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The Appraisal Practices Board
Working Group 3 –
The Measurement and Application of Market Participant Acquisition Premiums
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November 30, 2015

RE: Exposure Draft -- The Measurement and Application of Market Participant Acquisition Premiums

Dear Working Group Members,

The International Private Equity and Venture Capital Valuation Board (IPEV Board) appreciates and welcomes the opportunity to respond to the Board's Exposure Draft. We appreciate the fact that you considered our previous comments with respect to your Discussion Paper on this topic. There is great importance for the private equity investment community to be able to obtain and rely on consistently determined fair value estimates. Fair Value Measurement is a subject area where preparers, users, auditors and valuers face challenges in both estimating and understanding true measures of value.

The IPEV Board is in the process of updating the International Private Equity and Venture Capital Valuation Guidelines (IPEV Valuation Guidelines), launched in March 2005 and which were last revised in December 2012 (available at www.privateequityvaluation.com). We expect the current update to be completed by the end of 2015. The IPEV Valuation Guidelines provide the private equity industry with best practice in consistently estimating the fair value of investments compliant with IFRS and US GAAP. Valuation guidelines are used by the private equity and venture capital industry for valuing private investments and provide a framework for fund managers and investors to monitor the value of existing investments. The IPEV Valuation Guidelines have been endorsed by 42 private equity and venture capital associations around the world, including the Private Equity Growth Capital Council and the National Venture Capital Association in the United States.

As stated in our previous response, we believe that the private equity and venture capital industry would be best served if the APB's document were to cross reference the IPEV Valuation Guidelines for industry specific direction.

Based on our reading of the Exposure Draft, we provide additional targeted responses that we believe will be of assistance to prevent misunderstanding and misapplication.

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Our response to the Exposure Draft is specific with respect to the Portfolio Valuation section on pages 39 and 40. We seek to provide the APB and Working Group with practical input from the perspective of the global private equity industry. Our views should be considered from the perspective of industry best practice used in the private equity and venture capital, and not necessarily from the perspective of a technical independent valuation service provider with a broader audience. Because of the unique nature of the private equity and venture capital industry, in particular regularly valuing illiquid or infrequently traded assets, we can provide the Board and Working Group with our experience of the challenges inherent in exercising judgment to value such assets consistent with the principles espoused by both the IASB and FASB, in the alternative investment industry segment.

General Comments

We appreciate the Working Group's thoughtful approach to the topic of "control premiums." We believe you have substantially moved the discussion forward- when considering the valuation impact of "control."

We agree that a Market Participant Acquisition Premium (MPAP) as defined by the APB -is often paid upon acquiring an investee company. However, the acquisition MPAP would be included in the deemed acquisition fair value and inputs would be calibrated with valuation techniques to arrive at the estimate of fair value at subsequent measurement dates. A second MPAP would not and should not be added on top at subsequent measurement dates. We are very concerned that lines 968 through 978 could be misinterpreted or misunderstood in a way which would cause fair value estimates to include an additional Market Participant Acquisition Premium (MPAP) on top of the MPAP included in the purchase price and the acquisition determination of fair value. The on top MPAP would effectively double count a theoretical premium, and would deviate from the value derived using market participant assumptions as to what a market participant would pay at a given measurement date.

As we highlighted in our previous response to the APB and Working Group, for the private equity and venture capital industry, market participants do not think about fair value estimates or transaction prices in the context of premiums or discounts. They don't identify a price and then add a premium or deduct a discount. Further, while the price paid for an investment may mathematically be more or less than some other price (such as the exchange price prior to a buyout),that fact does not mean that valuation estimates, especially future valuation estimates for portfolio investments of Investment Companies, are arrived at using a premium or discount. In addition, for most PE/VC situations, the price paid by a "control" investor is the same as that paid by a "minority" investor. Artificially imposing or implying the need for an additional on top premium or discount when it does not exist in the real transaction world (the world of private equity and venture capital) would not provide a fair value estimate consistent with accounting standards.

We suggested the following wording changes for lines 968 to 978:

Consistent with the guidance in ASC 820, the Working Group believes that consideration of an MPAP ~~is~~ may not be appropriate when measuring the fair value of a controlling interest owned by an investment company on subsequent measurement dates when~~because (1) the application of an MPAP reflects the characteristics of the asset being measured (i.e., a controlling interest) and (2)~~ market participants acting in their "economic best interest" would ~~consider an MPAP~~invest at the same pro rata price at entry and would receive the same pro rata proceeds at exit. ~~when transacting for the asset.~~ The Working Group also believes~~that the existence of an MPAP is not inconsistent with guidance found in ASC. In addition~~, the price at which an investment company

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acquires ~~a~~ an ~~controlling~~ interest in a private company ~~often~~ should be calibrated with inputs and valuation techniques so that the initial fair value estimate and subsequent fair value estimates reflect market participant assumptions with respect to the exit price that various investors, both control and non-control, would receive. ~~implies a premium to the fair value of a minority interest in the subject entity under prior ownership.~~ Upon exiting the investment through a sale to other market participants, the investment company generally expects the price received to reflect ~~a comparable premium~~market participant assumptions and is generally allocated on a pro rata basis among all investors, based on their relative holdings.

Additional discussion regarding lines 968-999:

While we believe we understand the concepts you are articulating with respect to MPAPs, because the Private Equity and Venture Capital industry does not think about a transaction from the perspective of a premium or discount, we believe the way lines 968 and 978 were drafted will result in confusion as it is not consistent with the way such market participants arrive at value. The price paid may be more than the actively traded price, or the previous owners value. The excess price (MPAP) is not a seen as a control premium, especially in situations where investors are working in concert with one another and no individual investor has "control".

Further, lines 979 through 989 do not seem to acknowledge that when two investors purchase a company, one with control and one without control, generally they do not pay different pro rata prices. The MPAP described, on lines 988/9 while conceptually sound, is confusing to a private equity / venture capital reader because such investors don't think about premiums with respect to other nonaligned investors and because they don't think in terms of a discount to the controlling owner. Private equity investors do not price or think of transactions from the perspective of a control premium or a minority discount. They determine the price they are willing to pay based on facts, circumstances and return assumptions and then pay that price. Most agreements do not allow disproportionate returns. As such, while one investor may have "control," implicitly for private equity transactions there is no premium associated with control at acquisition because the "control" investor is aligned with the minority investor and returns are pari-passu.

We believe it is a positive addition to refer on lines 995-999 to the AICPA PE/VC Valuation Guide taskforce. We further believe readers of the document could be greatly helped by adding a reference to the IPEV Valuation Guidelines (www.privatequityvaluation.com) to assist in understanding Portfolio Valuation concepts from an industry perspective.

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We appreciate the opportunity to provide the Board with our feedback. We would be pleased to discuss any questions you may have with you. Please direct specific questions to David Larsen, 415-693-5330 or david.larsen@duffandphelps.com.

Very truly yours,

/s/ David L. Larsen

The International Private Equity and Venture Capital Valuation Board

David L. Larsen
Vice Chairman IPEV Board

The International Private Equity and Venture Capital Valuation Guidelines

The International Private Equity and Venture Capital Valuation Guidelines (IPEV Guidelines) were launched in March 2005 and were last revised in December 2012 and are in the process of being revised in 2015 to further reflect the need for greater comparability across the industry and for consistency with IFRS and US GAAP accounting principles. Valuation guidelines are used by the private equity and venture capital industry for valuing private equity investments and provide a framework for fund managers and investors to monitor the value of existing investments. The IPEV Guidelines are based on the overall principle of 'fair value' in order to be consistent with IFRS and US GAAP.

The International Private Equity and Venture Capital Valuation Board (IPEV Board) reports and is accountable to a general assembly composed of all the endorsing associations to manage the evolution of the guidelines going forward. The IPEV Guidelines have been endorsed globally by 42 national and regional trade associations, including the Private Equity Growth Capital Council and the National Venture Capital Association in the United States.

For more information: http://www.privateequityvaluation.com.

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