Accounting Standards Board
Aldwych House, 71-91 Aldwych, London WC2B 4HN
Telephone: 020 7492 2427 Fax: 020 7492 2399
www.frc.org.uk/asb

Stig Enevoldsen
Chairman
European Financial Reporting Advisory Group
Avenue des Arts 13-14
1210 Brussels
Belgium

19 April 2007

E-mail: commentletter@efrag.org

Dear Stig

IASB Discussion Paper 'Fair Value Measurement'

This letter sets out the ASB's comments on the draft EFRAG comment letter on the above IASB Discussion Paper. We are still finalising the ASB's response to the IASB and will forward you a copy when it is ready.

Overall, we agree with the EFRAG draft response, which sets out essentially the same concerns as the ASB response.

I note that, in a number of places in Appendix 2 to the draft letter (the proposed answers to Questions 6,10 and 12), EFRAG is specifically seeking comments from respondents. I attach the answers to those questions as set out in the proposed ASB response to the IASB, which I hope will provide some useful input to EFRAG in finalising the comment letter.

Yours sincerely

Ian Mackintosh

Ian Mackintosh
Chairman, Accounting Standards Board
DDL: 020 7492 2434

Extracts from proposed ASB response to the IASB

Q6. Does the exit price measurement objective in SFAS 157 differ from fair value measurements in IFRSs as applied in practice? If so, which fair value measurements in IFRSs differ from the measurement objective in SFAS 157? In those circumstances, is the measurement objective as applied in practice an entry price? If not, what is the measurement objective applied in practice? Please provide a basis for your views.

Some of the older IFRS standards that incorporate fair values were written up to ten years ago. Applying a new definition of fair value retrospectively on these standards may alter the original meaning. We therefore welcome the fact that the IASB will perform a standard-by-standard review of fair value measurements required by IFRS to measure consistency with any exposure draft proposals.

As mentioned in our covering letter we do not believe that, currently, fair value used in IFRS is the same as that mentioned in SFAS 157. As a start the notion of fair value in IFRS, with a number of exceptions, is based on entry and settlement prices not exit prices. Furthermore, entity specific prices are widely used because of a lack of liquid markets (these entity specific prices are not reliant on hypothetical markets and market participants in order to arrive at the price as required under level 3 of SFAS 157). There are a number of examples of such use in the current IFRS literature. We include a few such examples below, however, this is not meant to be an exhaustive list.

The requirements for recognition of finance leases at fair value in IAS 17 *Leases*, is for it to be based on the price paid by “knowledgeable, willing parties in an arm’s length transaction” not “market participants” as required in SFAS 157. This seems as likely to point to an entry value as much as an exit value. IAS 17 goes on to prescribe that the alternative measurement methodology for such leases is the present value of the minimum lease payments where the discount rate is required to be the interest rate implicit in the lease. Therefore, the present value of the lease payments will be transaction specific and not what a hypothetical market participant would pay for the lease.

IAS 19 *Employee Benefits*, when requiring the fair value measurement of the plan assets, specifies that in the absence of a market the fair value of plan assets is estimated by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets. Again, no reference is made to market participants.

IAS 38 *Intangible Assets* when discussing the measurement of fair values of an intangible asset acquired in a business combination notes that the most reliable estimate of fair value is the quoted market price which is "usually the current bid price". When considering revaluation of intangible assets the standard goes on to note that contracts for intangible assets are "negotiated between individual buyers and sellers, and transactions are relatively infrequent. For these reasons, the price paid for one asset may not provide sufficient evidence of the fair value of another." In fact, the standard allows an intangible asset to be carried at cost less amortisation and impairment losses if no active market for the asset exists. The exit price model of fair value in SFAS 157 appears to consider the price paid for another asset as being the fair value (as being the Level 2 measurement) and would not consider any other alternatives.

Q10. Does the transfer measurement objective for liabilities in SFAS 157 differ from fair value measurements required by IFRSs as applied in practice? If so, in practice which fair value measurements under IFRSs differ from the transfer measurement objective in SFAS 157 and how do they differ?

Yes. Under IFRS very few liabilities are currently required to be measured at fair value. The main exceptions relate to financial liabilities. On initial recognition the fair value for these is normally considered to be the transaction price (IAS 39 paragraph AG64). On later remeasurement for liabilities where no liquid markets exist and therefore valuation techniques are used, the fair value is based on the cash flows required to settle the liability. Therefore, in these circumstances there is a difference between the measurement objective in SFAS 157 and the fair value measurement practice under IFRS.

Q12. Do you believe that the provisions of SFAS 157, considered in conjunction with the unit of account guidance in IAS 39, would result in a portfolio based valuation of identifiable risks of instruments considered in aggregate, or an in-exchange exit price for the individual instruments? Please give reasons for your views.

We question whether the application of IAS 39 can be interpreted as to result in a valuation based on the risks of a portfolio considered in aggregate, for two reasons:

(1) paragraph AG72 of IAS 39 simply permits the use of mid-market prices as the basis for determining fair value of risks that are offset within the group of assets and liabilities; it does not describe the process of valuation in terms of treating the offsetting risks as a single unit of account;

2) applying this approach under the terms of paragraph 6 of SFAS 157 would require both the disaggregation of the risks inherent in individual financial assets or financial liabilities, and then aggregation of similar (but offsetting) risks across instruments. We think this is a more complex disaggregation and re-aggregation process than seems to be envisaged in the wording of paragraph 6.

We would suggest that the IASB clarifies its intentions in this area by means of amendment to IAS 39.