



Committee of European
Banking Supervisors

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CEBS PUBLISHES REPORT ON ISSUES REGARDING THE VALUATION OF COMPLEX AND ILLIQUID FINANCIAL INSTRUMENTS

The Committee of European Banking Supervisors (CEBS) has published today its findings on issues relating to the valuation of complex and illiquid financial instruments. The report puts forward a set of issues that should be addressed by institutions and accounting and auditing standard setters in order to improve the reliability of the values ascribed to these instruments. CEBS has prepared this in response to a request set out in the October 2007 roadmap of the ECOFIN on the financial market situation.

The analysis focuses on the following valuation related aspects:

- challenges for the valuation of complex financial instruments or instruments for which no active markets exist;
- transparency on valuation practices and methodologies as well as related uncertainty; and
- auditing of fair value estimates.

The work has been based on the experience gathered by its members in the course of their supervisory responsibilities. It also draws on work carried out in other fora, such as the Basel Committee on Banking Supervision (BCBS) and the Senior Supervisors Group (SSG) as well as on discussions with industry representatives.

CEBS has ensured that its findings are consistent with the recommendations of the Financial Stability Forum report on 'Enhancing Market and Institutional Resilience'. – which CEBS fully endorses – as well as with the findings of the Senior Supervisors Group in its report 'Observations on Risk Management Practices during the Recent Market Turbulence'.

The major findings can be summarised as follows:

1. On valuation challenges:

- accounting standard setters should consider the need for further guidance on measuring fair values when there is little market activity in the instruments concerned (or other instruments relevant to pricing).
- institutions should:
 - * enhance their practices and governance surrounding the use of modelling techniques;
 - * ensure that all appropriate risk factors are considered when determining a fair value; and
 - * improve risk management practices to ensure adequate risk assessment of transactions and appropriate management of exposures;
- institutions and standard setters should consider wider valuation-related issues, including:
 - * classification issues;
 - * importance of timely impairment and possible changes to impairment rules for assets available for sale;
 - * treatment of Day one profits and related reserves; and
 - * impact and management of the own credit risk.

2. On transparency aspects:

- institutions should enhance their disclosures on fair values and on valuation techniques;
- and

- accounting standard setters should review the disclosure requirements to enhance the information to be disclosed on fair values and valuation techniques.

3. On auditing aspects:

-auditing standard setters should pursue their efforts to enhance the guidance for the audit of fair value estimates.

CEBS recommends that institutions and standard setters address the issues included in the report. It is intended to re-assess developments in this area and to liaise on any follow-up measures with other fora, notably CESR and CEIOPS.

For more information, please refer to the full report which can be accessed on our website our website at <http://www.c-ebs.org/publications/other>.

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Committee of European Banking Supervisors (CEBS) is comprised of high level representatives from the banking supervisory authorities and central banks of the European Union. CEBS main tasks are to advise the Commission in the field of banking activities, to contribute to the consistent implementation of Community Directives and to the convergence of supervisory practices and to enhance supervisory co-operation. The Committee is chaired by Ms Kerstin af Jochnick. The CEBS Secretariat is based in London. The Secretary General of the Committee is Mr Andrea Enria.