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October 28, 2009

Exposure Draft: Fair Value Measurement
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

RE: Exposure Draft: Fair Value Measurement

Dear IASB Members:

The International Organization of Securities Commissions (IOSCO) Standing Committee No. 1 on Multinational Disclosure and Accounting (Standing Committee No. 1) thanks you for the opportunity to provide our comments regarding the International Accounting Standards Board (IASB or the Board) Exposure Draft, *Fair Value Measurement* (the Exposure Draft or the ED).

IOSCO is committed to promoting the integrity of international markets through promotion of high quality accounting standards, including rigorous application and enforcement. Members of Standing Committee No. 1 (SC1) seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein reflect a general consensus among the members of SC1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

We are supportive of the IASB's efforts to establish a single source of guidance for the use of fair value to achieve consistency and transparency in financial reporting. We also support the IASB and FASB's convergence efforts and are pleased that the Board used SFAS 157 as a starting point for developing this Exposure Draft. We understand that the Board plans to hold roundtable meetings on this Exposure Draft.

Definition of fair value and related guidance

Question #1: *The exposure draft proposes defining 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 date' (an exit price) (see paragraph 1 of the draft IFRS and paragraphs BC15-BC18 of the Basis for Conclusions). This definition is relevant only when fair value is used in IFRSs.*

Is this definition appropriate? Why or why not? If not, what would be a better definition and why?

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Yes, we generally believe the definition of fair value should incorporate an 'exit price' notion and this definition provides an appropriate and consistent definition of fair value. However, as noted in our response to Question #7, given the transfer restrictions associated with most liabilities we believe there may be limited circumstances in which fair value is the relevant measurement objective for a liability.

While current IFRS incorporate an exchange price notion, the definition and application has been deficient in a number of different areas including, among others, that current guidance does not indicate that the exchange should result from an orderly transaction and that such exchange price should be based on the price to sell the asset or transfer the liability rather than an entry price concept. We believe the proposed definition helps clarify these deficiencies.

We also understand that some of the recent debate in the U.S. over the role of fair value, particularly as it relates to the application of fair value during periods of market distress, has focused on whether the exit price notion in SFAS 157 resulted in a substantive change in the application and determination of fair value compared to an historical 'entry price' view. Some opponents of the current fair value guidance, such as SFAS 157, have suggested that an 'exit price' notion has exacerbated many of the problems witnessed in the capital markets over the course of the past 12-18 months. However, as noted in BC28, we understand that the Board has concluded that a current entry price and current exit price will be equal when they relate to the same asset or liability on the same date and in the same market. We understand that the Board also did not consider it important to make a distinction between a current entry price and current exit price and decided to define fair value as a current exit price. In light of this, we believe that in the Board's Basis for Conclusions for this standard and in its public communications about this project, the Board should emphasize that its decision to define fair value as a current exit price has a relatively limited impact on IFRSs and may ease some constituents concerns about use of a current exit price.

Scope

Question #2: *In three contexts, IFRSs use the term 'fair value' in a way that does not reflect the Board's intended measurement objective in those contexts:*

(a) In two of those contexts, the exposure draft proposes to replace the term 'fair value'; (the measurement of share-based payment transactions in IFRS 2 Share-based Payment and reacquired rights in IFRS 3 Business Combinations) (see paragraph BC29 of the Basis for Conclusions).

(b) The third context is the requirement in paragraph 49 of IAS 39 Financial Instruments: Recognition and Measurement that the fair value of a financial liability with a demand feature is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid (see paragraph 2 of the draft IFRS and paragraph BC29 of the Basis for Conclusions). The exposure draft proposes not to replace that use of the term 'fair value', but instead proposes to exclude that requirement from the scope of the IFRS.

Is the proposed approach to these three issues appropriate? Why or why not? Should the Board consider similar approaches in any other contexts? If so, in which context and why?

We agree with the Board's approach to identify IFRSs that use the term 'fair value' and determine whether the objective of that term used in each of the standards is consistent with the single framework established in the Exposure Draft. We understand that the Board has identified three areas (standards) where the proposed definition of fair value in the Exposure Draft differs from the objective in the particular standard. In these instances we agree with the Board's approach to replace the term used in each of the standards, where the measurement objective is different from the

definition of fair value in the Exposure Draft, with another term that reflects the intended measurement objective.

However, we disagree with the Board's approach with respect to the third context highlighted in the question and in BC29 related to the measurement of financial liabilities with a demand feature in which the Board proposes to retain use of the term 'fair value'. However, application of the prescribed methodology in IAS 39 for financial liabilities with a demand feature may result in a different measurement basis than the measurement basis that would be achieved by following the fair value framework in the ED but following the same 'fair value' terminology. The result will lead to confusion among preparers, auditors and investors and will be the only place in which fair value in other IFRS will not have the same meaning as in the ED. We believe that the Board should follow a similar approach as outlined in the first two contexts and replace the term used in IAS 39 for financial liabilities with a demand feature with a term that better fits the objective of that measurement.

The transaction

Question #3: *The exposure draft proposes that a fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place in the most advantageous market to which the entity has access (see paragraphs 8-12 of the draft IFRS and paragraphs BC37-BC41 of the Basis for Conclusions).*

Is this approach appropriate? Why or why not?

We agree that fair value should be determined based on a hypothetical transaction in an entity's most advantageous market to which the entity has access. We believe this is an improvement to SFAS 157 under US GAAP and is easier to understand because it simplifies the process that an entity will go through to identify the appropriate market which is founded on maximizing the transaction price.

Principal Market

While we support this approach, we are concerned with the introduction of a 'principal market' concept in paragraph 11 and we question what this discussion is trying to achieve. If an entity applies the guidance in paragraphs 7-10, why is there a need to also think about whether this market is the market with the greatest volume and level of activity for the asset or liability (which is defined as the principal market in paragraph 11)? In instances where the most advantageous market happens to differ from the market with the greatest volume and level of activity for the asset or liability, this could lead to confusion and inconsistent practice in determining which market to use.

Example: Company A is a widget manufacturer and has access to and sells Product X in two different markets at different prices (referred to as Market Y and Market Z). After considering transaction and transportation costs, Market Y generally yields a higher price than Market Z; however, Market Z has the greatest volume and level of activity for Product X.

The above example is similar to the example in IE19-IE21 except that this example introduces the concept of principal market included in paragraph 11. The principle identified in paragraph 8 would lead us to believe that Market Y would be considered the most advantageous market and the market used to price Product X. However, we believe paragraph 11 could lead some to believe that this determination should also consider which market would be considered the principal market.

We also believe the Board should clarify how paragraph 11 should be interpreted in situations where Market Y is an inactive market and Market Z is an active market. The last sentence in paragraph 11 indicates that an entity should apply the fair value hierarchy in measuring the fair value but does not

indicate whether the fair value hierarchy should also be considered in determining the appropriate market.

Can I have multiple markets for the same asset or liability?

The Exposure Draft explains that there may be situations where **businesses** within the same entity engage in different activities and enter into transactions in different markets. Under these circumstances, we are not sure whether paragraph 9 is suggesting that a single entity could identify more than one 'most advantageous market' or whether paragraph 9 is simply stating that the most advantageous market could be different for different entities that engage in different activities. We are not sure how common this is and the types of assets that the Board contemplated in reaching this conclusion. For instance, if this were applicable to financial assets, we would be troubled by an application that would identify different 'most advantageous markets' for the same asset.

We believe the Board should clarify its intent in the final standard, provide a discussion in the basis for conclusions for its rationale and an example illustrating the intent and application.

Market participants

Question #4: *The exposure draft proposes that an entity should determine fair value using the assumptions that market participants would use in pricing the asset or liability (see paragraphs 13 and 14 of the draft IFRS and paragraphs BC42-BC45 of the Basis for Conclusions).*

Is the description of market participants adequately described in the context of the definition? Why or why not?

We believe the description of market participants is adequately described in the Exposure Draft. Specifically, we believe that this definition effectively results in a more defined point estimate rather than incorporating additional uncertainty in the valuation concerning the knowledge of market participants that could result in a much wider range of values.

Application to assets: highest and best use and valuation premise

Question #5: *The exposure draft proposes that:*

(a) the fair value of an asset should consider a market participant's ability to generate economic benefit by using the asset or by selling it to another market participant who will use the asset in its highest and best use (see paragraphs 17-19 of the draft IFRS and paragraph BC60 of the Basis for Conclusions).

(b) the highest and best use of an asset establishes the valuation premise, which may be either 'in use' or 'in exchange' (see paragraphs 22 and 23 of the draft IFRS and paragraphs BC56 and BC57 of the Basis for Conclusions).

(c) the notions of highest and best use and valuation premise are not used for financial assets and are not relevant for liabilities (see paragraph 23 of the draft IFRS and paragraphs BC51 and BC52 of the Basis for Conclusions).

Are these proposals appropriate? Why or why not?

We agree that the fair value of an asset should be considered from the perspective of a market participant who will use the asset in its highest and best use in order to maximize the value for the asset or the group of assets within which the asset would be used. As described in paragraphs 22-24, the highest and best use should be considered from the perspective of a market participant and

differentiated between the value 'in use' with other assets (complementary assets) or 'in exchange' in which the highest and best use of the asset would provide maximum value on a standalone basis.

General

While we agree with many of the concepts in the Exposure Draft regarding the most advantageous market, market participant assumptions, highest and best use and valuation premise, we believe these concepts are interdependent and result from a more iterative process to determine the fair value rather than viewed as a step by step process that an entity would need to go through to determine the fair value. In the final standard, it would be helpful if the Board clarified when introducing these concepts that they should not be viewed in isolation when developing a fair value measurement.

Application of in-use valuation premise

Paragraph 22(a) of the Exposure Draft specifies that assumptions for highest and best use "shall be consistent for all of the assets of the group within which it would be used". The Exposure Draft also states in paragraph 23 that:

Both the in-use valuation premise and the in-exchange valuation premise assume that the asset is sold individually, ie not as part of a group of assets or a business. However, the in-use valuation premise assumes that market participants will use the asset in combination with other assets or liabilities, and that those assets and liabilities are available to those market participants.

We agree with the Board's approach and follow the distinction that the valuation should be based on the unit of account identified in other IFRS and to the extent that an individual asset provides maximum value in combination with other assets, then an in-use valuation premise should be used. We also understand that the application of this concept does not change the objective of measuring the individual asset. Paragraph BC59 discusses whether it would be appropriate to determine the fair value for the entire asset group, if the highest and best use were considered to be "in-use", and then use an allocation methodology to the individual asset. The Board reiterated that fair value should not be determined based on an allocation of fair value for the entire asset group.

Given that the assumptions for highest and best use need to be consistent for all assets within the "in-use" asset group, we do not understand the Board's rationale for precluding an allocation methodology and whether, in most circumstances, the direct measurement would differ from an allocation of fair value. In addition, Example 1 (paragraphs IE2-IE4) in the Illustrative Examples, indicates that it might be appropriate to follow an allocation methodology to determine the fair value of Assets A, B and C on the basis of the use of the assets as a group within the strategic buyer group. Also, paragraph B2(e) indicates that there may be situations where an entity may measure the asset at an amount that approximates its fair value in use when **allocating** the fair value of the asset group to the individual assets of the group.

Valuation premise for financial assets

The Exposure Draft precludes the use of an 'in-use' valuation premise for financial assets. This provision may result in divergence from US GAAP in situations where the highest and best use of the asset is used in combination with other assets. SFAS 157 does not provide restrictions on the valuation premise for financial assets and we understand there may be instances where the highest and best use is used in combination with complementary assets such as under master netting agreements and insurance / reinsurance contracts which might derive more value if sold in combination rather than on a standalone basis. We also question whether there could be circumstances in which the fair value of a standalone financial asset based on an in-exchange premise reflects a lower price due to the fact that the market for that financial asset is no longer active and perhaps market participants would assign higher value to that asset if combined with other financial assets.

This determination is also dependent on the unit of account / valuation and there may be more instances where an in-use valuation premise might derive more value. We recommend that the Board

revisit this provision and seek input from constituents to understand the implications of this decision prior to issuance of the final standard.

Question #6: *When an entity uses an asset together with other assets in a way that differs from the highest and best use of the asset, the exposure draft proposes that the entity should separate the fair value of the asset group into two components: (a) the value of the assets assuming their current use and (b) the amount by which that value differs from the fair value of the assets (ie their incremental value). The entity should recognize the incremental value together with the asset to which it relates (See paragraphs 20 and 21 of the draft IFRS and paragraphs BC54 and BC55 of the Basis for Conclusions).*

Is the proposed guidance sufficient and appropriate? If not, why?

The Exposure Draft identifies that there may be situations where an asset might not be used by the entity in a way that captures its highest and best use. The Exposure Draft then proposes certain disclosure requirements so that users can understand the components of the valuation related to both the (1) value of the assets assuming their current use and (2) the incremental value of the asset group assuming the asset groups' highest and best use.

While we agree with the ED's approach, we believe this is a practical solution rather than a conceptually pure answer. That is, the examples used to illustrate the application of this practical solution in paragraphs 20-21 and Example 2 of the Illustrative Examples, is a residual allocation to the land which is comprised of the excess of the fair value of the land (assuming its highest and best use) over the value of the factory based on the factory's current use.

We also believe this methodology may conflict with the following concepts elsewhere in the Exposure Draft:

Highest and Best Use: As noted in our response to Question #5, paragraph 22(a) states that assumptions about the highest and best use of the asset shall be consistent for all the assets of the group within which it would be used. In the examples referred to above, the highest and best use of the factory is its use in combination with the land and therefore an in-use valuation premise. The allocation methodology described in paragraph 20(a) follows this logic and results in the valuation of a factory based on its highest and best use under an in-use valuation premise. However, as noted in the example, the highest and best use of the land does not follow an in-use valuation premise; it follows an in-exchange valuation premise. Therefore, the assumptions about the highest and best use of the asset are not consistent for all assets of the group.

Measuring the individual asset: As noted in our response to Question #5, paragraph BC59 indicates that fair value should not be determined based on an allocation of fair value for an asset group. Although the valuation of land referred to in the examples above follows an in-exchange valuation premise, the actual recorded fair value of the land results from an allocated value which could be perceived as conflicting with the 'individual asset' concept discussed elsewhere in the ED.

Transformation costs

Example 2 in the list of Illustrative Examples adequately explains that when determining the highest and best use one needs to consider the costs of transforming the asset from its current use to determine whether the highest and best use is, in fact, something other than its current use. We believe the Board should emphasize this in the standard itself rather than just the illustrative example.

Application to liabilities: general principles

Question #7: *The exposure draft proposes that:*

(a) a fair value measurement assumes that the liability is transferred to a market participant at the measurement date (see paragraph 25 of the draft IFRS and paragraphs BC67 and BC68 of the Basis for Conclusions).

(b) if there is an active market for transactions between parties who hold a financial instrument as an asset, the observed price in that market represents the fair value of the issuer's liability. An entity adjusts the observed price for the asset for features that are present in the asset but not present in the liability or vice versa (see paragraph 27 of the draft IFRS and paragraph BC72 of the Basis for Conclusions).

(c) if there is no corresponding asset for the liability (eg for a decommissioning liability assumed in business combination), an entity estimates the price that market participants would demand to assume the liability using present value techniques or other valuation techniques. One of the main inputs to those techniques is an estimate of the cash flows that the entity would incur in fulfilling the obligation, adjusted for any differences between those cash flows and the cash flows that other market participants would incur (see paragraph 28 of the draft IFRS).

Are these proposals appropriate? Why or why not? Are you aware of any circumstances in which the fair value of a liability held by one party is not represented by the fair value of the financial instrument held as an asset by another party?

We generally believe the proposals are appropriate. The transfer notion reflects the extinguishment of the liability for the debtor but not a settlement of the amount owed to a creditor, resulting in an exit value. As pointed out in paragraph BC71 in the Exposure Draft, we understand that most liabilities contain legal restrictions on the ability to transfer those liabilities. In such instances, the Board has proposed a model which measures a liability based on the same methodology that the counterparty would use to measure the corresponding asset, which seems to result in an entry price rather than an exit price. We question the usefulness of this measurement objective for many financial and non-financial liabilities and whether a settlement or fulfillment notion would result in better decision-useful information to investors, particularly when the financial or non-financial liability contains transfer restrictions. As such, we believe there may be limited circumstances in which fair value is the relevant measurement objective for a liability.

Notwithstanding our comments above, we understand that the Board is providing additional guidance in paragraph 26 for instances in which there is no observable market price for the transfer of a liability. The Board goes on to state that an entity should measure the fair value of the liability based on the same methodology that the **counterparty** uses to measure the asset. This implies that an entity would need to identify each counterparty and understand the methodology employed to value the asset. We believe the standard could be improved by specifying that an entity evaluate the methodology that a **market participant** might use to value the corresponding asset rather than focusing on a specific counterparty.

The Board indicates in paragraph BC110(g) that the FASB, at the time this Exposure Draft was issued, was developing a staff position to clarify the measurement of liabilities at fair value in accordance with SFAS 157. The Board notes that if finalized, the proposal in the FASB staff position is expected to be largely consistent with the proposals in this Exposure Draft.

The FASB has finalized its project on providing additional guidance for measuring the fair value of liabilities through the issuance of an Accounting Standards Update (ASU). The ASU clarifies that in circumstances in which a quoted price in an active market for the identical liability is not available, a

reporting entity measures fair value using one or more of the techniques described in the ASU. The techniques described include:

- The quoted price of the identical liability when traded as an asset;
- The quoted prices for similar liabilities or similar liabilities when traded as assets; and
- Another valuation technique that is consistent with the principles of SFAS 157 (such as a present value technique).

The approach in the Exposure Draft is consistent with the first and third bullet point above but does not address whether it would be appropriate to also consider a quoted price for similar liabilities or similar liabilities when traded as assets. We believe this additional guidance would also be useful and encourage the Board to incorporate this in the final standard. We also believe the Board should provide guidance as to whether it believes that a quoted price of an identical liability when traded as an asset represents a Level 1 or Level 2 measurement.

Application to liabilities: non-performance risk and restrictions

Question #8: *The exposure draft proposes that:*

(a) the fair value of a liability reflects non-performance risk, ie risk that an entity will not fulfill the obligation (see paragraphs 29 and 30 of the draft IFRS and paragraphs BC73 and BC74 of the Basis for Conclusions).

(b) the fair value of a liability is not affected by a restriction on an entity's ability to transfer the liability (see paragraph 31 of the draft IFRS and paragraph BC75 of the Basis for Conclusions).

Are these proposals appropriate? Why or why not?

As noted in our comment letter on the Credit Risk in Liability Measurement Discussion Paper (Discussion Paper), we believe that initial measurement of a liability should incorporate credit risk if credit risk is present in pricing of the exchange for the liability. We are not certain how credit risk is priced into the exchange involving a non-financial liability since non-financial liabilities may not contain the same pricing characteristics as financial liabilities. We also can appreciate it is more difficult to determine the appropriate role of credit risk in subsequent measurement of a liability. We encourage the Board to consider and evaluate the feedback it receives on the Discussion Paper before issuing a final standard.

Fair value at initial recognition

Question #9: *The exposure draft lists four cases in which the fair value of an asset or liability at initial recognition might differ from the transaction price. An entity would recognize any resulting gain or loss unless the relevant IFRS for the asset or liability requires otherwise. For example, as already required by IAS 39, on initial recognition of a financial instrument, an entity would recognize the difference between the transaction price and the fair value as a gain or loss only if that fair value is evidenced by observable market prices or, when using a valuation technique, solely by observable market data (see paragraphs 36 and 37 of the draft IFRS, paragraphs D27 and D32 of Appendix D and paragraphs BC76-BC79 of the Basis for Conclusions).*

Is this proposal appropriate? In which situation(s) would it not be appropriate and why?

We believe the proposal is appropriate. The Board also states in BC79:

Although the Board did not change the recognition threshold, it proposes to amend IAS 39 to clarify that the fair value of financial instruments at initial recognition should be measured in accordance with the proposals in the exposure draft and that any deferred amounts arising from the application of paragraph AG76 are separate from the fair value measurement.

In its amendment to IAS 39, we believe the Board should explicitly reaffirm or amend its previous conclusion on the deferral of gains and losses where the fair value is not evidenced by observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets.

Valuation techniques

Question #10: *The exposure draft proposes guidance on valuation techniques, including specific guidance on markets that are no longer active (see paragraphs 38-55 of the draft IFRS, paragraphs B5-B18 of Appendix B, paragraphs BC80-BC97 of the Basis for Conclusions and paragraphs IE10-IE21 and IE28-IE38 of the draft illustrative examples).*

Is this proposed guidance appropriate and sufficient? Why or why not?

We agree that the proposals are appropriate and provide sufficient guidance. We believe the determination of whether markets are no longer active and transactions that are not orderly require significant judgment. The Board highlights in paragraph B7 that the Exposure Draft does not prescribe a methodology for making significant adjustments to transactions or quoted prices. The guidance further indicates that such adjustments should reflect appropriate risk adjustments including risk premium reflective of an orderly transaction between market participants at the measurement date under current market conditions.

We understand that there may be confusion as to how the risk premium should be considered. We believe the Board should emphasize and clarify the last sentence in paragraph B7 to describe how the risk premium should be determined consistent with the objective and that current market conditions should not be ignored during such determination.

Disclosures

Question #11: *The exposure draft proposes disclosure requirements to enable users of financial statements to assess the methods and inputs used to develop fair value measurements and, for fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period (see paragraphs 56-61 of the draft IFRS and paragraphs BC98-BC106 of the Basis for Conclusions).*

Are these proposals appropriate? Why or why not?

We agree with the proposals provided in the Exposure Draft.

Convergence with US GAAP

Question #12: *The exposure draft differs from Statement of Financial Accounting Standards No. 157 Fair Value Measurements (SFAS 157) in some respects (see paragraph BC110 of the Basis for Conclusions). The Board believes that these differences result in improvements over SFAS 157.*

Do you agree that the approach that the exposure draft proposes for those issues is more appropriate than the approach in SFAS 157? Why or why not? Are there other differences that have not been identified and could result in significant differences in practice?

In addition to the differences discussed elsewhere in this letter, paragraph BC110(d) highlights a significant difference between the Exposure Draft and SFAS 157 with respect to blockage factors. Although IAS 39 may specify the unit of account for all financial instruments as the individual instrument, the Board hasn't provided its rationale for why it believes it is appropriate to value all financial instruments on an individual basis rather than a portfolio basis, especially where an entity actually transacts on a portfolio basis.

We believe the Board should consider this further and provide its rationale in making the determination as to whether blockage factors should be considered in and outside of Level 1 and whether the same logic should apply to both financial and non-financial assets.

Other comments

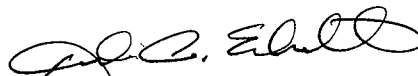
Question #13: *Do you have any other comments on the proposals in the exposure draft?*

Impairment disclosures for investments in associates

We support the disclosure of the methods and key assumptions used in determining fair values as this ensures transparency and accountability. Users of financial reports can use this information to understand how the methods and assumptions compare over time and with other entities. For similar reasons, this information should also be disclosed for impairment calculations, for both value in use and fair value less costs to sell. IAS 28 *Investments in Associates* requires impairment testing to be performed for investments in associates in accordance with the relevant requirements of IAS 39 and IAS 36 but contains no disclosure requirements. The Board should consider amending IAS 28 to require disclosures of methods and key assumptions relating to impairment consistent with other standards as a part of its annual improvements project.

We appreciate your thoughtful consideration of the comments raised in this letter. If you have any questions or need additional information on the recommendations and comments that we have provided, please do not hesitate to contact me at 202-551-5300.

Sincerely,



Julie A. Erhardt
Chairman

IOSCO Standing Committee No. 1