LIBA

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Director, Accounting Standards
Canadian Accounting Standards Board
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By email to: ed.accountingc@cica.ca

Dear Sir,

Measurement Bases for Financial Accounting – Measurement on Initial Recognition

I am writing on behalf of LIBA (the London Investment Banking Association) to comment on the IASB/CASB Discussion Paper Measurement Bases for Financial Accounting – Measurement on Initial Recognition, which was published on 28 November 2005. LIBA is, as you may know, the principal UK trade association for investment banks and securities houses; a list of our members is attached.

We commend the paper for raising the issue of measurement within the context of the Framework for the Preparation of Financial Statements ("the Framework") and agree that the Framework needs further development in this regard. However, we would like to record a number of concerns about the overall approach to this project:

- Although we understand from a practical perspective why the IASB/CASB have tried to split the project into phases - the debate on measurement is a complex one - we believe that focusing exclusively on initial measurement is a major flaw with the approach adopted. Initial measurement and subsequent measurement will in many cases be linked and the basis used for one will therefore be likely to have repercussions for the other. For example, distinguishing initial and subsequent measurement assumes that there is a clear distinction between the two, but in the banking industry - where valuations can occur on a daily or even on a real-time basis - this distinction can sometimes be unclear. In addition, we consider that the true debate around measurement will occur in respect of subsequent measurement, since in many circumstances initial recognition bases will be the same. Therefore, limiting the paper to the consideration of initial measurement in isolation reduces the weight of any decisions and/or conclusions reached, as they will need to be revisited as part of the extensive debate that is required on subsequent measurement. We would, therefore, recommend that the IASB consider initial and subsequent measurement concurrently, and even in these early stages open both questions to debate.

- From the Paper's introduction, we understand that it forms the first stage of work on considering measurement within the Framework, yet the paper goes beyond the point of merely characterising different measurement bases, concluding that fair value should be used on initial recognition, subject only to reliability. Furthermore, the Paper then provides guidance on how to measure fair value, proposing a four-level measurement hierarchy. Given that the Framework does not seek to define standards for any particular measurement or disclosure issue (see paragraph 2 of the Framework), we find it unclear what the IASB/CASB are seeking to achieve from this paper. We also find it unclear how or where the IASB plans to implement any final views that may be formulated on initial (or indeed on subsequent) measurement as part of this project. We believe the key initial objective of the project should be to explore more fully the different measurement bases available, and to use this to develop the principles behind and definitions of each relevant measurement basis. Determination of the "when" and "how" to measure different assets and liabilities should be done within the context of the relevant standard.

- Continuing on from the point above, the paper to provides significant guidance on how to measure fair value; this has resulted in substantial overlap, and some inconsistencies, with current IFRS as contained in IAS 39 and with the IASB's current project on Fair Value Measurements. Given the IASB have indicated that they will issue the FASB's final Fair Value Measurement standard as an IASB exposure draft later this year, we are unsure what status the fair value measurement proposals contained in the discussion paper have. We believe the IASB/CASB should provide a clear explanation of how this discussion paper, and the different stages of the overall project relate to the IASB's Fair Value Measurements project and seek any comments on "how" to fair value within the context of that project.

- The discussion paper adopts a "one-size-fits-all" approach to measurement, making the assumption that there will be one single measurement basis and focusing on what that basis should be. However, it is clear to us that different situations may warrant different measurement bases. For example, fair value could be considered to represent the break-up value for certain assets (although not necessarily the liquidation value), and so a value in use or deprival value may be more appropriate for accounts prepared on the going concern basis. As stated above, at this stage in the project the IASB/CASB should concentrate on developing definitions and principles of the different bases, and open for debate the issue of whether there is a need for a mixed measurement approach. This should be done in the context of the Framework and the specific standards in question.

- The paper concludes that for the purposes of external reporting, market value/fair value is more relevant than entity-specific measurement bases. The primary reason for this conclusion is that market forces will result in a single price (market value) for identical assets and liabilities. As a result, the discussion paper focuses on how to identify that single market value. The experience of our members in trading financial instruments across retail and wholesale markets and across borders is there is often no single most relevant market value for all entities. Despite the conclusion stated above, the discussion paper does acknowledge that multiple markets for identical assets or liabilities do exist and proposes that research be undertaken on this point. We support the IASB/CASB undertaking further research in this area since we consider that it could significantly change the conclusions reached in the Discussion Paper.

- In general, we agree that transaction costs should not be included in the value of an asset or liability unless they are recoverable, and are therefore an integral component of the fair value of the asset or liability. We consider that the notion of recoverability is crucial and this is reflected in the entity-specific measurement objectives, which support the assertion that a company would not incur such costs unless it believed they could be recovered through the future use of the asset or the liability. This would accordingly support, where appropriate based on recoverability, the recognition of such costs over the life of the associated asset or liability.

- As noted above, where transaction costs are captured in the fair value of an asset, it would be appropriate to include such costs in the carrying value of the asset. An example of this would be the cost of obtaining the appropriate legal opinions, etc in relation to the purchase of a listed instrument. Without those opinions, the instrument would be unmarketable. Thus, the opinions enhance the value of the instrument and so it would seem reasonable to reflect such costs in the value of the asset/liability as they are inseparable. By contrast, paying commissions to a broker to purchase a security does not add value to the underlying asset and would not be recoverable when selling the asset. Therefore, transaction costs of this nature should not be included in the value of the asset or liability.

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I hope that the above comments are helpful. We would of course be very pleased to expand on any particular points if there are aspects which you find unclear, or where you would like further details of our views in respect to this Discussion Paper or the indeed to the future Framework project.

Yours sincerely

Ian Harrison
Director

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