REDOVISNINGSRÅDET

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Canadian Accounting Standards Board
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Dear Sirs,

Re: Discussion Paper "Measurement Bases for Financial Accounting – Measurement on Initial Recognition"

This letter represents the views of the Swedish Financial Accounting Standards Council (SFRSC). We are very pleased that a debate on measurement has now been initiated.

We hope that this will comprise a broad and comprehensive debate on measurement issues and basic premises as regards the manner in which assets and liabilities are to be recognized in financial statements. A broad and comprehensive debate on measurement has become of the utmost importance for the future development of International Financial Reporting Standards. The significantly increased application of the International Financial Reporting Standards from 2005, the increased use of market-based measurement in more recent standards, and amendments proposed by IASB including more market-based measurement, have created an increased focus on measurement.

The Discussion Paper has been prepared by the staff of the Canadian Accounting Standards Board. The paper has been distributed for comments without the Canadian Accounting Standards Board, nor the IASB, presenting any kind of views on the issues concerned. The Discussion Paper presents and discusses a number of important issues and proposes a measurement hierarchy that we believe has clear merits. The paper is a good starting point for discussion of these very important issues. However, we have a number of serious concerns regarding the Discussion Paper as a base for a broad and comprehensive debate on measurement. Our key concerns are:

1. No proper discussion of what financial statements primarily should portray

2. No comprehensive and balanced analysis of current measurement issues

3. Conclusions on measurement have been drawn for initial recognition in isolation

4. Key conclusions based essentially on reference to financial markets

5. Reliability issues not given proper attention

6. Position taken on user needs without sufficient analysis and discussion

7. Conclusions made without communicated analysis and justification

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We have described below our prime concerns with the Discussion Paper. Responding within the scope of the detailed questions does not provide a sufficiently broad platform on which to air our concerns. Nevertheless, we have, in the enclosed appendix, provided answers to the questions on which we have been invited to comment. Due to the concerns we have as regards fundamental issues related to the Discussion Paper, we have not found it reasonable to make the thorough analysis required to provide comprehensive answers at this stage of the process. Certain of the questions should be further discussed, when a better base for debate and conclusions has been established.

Our key concerns

1. No proper discussion of what financial statements primarily should portray

In the discussion paper there is a short discussion of the key aspects of financial reporting but there is no clear reasoning as to how the stewardship objective and the concept of accountability relate to the predictive purpose and the manner in which these factors in the prime conclusions presented in the Discussion Paper .

We believe that a serious and conceptually sound discussion on measurement for financial accounting can not be performed without a discussion on the objectives of financial reporting.

2. No comprehensive and balanced analysis of current measurement issues

According to Chapter 1 of the main paper, the background to the project is that:

- Existing measurement standards and practices are inconsistent,
- a number of significant measurement issues remain unsettled, and
- the measurement provisions in existing conceptual frameworks are limited and out of date.

As the provision of a basis for improving measurement in financial reporting is the aim, we believe that the project should include an in depth analysis of the concerns and issues caused by inconsistent measurement standards, practice and only limited guidance on measurement in the conceptual frameworks. A comprehensive and balanced analysis of the impact on financial reporting of identified measurement problems is required. This analysis should give proper attention to financial, as well non-financial, assets and liabilities and provide a balanced view of the current situation, taking into account the fact that many assets and liabilities are not traded in active markets.

There is not much of an analysis in the Discussion Paper as regards the current impact on financial reporting due to inconsistent measurement standards, etc. The analysis that is included is not balanced. It has too great a focus on assets traded in active markets. The paper too quickly assumes the position that fair value is always superior as a measurement base and uses that perspective in making comparisons with other bases throughout Chapter 7.

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3. Conclusions on measurement drawn for initial recognition in isolation

The focus of the paper is solely on initial measurement, which we do not find to be appropriate. We believe that it might be difficult to draw valid conclusions about initial measurement without considering subsequent measurement. Initial and subsequent measurements are so interlinked that it can be questioned, whether it is at all relevant to discuss them separately.

The application of fair value measurement at initial measurement can be seen to prejudge subsequent measurement, as it is easy to see arguments developing which will suggest that there are no reasons to move from fair value, if deemed to be superior at initial measurement, to some other base at subsequent measurement.

4. Key conclusions based essentially on reference to financial markets

The Discussion Paper generally takes the view that "market value measurement has important qualities making it superior to entity-specific measurement, at least on initial recognition" (the short version paragraph 102). Reference is given to financial literature.

This tentative conclusion seems essentially to be based on arguments and examples relating to transactions in financial markets, in which market values may be relevant and reliable as they result from transactions in active markets involving low transaction costs. We agree that market value may be superior as a measurement base in such cases. However, we are not convinced that the heavy reliance on the notion of active markets is well-founded,

In a global environment active markets with low transaction costs do not generally exist outside of the financial markets. Furthermore, not even all financial market transactions in well-developed financial markets are performed under the conditions required to comprise an active market. This is acknowledged by the Joint Working Group of Standard Setters in “Draft Standard and Basis for Conclusions-Financial Instruments and Similar Items”, who arrived at a somewhat similar conclusion in identifying certain situations in which “prices (are) not determined by normal market interactions” or where there are infrequent transactions. In these situations, the Group concluded that the observed prices should not be used “as the primary basis for determining fair value”. See note 84, paragraph 243 of the main paper.

We, therefore, take the position that a more relevant Discussion Paper on measurement bases for financial accounting should consider the actual nature of the markets for an entity’s resources, and not what these markets could be or perhaps will be to, some degree, in the years to come. The Discussion Paper places an excess focus on fair values and gives to little attention to the analysis of other measurement bases. We conclude that the Discussion Paper does not have the focus in its analyses and discussions that it should have and that its tentative conclusions are not well-founded.

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5. Reliability issues not given proper attention

We are concerned about the manner in which reliability is treated in the Discussion Paper. Furthermore, the paper introduces the concept of "sufficient reliability to justify recognition in financial statements", in paragraph 230 of the main paper, without properly defining the meaning of this concept, which is not used in the Framework.

Consistent with our discussion in item 4 above, we do not think that fair value is capable of providing reliable estimations in a great number of situations outside financial markets, due to of the vulnerability to market imperfections. A few infrequent observable transactions do not constitute a market, in which reliable fair values can be applied. Processes for buying and selling financial instruments are different from processes for buying and selling industrial materials and supplies. Conclusions drawn from one type of market may not easily translate into another type of market.

As we are of the opinion that markets with observable market prices are the exception rather than the norm, we believe that this is an important observation, not only in terms of reliability, but also in terms of relevance.

We have noted the acknowledgements in paragraph 216 of the main paper that, in the absence of market prices, estimated fair values may be open to "significant measurement uncertainty". There are interesting discussions in the main paper concerning measurement uncertainty and examples of difficult measurement situations, as the business combination case, discussed below, but there are no clear discussions nor any suggestions and conclusions in the Discussion Paper as to the manner in which this should be taken into account.

A possible starting point for such a discussion is the common belief that the transaction price should be presumed to be the market price, unless there is convincing evidence to the contrary (as referred to in paragraphs 244-246, main paper) .

In the Discussion Paper there is an illustration of a business combination (paragraph 248, main paper) where the question is posed as to whether the consideration paid is the fair value. In the paper the conclusion is made that no one knows for certain, but that the essential question is whether one should, in fact, assume that this is the case. However, this essential question is not answered. Instead, a new question is posed, that is, whether the said amount in that case should be termed "fair value".

Addressing the essential question identified in the Discussion Paper, the choice is between using an indirect measurement of the net assets, i.e. consideration paid, in contrast to trying to directly measure the value of the net assets. In the latter case there are identification and estimation problems

Most inputs to a company's operations could be characterized as having multiple attributes (such as prices and terms, service level offered, quality, manufacturer's characteristics, etc.). When a direct valuation is used, instead of an indirect, one must identify these attributes and estimate the value of each of them. Thus, you have both identification problems and estimation problems (which has been recognized in other areas, e.g. in the revenue recognition project, in which the fair value approach has been (temporarily?) rejected for a customer consideration approach).

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In many situations, it is not possible to separate entity-specific values from fair values. The historical cost is not necessarily an entity-specific value; it might comprise the fair value of a bundle of attributes (which are not traded in a market). In the marketing literature, it has long been recognized that quite often goods are best seen as comprising a bundle of attributes.

It is acknowledged, in paragraph 250 of the main paper, that other situations involving unique assets or liabilities may be measured on initial recognition at their exchange prices, with no real possibility of obtaining independent evidence of fair value. These situations may include some specialized or self-constructed items of plant and equipment, and possibly some liabilities for unique warranties and other similar obligations. We believe that the paper heavily underestimates the significance of situations in which independent evidence of fair value is not available. Outside financial operations this is, instead, the rule, rather than the exception.

6. Position taken on user needs without sufficient analysis and discussion

In paragraph 60 (in the short version) the paper takes the position that "the more relevant financial statement measurement objective on initial recognition for investors and other external users is that entities be measured against market values and subject to the discipline of the market place rather than to entities' individual expectations". We do not believe that the Discussion Paper has presented convincing arguments in favor of this position. We note that paragraph 126 (of the main paper) poses a relevant question on this issue, and makes a proposal on the basis of a "conceptual analysis", but we take the position that the consequences of alternative measurement bases and how these are related to various users' needs would have to be analyzed and discussed in greater depth before any firm conclusion should be drawn.

Consider the recording of an asset at historical cost on initial recognition. In such a case, the presumption is, often, that the asset must have a value of at least this amount, otherwise the company would not be willing to pay such an amount. The asset could have a higher value, but in that case this will be manifested in future profits. However, the asset could also have a lower value, implying that the entity has made a bad deal. This will be manifested in future losses. A delayed recognition of a bad deal, i.e. the gradual revelation of the unfavourable state, has obvious disadvantages. New lenders or owners could invest additional capital unaware of this unfavourable state. The operations of the entity could continue with further value destruction. During a long period of time the chosen approach for handling this problem has been to test for impairment and, if necessary, make a write-down to the recoverable amount. There are problems associated with estimating this recoverable amount, e.g. to estimate future cash flows and to chose an appropriate discount rate. However, these problems must be compared to the problems inherent in an alternative approach, i.e. to value the asset directly. It should be clear from the argument above that there are substantial identification and estimation difficulties related to making direct fair value measurements for everything but the most simple of assets. Furthermore, in many cases, a direct measurement will lead to a net profit (or loss) being recognized at initial recognition. The problems associated with direct measurement on initial recognition are, in our opinion, more serious compared to testing for impairment.

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Regarding comparability, we share the opinion that comparability is a very important characteristic of accounting information. The majority of decisions are based on choices between different alternatives and involve relative assessments. However, comparability is of a very complex nature and it is not clear that the inter-temporal characteristics of fair value on initial recognition, which is one of the prime arguments for fair value in the Discussion Paper, are so important that they should override other concerns concerning e.g. identification and estimation difficulties for all transactions.

On a more fundamental level, the argument for fair value is related to the concept of opportunity cost. Differences in the relevance of this concept between investors and management have to be discussed. Investors definitely have a perspective where they continuously look for alternative uses of their funds. Management normally have more of a “going concern” perspective, where specific resources are locked in for a period and their view is generally that they will continue doing their business on an ongoing basis employing the resources they control, rather than selling them (a major explanation for this is the differences in transaction costs between trading shares and real assets i.e. restructuring a business). Therefore, a fair value approach of measuring assets and liabilities is not that relevant from a management perspective in the majority of business environments.

7. Conclusions drawn without communicated analysis and justification

There are too many instances in which important conclusions are drawn in the Discussion Paper without communicated, thorough analysis, discussions and justification. Examples of this are discussed above, see item 1, 4, 5 and 6. Presented below are some other examples:

The Discussion Paper includes, in the section discussing measurement date on initial recognition, an example of a purchase of a truck (paragraph 410-415, main paper). This example shows some of the consequences of measuring according to the proposed measurement hierarchy and at the date of initial recognition.

According to the example, profit should be recognized if the fair value of the truck increases from contract until delivery date. The truck example used may not clearly highlight the magnitude of the issue. If we, instead, focus on examples of really major investments, such as investments in infrastructure, oil rigs, computer chip factories, paper mills and steel mills, in which the construction periods extend over a number of years, it may become considerably clearer that the proposals could lead to that substantial amounts of profits and losses will be recognized on initial recognition.

In paragraph 414, of the main paper, it is stated, regarding the truck case, that “On the other hand, it may be argued that it is more relevant for the truck to be measured at its fair value on its acquisition date, because it does not become an asset of the entity that can be used in its cash-generating activities until that date. The gain then represents the consequences of contracting at a fixed price prior to obtaining the asset, and the entity has chosen to accept the risks of fixing the price at the contract date. The entity may have negotiated different terms, and it may be argued that reflecting a gain or loss on the contract provides useful information about the results of the entity’s contracting decisions, regardless of how the truck is accounted for subsequent to its initial recognition.”.

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It has not been clearly analyzed, substantiated or explained in the Discussion Paper why the gains and losses, calculated as the price difference between contract and control date, would provide useful information. The Discussion Paper provides the truck example and three sentences in paragraph 414 of the main paper.

Another issue, as regards situations as described above, relates to insufficient market price information, often making control date measurement unreliable. For assets which can not be delivered off the shelf, the fair value information available on date of control is, in most cases, not a fair value for the asset available for use on that date, but the fair value of an asset for delivery at a later date. In the case of major investments this refers to delivery several years in the future. Using price information for an asset which is different (i.e. an asset to be delivered at a later date) requires adjustments to reflect the value of the asset being recognized. This is, in many cases, a very difficult and costly exercise, if at all possible.

We are not at all convinced that measurement for initial recognition of assets should be based on measurement as of control date rather than as of contract date.

The Discussion Paper concludes in paragraph 196 of the main paper, without a discussion, that under the fair value measurement approach all transaction costs shall be expensed. Even if the conclusion is not new, we do believe that this should be further discussed. This issue has not been given proper attention in the Discussion Paper. We do not support reporting losses on initial recognition, corresponding to the transaction costs, for all acquisitions measured at fair value. We do not believe that this leads to superior information for users, but rather confuses users.

In paragraph 199 it is stated that transactions costs “that cannot be avoided, but must necessarily be paid in the future to achieve the fair value of an asset ...may meet the definition of a liability. In this case, they should be separately recognized as liabilities when the related asset or liability is recognized and measured at fair value. If these costs are not recoverable in the marketplace, they would be treated as expenses on recognition, rather then included in the fair value of the asset or liability.” We do not fully understand why reference is made to “may meet the definition of a liability” in the above case, as there seems to be no past (obligating) event, which is one of the conditions for the existence of a liability. A payment in the future for a sale that has not yet taken place (and that may not take place), is a future event, not a past event, according to our understanding. Furthermore, the reporting entity is not committed to sell and, therefore, not committed to incur transaction costs. We are, therefore, of the opinion that the language in paragraph 199 on the above issue would benefit from an explanation, so that it is made very clear as to the manner in which the criteria of the definition of a liability are met in the case at hand.

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Appendix

Response to the questions about which we have been invited to respond

Responding within the scope of the detailed questions does not provide a sufficient broad platform to air our fundamental concerns, as described above. Nevertheless, we have provided below answers to the questions upon which we have been invited to comment.

Question 1*—Do you agree that the list of identified possible measurement bases (see paragraphs 33-51 of the condensed version and paragraphs 69-74 of the main discussion paper) sets out the bases that should be considered? If not, please indicate and explain any changes that you would make.*

We believe that the list of measurement bases in the discussion paper includes those measurement bases that should be considered.

Question 2*— Do you agree with the working terms and definitions, and supporting interpretations, of each of the identified measurement bases (see paragraphs 33-51 of the condensed version and paragraphs 77-96 of the main discussion paper)? If not, please explain what changes you would make. In particular, do you have any comments on the term "fair value" and its definition (in light of the discussion in paragraphs 46-48 of the condensed version and paragraphs 88-93 of the main discussion paper)?*

We generally agree with the working terms and definitions of the identified measurement bases in the discussion paper. We have, however, contemplated the discussion on the term "fair value" and the need, if any, to attach a label to that concept which would include mention of the market value measurement objective. We have, however, concluded that the reasons to change the fairly well-known fair value label are not sufficiently strong to motivate such a change.

Question 3—*It is proposed that there are two fundamental sources of differences between the identified bases for measuring assets and liabilities on initial recognition:*

(a) Market versus entity-specific measurement objectives, and

(b) Differences in defining the value-affecting properties of assets and liabilities.

(See paragraph 52 of the condensed version and paragraph 97 of the main discussion paper.) This proposal and its conceptual implications are the subject of chapters 4 and 5. Do you agree that these are the fundamental sources of differences between asset and liability measurement bases on initial recognition? If not, please indicate the fundamental sources of differences you have identified, and provide the basic reasons for your views. For any different fundamental sources you have identified, please indicate how these might be examined and tested.

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We agree with the premise that (a) and (b) above reflect the fundamental sources of differences between asset and liability measurement bases on initial recognition. However, as reflected in item 4 of our cover letter, we do not think that the Discussion Paper satisfactorily explains the reason that financial literature and its reference to “efficient market price”, alone, should determine that which is to serve as the most relevant measurement base at initial measurement for financial reporting purposes.

Question 4—*The paper analyzes the market value measurement objective and the essential properties of market value.*

(a) Do you believe that the paper has reasonably defined the market value objective and the essential properties of market value for financial statement measurement purposes (see paragraphs 54-56 and 105-112 of the condensed version and paragraphs 99-110 and 236-241 of the main discussion paper)? If not, please explain why not, and what changes you would propose, or different or additional considerations that you think need to be addressed.

(b) Do you agree with the proposed definition of "market" (see paragraphs 55-56 of the condensed version and paragraphs 107-110 of the main discussion paper)? If not, please explain why you disagree, and indicate any changes you would make and any issues that you believe should be given additional consideration.

(c) Do you agree with the fair value measurement objective as proposed, and its derivation from the market value measurement objective (see paragraph 102 of the condensed version and paragraphs 111, 228 and 229 of the main discussion paper)?

See our response above regarding the reference to financial literature and its perceived importance for financial reporting measurement purposes.

Although we believe that “market” has been defined in a reasonable manner, we have some concerns. We note that the definition refers to “sufficiently” extensive exchange transactions to reach an equilibrium price and we suspect that there might be different views on what ”sufficiently” should mean in this context. We have further observed that the definition assumes the existence of parties ”who have access to publicly available information and expertise” (paragraph 109 in the main document). We have observed that there might be different rules and practices in markets around the world as regards the information which is required to be publicly available and we note, therefore, that the depth of the information available may vary between different markets which are setting prices deemed to be “market values”.

As reflected in item 4 in our cover letter, we do not agree with the conclusion in paragraph 102 of the short version of the Discussion Paper that fair values generally implies superior qualities, compared to the other measurement bases discussed in the paper.

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Question 5— *Do you agree with the definition and discussion of entity-specific measurement objectives (see paragraph 57 of the condensed version and paragraphs 112-116 of the main discussion paper) and their relationship to management intentions (see paragraph 58 of the condensed version and paragraphs 117-121 of the main discussion paper)? If not, please explain why you disagree.*

As reflected in item 5 of our cover letter, it is not always possible to separate entity-specific values from fair values and the replacement of indirect measurement by direct measurement may create both identification and estimation problems.

Although the discussion of management intentions in the Discussion Paper seems to be convincing from a measurement point of view, there are a number of aspects which are not addressed in this discussion, e.g. the role that stewardship and accountability should play. It seems to us that there is a case for entity-specific measurement when stewardship and accountability are regarded as important objectives for financial reporting.

Question 6*—Do you agree with the comparison of market and entity-specific measurement objectives (see paragraph 59 of the condensed version and paragraph 122 of the main discussion paper) and with the proposed conclusion that the market value measurement objective has important qualities that make it more relevant than entity-specific measurement objectives for assets and liabilities on initial recognition (see paragraphs 60-61 of the condensed version and paragraphs 123-129 of the main discussion paper)? If not, please explain your views.*

As reflected in our cover letter, item 6, we do not generally agree that the market value measurement objective is more relevant than entity-specific measurement on initial recognition. In principle, we believe that too large a portion of the Discussion Paper is based on experience from the financial markets, which are referred to as a norm, rather than as an exception, as regards efficiency and liquidity.

Question 7

(a) It is reasoned that there can be only one market (fair) value for an asset or liability on a measurement date (see paragraph 62 of the condensed version and paragraphs 131-138 of the main discussion paper). Do you agree with this conclusion? If not, please explain why you disagree.

(b) It is proposed that differences between apparent market values for seemingly identical assets or liabilities on initial recognition may be attributable to:

(i) Differences between the value-affecting properties of assets or liabilities traded in different markets, or

(ii) entity-specific charges or credits.

(See paragraph 63 of the condensed version and paragraphs 131-138 of the main discussion paper). However, the paper notes the existence of multiple markets for some assets and liabilities, and the possibility that they may be due to market access restrictions that require further investigation (see paragraphs 74-82 of the condensed version and paragraphs 95-109 of the main discussion paper).

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Do you agree with these proposals, within the caveats and discussion presented? If not, please explain why you disagree.

We do not agree that there can be only one market value on a measurement date. In fact, we find that the Discussion Paper (paragraph 135 in the main document) shows that market prices may vary, which may relate to other factors than those discussed in the paper. We believe that many market places are not efficient, which may create a range of market prices, not only relating to reliability issues.

Question 8—*Do you agree that a promise to pay has the same fair value on initial recognition whether it is an asset or a liability, and that the credit risk associated with a promise to pay enters into the determination of that fair value with the same effect whether it is an asset or liability (see paragraph 65 of the condensed version and paragraphs 142-147 of the main discussion paper)? If you do not agree, please explain the basis for your disagreement.*

From a theoretical point of view, one could argue that a promise to pay should have the same fair value on initial recognition regardless of whether it is an asset or a liability. This might be particularly true if financial reporting is to serve only to satisfy investors' needs from a buy and sell perspective. However, financial reporting should also satisfy needs such as stewardship and accountability, see cover letter item 1. If these needs are taken into account, fair values attributed to assets and liabilities are less relevant from an information point of view. Furthermore, the question raised may have more to do with subsequent measurement than with initial measurement, and should, therefore, be addressed in the context of a future project.

Question 9—*the paper makes the following proposals with respect to defining the unit of account of the asset or liability to be measured on initial recognition:*

(a) The appropriate individual item or portfolio unit of account on initial recognition is generally the unit of account in which the reporting entity has acquired the asset or incurred the liability (see paragraphs 67-70 of the condensed version and paragraphs 149-154 of the main discussion paper).

(b) The appropriate level of aggregation for non-contractual assets on initial recognition is the lowest level of aggregation at which an identifiable asset is ready to contribute to the generation of future cash flows through its sale or use (see paragraphs 71-73 of the condensed version and paragraphs 157-161 of the main discussion paper).

Do you agree with these proposals within the caveats and discussion presented? If not, please explain why, and in what respects, you disagree.

Although the above proposals have some merit, we have some concerns. Our comment on (a) above is that acquisitions could be made in a number of ways. Paragraph 161 says as follows: "Pending further study beyond the scope of this preliminary investigation, this paper proposes that the appropriate unit of account for non-contractual assets on initial recognition is the lowest level of aggregation at which an identifiable asset is ready to contribute to the generation of future cash flows." We read this to imply that the manner in which an entity buys financial instruments and the manner in which financial instruments are bundled, may determine is the unit of account. We do not understand why an entity acquiring individual

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instruments and then bundling them should measure the instruments differently than an entity acquiring the same instruments as a portfolio. On (b) we agree with what is indicated in paragraph 161 in the main document, i.e. further study is needed to deal with how to aggregate to the lowest level at which an identifiable, non-contractual asset is capable of contributing to the generation of future cash flows.

Question 10*—It is suggested that, in many cases, the best market source on initial recognition is the market in which the asset or liability being measured was acquired or issued. However, some significant situations are noted in which a different source may be appropriate, and research is proposed into possible multiple markets (see paragraphs 75-82 of the condensed version and paragraphs 162-182 of the main discussion paper). Do you agree that the paper provides a reasonable analysis of market sources and their implications on initial recognition? If not, please provide reasons for disagreeing, and indicate any additional analysis or research you would think should be carried out.*

As we have explained in our response to question 7, we do not agree that there could be only one market on a measurement date. The issue of multiple markets for identical items existing as indicated in paragragh 82 of the short version need to be investigated.

Question 11*—The paper concludes that transaction costs, as defined, are not part of the fair value of an asset or liability on initial recognition (see paragraphs 86-87 of the condensed version and paragraphs 193-200 of the main discussion paper). Do you agree with the proposed definition of transaction costs? Do you agree with the above conclusion? If you disagree, please explain your reasons and what you believe the implications of your different view would be for fair value measurement of assets and liabilities on initial recognition.*

We agree with the proposed definition of transaction costs. However, the line to be drawn between costs that are recoverable and other costs may involve implementation problems, which may lead to diverging practices if the proposal was to be implemented in practice. Furthermore, as indicated in item 6 of our cover letter, we argue that the value of an asset at acquisition has a value corresponding to the amount that has been paid for the asset in question. We question the relevance of implementation of fair values to the extent proposed, which is discussed in our cover letter, item 7. As a consequence, we do not agree that transaction costs should be expensed as proposed.

Question 12— *Do you agree with the proposal that, when more than one measurement basis achieves an acceptable level of reliability, the most relevant of these bases should be selected (see paragraph 89 of the condensed version and paragraph 202 of the main discussion paper)? If not, please explain why you disagree, and indicate how you would settle trade-offs between the relevance and reliability of alternative measurement bases.*

We are not sure what is meant by ”an acceptable level of reliability” and how and to what extent this would deviate from ”reliability”, which is the concept contained in the Framework. If one were to agree that financial statements should primarily be used for estimating future cash flows, then we might agree with what seems to be suggested, i.e. a focus on relevance to the detriment of reliability. As has been discussed in our cover letter, we tentatively take a different view on the objective of financial statements, i.e. that they should be used for purposes other than simply estimating future cash flows.

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Question 13*— Do you agree with the two proposed sources of limitations on measurement reliability—estimation uncertainty and economic indeterminacy—and supporting discussion (see paragraphs 90-100 of the condensed version and paragraphs 204-216 of the main discussion paper)? If not, please explain your view.*

We agree with the two proposed sources of limitations on measurement reliability above. However, we have two concerns. One concern relates to the use in the discussion paper of "sufficient reliability" and " an acceptable level of reliability" (see paragraph 202 in the main document). As has been noted above, we are not sure what this means and how it relates to "reliability" in the Framework. A second concern relates to the comment, to which we agree, in paragraph 216 in the main document, that an estimated fair value may be open to significant measurement uncertainty in the absence of a market price. We are, therefore, not sure as to the basis on which "sufficient reliability" is achieved under such circumstances.

Question 14—*Do you agree that fair value is the most relevant measure of assets and liabilities on initial recognition of assets and liabilities, and therefore should be used when it can be estimated with acceptable reliability (see analyses of fair value and alternative bases in chapter 7, and discussion of measurement date on initial recognition in paragraphs 179-180 of the condensed version and paragraphs 410-415 of the main discussion paper)? If not, please explain why.*

We do not agree that fair value is generally the most relevant measure of assets and liabilities. We refer to our comment letter, item 6 and to our discussion above on Q12. Fair value in efficient markets is one thing; estimated fair value in other market situations is another, which must be factored in when reaching conclusions as regards determining that which is relevant measurement on initial recognition.

Question 15*— do you agree that fair value is not capable of reliable estimation in some common situations on initial recognition (see paragraph 104 of the condensed version and paragraphs 232-277 of the main discussion paper)? More specifically, do you agree that:*

(a) A single transaction exchange price should not be accepted to be equal to fair value unless there is persuasive evidence that it is (see paragraphs 106-114 of the condensed version and paragraphs 243-252 of the main discussion paper), and

(b) A measurement model or technique cannot be considered to achieve a reliable estimation of the fair value of an asset or liability when the estimate depends significantly on entity-specific expectations that cannot be demonstrated to be consistent with market expectations (see paragraphs 115-118 of the condensed version and paragraphs 263-268 of the main discussion paper)?

Please provide explanations for your views on these questions if they differ significantly from the conclusions and supporting arguments presented in the paper.

We generally agree with the above points as regards that which should not be accepted as fair value. Furthermore, as we have pointed out before, we believe that the transaction price should be presumed to reflect fair value, unless there is convincing evidence to the contrary.

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Question 16*—Do you agree with the paper's analyses and conclusions with respect to the comparative relevance and reliability of:*

- *historical cost (see paragraphs 120-137 of the condensed version and paragraphs 281-319 of the main discussion paper);*
- *Current cost - reproduction cost and replacement cost (see paragraphs 138-154 of the condensed version and paragraphs 320-361 of the main discussion paper);*
- *Net realizable value (see paragraphs 155-161 of the condensed version and paragraphs 362-375 of the main discussion paper);*
- *Value in use (see paragraphs 162-169 of the condensed version and paragraphs 376-392 of the main discussion paper); and*
- *Deprival value (see paragraphs 170-178 of the condensed version and paragraphs 393-409 of the main discussion paper)?*

Please provide reasons for any disagreements, and any advice you may have as to additional analysis or research that you believe should be carried out.

We generally agree with the analyses with respect to the comparative relevance and reliability of the above measurement bases. However, we do not agree with the conclusions reached. The analyses are, in our opinion, made in a manner which puts fair value in pole position, rather than discussing the pros and cons of various measurement bases in a neutral context.

Although we generally agree with various aspects of the analysis with respect to the comparative relevance and reliability of the above measurement bases, we do not agree with the conclusions. The analyses are, in our opinion, made against the background of a view that fair values are deemed to be superior for measurement at initial recognition, rather than discussing pros and cons of various measurement bases in a neutral manner. As we have pointed out before, the underlying theme of the Discussion Paper seems to be that there are efficient markets around the world which are capable of establishing fair values in a reliable fashion. To the best of our knowledge, this is not the case and, therefore, much of the discussion in this part of the document seems to be founded on invalid grounds.

Question 17—*the paper discusses substitutes for fair value when the fair value of an asset or liability cannot be reliably estimated on initial recognition. Do you agree that, when other measurement bases are used as substitutes for fair value on initial recognition, they should be applied on bases as consistent as possible with the fair value measurement objective (see paragraph 186 of the condensed version and paragraph 417 of the main discussion paper)? If not, please explain why.*

We do not agree that substitutes for fair value on initial recognition should be applied on a basis as consistent as possible with the fair value measurement objective, as we do not believe that estimates of fair values have superior relevance in these cases. If fair values cannot be estimated reliably, a substitute thereof may lack relevance.

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Question 18*— Do you agree with the proposed hierarchy for the measurement of assets and liabilities on initial recognition (see Chapter 8)? If not, please explain your reasons for disagreeing and what alternatives you might propose.*

We believe that responding to the above question on the proposed hierarchy would implicitly mean buying into the leading themes of the Discussion Paper. As we have serious concerns on some of these themes, we do not respond to the question.

Question 19*— do you have comments on any other issues or proposals, including the proposals for further research (see paragraph 189 of the condensed version and paragraph 441 of the main discussion paper)? If so, please provide them.*

We have no other further comments.

Stockholm 17 May 2006

Yours faithfully,
The Swedish Financial Accounting Standards Council

Dennis Svensson
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