

IASB Fair Value Measurements Roundtable Summary Tokyo

On November 27, 2009, the IASB held a roundtable at the ASBJ offices in Tokyo, Japan, to discuss its Fair Value Measurements exposure draft (ED). Roundtable participants consisted of a cross-section of representatives including auditors, financial statement preparers, valuation experts and industry. The notes below represent the roundtable observers' interpretations of the discussions, focussing on issues that have not already been discussed in the Norwalk roundtable (held on 2 November 2009).

The following issues were identified by the IASB staff for discussion during the roundtable:

- Issue A – Fair value as an exit price
- Issue B – Fair value of liabilities
- Issue C – Fair value of non-financial assets and liabilities
- Issue D – Fair value in inactive markets
- Issue E – Fair value in emerging and transition economies
- Issue F – Jurisdiction-specific issues
- Issue G – US GAAP convergence

Issue A- Fair value as an exit price

When does a market-based exit price not reflect the present value of the expected future cash inflows and outflows from an asset or a liability?

- A participant indicated that there may be situations when the market value might seem simply "wrong", particularly with a view to the results of internal valuation models. It was assumed that cases exist in which the information available would not explain the differences. The participant asked the question how to deal with such situation. IASB staff reacted quite skeptical to this question, as the market value in an active market is deemed to be the FV. However, in specific situations, results of valuation models that differ substantially from pricing information can be an indication of potential market illiquidity.
- It was further asked how to deal with high volatility of market prices. E.g., if there are big jumps in prices, the underlying transactions may not be judged as orderly. In this context, the question was asked if the use of an average price would not better reflect the economic reality. As a response it was said that this question refers more to the "when" than to the "how", as pricing volatility in active markets does not change anything to the exit price at a specific point in time and a weighted average value would need to be seen rather as a new valuation concept than a method to derive fair value.
- Regarding the reference market, it was noted by IASB that most comment letters had criticized the departure from the FASB's approach. It is likely that there will be changes to this aspect, focusing on the primary market.

Issue B - Fair Value of Liabilities

1. Can the principles of ASU No. 2009-5 be applied in practice in IFRSs? If not, why not?

In general, most participants could not think of significant reasons why the ASU could not work in practice in IFRS.

2. When might the fair value of a liability not be equal to the corresponding asset's fair value?

- A participant from the insurance industry noted that the fair value concept needs to be brought in line with the rules of IAS 19 (which currently is not the case). IFRS 4 was not mentioned in this context.
- It was mentioned that restrictions to transfer liabilities should not be relevant for the valuation of the liability.

Issue C – Fair value of non-financial assets and liabilities

1. What specific additional guidance is needed to measure the fair value of non-financial assets and liabilities?

2. Are any of the proposals in the exposure draft inconsistent with measuring the fair value of non-financial assets and liabilities?

- Participants discussed whether a profit margin needs to be factored into the valuation of non financial liabilities, and it was expressed that this should only be the case if there is a matching asset to the liability. As a response, IASB representatives said that as the FV is defined as an exit price, a profit margin needs to be generally included.
- Regarding the highest and best use criterion, IASB representatives noted that this needs some deeper analysis and that changes were likely. Participants discussed as an example the case of land that was unused at an industrial company, and it was analyzed as to whether such land needs to be hypothetically transformed e.g. into a holiday resort (thus creating a higher FV for the unused land). Such situations were seen as highly judgmental, involving an usual degree of discretion, which should be limited. IASB representatives noted that the ED foresees that there is no need to search out alternative uses. Participants noted in this context that the current use should regularly be deemed as the best use.

Issue D – Fair value in inactive markets

Is the proposed guidance sufficient for measuring fair value when markets have become inactive (when they previously were active)? If not, what additional guidance do you think is necessary?

- A participant indicated that the reduced likelihood to transfer from fair value into amortised cost category, as provided by IFRS 9, the issue of FV in inactive markets has lost some of its sting. IASB staff responded that as complex assets are not eligible for amortised cost accounting under the new guidance, and as a switch between categories requires a change in business model, current consultations still unraveled many issues in this matter.

- It was mentioned that the right approach would be to split pricing effects that are due to a reduction of market liquidity from pricing effects that are based on a decrease of projected cash flows. Various participants agreed that such split is often difficult to be made.
- IASB staff agreed that the examples in the application guidance for illiquid markets (e.g. high volatility, decoupling of correlation of an index and an asset, etc) should not be read as a checklist.

Issue E – Fair value in emerging and transition economies

1. What proposals in the exposure draft are not applicable to emerging and transition economies? Why are they not applicable?

2. What specific additional guidance is needed?

- IASB staff noted concerns raised in comment letters related to potential lack of information to obtain fair values in accordance with the envisaged ED, as well as lack of human resources to cope with the technical challenges the ED poses.
- A participant from Taiwan noticed that he believes that at least in Taiwan such lack of HR does not exist. He also mentioned that in his view most of the cases that might be raised relating to lack of information can be dealt with in based on the guidance relating to inactive markets.
- IASB staff mentioned that they are in the process of gathering specific cases in which information deficits pervasive to emerging markets exist. Most of such cases that are on the table so far relate to particularly high pricing volatility as well as lack of liquidity. The issue of a liquidity adjustment to fair value was mentioned.

Issue F – Jurisdiction-specific issues

Are there measurement considerations specific to your jurisdiction that the exposure draft does not seem to have contemplated? If so, what are they?

No such issues were mentioned in the meeting.

Issue G - US GAAP convergence

1. Aside from the reference market and blockage factors, would you expect there to be a numerical difference between a fair value calculated using the proposals in the exposure draft and a fair value calculated using the Topic 820?

2. Have you learned anything from applying Topic 820 that the IASB should consider when finalising an IFRS on fair value measurement guidance?

- Participants mentioned that the guidance to be able to use comparable assets for the valuation of liabilities was very useful in specific circumstances. IASB representatives mentioned that this issue will be discussed again, not that the FV project has become a joint project.

Other topics:

- Disclosure: A participant mentioned that in his opinion, the disclosure requirements should be defined in more detail. In particular, it was stated that there should be a differentiation between entity specific estimates and market estimates. Further, the differentiation between level 2 and level 3 should be described in more detail, both in the standards and in terms of disclosure requirements. Another participant mentioned that he believes that there will be excessive disclosure. E.g., FV disclosure should not exceed those assets that are measured at FV in the statement of financial position.
- Non quoted equity: A participant from ASBJ mentioned that shares for which a wider range of possible values has been derived based on a professional valuation should be potentially valued at any of those values (within the range), rather than to rely on cost accounting. The latter might seem arbitrary, as all values in the defined range have the same validity. IASB staff mentioned that while this might be correct theoretically, as decision still needs to be made, and cost is a reliable factor to do so.