Valuology

International Accounting Standards Board
Columbus Building
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Canary Wharf
LondonE14 4HD
by email

30 December 2021

Dear Sirs,

Exposure Draft - Disclosure requirements in IFRS standards—a pilot approach

We thank you for your invitation to comment on the above proposals.

Our specific interest concerns the proposals to change the disclosure requirements in IFRS 13 *Fair Value Measurements*. We have therefore only responded to those question specifically related to these proposals, although generally we support the proposed move towards principles based objectives rather than prescriptive lists that can produce a tick box response. Better regulation is achieved by compliance with the desired outcome of a series of actions, not compliance with each action in isolation.

Valuology is a consultancy formed by two former directors of the International Valuation Standards Council (IVSC). While at the IVSC we were involved in extensive dialogue with the IASB and IFRSF staff during the development of IFRS 13 and subsequently on the development of education materials. Prior to this, the writer was also a member of the Valuation Resource Group set up by the FASB between 2007 and 2010 to advise on questions arising from the introduction of its fair value standard FAS 157 (now Topic 820). Our present role involves advising valuation providers and users on standards compliance and risk management. This has included advising financial regulators on valuations submitted by regulated investment funds on compliance with the appropriate valuation and financial reporting standards where concerns have arisen over the limited disclosures provided to help investors understand the values reported.

If you have any questions in respect of our response or feel that we can assist you in any way, please do not hesitate to contact us.

Yours faithfully,

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Responses to Questions on Proposed Amendments to IFRS 13 Fair Value Measurements

Question 6—Overall disclosure objective for assets and liabilities measured at fair value in the statement of financial position after initial recognition

Paragraphs BC62–BC73 of the Basis for Conclusions describe the Board's reasons for proposing the overall disclosure objective for assets and liabilities measured at fair value in the statement of financial position after initial recognition.

Do you agree that this proposed objective would result in the provision of useful information that meets the overall user information needs about assets and liabilities measured at fair value in the statement of financial position after initial recognition? If not, what alternative objective do you suggest and why?

Response:
We agree that it is preferable to set overall objectives for the required disclosures around fair value measurements. We have experienced situations where there is at least a suspicion that the reporting entity has gamed the hierarchy to categorise assets in Level 2 rather than Level 3 to avoid making disclosures which should be relevant to anyone relying on the statements.

For assets and liabilities measured at fair value in the statement of financial position after initial recognition, the Board proposes specific disclosure objectives that require an entity to disclose information about the:

(a) assets and liabilities within each level of the fair value hierarchy (paragraphs 103–106 of the [Draft] amendments to IFRS 13);

(b) measurement uncertainties associated with their fair value measurements (paragraphs 107–110 of the [Draft] amendments to IFRS 13);

c) reasonably possible alternative fair value measurements (paragraphs 111–113 of the [Draft] amendments to IFRS 13); and

(d) reasons for changes in their fair value measurements (paragraphs 114–117 of the [Draft] amendments to IFRS 13).

Question 7—Specific disclosure objectives for assets and liabilities measured at fair value in the statement of financial position after initial recognition

Paragraphs BC74–BC97 of the Basis for Conclusions describe the Board's reasons for proposing the specific disclosure objectives about assets and liabilities measured at fair value in the statement of financial position after initial recognition and discuss approaches that the Board considered but rejected.

(a) **Do you agree that the proposed specific disclosure objectives capture detailed user information needs about assets and liabilities measured at fair value in the statement of financial position after initial recognition? Why or why not? If not, what changes do you suggest?**

	Response: We agree that the disclosure objectives proposed in the Draft paragraphs 103-106 would be helpful in understanding where the fair value measurements of the assets and liabilities sit in the fair value hierarchy, and the effect they have on the entity's overall financial position.
(b)	**Do you agree that the proposed specific disclosure objectives would result in the provision of information about material fair value measurements and the elimination of information about immaterial fair value measurements in financial statements? Why or why not?**
	Response: While we support the proposed objectives and believe they should improve the quality and relevance of information about fair value measurements, we do have concerns with the subheading to paragraphs 107-110 inclusive: *"Measurement uncertainties associated with fair value measurements"*. No fair value measurement is a fact but an estimate of the price that would be received in a hypothetical sale on the relevant date. Where that estimate is based on a valuation technique requiring multiple inputs and adjustments of those inputs to reflect the properties of the specific asset (or liability) in question some uncertainty is inevitable. This will be the case for many assets categorised in Level 2 and all in Level 3. If the problem of overburdening users with excess information that is not material to the entity's overall financial position is to be avoided, some qualification or explanation of the sources of measurement uncertainty that require disclosure is needed. Where the entity appoints an external valuation expert, that expert will frequently be required to produce the valuation in accordance with specific valuation standards issued by their professional body. An example which is mostly, but not exclusively, relevant to real estate and tangible assets are the standards issued by RICS, a UK headquartered professional body but with members throughout the world. Along with other standards based on the International Valuation Standards the RICS standards require the valuer to disclose any "*material valuation uncertainty*". This is so a user of the valuation is made aware of any abnormal difficulties the valuer has experienced in assembling sufficiently reliable evidence to support their opinion. This could be due to the asset itself being unusual or to a sudden change in the market causing the only currently available data to be unreliable. The most recent example of the latter was the sudden onset of the Covid pandemic when it took time for reliable evidence of the impact on market sentiment and asset prices to emerge. However, it is also made clear that in the absence of any such abnormal circumstances, such a disclosure is inappropriate. It appears from BC63 that the Board set out with the intention that additional disclosures would be required if there were "material uncertainties" but then removed the qualifier "material" or "materiality" for the reasons explained in BC72. However, we are concerned that without a similar qualifying adjective the objective of avoiding financial statements being burdened with information of marginal relevance will not be met as cautious preparers seek to explain or

justify every fluctuation in the estimated value that could have arisen on the reporting date.

In most cases a brief explanation of the techniques and inputs used in preparing the fair value estimate will provide sufficient information for a user to understand how robust the estimate is. We, therefore, have no problem with the proposed text of 107-110. This reflects generally accepted best practice for valuation reporting. If the proposed subheading were changed to avoid reference to "measurement uncertainties" it would avoid the potential for attempts to be made to explain normal or inherent uncertainty. An alternative subheading could be: *Supporting disclosures for fair value measurements".*

Reasonably possible alternative fair value measurements:
We have greater concern over the proposed requirement for entities to disclose reasonably possible alternatives to the reported fair value. We note it is proposed that this will apply in all cases. Few markets are perfect. With the possible exception of assets in Level 1, all fair value measurements will have reasonably possible alternatives. The responsibility of the valuer is to use their skill and experience to determine what is the most probable of this range of possible alternatives. In most cases providing a range of possible values will not only undermine the most probable estimate but is potentially misleading. Users may assume that an equal probability attaches to figures that are higher or lower than the reported figure.

At best this requirement will lead to unnecessary complication as the range of reasonably possible alternatives will usually be within the observable and expected range of price variations in the relevant market. Where this is the case, such disclosure will exacerbate rather than ameliorate the very problem the project is aimed at resolving, i.e. removing disclosures containing detail immaterial to the financial performance of the reporting entity.

There will be examples where a reported value is particularly sensitive to a significant input which may not be capable of verification or which itself may be based on a qualified estimate. However, these will be rare. For financial reporting the fair value estimate is prepared, or at least reviewed, after the end of the relevant reporting period. Considering what impact a change in any input will have on the value looking forward is irrelevant. This is reinforced by the use of the past tense in the suggested actions in para 113 and by the Board's comments in BC88.

We believe the disclosure of a range of possible values will only be appropriate where it is not possible to determine a specific fair value measurement. This may be in cases where there is no active market for the asset, for example because it is highly specialised or where the market on the reporting date was significantly disrupted by external events. Both of these are cases where an external valuer acting under recognised valuation standards would report that their value was subject to material valuation uncertainty. In other cases, the provision of a range will add unnecessary cost and complication to financial reports. Accordingly, we believe that the proposal to make this a requirement for all fair value measurements would not achieve the objectives of the disclosure project.

	We recommend that the proposed paras 111-113 be removed, or at least 111 be amended so that it only applies where entity has reason to believe that the reported fair value is subject to unusual uncertainty, such as in the examples provided above.
(c)	**Do you agree that the benefits of the specific disclosure objectives would justify the costs of satisfying them? Why or why not? If you disagree, how should the objectives be changed so that the benefits justify the costs? Please indicate the specific disclosure objective(s) to which your comments relate.**
	Response: We agree, subject to the reservations above regarding the need to make it clear that only material valuation uncertainty should be disclosed, and a range of possible values only being required where there are conditions of material uncertainty that prevent a reliable single figure estimate being provided.
(d)	**Do you have any other comments on the proposed specific disclosure objectives?**
	We believe that a disclosure similar to that in IAS 40 75(e) would be beneficial for all assets reported at fair value and suggest the following could usefully be added to the list in the proposed IFRS 13 110: *The extent to which the fair value measurement is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the market for the asset or liability being valued.*
Question 8—Information to meet the specific disclosure objectives for assets and liabilities measured at fair value in the statement of financial position after initial recognition Paragraphs BC74–BC97 of the Basis for Conclusions describe the Board's reasons for proposing the items of information to meet the specific disclosure objectives about assets and liabilities measured at fair value in the statement of financial position after initial recognition, and discuss information that the Board considered but decided not to include.	
(a)	**Do you agree that entities should be required to disclose the proposed items of information in paragraphs 105, 109 and 116 of the [Draft] amendments to IFRS 13? Why or why not? If not, what changes do you suggest and how would they help an entity to meet the specific disclosure objective?**
	Response: We agree.
(b)	**Do you agree with the proposed items of information that are not mandatory but may enable entities to meet each specific disclosure objective? Why or why not? If not, what changes do you suggest and how would they help an entity to meet the specific disclosure objective?**
	Response: We agree.

Assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes

In paragraph 118 of the [Draft] amendments to IFRS 13, the Board proposes a specific disclosure objective that requires an entity to disclose information that enables users of financial statements to understand:

(a) the amount, nature and other characteristics of each class of assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes; and

(b) how the characteristics relate to the categorisation of those classes of assets and liabilities in the fair value hierarchy.

Question 9—Specific disclosure objective for assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes Paragraphs BC98–BC99 of the Basis for Conclusions describe the Board's reasons for proposing the specific disclosure objective for assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes.	
(**a**)	**Do you agree that the proposed specific disclosure objective captures detailed user information needs about assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes? Why or why not? If not, what changes do you suggest?**
	Response: We agree.
(b)	**Do you agree that this proposed specific disclosure objective would result in the provision of useful information about assets and liabilities not measured at fair value but for which fair value is disclosed in the notes? Why or why not?**
	Response: We agree that this should provide useful information.
(c)	**Do you agree that the benefits of the specific disclosure objective would justify the costs of satisfying it? Why or why not? If you disagree, how should the objective be changed so that the benefits justify the costs?**
	Response: If a fair value measurement has been prepared with appropriate diligence, we do not consider that the additional costs of providing the information proposed would be significant.
(d)	**Do you have any other comments about the proposed specific disclosure objective?**
	Response: No

Question 10—Information to meet the specific disclosure objective for assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes

Paragraph BC100 of the Basis for Conclusions describes the Board's reasons for proposing the items of information to meet the specific disclosure objective about assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes.

(a) Do you agree that entities should be required to disclose the proposed items of information in paragraph 120 of the [Draft] amendments to IFRS 13? Why or why not? If not, what changes do you suggest and how would they help an entity to meet the specific disclosure objective?

Response:
We agree.

(b) Do you agree with the proposed items of information that are not mandatory but may enable entities to meet the specific disclosure objective? Why or why not? If not, what changes do you suggest and how would they help an entity to meet the specific disclosure objective?

Response:
We agree, although in addition a description of the significant valuation techniques used in the fair value measurements may be useful information for many users.

Question 11—
Do you have any other comments on the proposed amendments to IFRS 13 in this Exposure Draft, including the analysis of the effects (paragraphs BC214–BC215 of the Basis for Conclusions) and the Illustrative Examples accompanying the Exposure Draft?

Response:
We have no further comments.