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Paris, the 6th January 2012

Madame Françoise FLORES
Chairman
EFRAG –European Financial Reporting Advisory Group

35 Square de Meeûs
B – 1000 BRUSSELS

Re : EFRAG Draft endorsement advice IFRS 13 Fair value measurement

Dear Mrs Flores,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned draft endorsement advice.

Our main concern is that this new standard on fair value measurement fails to address the main accounting issues raised by the financial crisis and the requests made by the G20 and ECOFIN to “improve standards for the **valuation of financial instruments** based on their **liquidity** and investors’ holding horizons”.

Hence, we are concerned that the new guidance does not take sufficiently into account the lessons learned from the crisis regarding the measurement of financial instruments in illiquid markets mainly in the following situations :

1. When financial markets (essentially for objective, technical reasons) are structurally **not able to provide a reliable information** (e.g. complex financial products such as CDO squared) ;
2. When financial markets become, **temporarily**, **unable to provide a reliable information** due to specific situations or events (e.g. current market environment of sovereign debts)

The lack of consensus, last summer, on the fact that some sovereign bond markets are active or inactive obviously demonstrate that IFRS 13 is not helpful to improve consistency and that some clarifications are needed on this issue in IFRS 13.

Moreover, beyond this obvious lack of response to the crisis, we consider that this standard is too conceptual to be workable in practice by using theorical notions such as “exit prices”, “hypothetical markets”, “highest and best use”.

The IASB should have launched a public consultation on the result of its standard-by-standard review of the references to fair value in IFRS in order to assess whether the term “fair value” as defined by IFRS 13 is still relevant in the context of a specific standard. Indeed, we believe that revising the definition of fair value, where currently used in IFRS, and defining it as an exit price, without discussing the measurement objective and the measurement basis of the standards affected, in light of the needs of financial statements users, may lead to conclusions that are not necessarily the most relevant. Such consultation not having taken place, we consider that it should now be undertaken.

For all the reasons stated above, we disagree with EFRAG’s draft conclusion on the assessment that IFRS 13 Fair value measurement satisfies the endorsement criteria. We consider, on balance, that the European Commission should not endorse IFRS 13 as currently stated.

Our detailed comments on the draft advice are set out in the Appendix I to this letter.

If you have any questions concerning our comments, we would be pleased to discuss them.

Yours sincerely,

Jérôme HAAS

Appendix I
Detailed comments

1 *EFRAG's initial assessment of IFRS 13 is that it meets the technical criteria for endorsement. In other words, it is not contrary to the principle of true and fair view and it meets the criteria of understandability, relevance, reliability and comparability. EFRAG's reasoning is set out in Appendix 2.*

(a) *Do you agree with this assessment?*

☐ *Yes* ☒ *No*

If you do not, please explain why you do not agree and what you believe the implications of this should be for EFRAG's endorsement advice.

(b) *Are there any issues that are not mentioned in Appendix 2 that you believe EFRAG should take into account in its technical evaluation of IFRS 13? If there are, what are those issues and why do you believe they are relevant to the evaluation?*

As a preliminary remark, we remain convinced that the debate on how to define fair value cannot be dissociated from the debate on when fair value is a relevant measurement basis. The issue of when to use fair value is an essential consideration in order to ensure that the measurement is determined in a manner which is consistent with the objective of using fair value in the first place.

The ANC disagrees with the EFRAG's initial assessment of IFRS 13 regarding the following criteria :

Relevance

The definition of fair value in IFRS 13 reflects only an exit price notion. We consider that limiting the concept of fair value to such a specific notion may not be relevant for <u>all</u> assets and liabilities. Namely, a distinction should be drawn between financial and non financial assets and liabilities that are different by nature. For instance, for financial assets and liabilities, an exit price is relevant only for those that are effectively actively traded by the entity as it better reflects the future cash flows associated with the business model. On the opposite, in the case of a business combination where it is necessary to allocate the transaction price to the individual assets and liabilities acquired, while the exit price may be considered a reasonable proxy for some items, we are not convinced that this would necessarily be the case for all items.

Having not done so previously, the IASB should launch a public consultation on the result of its standard-by-standard review of the references to fair value in IFRS in order to assess whether the term "fair value" as defined by IFRS 13 is still relevant in the context of a specific standard. Indeed, we believe that revising the definition of fair value, where currently used in IFRS, and defining it as an exit price, without discussing the measurement objective and the measurement basis of the standards affected, in light of the needs of financial statements users, may lead to conclusions that are not necessarily the most relevant.

We are also of the view that IFRS 13 presumes that efficient markets are available for most assets and liabilities. We believe, as it has been further illustrated by the recent financial crisis, that markets are not efficient and hence that the concept underlying this standard and the relevance of a fair value measurement can be challenged.

Lastly, the ANC observes that IFRS 13 is too conceptual. As a result it may be unworkable in certain circumstances. Indeed, for financial and non-financial assets and liabilities that are not quoted on active markets (i.e. most of assets and liabilities), it requires preparers to assess a fair value reflected in a theorical market with hypothetical market participants assuming a hypothetical highest and best use.

Reliability

We observe that level 3 measurement contains a significant amount of unobservable inputs, i.e. entity-specific assumptions on what a hypothetical market would be. As such, we question how the Board reconciles this fact with the conclusion that such a measurement does in fact represent a reliable exit price measurement.

In fact, we are definitely not convinced that a measurement based on a hypothetical market participant on a hypothetical market can be considered as a reliable market value, due to the level of entities' own assumptions involved. In any case, we still consider that level 3 measurements (which contain significant entities' own assumptions on hypothetical markets and liquidity) are very far from a reliable market value and remain convinced that additional work should be done on these topics in order to clarify how entities should measure items that are not traded in active markets. The recognition of the change in unreliable fair value of level 3 financial instruments in profit or loss (such as CDOs) has indeed raised major issues during the recent financial crisis, which have not yet been addressed by the Board. We also observe that IFRS 13 does not consider the possibility of a reliability threshold or a practicability exception for the measurement of fair value. We remain convinced that in certain circumstances, when fair value cannot be assessed reliably, exceptions should be made to the recognition or the measurement principles. For instance,

a) As expressed in our response on ED "IAS 39 financial instruments" classification and measurement, we believe that the use of fair value is not relevant for unquoted equity instruments whose fair value is not reliable;

b) As expressed in our response on "IFRS 3 R", we believe that reliable measurement should be maintained as one of the criteria to recognise an intangible asset separately from goodwill.

As a consequence, the ANC believes that IFRS 13 does not meet the criterion of reliability on these points.

Comparability

As a general remark, the ANC considers that comparability may be achieved through clear explanation in disclosure of the measurement method and assumptions used by an entity rather than by using a unique rule applied to all assets and liabilities.

Moreover, following the sovereign crisis last summer, it is obvious that IFRS 13 guidances (based on the 2008 EAP guidances) would not have helped to improve consistency in the determination of when a market become inactive.

Conclusion

Overall, the ANC considers that IFRS 13 does not meet the criteria for endorsement.

2 *EFRAG is also assessing the costs that are likely to arise for preparers and for users on implementation of IFRS 13 in the EU, both in year one and in subsequent years. Some initial work has been carried out, and the responses to this Invitation to Comment will be used to complete the assessment.*

The results of the initial assessment of costs are set out in paragraphs 3-10 of Appendix 3. To summarise, EFRAG's initial assessment is that costs to be incurred by preparers in implementing and applying IFRS 13 are not expected to be significant. IFRS 13 is likely to be neutral in terms of costs for users.

Do you agree with this assessment?

☐ *Yes* ☒ *No*

If you do not, please explain why you do not and (if possible) explain broadly what you believe the costs involved will be?

Assuming that IFRS 13 is "not expected to affect the current practice" (according to EFRAG's assessment), we would agree that costs to be incurred by preparers in implementing IFRS 13 are consequently not expected to be significant.

However, as mentionned above, it is very difficult to assess the application consequences of the new paradigms introduced by IFRS 13 such as "exit price", "principal market" or "highest and bset use". The review by preparers of all of their valuation methods and processes to ensure that they still comply with the new requirements may involve significant costs at inception.

3 *In addition, EFRAG is assessing the benefits that are likely to be derived from IFRS 13. The results of the initial assessment of benefits are set out in paragraphs 11-12 of Appendix 3. To summarise, EFRAG's initial assessment is that IFRS 13 will facilitate preparers in applying and users in better understanding the fair value measurements applied in financial statements and will help to improve consistency in the application of fair value measurement.*

Do you agree with this assessment?

☐ *Yes* ☒ *No*

If you do not agree with this assessment, please provide your arguments and indicate how this should affect EFRAG's endorsement advice?

Consistently with our comment in Q1 above, we disagree with EFRAG's assessment that IFRS 13 will facilitate a better understanding of fair value measurements due to the too theorical notions introduced by this standard.

Moreover, following the sovereign crisis last summer, it is obvious that IFRS 13 guidances (based on the 2008 EAP guidances) would not have helped to improve consistency in the determination of when a market become inactive.

4 *EFRAG's initial assessment is that the benefits to be derived from implementing IFRS 13 in the EU as described in paragraph 4 above are likely to outweigh the costs involved as described in paragraph 3 above.*

Do you agree with this assessment?

☐ *Yes* ☒ *No*

If you do not agree with this assessment, please provide your arguments and indicate how this should affect EFRAG's endorsement advice?

Overall, the ANC considers that significant implementation costs (see Question 2) will not be outweighed by the limited benefits (see question 1) resulting from the application of IFRS 13.