DUTCH ACCOUNTING STANDARDS BOARD (DASB)

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Date : Amsterdam, 17 April 2007
Re : **Comment on Discussion Paper Fair Value Measurements**

Dear Sirs,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to respond on your draft comment letter on the IASB's Discussion Paper Fair Value Measurements.

We support the IASB's objectives to (i) establish a single source of guidance for all fair value measurements required by IFRSs, (ii) clarify the definition of fair value and related guidance in order to communicate the measurement objective, and (iii) enhance disclosures about fair value.

In general we are of the opinion that the provisions of SFAS 157 are an improvement on the disparate guidance in IFRS. However, we stress that the fair value measurement objective and definition of fair value should not apply to all standards that currently use the term fair value. We believe the distinction between initial and subsequent measurement at fair value makes sence. Therefore, we are of the opinion that an exit price definition of fair value should not apply to initial recognition.

We share your concern that it's more important to identify and define the candidate measurement bases and criteria first. A comprehensive view on the various types of fair value and other types of current values is required. Only then can we have a fully informed and coherent debate about the circumstances in which the market-based exit price described in the paper should be used.

In the appendix of our response we have commented on the respective questions and comments in detail.

Yours sincerely,

Hans de Munnik
Chairman DASB

Appendix

Q1 In your view, would a single source of guidance for all fair value measurements in IFRSs both reduce complexity and improve consistency in measuring fair value? Why or why not?

We agree with your comments. However, we do not fully agree with the last sentence of paragraph A2.3. This suggests that an exit price is only an appropriate measure when markets are liquid and supply and demand are more or less in equilibrium. For initial recognition we agree with the above statement. For subsequent measurement we believe that an exit price can be an appropriate measure if and only if the measurement reliability criteria are satisfied. Therefore, we suggest to ask the Board for specific guidance to assess when fair value measurement (exit price) reliability criteria are satisfied and when not.

Q2 Is there fair value measurement guidance in IFRSs that you believe is preferable to the provisions of SFAS 157? If so, please explain.

We prefer the guidance in paragraph AG 76 of IAS 39 instead of the provisions of paragraphs 16 and 17 of SFAS 157. We believe that for initial recognition the transaction price (entry price) is the best evidence of fair value in the absence of observable market information or evidence to the contrary, as discussed in paragraph AG76 of IAS 39. See also our answer to Q11.

Currently it's not clear if IFRS 2 will be excluded in its entirety from the scope of the general guidance on fair value measurements. If the proposed fair value measurement guidance will apply to fair value measurements of share-based payments, we believe that parts of the current guidance on fair value measurements in IFRS 2 is more specific directed to fair value measurement of share-based payments.

We do not agree with your comment about the length of the guidance in SFAS 157 (A2.6). We believe that the guidance of SFAS 157 is not too extensive and is necessary to understand the measurement objective. Your comment relating to the length of the guidance is somewhat contradictory to your answer to question 25.

Q3 Do you agree that fair value should be defined as an exit price from the perspective of a market participant that holds the asset or owes the liability? Why or why not?

We agree with your comment that the IASB should consider per standard whether to use market-based prices or entity-specific values and when to use an exit price measurement objective or an entry price measurement objective. SFAS 157 gives only guidance for market-based exit values. Although we agree with the guidance in SFAS 157 for market-based exit price measurements, we do not believe that an market-based exit price definition of fair value should be applied to all existing IFRSs that currently refer to fair value. However, if for a certain asset or liability is decided that a market-based measurement is appropriate, we believe that for initial recognition an entry price and for subsequent recognition an exit price should be applied. We believe that for initial recognition the transaction price (entry price) is the best evidence of fair value in the absence of observable market information or evidence to the contrary. For subsequent measurement an exit price objective from the perspective of a market partcipant is appropriate, because it embodies current expectations about the future inflows associated with the asset and the future outflows associated with the liability from the perspective of market participants. The emphasis on inflows and outflows is consistent with the definitions of assets and liabilities in the IASB's Framework. Paragraph 49 of the IASB's Framework defines assets in terms of future inflows (economic benefits expected to flow to the entity) and liabilities in terms of future outflows (expected outflow form the entity of resources embodying economic benefits).

Q4 Do you believe an entry price also reflects current market-based expectations of flows of economic benefit into or out of the entity? Why or why not? Additionally, do you agree with the view that, excluding transaction costs, entry and exit prices will differ only when they occur in different markets? Please provide a basis for your views.

We do not agree with your comment that usually an exit price and an entry price on the same market (active and less active markets) will be different. In active markets with quoted prices or observable inputs other than quoted prices we believe that usually an exit price and an entry price will be the same. However, in the absence of observable market information it will be difficult to prove that an entry price is the same as or different from an exit price. Therefore, an entry price should be used for the initial recognition of assets and liabilities, because we believe that for initial recognition the transaction price (entry price) is the best evidence of fair value (exit price) in the absence of observable market information or evidence to the contrary.

Q5 Would it be advisable to eliminate the term 'fair value' and replace it with terms, such as 'current exit price' or 'current entry price', that more closely reflect the measurement objective for each situation? Please provide a basis for your views.

We agree with your views. We believe that it's necessary to eliminate the general term "fair value" and to describe the different measurement objectives as precise as possible. Terms such as "market-based exit price" and "market-based entry price" reflect more closely the measurement objective for each situation than the somewhat vague term "fair value".

It's conceptually confusing that the term fair value is reserved exclusively for the exit price measurement objective. Although SFAS 157 explains that in the same market the exit price will equal the entry price, it at least suggests that only an exit price can be a "fair value" (a value based on market expectations).

It will be necessary to review each standard and interpretation in existing IFRSs whether fair value means an exit price or an entry price.

Q6 Does the exit price measurement objective in SFAS 157 differ from fair value measurements in IFRSs as applied in practice? If so, which fair value measurements in IFRSs differ from the measurement objective in SFAS 157? In those circumstances, is the measurement objective as applied in practice an entry price? If not, what is the measurement objective applied in practice? Please provide a basis for your views.

We agree with your comments. Our understanding is also that many of the fair value references in existing IFRSs are not regarded as market-based exit prices.

In current practise in the Netherlands both under IFRSs as under Dutch GAAP fair value is generally considered an entry price (transaction price) for initial recognition. Under Dutch GAAP (Dutch Civil Code) a reporting entity is required to use an entry value (current cost) for subsequent measurement of tangibles, intangibles and inventories under the revaluation model. It's possible that in practise this approach is also applied to the fair value measurement of property, plant and equipment under IFRSs.

Another impression of current practise in the Netherlands is that the concept of different markets is not applied. Although this is conceptually not in line with SFAS 157, it will in general not lead to differences, because we believe that in most situations the entry price and the exit price will be the same.

Q7 Do you agree with how the market participant view is articulated in SFAS 157? Why or why not?

Yes, we agree with your concerns. However, we believe that these concerns relating to subjectivity in case of absence of observable market information should be dealt with by formulating specific guidance to assess when fair value measurement reliability criteria are satisfied and when not.

We believe that the market participant view is indeed generally consistent with the concepts of a knowledgeable, willing party in an arm's length transaction that are currently contained in IFRSs.

We are also of the opinion that the definition of market participants articulated in SFAS 157 is more specific and puts more stress on the requirements that market participants are not related parties to the reporting entity and are able to transact for the asset or liability.

Q8 Do you agree that the market participant view in SFAS 157 is consistent with the concepts of 'knowledgeable, willing parties' and 'arm's length transaction' as defined in IFRSs? If not, how do you believe they differ?

We do not agree that the market participant view is much more restrictive as the current concepts of "knowledgeable, willing parties" and "arms's length transaction". The example which is given in the draft comment letter is in our opinion not very strong, because we believe that under the current concepts to measure fair value within IFRSs a reporting entity should not consider transactions between related parties. This does not mean that a transaction between related parties can't be at fair value. However, the notion "at arm's length" is in our view intended to describe transactions between unrelated parties.

Q9 Do you agree that the fair value of a liability should be based on the price that would be paid to transfer the liability to a market participant? Why or why not?

From a conceptually point of view we agree. The fair value of a liability from the perspective of a market participant is the same regardless of how the reporting entity intends to settle the liability. The term "transfer" describes more accurately the fair value measurement objective in IFRSs. We agree with the arguments given by the IASB in paragraphs 23 and 24 of the Invitation to Comment. However, if the contract cannot be transferred then determining a transfer value is quite theoretical and will be quite difficult. Furthermore, in these kind of situations we do not believe that measuring liabilities at fair value based on the theoretical price that would be paid to transfer the liability.

Q10 Does the transfer measurement objective for liabilities in SFAS 157 differ from fair value measurements required by IFRSs as applied in practice? If so, in practice which fair value *measurements under IFRSs differ from the transfer measurement objective in SFAS 157 and how do they differ?*

We agree with your comment. It's also our understanding that the fair value of liabilities is measured in practice using a settlement measurement objective.

Q11 In your view is it appropriate to use a measurement that includes inputs that are not observable in a market as fair value at initial recognition, even if this measurement differs from the transaction price? Alternatively, in your view, in the absence of a fair value measurement based solely on observable market inputs, should the transaction price be presumed to be fair value at initial recognition, thereby potentially resulting in the deferral of day-one gains and losses? Please give reasons for your views.

We agree with the comments in the draft comment letter. In our view it is not appropriate to use a measurement that includes inputs that are not observable in a market as fair value at initial recognition instead of a different transaction (entry price). We believe that in the absence of a fair value measurement based solely on observable market inputs, the transaction price (entry price) should be presumed to be the fair value (exit price) at initial recognition, if there is no difference in markets, thereby potentially resulting in the deferral of day-one gains and losses. The transaction price (entry price) is the best evidence of fair value (exit price) in the absence of observable market information or evidence to the contrary, as discussed in paragraph AG76 of IAS 39. Therefore, we do not fully agree with the provisions of paragraphs 16 and 17 of SFAS 157.

Q12 Do you believe that the provisions of SFAS 157, considered in conjunction with the unit of account guidance in IAS 39, would result in a portfolio-based valuation of identifiable risks of instruments considered in aggregate, or an in-exchange exit price for the individual instruments? Please give reasons for your views.

We agree with your comments in the draft comment letter.

We believe that the provisions of SFAS 157, considered in conjunction with the unit of account guidance in IAS 39, can result in a portfolio-based valuation of identifiable risks of instruments considered in aggregate and not result in an in-exchange exit price for the individual instrument.

The reason for this view is that SFAS 157 does not specify the unit of account for an instrument that trades in a market that is not active (Level 2 and Level 3). Only for Level 1 fair value measurements, the unit of account for an instrument is the individual trading unit.

Q13 Do you agree that a fair value measurement should be based on the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability? Why or why not?

We agree with your comments. The fair value should be determined by reference to the principal market, i.e. the market in which the reporting entity most usually transacts. We also believe that it is important that a reporting entity need not continuously monitor multiple markets in order to determine which market is the most advantageous at the measurement date.

Q14 Do you agree that a fair value measurement should consider attributes specific to the asset or liability that market participants would consider in pricing the asset or liability? If not, why?

Yes, we agree with your comment in paragraph A2.49. We also share your concerns formulated in paragraphs A2.50-51.

Q15 Do you agree that transaction costs that would be incurred in a transaction to sell an asset or transfer a liability are an attribute of the transaction and not of the asset or liability? If not, why?

We do not fully agree with your comments. Transaction costs are an attribute of the transaction and not an attribute of the asset or liability. They should be considered separately from fair value, which is consistent with current IFRSs.

Q16 Do you agree that the risk of non-performance, including credit risk, should be considered in measuring the fair value of a liability? If not, why?

We agree with your comments. Although the risk that an obligation will not be satisfied by the reporting entity (non-performance risk including credit risk) effects the value at which that obligation would be transferred, we are of the opinion that this approach does not result in useful information.

Q17 Is it clear that the 'in-use valuation premise' used to measure the fair value of an asset in SFAS 157 is different from 'value in use' in IAS 36? Why or why not?

Yes, we agree. It is clear that the "in-use valuation premise" used to measure the fair value of an asset in SFAS 157 is different from "value in use" in IAS 36. It is explained that "Value in use" in IAS 36 does not result in a fair value measurement because the "value in use" is an entity-specific measurement and not a market-based measurement.

Q18 Do you agree with the hierarchy in SFAS 157? If not, why?

Yes, we agree with the hierarchy in SFAS 157. We do not understand your comments made in paragraph A2.60 sub b and c. Our view is that the proposed fair value hierarchy provides a basis for disclosing the quality of fair values.

Q19 Are the differences between the levels of the hierarchy clear? If not, what additional information would be helpful in clarifying the differences between the levels?

We agree with your comments. We also want to add the following comment. SFAS 157 does not define the unit-of-account for assets or liabilities measured at fair value except in Level 1 of the hierarchy. It is not fully clear to us why this difference is created. We believe that the unit-of-account should be the same for all levels of the hierarchy.

Q20 Do you agree with the provision of SFAS 157 that a blockage adjustment should be prohibited for financial instruments when there is a price for the financial instrument in an active market (Level 1)? In addition, do you agree that this provision should apply as a principle to all levels of the hierarchy? Please provide a basis for your views.

We have had extensive discussions about this issue. We are also not convinced that blockage adjustments should be forbidden. We want to add that in case of control it's very likely that the reporting entity will sell the controlled investment as a block to receive the control premium. In that situation we believe that P x Q does not lead to a market-based exit value. Therefore, we believe that in case of control there is reason to allow an exception to P x Q.

However, if the blockage adjustment relates to illiquidity of the market it's not very likely that the investment will be sold as a block if this leads to a lower price than the current market price. Therefore, in that situation we see less reasons to allow the exception to P x Q.

Q21 Do you agree that fair value measurements should be determined using the price within the bid-ask spread that is most representative of fair value in the circumstances, as prescribed by paragraph 31 of SFAS 157? Alternatively, do you believe that the guidance contained in IFRSs, which generally requires assets to be valued at the bid price and liabilities at the ask price, is more appropriate? Please explain the basis for your view.

We believe that fair value measurements should be determined using the price within the bid-ask spread that is most representative of fair value in the circumstances, provided that the price is consistently determined. Although a single bid-ask spread pricing method could maximize the consistency and comparability of fair value measurements, we are of the opinion that the resulting measurements would not be relevant in all situations. Therefore, reporting entities should use judgement in meeting the fair value measurement objective.

We suggest to introduce a presumption that in meeting the fair value measurement objective for assets and liabilities in very liquid markets, the appropriate quoted market price for an asset held is usually the current bid price and for a liability held the ask price.

We do not agree with your view that SFAS 157 is inconsistent on this issue. The price within the bid-ask spread that is most representative of fair value is not based on entity-specific circumstances, but is based on market-based information.

Q22 Should a pricing convention (such as mid-market pricing or bid price for assets and ask price for liabilities) be allowed even when another price within the bid-ask spread might be more representative of fair value? Why or why not?

We do not fully agree with your view. The principle should be that fair value measurements should be determined using the price within the bid-ask spread that is most representative of fair value in the circumstances and meets the information objectives as best as possible. Therefore, reporting entities should be obliged to use judgment in meeting the fair value objective.

However, we do agree with your view that for impracticability reasons (if costs > benefits) a reporting entity should be allowed to use a pricing convention.

Q23 Should bid-ask pricing guidance apply to all levels of the hierarchy, including when the fair value measurement includes unobservable inputs? Why or why not?

Yes. Bid-ask pricing guidance should apply to all levels of the hierarchy. This will lead to consistency between fair value measurements using bid and ask prices within Level 1 and fair value measurements using bid and ask prices within other levels of the hierarchy.

Q24 Do the disclosure requirements of SFAS 157 provide sufficient information? If not, what additional disclosures do you believe would be helpful to users and why? Alternatively, are there disclosures required by SFAS 157 that you believe are excessive or not beneficial when considered in conjunction with other disclosures required by IFRSs? Please provide a basis for your view.

The required disclosures about fair value measurements provide information that is useful to users of financial statements. The required disclosures enable users of financial statements to assess the extent to which fair value is used to measure assets and liabilities in periods subsequent to initial recognition and the inputs used for fair value measurements. Information about inputs allow users of financial statements to assess the relative reliability of the fair value measurements.

Q25 Does the guidance in Appendices A and B of SFAS 157 sufficiently illustrate the standard's principles and provisions as they would apply under IFRSs? If not, please specify what additional guidance you believe is needed and why.

We agree with the proposed additional illustrative examples.

Q26 Does the guidance in Appendices A and B of SFAS 157 sufficiently illustrate the standard's principles and provisions as they would apply in emerging or developing markets? If not, please specify what additional guidance you believe is needed and the most effective way to provide this guidance (for example, through additional implementation guidance or through focused education efforts).

We agree with your comment.

Q27 Please provide comments on any other matters raised by the discussion paper.

We suggest to insert general guidance to assess when (fair value) measurement reliability criteria are satisfied and when not.