Project	**Fair Value Measurement**
Topic	**Considerations for re-exposure**

Purpose of this paper

1. In May 2009 the Board published the exposure draft *Fair Value Measurement*. The Board received 160 comment letters on the proposals. After the comment period, the project became a joint project with the FASB with the goal to publish converged fair value measurement guidance in the second half of 2010. Re-deliberations began, together with the FASB, in January 2010.
2. The boards have completed their discussions of the fair value measurement principles.
3. This paper asks the Board to consider whether there is a need to re-expose a draft IFRS on fair value measurement.

Considerations for re-exposure

4. The IASC Foundation *Due Process Handbook* states that when considering the need for re-exposure, the IASB:
   (a) identifies substantial issues that emerged during the comment period on the exposure draft that it had not previously considered
   (b) assesses the evidence that it has considered
   (c) evaluates whether it has sufficiently understood the issues and actively sought the views of constituents

This paper has been prepared by the technical staff of the FASB and the IASCF for discussion at a public meeting of the FASB or the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the FASB or the IASB.

Comments made in relation to the application of IFRSs or U.S. GAAP do not purport to be acceptable or unacceptable application of IFRSs or U.S. GAAP.

The tentative decisions made by the FASB or the IASB at public meetings are reported in FASB *Action Alert* or in IASB *Update*. Official pronouncements of the FASB or the IASB are published only after each board has completed its full due process, including appropriate public consultation and formal voting procedures.

(d) considers whether the various viewpoints were aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions in the exposure draft.

Decisions taken since the exposure draft was published

5. The appendix to this paper lists the tentative decisions the Board has reached in the light of the comments received on the exposure draft.

6. Most of the changes that the Board has made have been made in response to suggestions by respondents. However, there is one change that the Board did not discuss in the exposure draft—the Board's tentative decision to require a disclosure of the effect of interdependencies or correlation of inputs when relevant (as part of the sensitivity analysis disclosure).

7. The staff notes the following:

   (a) this information is not currently required in the fair value sensitivity analysis disclosure for financial instruments in IFRS 7 *Financial Instruments: Disclosures*. However, to meet the objective in IFRS 7 to help users of financial statements evaluate the significance of financial instruments for an entity's financial position and performance, it could be argued that if disclosure of the effect of correlation between inputs is important information for making that evaluation, then this disclosure is already required under IFRS 7 (this objective is similar to that proposed in the Fair Value Measurement exposure draft)

   (b) some preparers of financial statements note in their IFRS 7 sensitivity analysis disclosures that they have not taken into account correlation between inputs (which might imply that they think it is relevant information). For example, one preparer states in its fair value sensitivity disclosure that 'in reality, changes in one factor may contribute to changes in another, which may magnify or counteract the sensitivities'

   (c) few comments received on the exposure draft addressed sensitivity analysis disclosures specifically, but some of those that did suggested

that the disclosure would be more useful if it provided information about the correlation between inputs

(d) in our informal outreach on sensitivity analysis, users of financial statements indicated that the sensitivity analysis disclosure would be more useful if it provided information about the correlation between inputs

(e) the IASB's Expert Advisory Panel on illiquid markets states that an entity might consider explaining whether the effect of the sensitivity analysis reflects the movement in a single input or a movement in all observable inputs.

Staff comments

8. Aside from correlation, as discussed above, we did not identify any substantial issues that emerged during the comment period that the Board had not considered previously. Any issues that were raised in the comment letters were discussed by the Board in the redeliberations. For the contentious issues, the Board sought the views of constituents to understand the various viewpoints before redeliberating the issue.

9. The staff thinks the Board has the following options:

    (a) **Option 1**: publish a revised exposure draft of **all** of the tentative decisions reached on fair value measurement

    (b) **Option 2**: publish a **limited scope** exposure draft of the sensitivity analysis disclosure, including the effect of correlation

    (c) **Option 3**: not re-expose

10. If the Board selects Option 1 or Option 2, the publication of an IFRS on fair value measurement will be delayed by the length of the comment period and the resulting comment letter analysis.

11. The following table summarises the timing of Options 1 and 2.

	Option 1: Full re-exposure	Option 2: Limited scope re-exposure
Timing	Publication of a final IFRS would be delayed by 5-6 months due to publication time and comment period (the exposure draft comment period was 120 days)	Timing would not be affected if the exposure period matches that of the FASB (the FASB staff has recommended 45 days; the FASB will decide on 31st March). However, it is more likely that the IASB will need to give a minimum of 90 days.

12. It is not clear to the staff that adding the effect of correlation to the sensitivity analysis disclosure is a change sufficient to warrant re-exposure.

Question 1
Which option in paragraph 9 does the Board wish to proceed with, and why?

13. The remainder of this paper is relevant only if the Board selects Option 2 or Option 3.

Process for finalising an IFRS on fair value measurement

14. If the Board selects Option 2 or Option 3, the staff thinks it is necessary to give possible respondents an opportunity to see and comment on the tentative decisions reached in the project.

15. The staff thinks this can be done by posting a Request for Views on the IASB website. The Request for Views could ask for feedback on the FASB's proposed amendments to FASB Accounting Codification Topic 820 (Fair Value Measurements and Disclosures), particularly where those proposals differ from the IASB's exposure draft (some of which are set out in the appendix to this paper).

16. After the FASB's exposure period ends, the IASB and FASB staff will analyse the comments received on the proposed ASU (and the IASB's Request for Views, if applicable). Those comments will form the basis for the re-deliberations, which the FASB and IASB will carry out together. The IASB will discuss effective date and transition requirements during those re-deliberations.

17. As a result, this paper does not ask the Board for permission to prepare a ballot draft of a final IFRS at this time. The Board will ballot the standard after the re-deliberations following the FASB's exposure period.

Question 2
Does the Board have any comments or suggestions about the process for finalising an IFRS on fair value measurement?

Appendix – Tentative decisions reached in the fair value measurement project

Topic	Tentative decision	Comparison with exposure draft proposals
1. Scope	**IFRS 2** Items within the scope of IFRS 2 *Share-based Payment* will be excluded from the scope of the fair value measurement standard, but IFRS 2 will retain the term 'fair value'. **IAS 17** Items within the scope of IAS 17 *Leases* will be excluded from the scope of the fair value measurement standard, but IAS 17 will retain the term 'fair value'. (March 2010) **Other** IFRS 3 *Business Combinations* will retain the term 'fair value' when referring to the measurement of reacquired rights. IAS 39 *Financial Instruments: Recognition and Measurement* will retain the term 'fair value' for measuring financial liabilities with a demand feature. IAS 19 *Employee Benefits* will retain the measurement of the reimbursement rights as the present value of the related obligation, but it will not describe that approach as a practical expedient for determining fair value.	**IFRS 2** Commentators found the term 'market based value' inconsistent with the measurement principles for some share-based payment transactions. **IAS 17** Commentators were concerned that an exit price notion might result in practice issues with lease classification. **Other** This is labelled as a measurement exception in IFRS 3. No further change was deemed to be necessary. IAS 39 states that for this purpose fair value is deemed to include the effect of the deposit floor. IAS 19 states that for this purpose fair value is deemed to be the present value of the related obligation. It is not described in IAS 19 as a practical expedient.
2. Definition of fair value	Fair value is the price that would be received to sell an	No change.

Topic	Tentative decision	Comparison with exposure draft proposals
	asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (January 2010)	
3. Reference market	The reference market for a fair value measurement is the principal (or most advantageous) market provided that the entity can access that market.	The exposure draft proposed that a fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place in the **most advantageous market** to which the entity has access.
	The principal market is the market with the greatest volume and level of activity for the asset or liability.	No change.
	There is a presumption that the principal market is the market in which the entity normally transacts. Entities do not need to perform an exhaustive search for markets that might have more activity than the market in which they normally transact.	Change in reference to principal market rather than most advantageous market, consistent with the Board's decision about the reference market.
	The determination of the most advantageous market considers both transaction costs and transportation costs. (January 2010)	No change.
4. Market participant view	A fair value measurement is market-based and reflects the assumptions that market participants would use in pricing the asset or liability.	No change.
	Market participants should be assumed to have a reasonable understanding about the asset or liability and the transaction based on all available information, including information that might be obtained through due diligence efforts that are usual and customary.	Clarifies that market participants do not all have the same level of information as each other or the reporting entity.

Topic	Tentative decision	Comparison with exposure draft proposals
	‘Independence’ in the description of market participants means that market participants are independent of each other; that is, they are not related parties.	No change.
	A price in a related party transaction may be used as an input to a fair value measurement if the transaction was entered into at market terms.	Clarifies a point that was implicit in the exposure draft.
	The unobservable inputs derived from an entity’s own data, adjusted for any reasonably available information that market participants would take into account, are considered market participant assumptions and meet the objective of a fair value measurement. (January 2010)	Clarifies a point that was implicit in the exposure draft.
5. Highest and best use	A fair value measurement of a non-financial asset considers its highest and best use by market participants.	No change.
	The highest and best use concept is relevant only for non-financial assets and is not relevant for liabilities or financial assets. The final standard will describe the meaning of physically possible, legally permissible, and financially feasible.	No change.
	Entities do not need to separate the fair value of an asset group into two components when an entity uses an asset in a way that differs from its highest and best use.	Commentators found this proposal (which is not in Topic 820) confusing and inconsistent with other fair value measurement principles.
	Entities will be required to disclose information about when they use an asset in a way that differs from its highest and best use (and that asset is recognised at fair value based on its highest and best use). (February 2010)	No change.

Topic	Tentative decision	Comparison with exposure draft proposals
6. Valuation premise	The concept of valuation premise is only relevant for non-financial assets and is not relevant for liabilities or financial assets.	No change for liabilities. For financial assets, does not change the result proposed in the exposure draft (see 'Offsetting market risks' and 'Offsetting counterparty credit risk' below). The clarification on financial assets was made in response to comments received on the exposure draft
	The final standard will describe the objective of the valuation premise without using the terms *in-use* and *in-exchange* because those terms are often misunderstood.	Commentators found the terminology confusing.
	The objective of a fair value measurement of an individual asset is to determine the price for a sale of that asset alone, not for a sale of that asset as part of a group of assets or business.	No change.
	When the highest and best use of an asset is to be used as part of a group of assets, the fair value measurement of that asset presumes that the sale is to a market participant that has, or can obtain, the 'complementary assets' and 'complementary liabilities'.	No change.
	Complementary liabilities include working capital but do not include financing liabilities. (February 2010)	Clarifies a point that was implicit in the exposure draft.
7. Liabilities	In the absence of a quoted price in an active market representing the transfer of a liability, an entity measures the fair value of a liability as follows: 1. Use the quoted price of the identical liability when traded as an asset (ie a Level 1 measurement), if that price is available.	Clarifies the principle in the exposure draft (it is not a new approach) and is consistent with Topic 820's approach. The measurement of liabilities was discussed in the round-table meetings.

Topic	Tentative decision	Comparison with exposure draft proposals
	2. If that price is not available, use quoted prices for similar liabilities or similar liabilities when traded as assets (ie a Level 2 measurement). 3. If observable inputs are not available, use another valuation technique such as: (a) an income approach (eg a present value technique), or (b) a market approach (eg using the amount that a market participant would pay to transfer the identical liability or receive to enter into the identical liability).	
	In the application of a present value technique, the final standard will describe the compensation a market participant would demand for taking on an obligation.	Commentators asked for more guidance on this.
	The transfer of a liability assumes that a market participant transferee has the knowledge and ability to fulfil the identical obligation.	Clarifies a point that was implicit in the exposure draft.
	An entity must determine whether the fair value of a liability when traded as an asset (the corresponding asset) represents the fair value of the liability. If an entity determines that the fair value of the corresponding asset does not represent the fair value of the liability, it must adjust the fair value of the asset accordingly.	Commentators found the exposure draft to be too restrictive on using the fair value of the corresponding asset in all cases. The revised requirement is consistent with the approach in Topic 820.
	The fair value of a corresponding asset represents the fair value of the liability whether or not that asset is traded on an exchange. The fair value of the corresponding asset	Clarifies a point that was implicit in the exposure draft.

Topic	Tentative decision	Comparison with exposure draft proposals
	should be measured using the methodology market participants would use.	
	A quoted price for a corresponding asset in an active market is also a Level 1 fair value measurement for the liability when no adjustments to that quoted price are required.	This was not explicit in the exposure draft but is consistent with Topic 820.
	The fair value of a liability includes the effect of non-performance risk, which represents credit risk or the risk that the entity will not be able to perform the obligation.	No change.
	The final standard will clarify what is included in non-performance risk, in addition to credit risk.	Commentators requested more guidance about non-performance risk.
	The fair value of a liability should not be further adjusted for the effect of a restriction on its transfer if the restriction is already included in the other inputs to the fair value measurement. (January 2010)	This was not explicit in the exposure draft but is consistent with Topic 820.
8. Own equity	The final standard will include guidance for measuring the fair value of an entity's own equity instruments. (January 2010)	No change.
9. Fair value at initial recognition	The transaction price might not represent the fair value of an asset or liability at initial recognition if, for example, any of the following conditions exist: • the transaction between related parties • the transaction takes place under duress or the seller is forced to accept the price in the transaction	Clarifies the proposal in the exposure draft.

Topic	Tentative decision	Comparison with exposure draft proposals
	• the unit of account represented by the transaction is different from the unit of account for the asset or liability measured at fair value • the market in which the transaction takes place is different from the market in which the entity would sell the asset or transfer the liability. (January 2010)	
10. Blockage factors	A fair value measurement prohibits the application of a blockage factor at any level of the fair value hierarchy. A fair value measurement in Levels 2 and 3 of the fair value hierarchy considers other premiums and discounts (except for a blockage factor) that market participants would consider in pricing an asset or liability at the unit of account specified in the relevant standard. (February 2010)	No change. There is confusion about what a 'blockage factor' is. Commentators were concerned that a fair value measurement does not include any discounts or premiums.
11. Offsetting market risks	The final standard will permit an exception to fair value measurement principles by permitting entities to use mid prices as a basis for establishing fair values for offsetting market risk positions (eg interest rate risk, currency risk or other price risk) and to apply the price within the bid-ask spread that is most representative of fair value to the net open risk position. To use this exception, an entity must: • manage its financial instruments on the basis of the net open risk positions in accordance with the entity's documented risk management strategy, and • manage the net open risk position in a consistent	Commentators were concerned that the unit of account in IAS 39 prevented them from considering the net open position to market risks. This approach is consistent with practice for entities applying IAS 39.AG72.

Topic	Tentative decision	Comparison with exposure draft proposals
	manner from period to period. In addition, the market risks that are being offset must be substantially the same, the financial instruments must share common characteristics and the financial instruments must be measured at fair value on a recurring basis. (March 2010)	
12. Counterparty credit risk	Entities are permitted to consider offsetting counterparty credit risk positions when measuring the fair value of financial instruments when there is a legally enforceable right of offset (eg a master netting agreement) with the counterparty in the event of default. (March 2010)	Commentators were concerned that the unit of account in IAS 39 prevented them from considering the net open position with a particular counterparty. This approach is consistent with practice for entities applying IAS 39.AG72.
13. Inactive markets	The guidance for measuring fair value in markets that have become less active pertains to when there has been a significant decline in the volume and level of activity for the asset or liability, not to when a market has always been inactive. The guidance focuses on whether an observed transaction price is orderly, not on the level of activity in a market. An entity should consider observable transaction prices unless there is evidence that the transaction is not orderly. If an entity does not have sufficient information to determine whether a transaction is orderly, it performs further analysis to measure fair value. (January 2010)	Commentators preferred to focus on when there has been a significant decline in market activity rather than when a market has always been inactive. This is consistent with the approach in Topic 820. Clarifies a point that was implicit in the exposure draft. Clarifies that an entity cannot conclude that a transaction is not orderly simply because it does not have sufficient information to make that determination.
14. Disclosures	The term ‘class’ will be defined on the basis of the following principles: • an entity should determine the appropriate classes of assets and liabilities based on the nature,	Commentators asked for more guidance about the meaning of class. This is consistent with the approach in Topic 820.

Topic	Tentative decision	Comparison with exposure draft proposals
	characteristics and risks of the assets and liabilities and their classification in the fair value hierarchy; • a class of assets and liabilities often will require greater disaggregation than the entity's line items in the statement of financial position; and • judgment is needed to determine the appropriate classes of assets and liabilities.	
	An entity will not be required to disclose information about the change in the nonperformance risk of a non-financial liability.	This requirement will remain in IFRS 7.
	An entity will be required to disclose its policy for determining when transfers between levels of the fair value hierarchy are recognised.	Commentators asked for more guidance on this. This is consistent with Topic 820.
	An entity will be required to disclose information about fair value measurements only after initial recognition.	Clarifies a point that was implicit in the exposure draft as other standards indicate the disclosures required at initial recognition of an asset or liability.
	For assets and liabilities that are recognised at fair value at each reporting period, an entity will be required to disclose a reconciliation of activity within Level 3 of the fair value hierarchy and information about transfers between Levels 1 and 2.	No change.
	An entity will be required to disclose fair value information by level in the fair value hierarchy for items that are not measured at fair value in the statement of	No change.

Topic	Tentative decision	Comparison with exposure draft proposals
	financial position	
	The final standard will not include guidance for assessing the significance of an input or significant changes in fair value.	No change.
	An entity will be required to disclose information about fair value measurements for financial instruments in an entity's interim financial statements.	No change.
	The final standard will require a sensitivity analysis disclosure for all Level 3 fair value measurements unless another standard does not require such a disclosure.	The exposure draft proposed such a disclosure for all fair value measurements. The tentative decision limits it to fair value measurements for which the Board determines it will provide relevant information.
	The objective of the sensitivity analysis disclosure is to provide users of financial statements with information about measurement uncertainty for Level 3 fair value measurements. That is, the disclosure does not represent a worst-case scenario and is not forward looking.	Commentators were confused about the objective of providing a sensitivity analysis about Level 3 fair value measurements. (Please note: this is different from the disclosure requirement about exposures to market risk in paragraphs 40-41 of IFRS 7.)
	The sensitivity analysis disclosure should consider the effect of the correlation between inputs, when relevant. (March 2010)	The Board did not discuss this in the exposure draft.