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**International
Accounting Standards
Board**

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.

These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting: **December 2008, London**

Project: ***IAS 39 Financial Instruments: Recognition and Measurement***

Subject: **Fair value measurement of financial instruments (Agenda Paper 6C)**

Introduction

1. This paper presents and analyses suggestions that participants have raised in the roundtables held in November and December 2008 in response to the credit crisis with regard to (i) the level of detail and extent and (ii) the authority of guidance on fair value measurement of financial instruments.

2. This paper focuses on whether any of the accounting issues raised by participants require the urgent and immediate attention of the boards to improve financial reporting and help enhance investor confidence in financial markets. The paper addresses this objective by using the following structure:
 - (a) participant's suggestion:
 - (i) concern

 - (ii) proposed solution

(b) staff summary analysis

(c) staff recommendation

Issue 1: Level of detail and extent of guidance

Participant's concern

3. Some participants were concerned that existing guidance for determining fair values for financial instruments was not sufficiently detailed and extensive, in particular regarding the following aspects:
 - (a) how liquidity spreads should be included in calculating fair values
 - (b) what a hypothetical (willing) buyer is.
4. These issues arise in particular in the context of markets that are no longer active as a result of the credit crisis.

Proposed solution

5. Some participants suggested that more detailed guidance on these valuation aspects be issued.

Staff summary analysis

6. The staff acknowledges that it is difficult to determine the fair value of financial instruments in circumstances where markets are no longer active. This issue was raised with the IASB earlier this year. In response to the requests for enhanced valuation guidance the Board formed an expert advisory panel that comprised measurement experts from preparers, auditors, users, regulators and others.
7. In October 2008 the IASB issued a summary report on the panel's discussions (expert advisory panel report) that includes a section describing practices used for measuring financial instruments when markets are no longer active.

8. Also in October 2008 the IASB issued several press releases that confirmed its belief that fair value measurement guidance in accordance with IFRSs and US GAAP is already consistent, in particular regarding:
 - (a) the clarification made on 30 September 2008 by the Office of the Chief Accountant of the US Securities and Exchange Commission (SEC) and the staff of the FASB regarding fair value accounting on the basis of the fair value measurement guidance in FASB Statement of Financial Accounting Standards No. 157 *Fair Value Measurements* (SFAS 157).
 - (b) FASB Staff Position (FSP) FAS 157-3 issued on 10 October 2008, which amended SFAS 157 to add an illustrative example of the existing principles in SFAS 157. This FSP was issued in response to concerns that SFAS 157 did not provide sufficient guidance on how to determine fair value when there is no active market for a financial instrument.
9. The staff notes that there is a project on fair value measurement on the IASB's active agenda with an exposure draft expected to be issued in the first quarter of 2009.
10. The staff asked participants to be more specific regarding the extra guidance they believe necessary. Although no specific issues were identified during the round table meetings, the staff have also offered to talk directly to participants to understand areas of concern (in fact, one such meeting is already planned).

Staff recommendation

11. The staff will assess any requests for additional guidance (including liaising with the FASB to ensure continued convergence), and report to the Board as and when relevant.
12. **Question to the Board: Does the Board agree with the staff recommendation? If not, why and what do you propose instead?**

Issue 2: Authority of guidance on fair value measurement

Participant's concern

13. Some participants were concerned that the recently issued guidance on fair value measurement (refer to paragraphs 7–8 of this paper) lacks authority in the context of IFRSs. They noted that neither the expert advisory panel report nor the press releases were approved by the IASB. Therefore, this guidance does not constitute IFRS requirements.

Proposed solution

14. Some participants suggested that the Board should approve the recently issued guidance on fair value measurement in order to give it authority.

Staff summary analysis

15. The staff notes that the recently issued guidance on fair value measurement will in part become authoritative because of two active projects of the IASB:
 - (a) the project to amend IFRS 7 *Financial Instruments: Disclosures* in order to enhance disclosures regarding fair value and liquidity risk. In October 2008 the IASB issued an exposure draft *Improving Disclosures about Financial Instruments—Proposed amendments to IFRS 7*. A final standard is expected to be issued in the first quarter of 2009.
 - (b) the project on fair value measurement (refer to paragraph 9 of this paper).
16. The staff also notes that the recently issued guidance on fair value measurement has to a large extent the character of implementation guidance and illustrative examples. In accordance with the IASB's principle-based approach to standard setting implementation guidance and illustrative examples are not an integral part of IFRSs. Therefore, transforming the recently issued guidance in its entirety into IFRS requirements would be inappropriate.

17. There were also practical reasons why the recently issued guidance on fair value measurement, in particular the expert advisory panel report, was not transformed into IFRS requirements:
- (a) It would have been inappropriate to include ‘real life’ examples (including some from US GAAP preparers) in a formal IFRS standard or interpretation. However, not including these examples would have made the document less practice-oriented and, thus, less useful for its intended purpose.
 - (b) The process chosen provided the best opportunity for the panel members to contribute towards identifying valuation practices regarding determining fair value in the context of markets that are no longer active. As noted in the report, this means that the practices discussed are not only solutions and not even necessarily best practice. This prevents the report from simply being adopted as IFRSs.
18. The staff acknowledges that for US GAAP and SEC requirements similar guidance was issued with authority. In the staff’s view that reflects:
- (a) the different approach to standard setting and the regulatory circumstances in the US; and
 - (b) that the IASB is at a different stage in the standard setting process because it has not yet issued a standard or exposure draft on fair value measurement. Thus, issuing authoritative guidance now would prejudge the development of that standard.
 - (c) The staff also notes that while a few have called for more authoritative guidance, many others have requested that the IASB not produce more guidance. As noted in the expert advisory panel report, the panel members believe that the fair value measurement requirements in IAS 39 are generally clear, and it is inappropriate (and unhelpful in the context of an area that requires significant judgement, such as fair value measurement in an inactive market) to produce such authoritative guidance.

Staff recommendation

19. The staff recommends that the Board not make the expert advisory panel report authoritative IFRS literature. The staff believes that appropriate parts of that guidance will become authoritative in the very short-term anyway, because of the two active projects of the IASB.

20. **Question to the Board: Does the Board agree with the staff recommendation? If not, why and what do you propose instead?**