

In International Financial Reporting Standards (IFRS) 13 Fair Value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement or valuation date. It is a market-based measurement, and not an entity-specific measurement. The assumptions that market participants would use when pricing the asset or liability under the current market conditions including assumptions about risk should be adopted. Therefore the definition of fair value in IFRS is generally consistent with the market value definition.

2.3.4.10 ***Market Rent.*** This is defined as the estimated amount for which a property would 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.

Where Market Rent is provided, the "appropriate lease terms" which it reflects should also be stated. The "appropriate lease terms" are terms that would typically be agreed in the market for the type of property on the valuation date between the market participants.

2.4 APPROACHES AND METHODS OF VALUATION

2.4.1 Introduction

2.4.1.1 The method of valuation used by a Valuer in any valuation is the means by which the Valuer arrives at an opinion of value after having ascertained all relevant facts pertaining to the property and the market.

2.4.1.2 There are three generally recognised approaches to the determination of value. They are comparison, cost and income approaches. Within these approaches are different methods. The common methods of valuation are the Comparison Method, the Cost Method, the Income Method, the Residual Method and the Profits Method.

2.4.2 Details

2.4.2.1 This Guide on the methods of valuation is meant to provide Valuers the considerations for the use of the appropriate method of valuation, with the minimum requirements for each method being spelt out.

2.4.2.2 The rationale for adopting a method or methods of valuation has to be explained in the valuation report.

2.4.2.3 The Valuer is encouraged to use, apart from the main method of valuation, additional methods of valuation as a cross-check to the main method of valuation.

2.4.2.4 While there is no single universal method for all types and purposes of valuation, a Valuer should use his professional judgement to determine the appropriate method when carrying out the valuation. The method of valuation should be stated in the valuation report with a brief description.

2.4.3 Comparison Method

2.4.3.1 The direct comparison method can be used in all valuations where there are adequate transactions or other information to indicate the level of value for the property.

2.4.3.2 The comparison method relies on the presence of market transactions within a reasonable period from the date of valuation to provide an indication of value. It is supported by the theory that the market value of a property bears a close relationship to the values of similar properties which have been transacted.

2.4.3.3 The method is concerned with the identification and measurement of the effect that the presence or absence of some characteristics has on the price/rental of competitive (comparable) properties. The approach is to find properties that are transacted in the current market and resemble the subject property and to make the appropriate adjustments to reflect differences between them.

2.4.3.4 In applying the comparison method, the Valuer should have knowledge of the state of the local market, the subject and its comparables, and the typical buyer preferences and price movements.

2.4.3.5 Comparables used in arriving at the value of the property should preferably be stated in the valuation report.

2.4.3.6 For each of the stated comparables, the information required to be disclosed are the identification of the comparable (by way of address and/or legal description), property type, tenure, land or floor area (where applicable), the date of transaction, the consideration in monetary terms and any other information deemed necessary.

2.4.3.7 Other information relevant to the use of the comparison method, and may be included in the valuation report is the analysis of the comparables vis-à-vis the subject property.

2.4.4 Cost Method

2.4.4.1 The cost method of valuation is based on the rationale that the value of the property comprises two components: the value of improvements and the value of land. It is appropriate in the valuation of properties with few or no market transactions, such as schools and shipyards.

2.4.4.2 The method involves the estimation of the value of the site as if it were vacant, using the comparison method. The amount of depreciation and obsolescence is then estimated and deducted from the cost of improvements to arrive at the depreciated replacement or reproduction cost. This is then added to the land value to derive the capital value of the property.

2.4.4.3 The information or assumptions used in the valuation should preferably be shown in the report.

2.4.5 Income Method

2.4.5.1 The income or investment method of valuation is a method of estimating the present worth of the rights to future benefits to be derived from the ownership of a specific interest in a property under given market conditions. In property valuation, these rights are often expressed as future income in the form of the prevailing and sustainable rent.

2.4.5.2 The income method may be used for income generating properties if adequate rental information of comparable properties is available.

2.4.5.3 Methods that fall under the Income Method include :

a. income capitalisation, where the estimated fully leased net income is capitalised to perpetuity or over the remaining term of the lease from the date of valuation, where applicable, at an appropriate capitalisation rate.

b. Discounted Cash Flow (DCF) analysis involving the projection of future cash flows over an assumed investment holding period (typically 10 years) and discounted to a present value.

2.4.5.4 Income Capitalisation: From the current market rent, the outgoings that would be incurred in the management and maintenance of the property, should be deducted. Other expenses including insurance, taxes and other losses of income such as rental abatements and vacancies, should also be allowed.

2.4.5.5 The net income is then capitalised at a suitable rate of return to arrive at the capital value of the property.

2.4.5.6 Where contracted rent(s) exist within the property, these rents have to be taken into account and appropriate reversionary adjustments have to be made.

2.4.5.7 The capitalisation rate used should be supported by such rates for comparable properties or by data compiled, verified and analysed by the Valuer.

2.4.5.8 The comparable rents and the outgoings and other expenses should preferably be stated in the report.

2.4.5.9 Discounted Cash Flow Analysis: The estimated revenue cash flow should reflect the property's specific leasing pattern including rent reviews, lease renewals or re-letting on lease expiry, letting-up allowances, leasing commissions, non-recoverable outgoings and anticipated capital expenditure for refurbishment or upgrade.

2.4.5.10 A wide range of assumptions will be made, including a target internal rate of return, rental growth, sale price of the property at the end of the investment horizon, costs associated with the initial purchase of the property and also its disposal at the end of the investment period.

2.4.5.11 Typically in a 10-year cash flow, it is assumed that the property is sold at the commencement of the eleventh year of the cash flow.

2.4.5.12 The discount rate adopted should reflect market and property-specific risks. The adopted discount rate should be supported by such rates for comparable properties or by data compiled, verified and analysed by the Valuer.

2.4.6 Residual Method

2.4.6.1 The residual method may be used for the valuation of the following types of property :

a. A vacant or undeveloped site where planning permission for development has been, or is likely to be, obtained;

b. A property with an existing building which has the potential to be upgraded via a change of use or general improvements; and

c. A property with an existing building which has no economic value and where planning permission has been, or is likely to be, granted for its demolition and replacement.

2.4.6.2 In all three cases, if direct comparables can be obtained, a valuation by the comparison method may also be appropriate.

2.4.6.3 The approach is to estimate the gross development value of the property which is the capital value of the developed or improved site assuming full completion of the proposed development. What remains after the deduction of all costs incurred in the development or improvement is the residual value of the land with development potential.

2.4.6.4 Information on the comparables used in determining the gross development value and other cost data should preferably be shown in the report.

2.4.7 Profits Method

2.4.7.1 The profits method is usually applied to the valuation of properties with trading potential and where the market comparables and current market rents for similar properties are not available. The rent for the property needs to be ascertained from the income receivable for the conduct of the business sited on the property.

2.4.7.2 The estimated gross receivable income must be established by reference to past records and must be reasonable and supportable by comparable properties in the same industry.

2.4.7.3 The costs of operating the business must also be established by reference to current and projected rates as can reasonably be supported and cross-checked with past records of such costs.

2.4.7.4 The allowances used in the valuation for the operator's capital, risk and entrepreneurship must be supported.

2.4.7.5 The capitalisation rate applied to the net rent to arrive at the capital value of the property must be supported by market evidence.

2.4.7.6 The steps involved and the information used should preferably be shown in the report.

2.4.8 Departure Provision

2.4.8.1 When other approaches or variations of, and to, the above stated methods are applied, these must be fully explained and the data used in the valuation must be substantiated by market evidence.

2.5 PROPERTY INSPECTION AND REFERENCING

2.5.1 Introduction

2.5.1.1 In the valuation process, inspection of the property must be carried out. Valuers are expected to carry out adequate inspection to produce the valuation.

2.5.1.2 Referencing of the property is also important in the process. It identifies the property legally, physically and geographically. Relevant data and materials that may affect the value of the property have to be collected and collated.

2.5.2 Details

2.5.2.1 Proper inspection and referencing of the property must be carried out by the Valuer or designated valuation assistant, except for revaluation cases carried out in accordance with Guide 2.7 on Revaluation.

2.5.2.2 Inspection

a. The Valuer or valuation assistant has to identify the property physically by the address of the property, the survey maps, cadastral maps, strata title plans and/or legal description.

b. A structural or building survey is not expected to be carried out. However, the exterior and interior of the property must be inspected. The following details are to be reported accurately as far as they are visible :

i. age, use, accommodation, description of finishes and fixtures, type of construction, services and facilities available;
ii. areas of the land and building where applicable;
iii. apparent state of repair and maintenance; and
iv. characteristics of the locality, accessibility and the availability of amenities that may affect the value.

c. In cases of properties without strata titled areas, the Valuer may have to measure the buildings or verify the measurements of the building plans provided.

d. The characteristics of the locality, the property type and the relevant property market conditions also need to be noted.

e. In the event that an internal inspection of the property is not possible, the Valuer must clearly specify this limitation in the report.

2.5.2.3 Referencing

a. In referencing of the property, the Valuer must ascertain and include the following in the report :

i. the relevant title details and the legal description of the land;
ii. interests in the property in respect of the tenure, terms of lease (if leasehold), current registered owner(s), and the relevant restrictions etc; and
iii. planning and statutory requirements.

b. The searches of the relevant title documents, planning and statutory requirements can be obtained from the respective government departments and statutory boards.

c. Where any of these findings, conditions and restrictions affects the valuation, they have to be stated in the report. Where the relevant title details and documents are not available even after undertaking the relevant searches, assumptions have to be made and clearly stated in the report.

2.5.3 Explanation

2.5.3.1 Proper inspection and referencing are important in the determination of the valuation. Professional etiquette and decorum are to be adhered to when carrying out physical inspections of the property.

2.5.3.2 The hand-written inspection notes and findings, title searches and title documents, and the data collected and collated for analysis are normally not included in the report to the client. These working papers should be kept for record and future references.

2.5.4 Disclosure Requirements

2.5.4.1 The disclosure, assumptions and qualification statements as mentioned earlier have to be stated clearly in the reports.

2.6 VALUATION REPORT

2.6.1 Introduction

2.6.1.1 The valuation is conveyed to the client in the form of a report. It must therefore be clear and not misleading as the valuation report can be acted upon by the client without any reference to the Valuer (unless a specific reservation has been made).

2.6.1.2 The valuation report must convey to the reader a clear understanding of the opinion expressed by the Valuer, the basis of valuation used and the assumptions and information on which it is based.

2.6.2 Details

2.6.2.1 The valuation report must provide sufficient information to permit those who read and rely upon the report to fully understand its information/data, reasoning, analyses and conclusions. It must state any assumptions and limiting conditions upon which the valuation is based.

2.6.2.2 The contents of the valuation report should comprise the following :

a. *Instructions* - the report should clearly state the party who gave instructions to carry out the valuation and the date of instruction.

b. *Property to be valued* - the name/address of the property to be valued should be clearly stated in the report.

c. *Purpose of valuation* - the report must clearly state the purpose of the valuation.

d. *Date of valuation* - the material date of valuation of the property which by default would be the date of the valuation report. However, where this is not the case, then the date of valuation must be clearly stated.

e. *Date of inspection* - the report must contain the date on which the property was inspected. If no inspection was carried out, a statement of qualification or explanation should be made.

f. *Description of the property* - this should cover the following :

   i. *Location* - the road along which the property is located, the distance of the property in relation to the city/business centre, a brief description of the neighbouring developments.

   ii. *Site Description* - to briefly describe the configuration of the site and giving the estimated dimensions of the frontages and depth of the site; topography of the site, visibility, any unusual physical characteristic of the site and ingress/egress and access.

   iii. *Physical description of the property* -
   (1) For completed buildings or buildings under construction -- to give details of the type of construction and the improvements, the usage, building area (strata area, gross floor area, net/lettable floor area etc) and available building services (where applicable).

   (2) For proposed developments (where no construction work has commenced or where the development is under the planning stage) -- to describe the proposed development as in (1) above where information is available. Otherwise, data on the proposed development (as proposed by the

developer or assumed based on planning guidelines) such as proposed plot ratio, floor area (gross and/or net/lettable area), usage etc must be stated.

iv. *Condition* - the Valuer is to report the state of repairs and maintenance the property is in. The physical inspection of the property by the Valuer does not normally form part of a structural survey nor a testing of the building services, unless specifically stated in the report.

v. Any other relevant information.

g. *Tenancy/lease details* - where relevant, tenancy/lease details must be included. Any terms and conditions contained in the lease agreement which may affect the value of the property must be highlighted in the report. The Valuer has to make a qualification if the tenancy details or lease agreement(s) are not made available by the client/ registered owner of the property.

h. *Planning details* - the report must give particulars of planning details as contained in the latest edition of the Master Plan and any other planning guidelines such as the street block plans, special and detailed control plans.

i. *Title particulars* - the title particulars must be provided.

j. *Assumptions* - the report must clearly state all assumptions adopted in arriving at the opinion of the market value of the property.

k. *Method of valuation* - the method(s) of valuation used must be clearly stated.

l. *Opinion of value* - the report must contain a clear and unambiguous statement of value. If more than one method of valuation is used, then the value derived from each approach should preferably be shown. The final opinion of value must be expressed as a single value.

   The Valuer must reveal and explain in detail the logic used to reconcile the values derived under the various approaches.

m. *Signature of Valuer* - the report must be signed by a licensed Valuer and the licence or registration number should be included after his/her signature.

n. *Appendices* – the appendices to the report should contain most if not all of the following :

   i. Photographs of the property - external and internal view(s) whenever possible;
   ii. Location Plan showing the subject property;
   iii. Site Plan - to demarcate the subject site;
   iv. Site Layout Plan (where appropriate);
   v. Floor Plans (where appropriate);
   vi. Tenancy Schedule (where appropriate and available);
   vii. Limiting Conditions - To comply with General Guide 1.4; and
   viii. Workings as appropriate.

o. Any other information which the Valuer considers will enhance the reader's understanding of the property and the appraisal.

p. *Optional items* -

   i. Road Line Plan and Railway Protection Plan, and Drainage and Sewerage Reserve Plan are normally not included in the reports. The Valuer has to make a qualification on its exclusion and assume that the property is not materially affected by any proposed road or drainage schemes. However, whenever possible, the relevant plans should be included in the valuation report.

ii. *Utilities/Infrastructure* - a comment on the availability of the various public utility services and infrastructure should be made in the report.

iii. *Taxes* - the report should state the assessed value of the property for property tax purposes, the current tax rate and the amount of tax payable.

iv. *Ground/Annual rents* - where appropriate, the report should reflect the ground rent or annual rent payable on the property.

2.6.2.3 If the valuation report is prepared for a listed company or for prospective listing on the relevant State's Regulatory Authority or Stock Exchange, then the report should comply with the requirements set down in the relevant Guidelines or Listing Manual.

2.6.2.4 A valuation certificate may be issued upon request by the client. The certificate is usually needed as an enclosure in published statements such as in the prospectus of an Initial Public Offer or in the annual reports of listed companies.

2.6.2.5 The practice of issuing a valuation certificate in lieu of a valuation report is strongly discouraged.

2.6.2.6 The valuation certificate should be brief and the contents should be presented in either one or two pages. The contents should comprise the following :

a. *Property to be valued* - the name/address of the property to be valued should be clearly stated in the certificate;

b. *Date of valuation* - the material date of valuation of the property by default would be the date of the valuation report. However, where this is not the case, then the date of valuation must be clearly stated;

c. *Description of the property* - to give a brief summary;

d. *Tenancy/lease details* - where relevant, a brief summary of tenancy/lease details must be included. Any terms and conditions contained in the lease agreement which may affect the value of the property must be highlighted. The Valuer has to make a qualification if the tenancy details or lease agreement(s) are not made available by the client/ registered owner of the property;

e. *Planning details* - particulars of planning details as contained in the latest edition of the Master Plan and any other planning guidelines such as the street block plans, special and detailed control plans;

f. *Title particulars* - the title particulars must be provided; and

g. *Assumptions* - must clearly state all assumptions adopted in arriving at the opinion of the market value of the property.

2.6.3 Explanation

2.6.3.1 The above are the minimum requirements to be contained in a valuation report and valuation certificate.

2.7 RE-VALUATION

2.7.1 Introduction

While the general rule remains that a valuation should be communicated to a client only by way of a detailed report, letters and/ or valuation certificate in lieu of a detailed report may be used in communicating an opinion of value to the client in certain limited cases such as a revaluation. A re-valuation is an assessment of the property whereby a valuation was done previously by the same professional or firm. It can be a full report or desktop (that is, relying on the actual inspection records of the previous report but without carrying out a new inspection).

2.7.2 Details

2.7.2.1 Re-valuation is to be undertaken like any other valuations and is subject to the relevant Guides referred to.

2.7.2.2 However, there may be instances when re-valuations are undertaken without the benefit of a physical inspection of the property.

2.7.2.3 Re-valuation without a physical inspection of the property can only be provided if :

a. It is prepared in for a property, which was previously valued by the same firm. The property must have been previously inspected following the Guide 2.5 on Property Inspection and Referencing;

b. There should not be any additions or alterations carried out on the property since the last inspection;

c. Re-valuation must not be undertaken for cases whereby no previous inspection and valuation report has been prepared by the firm; and

d. Re-valuation without re-inspection should not be carried out if the previous valuation report (with physical inspection of the property) is more than three years prior to the date of valuation.

2.7.2.4 The Valuer has to qualify in the re-valuation that the valuation is based solely on the condition of the property as stated in the previous valuation report and that neither a new physical inspection nor fresh title searches have been carried out.

2.7.3 Explanation

2.7.3.1 Firms are encouraged to undertake only valuation with reporting in accordance with Guide 2.5 (Property Inspection and Referencing) and Guide 2.6 (Valuation Report). Re-valuations without a physical inspection of the property should be carried in accordance with this Guide. Practices such as 'kerb-side valuation' or 'indicative valuation in writing', where no inspections have been conducted, do not conform to acceptable valuation standards and are not recognised.

BUSINESS VALUATION

3.1 GENERAL VALUATION CONCEPTS AND PRINCIPLES

3.1.1 Introduction

3.1.1.1 This Guide provides an explanation of the general valuation concepts and principles relating to business valuation.

3.1.2 Asset Concepts

3.1.2.1 Assets are used in accounting which distinguishes between current assets and fixed assets.

3.1.2.2 Current assets are assets not intended for use on a continuing basis in the activities of an enterprise such as stocks, debtors and cash in bank and in hand. Under certain circumstances, real estate, normally treated as a fixed asset may be treated as a current asset. Examples include improved real estate held in inventory for sale by real estate developers.

3.1.2.3 Fixed assets are tangible and intangible assets which fall into two broad categories, namely, property, plant and equipment and other long-term assets.

a. *Property, plant and equipment* - Assets intended for use on a continuing basis in the activities of an enterprise including land and buildings, plant and equipment, and other categories of assets, suitably identified.

b. *Other long-term assets* - Assets not intended for use on a continuing basis in the activities of an enterprise, but expected to be held in long-term ownership including long-term investments, long-term receivables, goodwill, expenditures carried forward, and patents, trademarks, and similar assets.

3.1.3 Price, Cost and Value

3.1.3.1 Price is a term used for the amount asked, offered, or paid for a good or service. It is a historical fact, whether it is publicly disclosed or retained in private. Due to the financial capabilities, motivations, or special interests of a given buyer and seller, the price paid for goods or services may or may not have any relation to the value which might be ascribed to the goods or services by others. Price is, however, generally an indication of a relative value placed upon the goods or services by the particular buyer and/or seller under particular circumstances.

3.1.3.2 Cost is the price paid for goods or services, or the amount required to create or produce the good or service. When completed, it is a historical fact. The price paid for a good or service becomes its cost to the buyer.

3.1.3.3 Value is an economic concept. It refers to the monetary relationship between goods and services available for purchase and those who buy and sell them. Value is not a fact, but an estimate of the worth of goods and services at a given time in accordance with a particular definition of value. The economic concept of value reflects a market's view of the benefits, which accrue to one who owns the goods or receives the services as at the effective date of valuation.

3.1.4 Principles of Valuation

3.1.4.1 *Reliance on Projected Benefits*

3.1.4.1.1 There is often more than one point of view in business valuation when projections are made. Historical facts are considered more credible evidence than projections. Hence projections will be useful depending on their validity based on information available as at the valuation date.

3.1.4.1.2 The value of a business is essentially the sum of the expected future benefits to its owners discounted to a present value at an appropriate rate. The market for capital usually determines the appropriate discount rate for an investment value. For market value the appropriate rate should be market derived ie derived from analyses of market sales.

3.1.4.1.3 Projecting future benefits and determining an appropriate discount rate is challenging. The accepted methods of estimating value using current or historical financial data often require adjustments to reflect the impact of future expectations, and other considerations such as expected growth rates, inflationary rates and market trends.

3.1.4.2 *Impact of Controlling Ownership Interest*

3.1.4.2.1 The distribution of ownership, and hence its control, can affect the value of a particular business interest. Minority or non-controlling shareholders lack control over various decisions affecting the business enterprise. In most cases, a non-controlling ownership interest is worth less than its pro-rata portion of the value of the entire business entity. Certain State regulations can affect the respective rights of controlling and non-controlling shareholders.

3.1.4.3 ***Impact of Marketability***

3.1.4.3.1 Ready marketability adds value to a security. Marketability refers to the ability to convert the asset to cash very quickly at minimal costs with a high degree of certainty of realising the anticipated proceeds. Both controlling and minority ownership interests may suffer from lack of marketability. The impact of marketability factor is influenced by both internal and external facts and circumstances as at the valuation date. The market pays a premium for liquidity and demands a discount for lack of liquidity. Hence, business interests that lack ready marketability are generally less valuable than comparable business interests that are readily marketable.

3.1.4.4 ***Sum of Parts Not Necessarily Equal to Whole***

3.1.4.4.1 The sum of the values of fractional interests in a business is not necessarily equal to the value of the entire ownership interest of the business. Each situation should be examined to ensure an appropriate value is obtained.

3.1.4.5 ***State of the Market***

3.1.4.5.1 It is important to understand the concept of active market in the accounting context. An active market is one where all of the following conditions exist :

- the items traded within the market are homogeneous
- willing buyers and sellers can normally be found; and
- prices are available to the public.

3.1.4.5.2 In the context of business valuation, the direct comparison method would not be useful in an inactive market. Other methods using income or cost method may have to be adopted to determine the fair value.

3.2 FAIR MARKET VALUE BASIS OF VALUATION

3.2.1 Introduction

3.2.1.1 A standard of value refers to the type of value being sought such as fair market value or investment value. A premise of value is the assumption as to the set of actual or hypothetical transactional circumstances applicable to the subject valuation such as going concern or in liquidation. In many situations, the standard of value is legally mandated whether by law or between the parties involved. This Guide provides explanation to the various terms used in business valuation. It focuses on fair market value and other non-market value terms.

3.2.2 Details

3.2.2.1 *Fair Market Value*

3.2.2.1.1 Fair market value is a widely recognised and accepted standard of value related to business valuation. It refers to the amount at which business would change hands between a willing seller and a willing buyer when neither is acting under compulsion and when both have reasonable knowledge of the relevant facts. It is the price at which a transaction could be expected to take place under conditions existing at the valuation date. The term "fair market value" is similar to the term "market value" used in real estate valuation.

3.2.2.2 *Market Value*

3.2.2.2.1 Market value as used in real estate valuation is defined as the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

3.2.2.3 *Investment Value*

3.2.2.3.1 In real estate, investment value refers to the value of property to a particular investor, or a class of investors, for identified investment objectives. This subjective concept relates a specific property to a specific investor or group of investors with identifiable investment objectives or criteria. In business valuation, this terminology is also similarly applied to refer to the specific value of business to a particular investor, or a class of investors, based on individual investment requirements. Investment value to a particular owner or investor may differ from fair market value because of differences in estimates of earning power, perception of degree of risk and the required rate of return, financing cost, and tax status which may give specific advantage to the investor concerned.

3.2.2.4 *Intrinsic Value*

3.2.2.4.1 It represents an analytical judgment of value based on the perceived characteristics inherent in the investment. An investor may thus consider the inherent value as the "true" or "real" worth of an item based on an evaluation of available information. When other investors also arrive at the same conclusion, then the inherent value may become the fair market value.

3.2.2.5 *Fair Value*

3.2.2.5.1 In business valuation, the term "fair value" is usually a legally created standard of value that applies to specific transactions. Unfortunately, fair value may not necessarily mean fair market value in practice.

3.2.2.5.2 Under the International Financial Reporting Standards 13, Fair Value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement or valuation date.

3.2.3 Premises of Value

3.2.3.1 Almost all businesses are valued under each of the following four premises of value.

a. *Value as a going-concern*
It refers to value in continued use and as a going-concern business enterprise.

b. *Value as an assemblage of assets*
It refers to value in place but not in current use in the production of income, and not as a going-concern business enterprise. It is the value of a group of assets assembled together.

c. *Value as an orderly disposition*
It refers to value in exchange with the expectation that all of the assets of the business enterprise will be sold individually. They will also enjoy normal exposure to the market.

d. *Value as a forced liquidation*
It refers to value in exchange with the expectation that all the assets of the business enterprise will be sold individually. They will experience less than normal exposure to the market, and usually result in a lower value.

3.3 DEFINING AND DESCRIBING BUSINESS INTEREST

3.3.1 Introduction

3.3.1.1 In the valuation process, proper determination of the business interest to be valued must be done. Valuers are expected to carry out adequate collection of data to produce the valuation.

3.3.1.2 Defining the assignment and description of the business entity is an important part of the valuation process. It identifies the specific business interest and its characteristics to be valued. Relevant data and materials that may affect the value of the business have to be collected and collated. This Guide sets out the details of the business interest to be valued and the need for specifying the details.

3.3.2 Details

3.3.2.1 *Description of Business Entity*

3.3.2.1.1 If the entity is incorporated or registered as a company, both the official name and country of incorporation are required in order to define the entity and its territorial rights. Two or more companies that are incorporated in different countries may have identical names. The law of the country may have a bearing on the value of a particular business interest. If the entity is not incorporated, some other structure, form and name must be specified. These may include sole proprietorships, partnerships, limited liability partnerships, and cooperatives or real estate investment trusts.

3.3.2.2 *Description of Business Interest*

3.3.2.2.1 The asset, property or business interest to be valued must be made clear and precisely described. Ownership interest in an entity is not the same as direct ownership of the underlying assets of the business entity. If a partial interest in an entity is to be valued, the proportionate relationship of the partial interest to the entire interest is to be determined. If the business to be valued is only a portion of the entire entity such as a branch, it is necessary to state explicitly which aspects are included in the valuation assignment.

3.3.2.3 *Equity or Invested Capital*

3.3.2.3.1 The elements of equity and debt in an entity to be included need to be clear. Equity means ownership interest. In a company, equity is usually represented by shares or stocks. If there is more than one class of shares or stocks in a multiclass capital structure, and only one class of share is to be valued, then there should be a statement specifying which class of equity the value purports to represent. In the case of a sole proprietorship or partnership, equity is represented by the sole proprietor's interest or partners' capital respectively.

3.3.2.3.2 Invested capital of an entity is often not clearly defined. If it is used, a definition should be given. Invested capital is usually used to refer to all equity and interest-bearing debt whether long-term or short-term. However, it has also been used to mean all equity and long-term debt, and in other cases, company's cash is excluded in the assets when invested capital is used.

3.3.2.4 ***Enterprise Value (Comments : To add Business Value which generally indicates the economic value of a business)***

3.3.2.4.1 It is generally used to represent the aggregate value of the company and therefore used synonymously as Market Value of Invested Capital (MVIC). In other words, Enterprise Value (EV) refers to equity plus total debt. For listed companies, EV represents market value of the company's shares plus total debt. The market value of the company's share is the total number of shares multiplied by the share price.

3.3.2.4.2 However, enterprise value has also been used to mean aggregate value of minority shares, or value of equity shares. If this term is used, it should be clearly defined.

3.3.2.5 ***Interests Other than Direct Freehold Ownership***

3.3.2.5.1 If the ownership is something other than direct fee simple ownership of the share or stock of partnership, the ownership interest should be specified. The interest may be a life interest or a reversionary estate. (Comments: valuation may involve either a specific period of interest or a freehold interest and either should be specified)

3.3.2.6 ***Characteristics of Specific Ownership Interest***

3.3.2.6.1 Two important aspects that need to be examined are the control (or minority) issue and the degree of marketability issue. The ownership interests should be clearly stated. The rights of control usually add value to shares, particularly making them worth much more than non-controlling shares. Generally, the degree of control can be clearly identified and stated. In addition, the degree of marketability or lack of it should be stated.

3.4 VALUATION REPORT

3.4.1 Introduction

3.4.1.1 The valuation is conveyed to the client in the form of a report. It must therefore be clear and not misleading as the valuation report can be acted upon by the client without any reference to the Valuer (unless a specific reservation has been made).

3.4.1.2 The valuation report must convey to the reader a clear understanding of the opinion expressed by the Valuer, the basis of valuation used and the assumptions and information on which it is based. This Guide sets out the details that should be included in a business valuation report.

3.4.2 Details

3.4.2.1 The length, type and content of a business valuation report may be influenced by :

- The client;
- Any applicable regulatory requirements;
- The type of business ownership interest being valued; and
- The nature of the business valuation.

3.4.2.2 A business valuation report must

- Clearly and accurately set forth the valuation in a manner that will not be misleading;
- Contain sufficient information to enable those who receive or rely on the report to fully understand it; and
- Clearly and accurately disclose any extraordinary assumption or limiting condition that directly affects the valuation, and indicate its impact on the concluded value.

3.4.2.3 Each written business valuation report should comply with the following disclosure requirements :

a. The report should clearly state the instructing party and the date of instruction;

b. Identify and describe the business or the business ownership interest that is the subject of the valuation;

c. State the purpose of the valuation and the client's intended use of the valuation opinions and conclusions;

d. Define the standard of value to be estimated;

e. Indicate the material or "as of" date of the valuation and the date of the valuation report;

f. Describe the valuation process;

g. Set forth the information considered, the analytical procedures followed, and the reasoning that supports the valuation opinions and conclusions;

h. Explain the Valuer's rationale for the valuation methods used and the valuation procedures considered;

i. Set forth any additional information that may be appropriate to demonstrate compliance with or clearly identify and explain permitted departure from, the requirements of any known global standards;

j. The report must be signed by a qualified Valuer;

k. The report is also to be dated;

l. The appendices to the report should contain most, if not all, of the following :

    i. Limiting Conditions; and
    ii. Any other information and its sources which the Valuer feels will enhance the reader's understanding of the business entity and the valuation.

3.4.2.4 A valuation certificate may be issued upon request by the client. The certificate is usually needed as an enclosure in published statements such as in the prospectus of an Initial Public Offer or in the annual reports of listed companies.

3.4.2.5 The practice of issuing a valuation certificate in lieu of a valuation report is strongly discouraged.

3.4.3 Explanation

3.4.3.1 The above are the minimum requirements to be contained in a valuation report and valuation certificate. In specific cases such as that for submission to the relevant State's Regulatory Authority or Stock Exchange, the valuation report should comply with additional requirements as specified by the user or client of the report and the relevant Guidelines or Listing Manual.

3.4.3.2 *Exclusion clause*
The Valuer may not be in a position to conduct financial due diligence of the client/company nor in a position to conduct business intelligence or fraudulent checks on the client/company. This should be clearly stated in the exclusion clause at the outset.

3.5 APPROACHES AND METHODS OF VALUATION

3.5.1 Introduction

3.5.1.1 Business valuation is one of the major types of valuation used to arrive at the worth of an entity or a business concern. As opposed to real estate valuation which is concerned with estimating the value of a real property, business valuation's main focus is to arrive at the worth of a business. Unlike real property, a business comprises both tangible as well as intangible assets, and deals with certain assets which may be removed, destroyed, merged and relocated elsewhere. It is not affected by the location in which the business is being operated. Hence, the most significant value base of the business is the expected profitability and future cash flow expected of the business operations.

3.5.1.2 In view of the nature of a business, the valuation of its worth is subject to variations because of the composition of the assets, purpose of valuation and the methods of valuation used.

3.5.2 Details

3.5.2.1 This Guide explains the nature of business valuation and the methods adopted in valuation and highlights the various causes for variations in valuation.

3.5.3 Common Approaches to Valuation

3.5.3.1 The common approaches to business valuations are similar to those that are used in real estate valuations. The three approaches are income, cost and market approaches. Within each of these approaches, there are different methods employed in business valuations. An examination of these various methods will reveal the many variations and computations which could be derived to arrive at a fair market value of the business concerned.

3.5.4 Methods within Each Approach

3.5.4.1 *Income Approach*

3.5.4.1.1 In the income approach to valuation, the value of the business is obtained by converting all future benefits into present value. The two common methods are the discounting and capitalisation methods. In the capitalisation method, a current or projected economic benefit is divided by a capitalised rate whereas in the discounting method, projected future economic benefits are discounted to a present value. The capitalisation method is equivalent to the years purchase or yield method commonly known as the income method used in real estate valuation. The discounting method is equivalent to the discounted cashflow method used in real estate valuation.

a. *Discounting Method*

In economic theory, the discounting method is the best way to value any investment since it is based on the premise that a financial investment is the sum of all the future benefits it will provide for the investor, each discounted at a discount rate that reflects the time value of money and the degree of risk of receiving the benefits expected.

b. *Capitalisation Method*

The capitalisation method is essentially a short version of the discounting method. Instead of projecting each year's benefit, capitalisation assumes a fixed amount that remains constant throughout in the future. The capitalisation rate and discount rate are related through the growth rate. If the growth rate is estimated accurately the capitalisation method will produce an indicative value exactly the same as that produced by the discounting method.

3.5.4.2 *Cost Approach*

3.5.4.2.1 In the cost or asset-based method, the adjusted net asset method or excess earning method may be used. In the adjusted net asset method, all assets and liabilities are adjusted to current values and added up giving a resulting net asset value. In the excess earning method, a collective valuation of all intangible assets is added to the value of tangible assets.

3.5.4.3 *Market Approach*

3.5.4.3.1 In the market approach, it is based on the assumption that arm's length transactions of similar businesses will provide good evidence of value. This is equivalent to the direct comparison method used in real estate valuation. Almost all transactions in publicly traded securities are at arm's length. Hence comparable companies or what is often termed as guideline companies as preferred by the business valuation community are used to provide the evidence. The primary criterion for comparison is line of business although the preference is for comparable companies possessing similar risk characteristics rather than producing similar products or services. At least three companies should be used as a basis for comparison although the preference is for five and more. The better the comparability, the fewer companies are needed. The three methods that can be used are :

a. *Guideline Public Company Method*
This method relates market value multiples for public company stocks to fundamental financial variables for the subject company.

b. *Guideline Merger and Acquisition Method*
This method relates market value multiples from sales of entire companies or controlling interests to fundamental financial variables for the subject company.

c. Other market evidence such as prior transaction, offers and buy-sell agreement.

3.5.4.3.2 Previous transactions and other situations may provide valuable evidence of value. However, there is the need to ensure that the information is comparable in terms of time and whether the transactions are arm's length.

3.5.5 Explanation

3.5.5.1 *Variations in Income Approach*

3.5.5.1.1 Possible variations in the methods used in the income approach can be due to the following :

- *Measures of return.* There is a tendency to use net cash flow as a measure of the future benefit but other measures of return have been used such as net income.
- *Capital base.* The benefit or income that is available can be attributed to the common equity or to all invested capital.

a. *Preference for Net Cash Flow*
Net cash flow is the amount that is available for the investors to take out of the business for use without undermining the ongoing operations of the business whereas net income does not measure the actual income available to the investor.

b. *Capital Base*

Whether the capital base is common equity or all invested capital, the appropriate net cash flow and discount rate should be used as follows :

For common equity, the net cash flow should be based on those available to common equity owner, that is, net income after entity-level income tax before personal income tax. The discount rate used should be equity cost of capital. Whereas for all invested capital, the net cash flow (free cash flow) should be those available to all invested capital holders, that is, after tax affecting the tax-deductible interest cost of debt. The discount rate used should be weighted average cost of capital (WACC). WACC is derived from the following formula :

WACC = (ROE x [Equity / (Debt + Equity)]) +
(cost of borrowing x [Equity/(Debt + Equity)])

Net Cash flow (NCF) = net profit + interest expense
– net capital expenditure (CAPEX)
– net changes in working capital
– tax shield on interest expenses

Working capital = current assets – current liabilities

Tax shield = Tax rate x interest expense

Equity value may be estimated by discounting returns available to all invested capital and deducting the market value of senior capital, that is, preferred stocks and interest-bearing debt.

c. *Estimating Terminal Value*
As most equity investments are considered to have a perpetual life, it is only practical to project reliable future cash flows for a limited period ranging from 3 to 10 years. For Real Estate Investment Trusts (REITs), a common period of 10 years is adopted. The present value of the expected future cashflow beyond the specific projection period is captured by estimating a terminal value and discounting that terminal value to a present value for the number of years of the projection period.

d. *Mid-year Discounting*
Unless otherwise stated, it is always assumed in the calculations that receipt of cash flows is at the end of each year. If cash flows are received evenly throughout the year, the computations can be modified to assume cash flow for the year to be received at the middle of the year rather than at the end of the year by deducting 0.5 from the exponent applied to the discount rate. The mid-year convention will result in a higher present value than the year-end convention since cash flows are received earlier.

3.5.5.2 *Variations in Cost Approach*

3.5.5.2.1 The cost approach or the adjusted net asset method (also called the asset accumulation method) is based on the assumption that a buyer would not pay more than it would cost to create an entity of equivalent utility, that is, the economic principle of substitution. Hence, all assets and liabilities whether tangible and intangible are adjusted to fair market value. The value of the equity is indicated by the net of the adjusted asset minus liability values. As the assets of a company may include real estate, and plant and machinery, the business Valuer would need to have some familiarity with the approaches and methods used in valuing these assets.

3.5.5.3 *Variations in Market Approach*

3.5.5.3.1 The use of market data for comparison is preferred by most investors and the courts as in real estate valuation where the market comparison method is the most preferred. However, this approach depends on the availability of suitable comparables.

a. *Guideline Public Company Method*

The comparison is made based on multiples of publicly traded securities prices to the company fundamental financial variables such as net income, pretax income, gross cashflow, EBIT, sales etc. The value multiple is essentially the inverse of the capitalisation rate for each respective variable. The multiples used can be based on equity value multiples or invested capital multiples.

Selection of multiples

The preference in multiples selection is to make a comparative analysis of the fundamentals of the subject company with those of the guideline companies. It is essential to select multiples for which there are adequate reliable data and place more weight on multiples with least statistical dispersion among guideline companies.

b. *Guideline Merger and Acquisition Method*

Data on Mergers and Acquisitions (M&A) may not be easily available, hence various sources may have to be explored to obtain information. The number of guideline companies is usually limited particularly those based on arm's length transactions. It is always necessary to investigate whether the transaction between parties is arm's length.

In addition, because M&A transactions are not concluded on the same date as the material valuation date for subject companies, there is a need for adjustment to be made for time differences. There is also the need to determine what was included with what is being valued for subject companies and adjust the values for any differences.

Mergers and acquisitions usually represent transactions with different controlling interests. When valuing a controlling interest, there is usually no minority adjustment needed for most cases, and a discount for lack of marketability may be considered on a case-by-case basis. When valuing a minority interest, it is usual to provide for a minority interest discount and to account for lack of marketability.

The above discussions highlight the causes for variations in business valuations. There is no one correct way of classifying valuation methods. Hence, to avoid inconsistency in the approach, the Valuer is to fully understand the nature and purpose of the valuation, and apply the correct method and procedures to arrive at the value. Another method may be used as a check.

3.6 VALUATION OF INTANGIBLE ASSETS

3.6.1 Introduction

3.6.1.1 An intangible asset has special characteristics. It refers to an identifiable non-monetary asset without physical substance which is held for use in production or supply of goods and services. Traditionally it refers to business goodwill. In recent years, it is used to refer to any definable commercially transferable interest in any items included in the following :

a. Patents, inventions, processes, designs, trade secrets or know-how;
b. Copyrights, literary, musical or artistic compositions;
c. Trademarks, trade names or brand names;
d. Franchises or licenses;
e. Systems, procedures, forecasts;
f. Computer software; and
g. Other similar items which derive their value not from physical attributes but from their intellectual content or other intangible asset.

3.6.1.2 It should be noted that certain kinds of intangible assets are also referred to as intellectual property registered under legislation for protection. The methods of valuation used for valuing intangible assets are similar to those used for real estate valuation.

3.6.2 Details

3.6.2.1 This Guide relates to the valuation of intangible assets and its reporting. It highlights the scope of work, the information needed and the methods used.

3.6.3 Valuation Report

3.6.3.1 The following should be identified :

a. The asset to be valued;
b. Interest to be valued;
c. Date of valuation;
d. Purpose of valuation;
e. Definition of value;
f. Methods of valuation;
g. Assumptions made;
h. Limiting conditions;
i. Restrictions, agreements and other factors that may influence value; and
j. Sources of information.

3.6.3.2 Information Required for Valuation

a. General description and analysis of what constitutes the intangible asset. To have economic value, intangible asset should have the following characteristics :

   i. It is capable of being identified and recognised;
   ii. It is subject to legal existence and protection which may be incorporated within a larger entity;
   iii. It is subject to ownership and legally transferable;
   iv. It is capable of generating some measurable amount of economic benefit; and
   v. It can potentially enhance the value of other assets with which it is associated.

b. Description of specific asset to be valued. The particular intangible asset being valued should be clearly identified. The description should provide a complete identification of relevant transactions, and may also specify physical, functional, technical or economic parameters to identify the particular intangible asset. Other relevant information includes :

i. The cost, manner and date of acquisition;
ii. The date on which the asset was previously valued;
iii. Agreements or understandings entered into (or expected to be entered) that relate to the use or sale of the asset;
iv. The economic outlook of the market in general and the outlook of the specific asset in particular; and
v. Such other factors which, in the opinion of the Valuer, are appropriate for consideration.

3.6.4 Methods of Valuation

3.6.4.1 Judgement should be used to select the appropriate approaches (such as market, cost or income) to be adopted and the method(s) within such approaches that best indicate the value of the asset.

3.6.4.2 *Market Comparison Method*

3.6.4.2.1 The market comparison method relies on identification of similar intangible asset sold under similar conditions. This method requires the presence of an active market involving comparable assets. The method involves identifying comparable intangible assets in terms of general standards of comparability such as functions, contractual terms, risks, and economic conditions. More specifically the comparable intangible assets should have the following characteristics :

a. Be used in similar products or processes within the same industry or market;

b. Be in the same stage of development and possess a similar degree of uniqueness;

c. Have similar profit potential including a consideration of capital investment and start-up expenses required and the risks to be assumed; and

d. Have similar terms such as exploitation rights, geographic limitations, exclusivity, duration, and functions or services to be performed.

3.6.4.3 ***Cost Method***

3.6.4.3.1 The method involves the estimation of the cost to reproduce or replace or to pay or purchase the subject intangible asset. The replacement cost includes the cost of labour, materials, overheads and profits during the development as well as the design, and other fees such as legal costs and taxes.

3.6.4.4 ***Income Method***

3.6.4.4.1 The method focuses on the income-producing capacity of the intangible asset. It relies on estimates, future earnings, the duration of income streams, and risks associated with the realisation of the forecasted income. More specifically, it considers the following :

a. The income generation capacity of the subject intangible asset and forecasts the future stream of earnings or cash flow;

b. The expected remaining useful life of the intangible asset, how long is the economic benefit, which may depend on the product life cycle; and

c. The risk associated with receiving anticipated benefits, as may be measured by the discount rate reflecting the opportunity cost of capital, inflation, liquidity, risk premium and real interest.

3.6.4.4.2 It should be noted that the accuracy of the income method depends on the sensitivity of the projections, discount rates, and useful lives adopted.

3.6.4.4.3 The income method has commonly been used to assess the business goodwill which refers to the value of an entity over and above the value of its assets. It is determined by the capitalisation of excess earnings or income, that is, the existence of earnings above a fair return on all other business assets. The procedure involves first determining the actual net operating profit from the total historical costs of tangible and intangible assets. The normal net profit related to the value of the assets employed in business is then calculated. The super profit is worked out from the difference between the net operating profit and normal net profit. The value of goodwill is determined based on the present value of the super profit over the period at an appropriate discount rate.

3.6.5 Explanation

3.6.5.1 The final opinion of value should reflect the appropriateness of each method, and the reliability of the data supporting each method. Only those approaches and methods deemed appropriate for dealing with the valuation in question should be considered, giving reasons for using them.

3.7 VALUATION FOR FINANCIAL REPORTING

3.7.1 Introduction

3.7.1.1 In the preparation of the financial reports, valuations are required for different accounting purposes. The International Accounting Standard (IAS) 1 prescribes the basis for presentation of general-purpose financial statements to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities.

3.7.1.2 This Guide assists Valuers to understand the requirements under the International Financial Reporting Standards (IFRS) 13 on Fair Value Measurement, and to prepare the valuation to meet the applicable requirements.

3.7.2 Details

3.7.2.1 It is necessary to identify the asset to be valued and to confirm how that asset is used or classified by the reporting entity. The treatment of real estate may differ depending on whether it is used for purpose of the entity's business, is held as an investment asset or is treated as stock in the case of developers. The financial instruments that are held to receive cash flows may be treated differently if the basis of payment is different. Intangible assets acquired through a merger or acquisition may be treated differently from those that are currently owned by the entity.

3.7.2.2 The relevant assumptions with regards to how the assets are to be held or classified or will continue to be used as part of the business should be stated.

3.7.3 Basis of Value

3.7.3.1 The concept of fair value is used in accounting. IFRS 13 Fair Value Measurement defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement or valuation date. IFRS 13 provides that the measurement of a liability assumes that it is transferred to a market participant on the valuation date.

3.7.3.2 The IFRS emphasises that fair value is a market-based measurement, not an entity-specific measurement. When measuring fair value, it should be based on the assumptions that market participants would use when pricing the asset or liability under current market conditions, including assumptions about risk.

3.7.3.3 The IFRS assumes that the transaction to sell the asset or transfer the liability takes place in the principal market for the asset or liability or, in the absence of a principal market, in the most advantageous market for the asset or liability.

3.7.3.4 The principal market is the market with the greatest volume and level of activity for the asset or liability that can be accessed by the entity.

3.7.3.5 For a non-financial asset ie real estate, the highest and best use of the asset should be determined. This is whether the asset is used in combination with other assets or on a stand-alone basis.

3.7.3.6 The appropriate valuation methods adopted should consider the use of relevant observable inputs rather than unobservable inputs.

3.7.4 Fair Value Hierarchy

3.7.4.1 The IFRS establishes a fair value hierarchy that categories the inputs used for valuation into three levels.

3.7.4.2 The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liability (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

3.7.4.3 Level 1 inputs are quoted prices in active markets for items identical to the asset or liability being valued that the entity can access at the valuation date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs, but must be developed to reflect the assumptions that market participants would use when determining an appropriate price for the asset or liability.

3.7.5 Valuation Approaches

3.7.5.1 The IFRS describes the following approaches may be used to determine fair value: market, income and cost approaches.

PLANT AND MACHINERY VALUATION

4.1 GENERAL VALUATION CONCEPTS AND PRINCIPLES

4.1.1 Introduction

4.1.1.1 This Guide provides an explanation of the general valuation concepts and principles adopted in plant and machinery valuation.

4.1.2 Asset Concept

4.1.2.1 Assets are used in accounting which distinguishes between current assets and fixed assets.

4.1.2.2 Current assets are assets not intended for use on a continuing basis in the activities of the enterprise such as stocks, debtors and cash in bank and in hand. In certain circumstance, real estate, normally treated as a fixed asset may be treated as a current asset. Examples include improved real estate held in inventory for sale by real estate developers.

4.1.2.3 Fixed assets are tangible and intangible assets which fall into two broad categories, namely, property, plant and equipment and other long-term assets.

a. *Property, plant and equipment* - Assets intended for use on a continuing basis in the activities of an enterprise including land and buildings, plant and equipment, and other categories of assets, suitably identified.

b. *Other long-term assets* - Assets not intended for use on a continuing basis in the activities of an enterprise, but expected to be held in long-term ownership including long-term investments, long-term receivables, goodwill, expenditures carried forward, and patents, trademarks, and similar assets.

4.1.3 Price, Cost and Value

4.1.3.1 Price is a term used for the amount asked, offered, or paid for a good or service. It is a historical fact, whether it is publicly disclosed or retained in private. Because of the financial capabilities, motivations, or special interests of a given buyer and seller, the price paid for goods or services may or may not have any relation to the value which might be ascribed to the goods or services by others. Price is, however, generally an indication of a relative value placed upon the goods or services by the particular buyer and/or seller under particular circumstances.

4.1.3.2 Cost is the price paid for goods or services, or the amount required to create or produce the good or service. When completed, it is a historical fact. The price paid for a good or service becomes its cost to the buyer.

4.1.3.3 Value is an economic concept. It refers to the monetary relationship between goods and services available for purchase and those who buy and sell them. Value is not a fact, but an estimate of the worth of goods and services at a given time in accordance with a particular definition of value. The economic concept of value reflects a market's view of the benefits, which accrue to one who owns the goods or receives the services as at the effective date of value.

4.1.4 Principles of Valuation

4.1.4.1 Utility refers to the usefulness or satisfaction one receives from a good or service. In valuation, land value is established by evaluating its utility in terms of the legal, physical, functional, economic, and environmental factors which govern its productive capacity.

4.1.4.2 The principles of valuation applied in valuing plant and machinery include substitution, anticipation or expectation.

a. *Substitution*
A prudent buyer will pay no more than for an asset than the cost of acquiring an equally desirable substitute in the open market. It supports the premise that a buyer will not pay any more for a plant and machinery than the cost of reproducing or buying a similar plant and machinery.

b. *Anticipation*
The current value of an asset depends on the anticipated utility or income that will accrue to the asset owner in the future. The present value of an asset depends on the expected future benefits of ownership. This principle is often used in the income method.

4.2 FAIR MARKET VALUE BASIS OF VALUATION

4.2.1 Introduction

4.2.1.1 As in real estate or business valuation, it is necessary to set out the basis of valuation for plant and machinery. This guide sets out the various terms used in plant and machinery valuation.

4.2.2 Details

4.2.2.1 *Premise of Value*

4.2.2.1.1 A standard of value refers to the type of value being sought such as fair market value or liquidation value. A premise of value is the assumption as to the set of actual or hypothetical transactional circumstances applicable to the subject valuation such as in continued use or in liquidation. In many situations, the standard of value is legally mandated whether by law or between the parties involved.

4.2.2.1.2 In plant and machinery valuation, the Valuer deals with a variety of assets which can be moved. In general three categories of value can be recognised based on the anticipated use of the asset as follows :

- Sale for removal for a similar use or an alternative use;
- Continued use of the asset for the purpose for which it was designed and acquired; and
- Liquidation.

4.2.2.2 *Fair Market Value*

4.2.2.2.1 Fair market value is defined as the estimated amount that may reasonably be expected for a property in an exchange between a willing buyer and a willing seller, neither under any compulsion to buy or sell, and both fully aware of all relevant facts as of a specific date. This definition is similar to the "market value" used in real estate valuation or the "fair market value" used in business valuation.

4.2.2.2.2 This concept is usually used when valuing plant and machinery for sale or purchase purpose.

4.2.2.3 *Fair Market Value for Continued Use*

4.2.2.3.1 If the asset is to be assessed for its continued used or installed, the fair market value in continued use is similarly defined except that the buyer and seller are fully aware of all relevant facts including installation and assuming that the business earnings support the value reported. This amount includes all normal direct and indirect costs such as installation and other assemblage costs to make the property fully operational.

4.2.2.4 *Liquidation Value*

4.2.2.4.1 There are three premises of value for liquidation as follows :

a. Orderly liquidation value refers to the estimated amount that could be typically realised from a liquidation sale, given a reasonable period of time to find purchaser with the seller being compelled to sell on an as-is, where-is basis, as of a specific date;

b. Forced liquidation value refers to the estimated amount that could be typically be realised from a properly advertised and conducted public auction with the seller being forced to sell with a sense of urgency on an as-is, where-is basis as of a specified date; and

c. Liquidation value in place refers to the estimated amount that could typically be realised from a failed facility, assuming the entire facility would be sold intact with a limited time to complete the sale as of a specified date.

Valuers shall not provide a Liquidation or Forced Sale Value unless specifically requested by the clients. In all such instances the Valuer shall provide the assumptions on which such value is based.

4.2.2.5 ***Other Concepts of Value***

4.2.2.5.1 Salvage value refers to the estimated amount that may be expected for the whole asset or a component of the asset that is retired from service for possible use elsewhere.

4.2.2.5.2 Scrap value is the estimated amount that could be realised for the asset if it were sold for its material content, not for a productive use.

4.2.2.5.3 Insurable value refers to the replacement cost new less accrued depreciation considered for insurance purposes as of a specified date.

4.2.2.6 *Valuation Bases Other Than Fair Market Value*

4.2.2.6.1 Although the majority of the valuations involve fair market value, there are circumstances that call for bases other than fair market value. It is essential that both the Valuer and valuation users clearly understand the distinction between fair market value and non-market value based valuations, and the effects (if any) the differences between these concepts may have upon the applicability of the valuation.

4.2.2.6.2 For those purposes the Valuer shall state the purpose and the basis of valuation clearly in the valuation report. The Valuer shall distinguish that the valuation is not a fair market value estimate if the assignment is on a basis other than fair market value.

4.3 CLASSIFICATION AND REFERENCING

4.3.1 Introduction

4.3.1.1 In the valuation process, inspection of the asset must be carried out and relevant information collected to produce the valuation.

4.3.1.2 Classification and description of plant and machinery are particularly important. Proper referencing should be carried out to identify the asset. Relevant data and materials that may affect the value of the asset have to be collected and collated.

4.3.2 Details

4.3.2.1 *Classification and Description*

4.3.2.1.1 An important aspect of plant and machinery valuation is the proper classification and description of the assets. This will facilitate the collection of appropriate information. The typical classes are production machinery; support equipment; motor control centres and switchgear; power wiring; process piping; foundations and structural supports; material handling and storage equipment; general plant equipment; plant and motor vehicles; locomotives, aircrafts, boats, ferry and offshore vessels, laboratory and test equipment; office furniture, fixtures and equipment; computer equipment; tools; special tooling; patterns and templates; construction in progress; and other special classes and inventory.

4.3.2.2 *Identification and Listing*

4.3.2.2.1 Another aspect is the proper identification and listing of the machinery. Both a macro and micro approach should be adopted. A macro approach is used to understand the entire manufacturing process by identifying major components contributing to the design capacity of the plant. A micro approach is used to find out the individual characteristics of the equipment by listing individual machines and identifies the specification of the equipment such as brand name, capacity, model number, serial number, type of power, and dimensions if possible.

4.3.2.3 *Sampling*

4.3.2.3.1 Sampling may sometimes be undertaken to value large amounts of inventories or other tangible assets without actually inspecting each item. Sampling is generally appropriate when the sample is likely to be an accurate reflection of the whole. Before undertaking the sampling technique, the Valuer should explain to the client the limitation of this form of valuation and obtain the client's agreement to use the method. The method should then be properly disclosed in the valuation report.

4.4 VALUATION REPORT

4.4.1 Introduction

4.4.1.1 The valuation is conveyed to the client in the form of a report. It must therefore be clear and not misleading as the valuation report can be acted upon by the client or third parties without any reference to the Valuer (unless a specific reservation has been made).

4.4.1.2 The valuation report must convey to the reader a clear understanding of the opinion expressed by the Valuer, the basis of valuation used and the assumptions and information on which it is based.

4.4.2 Details

4.4.2.1 In the event of a large number of assets being valued, it may be useful to produce an Executive Summary in the valuation report to highlight the key assets valued and other important information found. The content of the valuation report should contain the following headings :

- Premise of value
- Identification of asset
- Purpose of valuation
- Effective date of valuation
- Date of inspection
- Description of asset
- Method of valuation
- Opinion of value
- Signature of Valuer.

4.4.2.2 The valuation report must provide sufficient information to permit those who read and rely upon the report to fully understand its information/data, reasoning, analyses and conclusions. It must state any assumptions and limiting conditions upon which the valuation is based.

4.4.2.3 The appendices attached to the report should contain most if not all of the following:-

a. Photographs of the assets;
b. Schedule or inventory of plants and machinery valued;
c. Limiting Conditions; and
d. Any other information which the Valuer feels will enhance the reader's understanding of the asset and the valuation.

4.4.2.4 If the valuation report is prepared for a listed company or for prospective listing on the relevant State's Regulatory Authority or Stock Exchange, then the report should comply with the requirements set down in the relevant Guidelines or Listing Manual.

4.4.2.5 A valuation certificate may be issued upon request by the client. The certificate is usually needed as an enclosure in published statements such as in the prospectus of an Initial Public Offer or in the annual reports of listed companies.

4.4.2.6 The practice of issuing a valuation certificate in lieu of a valuation report is strongly discouraged.

4.4.3 Explanation

4.4.3.1 The above are the minimum requirements to be contained in a valuation report.

4.5 APPROACHES AND METHODS OF VALUATION

4.5.1 Introduction

4.5.1.1 Plant and machinery valuations are required for various reasons similar to those of other assets. The methods of valuation are similar to those for valuing real estate and business. There are three generally recognised approaches to the determination of value. They are comparison, cost and income approaches. Within these approaches are different methods. The common methods of valuation are the Comparison Method, the Cost Method, and the Income Method. There are, however, certain issues which pertain to plant and machinery valuations which need to be considered here.

4.5.1.2 This Guide sets out the various methods for preparing a plant and machinery valuation.

4.5.2 Details

4.5.2.1 The rationale for adopting a method or methods of valuation has to be explained in the valuation report.

4.5.2.2 The Valuer is encouraged to use, apart from the main method of valuation, additional methods of valuation as a crosscheck to the main method of valuation.

4.5.2.3 While there is no single universal method for all types and purposes of valuation, a Valuer should use the appropriate method in carrying out the valuation. The method of valuation should be stated in the valuation report with a brief description.

4.5.2.4 Although the fair market value concept is often used, other concepts of values may be used. The Valuer should state the reason for such use.

4.5.3 Methods of Valuation

4.5.3.1 Cost Method

4.5.3.1.1 The cost method of valuation is based on the rationale that the value of the subject asset can be estimated on the basis of its cost.

4.5.3.1.2 The Valuer begins with the current replacement cost of the asset being valued and then deducts the loss in value caused by obsolescence.

4.5.3.1.3 It should be noted that the cost estimated should include the assemblage costs. Typical assemblage costs include sales tax; costs of dismantling, moving and setting in place; freight costs necessary to get the assets to the owner's site; rebuilding or retrofitting costs; installation costs including connections, foundations; connection costs including piping, wiring and instrumentation; design, engineering or evaluation costs; start-up and testing costs; and any other direct or indirect costs that are normally required to place the asset in service.

4.5.3.2 Comparison Method

4.5.3.2.1 The comparison method can be used in all valuations where there are adequate transactions or other information to indicate the level of value for the subject asset.

4.5.3.2.2 The comparison method relies on the presence of market transactions to provide an indication of value. It is supported by the theory that the market value of an asset bears a close relationship to the values of similar assets which have been transacted.

4.5.3.2.3 The Valuer analyses recent sales of assets that are similar to the subject asset. He will then make adjustment to the selling prices of comparables to equate them to the characteristics of the assets being valued. The adjustment factors include effective age, condition, capacity, features, location, manufacturer, quality, quality, time of sale and type of sale.

4.5.3.3 ***Income Method***

4.5.3.3.1 The income or investment method of valuation is a method of estimating the present worth of the rights to future benefits to be derived from the ownership of a specific asset under given market conditions. In valuation, these rights are often expressed as future income in the form of the prevailing and sustainable rent.

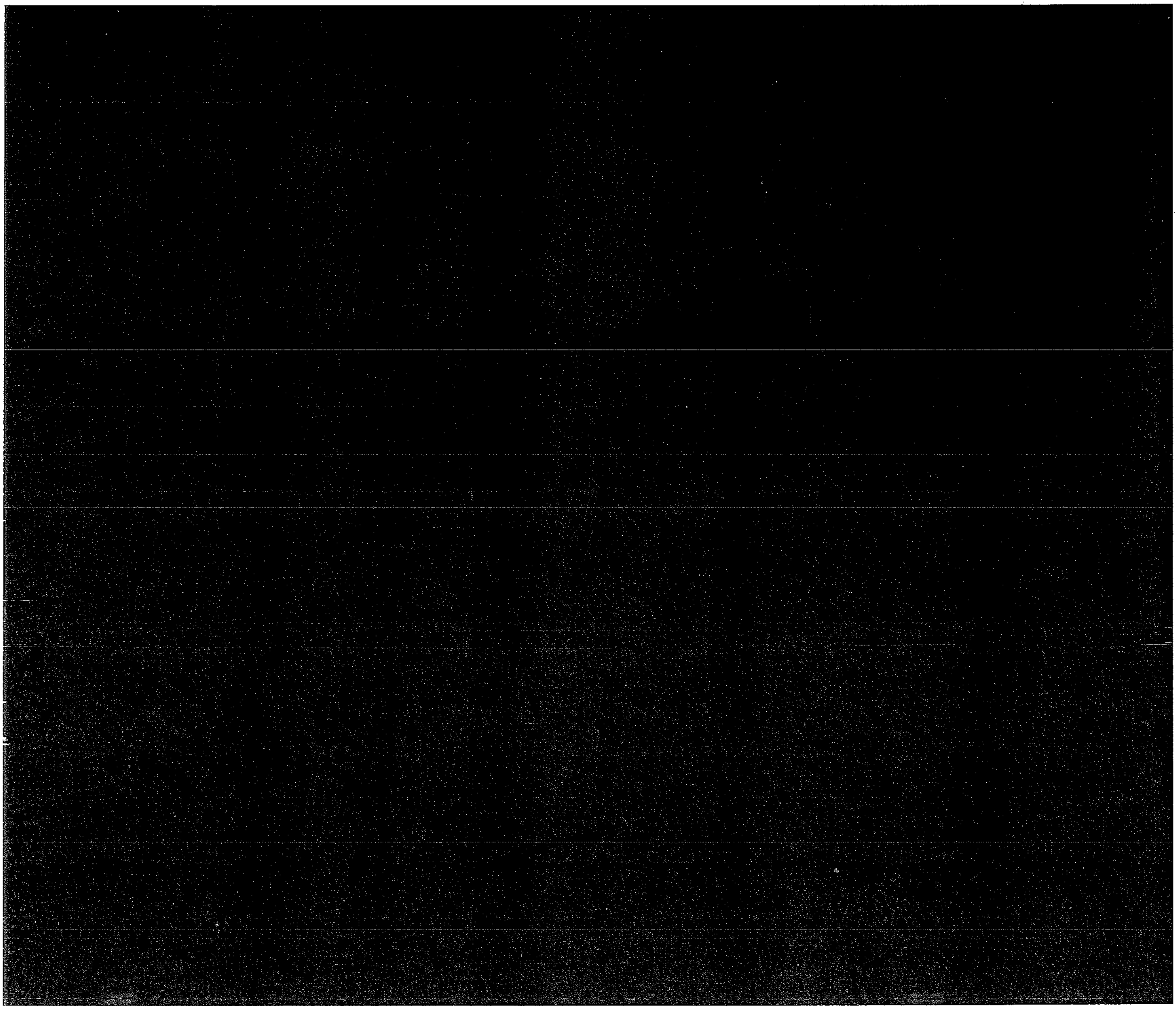
4.5.3.3.2 The Valuer measures the present value of the asset's expected future returns. Two methods typically used to value machinery and equipment are the direct capitalisation method and the Discounted Cash Flow (DCF) method.

4.5.3.3.3 The direct capitalisation method measures value by dividing a projected income stream by a capitalisation rate. It assumes that there will be no variation in the capitalisation rate and no termination of the income stream.

4.5.3.3.4 The DCF method estimates the future periodic income and residual value, and discounts them to a present value using a discount rate. It is based on an invested capital, net cash flow basis without considering the effects of finance and taxes.

4.5.4 Departure Provision

4.5.4.1 When other approaches or variations of, and to, the above stated methods are applied, these must be fully explained and the data used in the valuation must be substantiated by market evidence.



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