28 August 2009

Mr Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West VIC 8007

Via email: standard@aasb.gov.au

Dear Mr Stevenson

Comments on Exposure Draft 181 Fair Value Measurement

Thank you for the opportunity to comment on the AASB Exposure Draft 181 Fair Value Measurement. CPA Australia, The Institute of Chartered Accountants in Australia (the Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have considered the above exposure draft and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government, academia throughout Australia and internationally.

Our response to matters on which specific Australian comment is requested is included in the attached Appendix. Also attached for your consideration is our submission to the IASB which includes our responses to the specific IASB questions for comment.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at mark.shying@cpaaustralia.com.au, Kerry Hicks (the Institute) at kerry.hicks@charteredaccountants.com.au, or Tom Ravlic (NIA) at tom.ravlic@nia.org.au.

Yours sincerely

Geoff Rankin
Chief Executive Officer
CPA Australia Ltd

Graham Meyer
Chief Executive Officer
Institute of Chartered Accountants

Andrew Conway
Chief Executive Officer
National Institute of Accountants

The AASB would particularly value comments on whether:

(a) there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:
- **(i) not-for-profit entities; and**
- **(ii) public sector entities.**

The potential issue for these types of entities is whether the use of depreciated replacement cost in paragraph 33 of AASB 116 *Property, Plant and Equipment* is still considered to be an appropriate proxy for fair value, given that fair value is being defined as an exit price. We suggest that the Board give this issue further consideration so that any such issues are clarified to avoid confusion and divergence in practice.

(b) overall, the proposals would result in financial statements that would be useful to users; and

Overall, the proposals would result in useful financial statements however, we do have some concerns about certain aspects of the proposals which appear overly burdensome such as some of the disclosure requirements. Please refer to our comments to the IASB questions for further information about our concerns.

(c) the proposals are in the best interests of the Australian economy.

The proposals are in the best interests of the Australian economy, however we do have some concerns about certain aspects of the proposals. Please refer to our comments to the IASB questions for further information about our concerns.

28 August 2009

Sir David Tweedie
International Accounting Standards Board
30 Cannon Street
LONDON EC4M 6XH
United Kingdom

Via "Open to comment" page on www.iasb.org

Dear Sir David

Comments on Exposure Draft ED/2009/5 Fair Value Measurement

Thank you for the opportunity to comment on the IASB Exposure Draft Fair Value Measurement. CPA Australia, The Institute of Chartered Accountants in Australia (the Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have considered the above exposure draft (ED) and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government, academia throughout Australia and internationally.

General comments

We support the proposals in the ED to have a single reference point on fair value and appropriate guidance on the application of fair value measurement. Some of our key concerns include the onerous and rules-based disclosures, and the proposals relating to liabilities, such as the fair value of a liability is not affected by a restriction on an entity's ability to transfer the liability. We also continue to encourage the IASB to work with the FASB to achieve convergence.

Our responses to specific questions are included in the attached appendix.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at mark.shying@cpaaustralia.com.au, Kerry Hicks (the Institute) at kerry.hicks@charteredaccountants.com.au, or Tom Ravlic (National Institute of Accountants) at tom.ravlic@nia.org.au.

Yours sincerely

Geoff Rankin	Graham Meyer	Andrew Conway
Chief Executive Officer	**Chief Executive Officer**	**Chief Executive Officer**
CPA Australia Ltd	**Institute of Chartered Accountants**	**National Institute of Accountants**

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?

We consider the definition to be appropriate, as it not only aligns with US GAAP, but provides clarity about what fair value means.

In relation to the liability aspect of the definition, we note that the 'transfer of liability' wording in the definition is not entirely appropriate as we understand that in Australia and other common law jurisdictions it is often not legally possible to transfer a liability. We consider that these words should be reviewed further by both the IASB and the FASB to ensure the wording appropriately reflects the measurement attributes of the liability as outlined in paragraph 28 of the ED.

A more appropriate method of describing the concept would be the amount for which the liability would be settled. The liability settlement concept could then be used to value a liability either with or without a corresponding asset, which would address the issues identified in paragraphs 27 and 28 of the ED. The reference to the price that would be paid "to transfer a liability" in the definition of fair value is not entirely appropriate because it is not always legally possible to transfer a liability.

There may also be some practical implications as a result of defining fair value as an exit price, such as whether the use of depreciated replacement cost in paragraph 33 of IAS 16 *Property, Plant and Equipment* is still considered to be an appropriate proxy for fair value. Although paragraph 38(c) in the ED makes reference to current replacement cost, it is not clear whether this is the same as depreciated replacement cost as neither term is defined. We suggest that the Board give this issue further consideration so that any such issues are clarified to avoid confusion and divergence in practice.

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 proposed approaches to these three issues because the proposed definition of fair value could not apply in these circumstances. We are not aware of any other issues that would require a similar approach.

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 do not think that the guidance in paragraphs 9-11 is very clear. It appears that even though paragraph 8 requires the most advantageous market to be used, the guidance actually points towards the principal market as being the most advantageous market. Paragraph 9 states that the most advantageous market is to be considered from the perspective of the reporting entity, therefore if an entity transacts in the principal market, then this would be considered to be the most advantageous. Paragraph 10 assumes that the market that is normally transacted in is the advantageous market and paragraph 11 assumes that the principal market is the advantageous market.

We agree with the view in paragraph BC40 that entities aim to maximise profits and so would look to the most advantageous market. However, if the entity cannot transact in that market, then it should not be using that market to obtain a value. This seems to be implied in the footnote to paragraph 11, however should be made clearer and should be included in the paragraph itself instead of as a footnote.

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 do not agree with the second footnote to paragraph 13 and think that the wording as per SFAS 157 to be more appropriate in relation to market participants being independent of the reporting entity. We believe this is important because it makes it clear that the fair value measurement is market-based and not entity-specific.

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 24 of the draft IFRS and paragraphs BC51 and BC52 of the Basis for Conclusions).

Are these proposals appropriate? Why or why not?

Proposals (a) and (b) are appropriate, however we do not agree with (c) in relation to liabilities. Although the Board concludes in BC52 that alternative methods of discharging a liability are not ways in which a liability can be used, we do not agree with this view. We think that if assets can be viewed as having more than one use (whether in use or in exchange), a similar analogy can be used for liabilities. In other words, just as a market participant would seek to maximise profits from an asset, a market participant would seek to maximise gains from a liability (which would also represent the most advantageous market). Therefore where a liability can be settled or extinguished by more than one way, such as payment of a penalty, then the fair value should reflect this lowest price.

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 recognise 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?

We do not agree with the proposal to split the fair value of the asset into two components, as it is unnecessary and would be more confusing to users of the financial statements rather than providing useful information. If fair value is required based on the highest and best use of the asset, then it does not make sense to then split the value into separate components. Increase in compliance costs relating to such a proposal would seem unnecessary for little information benefit to users.

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 a liability (eg for a decommissioning liability assumed in a 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?

(a) Refer to our comments in Question 1.
(b) We question the presumption of symmetry between the fair value of an asset and the fair value of a liability, because it does not take account of the fact that market participants may hold different views as a holder of the asset versus the acquirer of a liability.
(c) We agree that present value and similar techniques should be used to estimate the fair value of the liability in these circumstances.

Question 8
The exposure draft proposes that:

(a) the fair value of a liability reflects non-performance risk, ie the risk that an entity will not fulfil 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?

We agree with the proposal in (a) as this is consistent with our understanding of the fair value measurement of a liability, as noted in our comment letter on the Discussion Paper DP/2009/2 Credit Risk in Liability Measurement. However, we do not agree with (b) for the reasons outlined in our response to question 1. If fair value was defined with a liability settlement concept, then paragraph 31 and BC75 would not be required.

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 recognise 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 recognise 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 do not think that reference to another IFRS is appropriate in the accounting for any resulting gain or loss on initial recognition. We believe that the accounting for any gain or loss upon initial recognition should be dealt with in the fair value measurement standard, as it should be a function of the measurement model, not the type of asset or liability that is being fair valued.

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?

The proposed guidance appears appropriate and sufficient. However, we would recommend that the IASB get input from the International Valuations Standards Council (IVSC) on the wording in paragraph 38, since some of the valuation professionals in our constituency feel that this paragraph is confusing and does not need to duplicate guidance already existing within the valuations industry.

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?

While we understand the attention on disclosures as a result of the recent global financial crisis, we consider some of the disclosures to be onerous and overly rules based. In particular we are concerned with:

- The requirement to prepare a reconciliation (paragraph 57e). Reconciliations are generally too detailed and confusing and do not provide useful information.
- The requirement to disclose the fair value hierarchy level for assets and liabilities not measured at fair value in the statement of financial position (paragraph 58). We consider disclosing the fair value of these items to be sufficient.
- The disclosures in paragraph 60, for the reasons mentioned in our response to question 6.
- The amendment to IAS 34 *Interim Financial Reporting* to require almost all the fair value measurement disclosures. An interim financial report already requires disclosure of the nature and change of estimates if material (paragraph 16d) which captures the requirement to disclose material changes in fair value. Therefore we do not consider that the fair value disclosures should be prescribed in interim financial reports.

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?

We generally agree with the approach the ED proposes, however would encourage the IASB to continue to work with the FASB in achieving convergence.

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

Paragraphs BC65 and BC66 are confusing and irrelevant and should be removed from the basis for conclusions.