ASC
ACCOUNTING STANDARDS COUNCIL

10 Sep 2010

International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
United Kingdom

(By online submission)

Dear Sir

RESPONSE TO ED/2010/7 - MEASUREMENT UNCERTAINTY ANALYSIS DISCLOSURE FOR FAIR VALUE MEASUREMENTS

The Accounting Standards Council (ASC) appreciates the opportunity to comment on the Exposure Draft on Measurement Uncertainty Analysis Disclosure for Fair Value Measurements issued by the International Accounting Standards Board (IASB) in June 2010.

General

Whilst the disclosure of the effect of correlation between significant unobservable inputs could, to the extent that it is relevant and a key driver in fair value measurement, provide useful and meaningful information to users of financial instruments, due consideration should be given to the practical challenges that reporting entities are likely to encounter in complying with this new requirement.

We strongly recommend that the IASB consider all aspects of the proposals carefully to arrive at a standard that best balances cost and benefit. Our comments and suggestions are provided in the responses to the ED proposals below.

Question 1
Are there circumstances in which taking into account the effect of the correlation between unobservable inputs: (a) would not be operational (e.g. for cost-benefit reasons); or (b) would not be appropriate? If so, please describe those circumstances.

(a) We believe that it would be an operational challenge to, in the first instance, ascertain the degree to which unobservable inputs are correlated. While a reporting entity may be able to perform high-level estimates for risk-profiling purposes, building a capacity to quantify the effect of correlation among what could be multiple unobservable inputs would involve the development of complicated valuation techniques by a team of quantitative analysts. For added perspective, we note that, at present, most of the valuation models employed in the market place are single-variant models (i.e. valuations are obtained by changing a single input while holding the remaining constant). Multi-variant models that consist of correlated variables are not common.

This problem is particularly pronounced for certain instruments. For instance, the valuation methodology used to estimate the fair value of a privately-held entity generally incorporates many unobservable inputs (e.g. projected cash flows, growth rates, discount rates, terminal values) that could have a significant effect on the valuation of the entity. Determining the extent to which (a) these inputs could be correlated with each other and (b) the effect of correlated inputs upon fair value would be extremely complex and time consuming. In this regard, we note that the FASB has already, in BC68 of the FASB ED (Topic 820 *Fair Value Measurement and Disclosures*), tentatively concluded that it is not operationally feasible to undertake such an exercise for investments in unquoted equity instruments in view of the complexity involved, the lack of in-house resources to perform the disclosure as well as the value investors of such entities place on the sensitivity disclosures.

Supporting a valuation framework of with this level of complexity as well as the ongoing disclosure requirements will involve significant investments in infrastructure of a magnitude which we would expect to be at least the same as that required to develop the original Level 3 fair value measurement itself. Although BC20 of the ED states that "…an entity should not be required to disclose quantitative information about the degree of correlation between unobservable inputs (e.g. it is not necessary to perform a statistical analysis such as a regression analysis using two independent variables to determine the r-squared)…", we believe that the use of statistical analysis and valuation models to determine the impact of a different combination of unobservable inputs on fair value would be unavoidable. As such, obviating the disclosure requirement does not, in our opinion, do away with the need to use complex valuation techniques and relevant supporting systems to decide whether unobservable inputs are meaningfully correlated in the first place.

(b) Circumstances under which the proposal would not be appropriate would be where fair value is being determined for non-financial or intangible assets e.g. goodwill, fixed assets. For example, in the case of investment properties, valuations are usually performed by independent professional valuers who would judgementally determine a point estimate within a range of fair values estimated from a range of valuation techniques (e.g. direct comparison method, discounted cash flow method, capitalization approach), each of which could have multiple inputs. Having to consider the effect of correlation between unobservable inputs in such situations would undoubtedly increase the complexity and subjectivity of the valuation process, and the output is unlikely to be decision-useful.

Accordingly, the disclosure requirements, if the Board decides to go ahead with the proposal, should <u>exclude non-financial assets and liabilities</u>. The exclusion of non-financial items would also be more consistent with the current IFRS 7 requirements, where market sensitivity disclosures covers financial assets and liabilities only, and can help to ease undue reporting burden.

Question 2

If the effect of correlation between unobservable inputs were not required, would the measurement uncertainty analysis provide meaningful information? Why or why not?

We believe that the current requirement as outlined in para 27B (e) of IFRS 7 remains adequate. However, if the Board believes that the measurement uncertainty analysis would add further disclosure value, we would suggest a slight variation to the disclosure template as attached at the end of the comment letter.

Question 3

Are there alternative disclosures that you believe might provide users of financial statements with information about the measurement uncertainty inherent in fair value measurements categorised within Level 3 of the fair value hierarchy that the Board should consider instead? If so, please provide a description of those disclosures and the reasons why you think that information would be more useful and more cost-beneficial.

One possible option is for reporting entities to provide management estimates of the lower and upper bounds representing a specified (e.g. 95%) confidence interval of possible values around the reported fair value. Entities could disclose all necessary assumptions, including correlations where relevant. Users of the financial statements can assess the adequacy of these assumptions and perform necessary adjustments that it may not be pragmatic of operationally feasible for the entity to undertake.

Other comments

Notwithstanding our proposal to retain the current disclosure requirements under IFRS 7 and not require additional measurement uncertainty analysis as proposed in the ED, should the Board decide to proceed with the ED, we suggest that the title of the standard be amended to "*Disclosure of Uncertainty in Fair Value Measurement*" for simplicity and greater understandability. Also, the word "significant" in paragraph 1(b) of the ED would be more appropriately referenced to with regard to the impact on fair value measurement, rather than to unobservable inputs, as it is possible that insignificant inputs in terms of materiality (i.e. with respect to profit or loss and total assets, total liabilities or with respect to total equity) could have a significant impact on fair value measurement. As such, paragraph 1(b) could be amended as follows – "for < *significant* > fair value measurements using ~~*significant*~~ unobservable inputs (Level 3), the effect…"

Conclusion

In summary, based on a cost/benefit analysis, we recommend that the Board retain the current disclosure requirements under IFRS 7 and not require correlations to be taken into account in the measurement uncertainty analysis as proposed in the ED, as we believe that the current requirements under IFRS 7 is already sufficient in terms of fair value measurement disclosures. We hope that our comments will contribute to the IASB's deliberation on this exposure draft. Should you require any further clarification, please contact Ms Kate Ho (kate_ho@acra.gov.sg).

Yours faithfully

Dexter Tan (Mr)
Secretary, Accounting Standards Council

		Difference in FV from using different unobservable inputs that could have reasonably been used				
		FV changes to P/L		FV changes to OCI		
	Fair value at 31/12/X9	Increase in FV	Decrease in FV	Increase in FV	Decrease in FV	Significant unobservable inputs
Debt securities:						
Resident mortgage-backed securities	xx	xx	xx			
Etc						
Unquoted equity investments:						
Other equity investments	xx			xx	xx	
Etc						
Total	xx	xx	xx	xx	xx	