HOW APPRAISERS DEVELOP FAIR VALUE

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ABSTRACT: *Management is responsible for its own financial decisions. If we take into account, that fair value concept was shown in financial crisis as something that does not work anymore in this way; there is a big need to develop it for the future. Non-professional readers of financial statements believe, however, that company financials are the work of the public accounting firm that had signed the audit certificate. The main reason for bringing this point up is that when companies disclose Fair Value (FV) information in their financial statements, they are taking responsibility for the values disclosed. Management may often be encouraged to utilize the services of an outside professional, but at the end of the day, the outside appraiser is a hired gun. Although the appraiser has to take responsibility for his own work, hiring the appraiser does not absolve management of its ultimate responsibility. The obverse of this is also true. Management does not have to hire the appraiser to develop any fair value disclosures made in the financial statements. Developing FV information is not recommended as a do-it yourself undertaking, there is nothing in Generally Accepted Accounting Principles (GAAP) or Securities Exchange Commission (SEC) regulations, however, that requires an outside appraiser.*

KEY WORDS: *fair value; financial executives; appraisers; SEC; GAAP; accounting; financial crisis.*

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1. BASIC VALUATION PRINCIPLES

It is important to note that this is not a do-it-yourself guide for appraisals and valuation. There is a need of financial executives to understand what appraisers do, understand why they do it, and understand what the resulting valuation answers mean. Thus appraisers, looking for guidance in implementing Financial Accounting Standards Board (FASB) FV pronouncements, can skip this. Many books and articles describe the basic principles of valuation. Essentially, an appraiser uses one or more of

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three approaches to value. Only three principles or approaches can be used to determine the value, and every appraisal technique is simply a variation of one of these.

The *cost approach* asks what it would cost today to acquire the same or similar assets. If you are valuing a building, the upper limit on value is going to be the price you would have to pay a contractor today to build the same building. A rational buyer would not acquire an existing building at a price of 120 money units (MU) if a new building could be constructed at 100 MU. Similarly, in valuing machinery and equipment, we look to the prices of new assets from the manufacturer. Where necessary, adjustments are made for technology and productivity improvements. The cost approach is highly reliable in dealing with tangible professional property and real estate. It is not generally used by appraisers in valuing financial assets, such as the income stream to be derived from security.

The *market comparable approach* looks to the market to see what the same or similar assets are actually selling for. For example, if you have 2005 Buick for-door sedan that you want to sell, how to determine its value? You go to classified ad pages and see how much other similar Buicks are selling for. Maybe no 2004 model is advertised, but 2003 and 2005 modes are offered. You would than compare your car with those advertised and estimate what yours would bring. The market comparable method works very well when a well-established market exists. It is not ordinarily utilized by appraisers for intangible assets.

The *income approach* asks what investors are willing to pay for an asset with a given income stream in the future. Investors, and hence appraisers, adjust for perceived risk. To value an asset using the income approach requires a good projection of future income cash flows and choice of a proper discount rate. Whenever possible, appraisers prefer to utilize someone else income projections, in as much as specifics are better known by the principals. The appraiser, in turn, is usually responsible for the choice of the discount rate. The higher the discount rate is chosen, the lower the value, and vice versa. Of course, using of this method these days is very complicated. In the age of financial crisis, potential future cash flows are simply unpredictable.

Generally speaking, appraisers are required by professional standards to use all three valuation approaches in every assignment. As a practical matter, this is not usually possible. So one of the first decision that must be made is to determine how many of the approaches can be used.

2. CORRELATING THE ANSWER

Appraisers are required, by professional standards, to evaluate the strengths and weaknesses of each value indication. Basically, we look at the information base utilized in each approach and weight more heavily the answers that were derived from reliable sources. Similarly, the cost approach is often accurate for the building, but perhaps there is no land available in this business market, so the derived land value is relatively uncertain. The possible permutations and combinations are unlimited.

The bottom line is that the appraiser has to perform professional responsibilities by exercising judgment. Thus, in advance, it is probably unlikely that an appraiser will be able to say which of the tree approaches is going to work out best in any specific situation. By setting up a hierarchy of valuation approaches, always putting the market approach on top, inevitably the FASB seems to downgrade the reliability of the income approach and the cost approach. The FASB is putting its thumb on the scale, in advance. It is telling valuation specialists, auditors and financial statement users that using the income approach, much less the cost approach, is less reliable.

Yet Machinery and Equipment (M&E) appraisers have traditionally used he cost approach. In fact, using the market approach in an allocation of purchase price will positively give the wrong answer. These days it appears that the FASB may be rethinking its position on the reliability and relevance of the cost approach for M&E in the allocation situation.

3. VALUE IN USE VERSUS VALUE IN EXCHANGE

What may seem like an esoteric subject fit only for the appraisers – how to determine FV – may turn out to have a greater impact on financial reporting than the adoption of *SFAS 141* and *SFAS 142.* How should we determine the fair value of long – lived assets, usually Property, Plant and Equipment (PP&E)? This is not an esoteric question, because as we will see, appraisers use two separate premises of value, and the choice will affect the amount allocated to PP&E. The fewer money units allocated to PP&E, the lower will be annual depreciation charges, and the consequence would be more allocated to goodwill, which is not amortized anymore. Consequently, by choosing one premise of value over another, there will be a significant change in reported income. The issue, then, is what the correct premise of value is.

The difference between two premises is as simple as whether you are buying or selling an asset. If I am selling a 2002 Corvette to a dealer, I will receive for example 29 000 MU. However, if I go to the same dealer and buy 2002 Corvette, the dealer will charge some 39 000 MU. The premise of the value in this case is the answer to the question, "Are you buying or selling?" This concept is referred to by appraisers as determining Value in Exchange. It represents the current market price and requires specification of the appropriate market, in this case wholesale versus retail.

There is another premise of value, which appraisers refer to as Value in Use. Over the last 50 years, appraisers have developed a standard methodology or approach to determine for purposes of purchase price allocation, the FV of PP&E on an accurate and cost effective basis. We refer to this as Value in Use (VIU) premise of value, and it has worked well. The alternative approach, Value in Exchange (VIE), seems now to be preferred by the FASB because of its emphasis on market participants and market transactions. VIE provides a different and usually lower value for PP&E. Although corporate officers might welcome this change in valuation concepts, because of its immediate favorable impact on reported income, as appraisers we raise the question, "Are we moving forward, or backward, if we adopt the FASB VIE concept of FV, at least for purchase price allocation?"

Value in use is defined as *an amount of money that would be exchanged between a willing buyer and the willing seller with the equity to both, neither being* *under any compulsion to buy or sell and both being fully aware of the relevant facts, assuming that the assets will continue to function in its present capacity as a part of an ongoing business enterprise at its present location.*

Value in exchange is defined as *an amount of money that would be exchanged between a willing buyer and the willing seller with the equity to both, neither being under any compulsion to buy or sell and both being fully aware of the relevant facts as of a certain date.* Market value excludes the cost of installation, foundations, piping and power wiring applicable to each machine unit and does not consider its contributory value as a part of an ongoing business enterprise at its present location.

The italicized portions of the standard definitions highlight the two different concepts. VIU is premised on the assumption that, in a business combination, the buyer acquired a going concern. The buyer should identify what it would cost today to have the same or similar assets in place, up and running and producing the output at the existing level.

Some of the equipment may be new state of the art, whereas others may be older technology, ever fully depreciated, that is still capable of cost-effective production. The fact is that the day before the business combination, the assets were working and producing, and we assume that no change occurs the next day simply because of new ownership. The purchase price for the business included as part of the going concern values the fact that existing equipment has been installed, tested and debugged and that the various components in, say, an assembly line are balanced. Although not handled in the SFAS 141 allocation, the fact that the seller has a skilled and assembled workforce also adds value.

In short, The VIU approach takes the perspective of the buyer. We look at the specific company and associated assets on an as – is, where – is basis. The purchase price for the overall business presumably was arrived at after due intelligence by the buyer, which understands what it is getting and what it is not getting, in terms of productive capacity.

The valuation methodology for VIU is straightforward. In theory, we identify all the assets, determining the costs today, including freight on, installation, testing and debugging. Then, based on physical inspection on the assets, the professional appraiser determines the age and actual condition of the subject assets and determines the depreciation from all causes. The assumption is that while the assets could be replaced with new like – kind equipment, the fact is that they will not be replaced. Instead, the old assets will be retained, but by using the older assets that are both physically worn and may be less than current technology, there is a cost penalty for existing assets in contrast to all – new complement. It is the appraiser’s duty to apply professional judgment as to the amount of depreciation from all cause that exists at the date of business combination. Note that the appraiser’s definition of depreciation is based on physical inspection and current technology, not on arbitrary accounting lives applied to original cost for purposes of financial reporting.

As a practical matter, appraisers usually do not determine the cost new of every asset, and separately determine the freight on, installation, testing and debugging. There are not enough appraisers in the world to do this. As a shortcut, appraisers will often take a client’s property record system. If the original cost of the asset is available, and the original date of acquisition, appraisers are able to apply either standard or proprietary indexes to that original cost. That provides the appraiser with a reasonable approximation of the cost today to acquire the same complement. Obviously, for major pieces of equipment, the appraiser has to test for indexing for accuracy by obtaining quotation from suppliers. The indexes are usually accurate, and appraisers find this approach providing a precise, ye cost effective answer.

VIE takes a different perspective. It asks one of two questions: (1) what would it cost if we *bought* these assets in the open market , either from a dealer in used equipment or at auction?, or (2) what could we *sell* assets for, as – is and where – is to a dealer or at an auction? The answers to these two questions are obviously different as discussed previously with the example of 2002 Corvette.

Before we can apply a VIE approach to meeting the needs of SFAS 141 – if that is the desired methodology – someone has to tell us whether the exchange is *buying from* or *selling to* the market. In the used equipment business, because of relatively low asset turnover, the difference between bid and ask price can go as high as 50%, while in our real example with Corvette, is approximately around 25%.

Historically, appraisers have not used a VIE approach very often in allocations of purchase price, but for financing, appraisers do use VIE. Why we use VIU for allocation of purchase price and VIE for financing? The two different premises represent two different types of transaction. The allocation represents the interest of the buyer in the business, which will use the assets for the purpose for which they were acquired. A bank, or other lending institution, does not want to run a business if the borrower is unable to meet the loan agreement. In the relatively rare cases when the lender takes over physical assets in settlement of a loan, the first thing that is done is to try to sell the assets, usually piece – meal, to a dealer or through an auction.

Thus the lender wants an appraisal that tells it what is the maximum amount that could be realized if the assets were to be sold separately, and not as a part of going concern, at this point the concern is not going, which is why the bank now owns the assets. If the old management could not make a go of the business, the chances of the bank or other lender doing so are usually remote. In short, the bank wants a worse – case scenario, which means selling the assets on a more or less distress basis.

It is easy to see now that the two premises of value in exchange and in use have their place. They are different in terms of the answer provided by an appraiser. They each are FV but to a different person for a different purpose. By and large, the VIE, even using the price from the dealer, is going to be lower than the developed from the VIU premise. The price of an asset new from a manufacturer always puts an upper limit on the used equipment price, but there is no lower limit. Particularly, when the economy is far from robust, auction prices and hence dealer prices are usually low. Auction prices are often determined in a bankruptcy or liquidation situation, where there is the pleasure on the seller. Dealers who buy at auction, and then resell to customers, have a pressure to turn their inventory as quickly as possible.

A second difference occurs in how to deal with inbound freight, installation and debugging. Present GAAP requires that these costs should be capitalized as the part of the cost of an asset. This appears reasonable, because without freight, installation and debugging, no assembly line, or other production process, could conceivably work. GAAP, in effect, defines *Cost* as including everything necessary to make the asset fit for the function for which it was acquired.

These cost, and they can easily approach to 10% or more of the vendor price, are going to be lost as and when the assets have to be sold to someone else. Obviously, a used equipment dealer will not pay for the original installation and freight because it now has to pay reinstall the asset and pay freight to get it to the warehouse.

These commonsense issues require an appraiser always to ask the client, “What is the purpose of this valuation?” The appraisers answer is going to depend on what he hears the client wants. So, contrary to cynical opinions, the fact that the appraiser provides useful answer to the client is not because he is selling answers, but because values do differ depending on the assumed transaction.

One word of caution to lenders: More than once, unscrupulous borrowers have given a lending institution an appraisal report that was requested for placement of insurance. Remember that insurance appraisal values are based on current replacement cost, not necessarily adjusted for physical and functional depreciation. Insurable values are usually at the highest end of the range of values for any asset, and values for collateral are at the lowest end of the range.

Put yourself in the place of an appraisal firm that gets a call from a very unhappy bank, stating that “Your appraisal reported dated six months ago shows that asset values are X. We just took over the assets and tried to sell them and the maximum we can get is 0,3X. We want you, the appraiser, to make up the difference because of your professional negligence.” This actually has happened, and appraiser merely points to the wording in the appraisal report that clearly specified the premise of value, insurance placement, and said nothing about the value of the assets in the used equipment market that the bank really had needed.

In effect, the borrower understood the valuation business much more clearly than did the banker, and took advantage of this lack of knowledge. The appraisal firm did its job, and the misuse of the final valuation report could not be traced back to the appraiser.

4. CAN FAIR VALUE BE AUDITED?

If the Public Company Accounting Oversight Board (PCAOB) truly believes that certain FV information, essentially that derived from management judgment or assertions about the future cannot be audited, this puts the FASB in a tight spot. In situation where there is an active market, with several market participants, appraisers can develop the information and auditors can verify the data.

The problem is that for many types of valuation, particularly intangibles, there is no active market with market participants. Just a simple example will suffice: Suppose that an appraiser is asked to value the TIDE® brand name, owned by P&G. As will be discussed later, the valuation of intangibles inherently requires projections about future sales price and volume, as well as future expenses. In turn, this obviously requires some assumptions about future consumer demand, competitive conditions and technology. Just imagine that some Japanese technology company invents an ultrasound washing machine. What is the impact on current models of washing machines and the demand for detergents? What if Colgate comes out with a new detergent that is really better than TIDE? What happens if a new style of grunge clothing takes hold and people wash their clothes less often? None of these scenarios is particularly likely, but the chances of any one of them happening are more than zero.

Getting back to the valuation of TIDE, the appraiser would talk to P&G management and obtain an understanding of their projections for volume and price. The appraiser would discuss the future demand, competitive conditions and technology, and arrive at the judgment as to whether P&G own projections are reliable enough to utilize in valuing the brand name.

The point is that appraisers make judgments every day, and in the final analysis most valuations are based on the appraiser's judgment. The PCAOB is correct: You cannot prove the judgment is correct. Similarly, you cannot prove a negative, but does not stop the people from leaving their umbrellas at home because they do not think it will rain today. You cannot prove it will rain, but most people are willing to go with the odds, knowing that once in a while it will be wrong and when it does rain they get wet. Meanwhile, they have not had the bother of carrying an umbrella for at least 30 days when it truly was needed.

Put another way, anyone who makes a judgment call risks being wrong, even though they are correct more often than not. Most judgment call made by an appraiser – in this case the future sales revenue and expenses of TIDE – are correct. The values so derived are accurate enough for most business decisions. That is why for example the United States spends more than 1 billion dollars on appraisals each year. It is cost effective.

But to try and prove that any one valuation is correct is impossible. A skeptical auditor can always pick holes in any appraisal report. There never has been, and never will be, a totally bulletproof valuation – unless someone who wants the value of 100 shares of for example Cisco stock and you can go to The Wall Street Journal and get the closing price yesterday. Even that does not absolutely guarantee that you could call Merrill Lynch next morning at 9:30 when the market opens and obtain that exact price to the penny.

When the PCAOB, or the FASB, states that they are uncomfortable with the judgments in developing FV, they are correct. They should be uncomfortable – except for the alternative. Complaints about difficulty of auditing management judgment, and appraiser's assumptions, have validity. However, one should not forget that today's financial reporting already has numerous assumptions, most of that based on management judgment. Somehow auditors are able to work around these imprecise values by looking at past experience and applying their own judgment.

The problem for an auditor today is that the PCAOB is coming in and auditing the auditors work. Thus, anytime a financial scandal occurs, it is easy to review the audit work papers. After the fact, if something did go wrong, it is easy for government auditor to question: "Why did you accept this value, this management assertion, this liability estimate?" Hindsight is easy, and auditors are trying to protect themselves more than ever, with the threat of a PCAOB review of each audit, there are going to be extraordinary efforts to verify values developed by appraisers. At the end of the day, this is impossible.

Ultimately, the choice is going to come down to auditors applying their judgment of the appraiser's judgment regarding management's assertions. Maybe it will be only one time out of a hundred, but all three will be wrong and the situation will have been set up for the financial press, the SEC and the PCAOB to demand reform of the system. One of the prices we pay for relevant and useful information is the chance that once in a while it will turn out not to have been reliable.

Relevance and reliability are the touchstones of the FASB, according to its own objectives of financial reporting. The fact is that tension sometimes exists between relevance and reliability. It is much easier for the business press to come up with the numerous examples of the unreliability of certain information than it is to complain about relevance of required GAAP disclosures, including FV.

In as much as this topic has no permanent answer, we will not discuss it further. The reader, however, should keep in mind that at some point, the FASB is either going to have to change its attitude toward company – specific information or back off its commitment to FV financial reporting. We predict that more than 100 years of appraisal and valuation experience – showing that company information is usually valid – will grudgingly be accepted by FASB, and that push for FV financial reporting will continue.

5. MARKET PARTICIPANTS

As noted earlier, the FASB holds strongly to the belief that the only valid value information is that derived from the market. They admit, indirectly that there may be different markets, with different prices. Appraisers, therefore, are supposed to select the appropriate market and derive transaction prices from the market.

This concept of the appropriate market, and market participants within the market, was illustrated previously with our example of a used car. An individual owner can sell his used vehicle privately through newspaper ads or to a dealer. These are two separate markets, with different prices and hence separate values to the owner. In one case, selling to the dealer, it is a quick transaction with a little effort, but at a lower price. Selling a used car to a private party utilizing newspaper ads is going to take longer, involve numerous inquiries from buyers who may not be interested, and acceptance of risks involved in test drives and bad checks. On balance, however, one will receive a higher price. The reason is that the individual buyer will pay for a similar car at a used car dealer. From the buyer's perspective, acquiring a car from private party involves risk as to possible mechanical defects. Buying from a dealer, while not guaranteeing a perfect car, at least has the advantage that the dealer could fix something that subsequently turns out to be defective.

One more piece of the puzzle has to be addressed. From the perspective of new – car dealer accepting used car in trade, there are two alternatives. The dealer can fix up the car, put it in inventory, and sell it at the price close to retail price. Alternatively, the dealer can decide to wholesale the car at a local auction, receiving less for the vehicle but not having to make repairs and cover the cost of keeping it in inventory until it is sold.

Essentially, what the FASB means by looking to market participants is first to identify the relevant market, and then do enough research to find out what such participants are actually paying for the subject asset. So far most readers would consider what was said about to be little more than common sense, although they might not have thought about these issues in these terms, it does not appear as though any difficult decisions have to be made.

Nonetheless, the question of just who is market participant is often in dispute. As an example, consider an auto parts supplier, for example an Original Equipment Manufacturer (OEM) whose customer base is the ten major automobile manufacturers such as Toyota and Ford. The customer relationship with the OEM has with the ten firms are clearly important. The ability to call on the appropriate buyers, the reputation for the delivery and price, and the quality of the parts produced are all issues that, when performed satisfactorily, lead to more business in the future.

In deciding whether to acquire such a company, the prospective buyer would perform significant due diligence on the targets reputation in the industry, its product line, its workforce, and its proprietary patents and technology. Each of these attributes is an intangible asset identified by the FASB and discussed in detail on the previous pages. For another purpose of this discussion, market participants, we must focus just on the customer relationships.

What is the real value of the target company's relationships with Toyota, Ford and the other major auto makers? To another auto parts company, the relationships may not be worth much. Why? Because that prospective buyer already calls on the same ten buyers. In fact there are only ten prospective customers in the world, and most of the major parts suppliers already sell to virtually all of them.

Thus, and this is the point, customer relationships that the target company has are really worth very little, if anything, to another auto parts company. However, consider a financial buyer, a private equity firm, for example. These groups raise large amounts of money to invest in individual companies. They hope to turn around the target and sell it someone else, or to have Initial Public Offering (IPO). To a financial buyer that is not already into the auto parts business, what is the value of relationships the target has with customers? Now the shoe is on the other foot. A financial buyer has no existing relationships, it must maintain the goodwill of the auto companies to this supplier or the buyout will be a failure.

Now comes the valuation dilemma. Are the customer relationships worth only a nominal amount to another supplier, or are they worth a lot to the financial buyer? As we have seen elsewhere from the perspective of an appraiser, either answer is correct depending on who the buyer is.

The concept of market participants is used in broadest sense. In practice, this means that the customer relationships have to be valued in relation to prospective buyers who are not already in the industry, even though for practical terms those may be the only realistic acquirers. Given the pressure the major auto companies are under, they are very reluctant to have a major supplier who is not already intimately familiar with the industry and its requirements. Thus, by far the most likely buyer for an auto parts company s another firm in the same industry, one to whom the target customer relationships may have little value.

Lest this seem like an esoteric or theoretical point, keep in mind that financial reporting consequences are far reaching. If one assigns a low or nominal value to the customer relationships in the purchase price allocation, the more of the total purchase price ends up in goodwill. Remember that goodwill does have not to be amortized, although it does have to be periodically tested for impairment. If a high value is assigned to customer relationships, then obviously less is assigned to the goodwill. The downside, however, is that those customer relationships usually have a relatively short life, and the amount assigned must be amortized over that short life. Consequently, evaluating the value of customer relationships in terms of a broad concept of market participants will likely cause a significant decline in subsequent reported earnings. Accounting, unlike the physical sciences, is not based on uniform relationships like the laws of gravity.

Accounting is manmade, so it is not possible to say than one or another of the alternatives to valuing customer relationships in terms of market participants is correct and the other alternative is wrong. Either is right and either can be considered wrong. The FASB and the SEC have chosen the alternative that tends to lower reported earnings.

6. SELECTING AN APPRAISER

A strong argument can be made that as with other professional services, experience is the best teacher. In fact, experience is essentially the only teacher because very few formal college programs exist on appraisals and valuation. Virtually all appraisers today learn directly on the job. Just as you would want to surgeon who had performed many gall bladder operations if you suffered a severe attack, so too you should want an appraiser or appraisal firm, that has had a lot of experience.

However, experience in the valuation business may not be the same as experience in valuating a specific type of an asset. The single most common question asked of any appraiser by a prospective new client is, “What other companies in our industry have you appraised?” The implication always is that unless you have great familiarity with a specific industry, you probably are not qualified, and that assumption may be based on experience with other professions.

Fortunately or unfortunately, this is not the case for business valuations. There are appraisers who specialize in real estate, or sport teams, or media, but any competent appraiser could readily perform an appraisal in any of these areas. The reason is straightforward: as we have seen, there are three and the only three approaches to valuing any asset. Once you understand the principles and application of these principles, all valuations fall under one or more of these approaches.

If a prospective client is selecting an appraiser, make sure the individual or firm has significant overall valuation experience. It is questionable whether for example ten years of experience is sufficient to have provided an appraiser with sufficient range of issues and industries that he can take on virtually any valuation assignment. With regard to fees, although appraisers may not like it, there is nothing wrong with a client insisting on obtaining a firm fee estimate. In the unlikely circumstances that unforeseen things occur, the appraiser will come back for an additional fee.

7. CONCLUSION

Management is ultimately responsible for the FV information disclosed in financial statements. Although there is nothing in GAAP or SEC instructions that require use of outside valuation specialists, most companies are choosing to delegate or to outsource this task. Under current Sarbanes – Oxley Act requirements, a company's own auditors cannot perform any valuation that they will be auditing, so companies choose valuation specialists either from independent appraisers and appraisal firms or from one of the other accounting firms.

The one thing that should be clear at this point is that there is no such thing as "the" value of any asset. Is the asset going to be used for its present function or will it be sold? The value in each case is different. Will the asset be sold or acquired in the retail market or wholesale market? The value in each case is different. Is the value being determined for insurance purposes or for loan collateral? The value in each case is different again.

The FASB has asserted that so-called market valuations are more reliable and have a higher standing in their hierarchy than values derived from cost or income approaches to valuation. We do not share this belief, and in the long run this unsubstantiated assertion is going to come back and haunt the FASB, but meanwhile they write the rules and we follow them.

Admittedly, it is difficult to audit professional judgment, and auditors are going to have to utilize their judgment in opining on FV information developed by others, either management or valuation specialists. We have asserted, and fully believe, that to appraisers given the same assignment will come within 10% of each other in their final value indications. This may or may not be close enough for auditors, the SEC, and the PCAOB. Nonetheless, given the judgment and assumptions inherent in any valuation, this appears reasonable, and furthermore, irrespective of one's desires, that is as close as will get.

It is our further belief that any competent appraiser, with a minimum of perhaps ten years' experience, is capable of performing most valuations for financial reporting. Irrespective of the industry or type of asset, the final definition of FV assumes what a willing buyer and a willing seller might transact a purchase and sale. Appraisers use specific techniques and methodologies in developing these assumptions about market participants. These range from verifying actual transactions for similar assets to involving discounting future cash flows and income. In a significant number of valuations for financial reporting, those involving allocation of purchase price, appraisers determine FV through physical inspection and developing the current replacement cost of the assets.

Consequently, all three approaches to value (cost method, market method and income method) and the two major premises of value (Value in Use and Value in Exchange) are utilized by appraisers. As long as financial managers understand what these are and can provide proper direction to the appraiser, the resulting values will surely suffice for financial reporting.

Only when the results of a valuation are going to directly affect cash flows of the parties (divorce or gift tax) will appraisal reports from either party likely differ. This is all about financial reporting, not about dispute settlement, so we wanted to alert readers as to why two appraisers can at times provide widely different answers. In those situations, the differences can be narrowed, if not eliminated, if the same assumptions about the future are used by both parties. Perhaps that is wishful thinking when dealing with an ex-spouse or the IFRS, but it does get to the heart of any questions about the answers or how the appraisers arrived at the answers.

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