



October 26, 2005

Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk CT 06856-5116

Re: Proposed SFAS 141 Business Combinations Revision  
Technical Director File Reference No. 1204-001

To Whom It May Concern:

On behalf of the more than 18,000 members of the Appraisal Institute, we thank you for this opportunity to respond to your June 30, 2005, Exposure Draft, as referenced above.

The existence of an acquisition of an existing business to form a business combination involves many issues that may or may not be common to the notion of a "fair value" definition. As we have discussed before in our response to the proposed *Fair Value Measurements*, the appraisal profession distinguishes the term "market value" from a series of other types of value. For purposes of our response to the exposure draft (each taken from the Appraisal Institute's *The Dictionary of Real Estate Appraisal*, Fourth Edition, 2002), these include:

- a. **Value in Use** – The value a specific property has to a specific person or specific firm as opposed to the value to persons or the market in general.
- b. **Use Value** – 1. In economics, the attribution of value to goods and services based upon their usefulness to those who consume them. 2. In real estate appraisal, the value a specific property has for a specific use; may be the highest and best use of the property or some other use specified as a condition of the appraisal.
- c. **Investment Value** – The specific value of an investment to a particular investor or class of investors based on individual investment requirements; distinguished from market value, which is impersonal and detached.
- d. **Market Value** – The most probable price, as of a specified date, in cash, or in terms equivalent to cash, or in other precisely revealed terms, for which the specified property rights should sell after reasonable exposure in a competitive market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under undue duress. (Note: this is one

of several recognized definitions, but is perhaps the most widely used in real estate in the United States.)

We understand the Objective of FASB Statement No. 141 and are particularly interested in how it can seamlessly fit into a context of fair value accounting. Although we recognize that real property often plays a small role under this standard, we continue to believe there are important concepts from our body of knowledge that can inform the discussion. As background for our remarks, we offer the following preliminary comments, which will use terms and concepts that may be slightly different than those commonly used in accounting. They are offered for purposes of explanation and, we hope, a fresh perspective on issues embedded in FAS 141 as they are in the remainder of fair value accounting.

1. In real estate, distinction is made between price and value. Under Uniform Standards of Professional Appraisal Practice (USPAP) and generally accepted valuation principles (GAVP), “value” must be specifically identified and defined before any appraiser may proceed with an assignment, lest the assignment be potentially misleading.
2. The market creates value, but rarely if ever through a single transaction. It is the collective actions of market participants, faced with a wide spectrum of alternatives that combine to create market value for particular assets, or liabilities. Appraisal concepts of “Highest and Best Use” and the “Principle of Substitution” provide the basis for systematic problem-solving processes in which appraisers follow generally accepted procedures to sift through alternatives before arriving at the market value of a particular property.
3. These notions, concepts, and examples lead us to conclude that there are at least two central questions that must be answered under FAS 141 in accounting for purchase prices. First is the question of how to recognize, quantify, and account for the price in market terms. Second is how to distinguish between the fair values of the asset and liability components and any excess or deficit amount that may be derived with fair values are compared with a fair representation of the purchase price.
4. In FASB’s definitions, statements of standards, and explanations we note that a move away from “allocations” of some forms of value in favor of valuations of the assets and liabilities in question appears to be an integral part of the fair value standards. In appraising real estate, the real estate’s market value does not change with the owner as of a given value date. Land value does not change with arbitrary “allocations” of a purchase price to the improvements on the land, leaving a larger or lesser amount as a residual to “allocate” to land. When real estate is sold as part of an enterprise, as in a business combination, the real estate’s market value as of the date of value does not change with the details of the business combination, who the acquirer and acquiree may be, or other non-market considerations. The same is true for the valuation of other forms of fixed assets, as recognized under USPAP and the standards of the International Valuation Standards Committee.

We recognize that this is an overly simplistic view. It is offered, however, provide a baseline for concepts that we perceive to be buried in a mass of communications and standards that threaten to

overcome good intentions, incredibly excellent hard work by so many, and a goal that is crucial to the economic and social health of the world community, let alone the U.S.

We offer the following comments as our views on selected questions raised in your Proposed SFAS 141 Business Combinations Revision (FAS-141R):

**Question 4: Do paragraphs A8-A26 provide sufficient guidance for measuring the fair value of the acquiree? If not, what additional guidance is needed?**

Our primary concern relates to the equating of “exchange price” to the fair value of the acquiree. A8 states that “the objective of measuring the fair value of the acquiree is to estimate the price at which 100 percent of the acquiree could be exchanged in a current transaction between knowledgeable, unrelated, willing parties when neither party is acting under compulsion.”

When real estate transactions occur, they occur at a price. They may or may not occur at market or fair value. It is the collective behavior of markets, and the weighting of market evidence including, but not limited to, market transactions from which market value is derived. We realize that the language of “price” is consistent with the language in the proposed *Fair Value Measurements* standard; however, price may be influenced by many factors.

The market value definition above shows that appraisers must distinguish, for example, between a price for a property paid by cash or its equivalent, or a price that reflects some potential increase or decrease in the consideration that is attributable to financing rather than to the real estate. The specific use of an appraisal will dictate whether some departure from a cash or equivalent price is permitted, or even required. Under any circumstances, the appraiser is bound by standards to perform a valuation in accordance with standards and in a relevant and meaningful manner.

Additionally, it is clear that businesses may acquire all or part of the assets and/or liabilities of another business for a variety of reasons. The consideration may be paid in forms that should be subjected to the same rationales as those applied by a real estate appraiser. For example, if payments are not made in cash, then cash equivalents, present values, speculative risk, uncertain participations, and other possible factors must be quantified from a market perspective. We would therefore encourage you to consider adding the element of payment/consideration terms in your treatment of fair value in the same way that valuation professionals consider it a factor in translating price to an indication of market value.

**Question 7: Do you agree that the costs that the acquirer incurs in connection with a business combination are not assets and should be excluded from the measurement of the consideration transferred for the acquiree? If not, why?**

Our perspective here is fairly limited. For the purposes of real property valuation, while transaction costs must be considered as part of any business decision, they are not considered part of the value of the acquired asset. While your language in this draft seems to be generally consistent with the language proposed in the October 21, 2005, draft of the *Fair Value Measurements* standard—which indicates that “the price in the reference market for the asset or liability shall not be adjusted for transaction costs” —there appear to be other accounting standards (e.g. FAS 34 and other historical cost standards) that treat cost differently. It seems that one challenge will be to determine how best

to reconcile concepts that are defined and/or treated differently under fair value standards versus traditional GAAP accounting standards.

**Question 12: Do you believe that there are circumstances in which the amount of an overpayment could be measured reliably at the acquisition date? If so, in what circumstances?**

Valuation professionals can provide an opinion of value at the acquisition date that might suggest there has been an overpayment; however, that value opinion may be different from the perspective of the client. This relates to the distinction between investment value and fair (or market) value. There are certainly circumstances in which an acquirer is willing to pay above the odds in order to acquire a specific entity or asset for non-market reasons not shared by other potential buyers. For example, a purchaser might buy property to establish a monopoly, or to control land in a given location, paying a premium that exceeds the concepts inherent in the market value definition. In such cases, the consideration paid might be more than the fair value. Appraisers would normally discover the situation as a part of their market data investigations and verifications, making adjustments accordingly in their analysis.

**Question 18: Do you believe it is appropriate for the IASB and the FASB to retain those disclosure differences? If not, which of the differences should be eliminated, if any, and how should this be achieved?**

Conceptually, we believe that disclosure differences should be eliminated if possible and that the respective Boards should continue to work on this matter. We understand from our international colleagues that there are those that feel that a fundamental, global debate on measurement has not yet taken place and that such a discussion needs to happen before fundamental changes to existing measurement standards are made. Any broad discussion on this matter should actively include the International Valuation Standards Committee and other valuation standard-setters or organizations as appropriate.

**Public Roundtable Meeting**

The Appraisal Institute looks forward to sending its representative, James Moran, MAI, to the roundtable on October 27, 2005, in Norwalk, CT. Mr. Moran can be reached as follows:

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Regards,



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