The Japanese Institute of
Certified Public Accountants
4-4-1, Kudan-Minami, Chiyoda-ku, Tokyo 102-8264 JAPAN
Phone: +81-3-3515-1130 Fax: +81-3-5226-3355
e-mail: kigyokaikei@jicpa.or.jp
http://www.hp.jicpa.or.jp/english/

September 28, 2009

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Comments on the Exposure Draft *Fair Value Measurement*

To the Board Members:

The Japanese Institute of Certified Public Accountants appreciates the continued efforts of the International Accounting Standard Board (IASB) on the financial crisis and welcomes the opportunity to comment on the exposure draft *Fair Value Measurement*.

As this project is expected to promote convergence with US GAAP, we agree with the general direction of the effort. However, we also believe that further consideration should be given to consistency with related accounting standards, such as IFRS 3 *Business Combinations* and IAS 36 *Impairment of Assets*, that also require fair value measurements.

The following is our response to the items in 'invitation to comment' with which we disagree or have questions or concerns.

Scope

Question 2

> In three contexts, IFRSs use the term 'fair value' in a way that does not reflect the Board’s intended measurement objective in those contexts:
>
> (a) In two of those contexts, the exposure draft proposes to replace the term 'fair value' (the measurement of share-based payment transactions in IFRS 2 Share-based Payment and reacquired rights in IFRS 3 Business Combinations) (see paragraph BC29 of the Basis for Conclusions).
> (b) The third context is the requirement in paragraph 49 of IAS 39 Financial Instruments: Recognition and Measurement that the fair value of a financial liability with a demand feature is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid (see paragraph 2 of the draft IFRS and paragraph BC29 of the Basis for Conclusions). The exposure draft proposes not to replace that use of the term ‘fair value’, but instead proposes to exclude that requirement from the scope of the IFRS.
>
> Is the proposed approach to these three issues appropriate? Why or why not? Should the Board consider similar approaches in any other contexts? If so, in which context and why?

Comment:

We believe that the term "fair value" in paragraph 49 of IAS 39 should be replaced.
If the term "fair value" is intended to have different meanings depending on the context, understanding of the text would be difficult. In order to avoid confusion and difficulties in application, if the intended meanings are different, the terms used should also be different.

The transaction

Question 3

> The exposure draft proposes 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 (see paragraphs 8–12 of the draft IFRS and paragraphs BC37–BC41 of the Basis for Conclusions).
> Is this approach appropriate? Why or why not?

Comment:

We believe that, in fair value measurement, it is appropriate to employ the assumption that the transaction to sell the asset or transfer the liability takes place in the principal market of the asset or liability.

We believe that, in cases where there is a most advantageous market to which the entity has access, other than the principal market of the asset or liability, it is important to consider constraints such as degree of access to the most advantageous market for market participants. We further believe that if such constraints are not considered, the fair value measurement, based on the price quoted in the most advantageous market, would not lead to appropriate determination of exit price.

Question 4

The exposure draft proposes that an entity should determine fair value using the assumptions that market participants would use in pricing the asset or liability (see paragraphs 13 and 14 of the draft IFRS and paragraphs BC42–BC45 of the Basis for Conclusions). Is the description of market participants adequately described in the context of the definition? Why or why not?

Comment:

Following on our comments to Question 3, we believe that, in the context of the definition “market participants”, the reference to “the most advantageous market" is not appropriate.

Application to assets: highest and best use and valuation premise

Question 6

When an entity uses an asset together with other assets in a way that differs from the highest and best use of the asset, the exposure draft proposes that the entity should separate the fair value of the asset group into two components: (a) the value of the assets assuming their current use and (b) the amount by which that value differs from the fair value of the assets (ie their incremental value). The entity should recognize the incremental value together with the asset to which it relates (see paragraphs 20 and 21 of the draft IFRS and paragraphs BC54 and BC55 of the Basis for Conclusions). Is the proposed guidance sufficient and appropriate? If not, why?

Comment:

We believe that such separation into components, as described in the exposure draft, is not appropriate.

In the case described in BC54 of the exposure draft, we believe that the value of the factory building should be determined at nil. It is inconsistent to measure the fair value of the factory land as difference between the fair value of the land itself as that of whole factory based on the highest and best use of the asset assumption and the value of the factory building in the current use, which is to be a basis on subsequent depreciation to be used continuously. If depreciation of the building is given priority to reflect the consumption of economic resources on financial reporting, fair value measurement would be irrelevant to that purpose since it does not reflect current use conditions.

Application to liabilities: general principles

Question 7

The exposure draft proposes that:

(a) a fair value measurement assumes that the liability is transferred to a market participant at the measurement date (see paragraph 25 of the draft IFRS and paragraphs BC67 and BC68 of the Basis for Conclusions).

(b) if there is an active market for transactions between parties who hold a financial instrument as an asset, the observed price in that market represents the fair value of the issuer's liability. An entity adjusts the observed price for the asset for features that are present in the asset but not present in the liability or vice versa (see paragraph 27 of the draft IFRS and paragraph BC72 of the Basis for Conclusions).

(c) if there is no corresponding asset for a liability (e.g. for a decommissioning liability assumed in a business combination), an entity estimates the price that market participants would demand to assume the liability using present value techniques or other valuation techniques. One of the main inputs to those techniques is an estimate of the cash flows that the entity would incur in fulfilling the obligation, adjusted for any differences between those cash flows and the cash flows that other market participants would incur (see paragraph 28 of the draft IFRS).

Are these proposals appropriate? Why or why not? Are you aware of any circumstances in which the fair value of a liability held by one party is not represented by the fair value of the financial instrument held as an asset by another party?

Comment:

We consider these proposals appropriate. In this respect, we understand that determination of fair value of liabilities basically applies in initial measurement of financial liabilities, and subsequent measurement of those such as derivatives, of which the market exists, and exit prices can be measured.

Application to liabilities: non-performance risk and restrictions

Question 8

The exposure draft proposes that: (a) the fair value of a liability reflects non-performance risk, ie the risk that an entity will not fulfill the obligation (see paragraphs 29 and 30 of the draft IFRS and paragraphs BC73 and BC74 of the Basis for Conclusions). (b) the fair value of a liability is not affected by a restriction on an entity's ability to transfer the liability (see paragraph 31 of the draft IFRS and paragraph BC75 of the Basis for Conclusions). Are these proposals appropriate? Why or why not?

Comment:

(a) In the process of measurement of liabilities, in certain limited circumstances, a requirement to reflect non-performance risk may result in providing additional useful information. However, we believe that fair value of liabilities should not reflect non-performance risk in cases of non-financial liabilities, when the effect of non-performance risk cannot be measured directly and/or in cases when reflection of non-performance risk would not be relevant for financial reporting purposes.

(b) We consider that by not reflecting a restriction of an entity's ability to transfer the liability would simplify the valuation process. However, it is doubtful that such basis of measurement would provide more useful information.

Fair value at initial recognition

Question 9

The exposure draft lists four cases in which the fair value of an asset or liability at initial recognition might differ from the transaction price. An entity would recognise any resulting gain or loss unless the relevant IFRS for the asset or liability requires otherwise. For example, as already required by IAS 39, on initial recognition of a financial instrument, an entity would recognise the difference between the transaction price and the fair value as a gain or loss only if that fair value is evidenced by observable market prices or, when using a valuation technique, solely by observable market data (see paragraphs 36 and 37 of the draft IFRS, paragraphs D27 and D32 of Appendix D and paragraphs BC76–BC79 of the Basis for Conclusions). Is this proposal appropriate? In which situation(s) would it not be appropriate and why?

Comment:

We consider the proposal appropriate.

However, since the proposal in paragraph D32 of the exposure draft, as amendment to paragraph AG76 (b) of IAS 39, does not clearly indicate the accounting treatment for the deferred difference, the presentation of the deferred difference should be clarified in the final standard.

Valuation techniques

Question 10

The exposure draft proposes guidance on valuation techniques, including specific guidance on markets that are no longer active (see paragraphs 38–55 of the draft IFRS, paragraphs B5–B18 of Appendix B, paragraphs BC80–BC97 of the Basis for Conclusions and paragraphs IE10–IE21 and IE28–IE38 of the draft illustrative examples). Is this proposed guidance appropriate and sufficient? Why or why not?

Comment:

We consider the proposed guidance appropriate.

However, in paragraph B5, we believe that consideration should be given to add a phrase that "undesirable price or decline in liquidity is not the same as distressed sale or forced liquidation".

Disclosures

Question 11

The exposure draft proposes disclosure requirements to enable users of financial statements to assess the methods and inputs used to develop fair value measurements and, for fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period (see paragraphs 56–61 of the draft IFRS and paragraphs BC98–BC106 of the Basis for Conclusions). Are these proposals appropriate? Why or why not?

Comment:

We consider that these proposals are basically appropriate. However, the following points require further consideration:

1. We believe that consideration should be given to establish the disclosure requirements related to fair value measurement after initial recognition.
   For example, paragraph 35 of the exposure draft states that, in many cases, an entry price of an asset or liability will equal its fair value at initial recognition. Therefore, there should be clarification as to whether there should be a requirement as to disclosure of "the methods and the inputs used in the fair value measurement, and the information used to develop those inputs" called for in paragraph 57(d) of the exposure draft. It should also be clarified as to whether the disclosure in paragraph 56 of the exposure draft requires in the subsequent period after impairment loss is recognized using the fair value under IAS 36. Paragraph 59 of the exposure draft clearly states that the required disclosure pertains to each class of liability measured at fair value after initial recognition.

2. With respect to the disclosure example in IE12 of the exposure draft, derivatives may be recognized either as an asset or a liability. IE40 and IE41 of the exposure draft provide for the same disclosure requirements to apply to both assets and liabilities. However, since it is unclear as to whether derivatives recognized as assets should be disclosed separately from those recognized as liabilities, the appropriate disclosure basis should be clarified.

3. Although paragraph 60 of the exposure draft provides for disclosure requirements in cases when an asset is used together with other assets, and its highest and best use

differs from its current use; as indicated in our comments to Question 6, we do not agree with such measurements, and accordingly, do not agree with such disclosure requirements.

Other comments

Question 13

Do you have any other comments on the proposals in the exposure draft?

Comment:

1. We believe that further consideration should be given to consistency with related IFRSs, which require fair value measurement such as IFRS 3 *Business Combination* and IAS 36 *Impairment of Asset.*

2. Paragraphs 32 and 33 of the exposure draft require fair value measurement of equity instruments. Although we expect these provisions to apply, for example, to treasury stock, the scope of the application should be clearly stated in the standards. In addition, paragraphs IE40 and IE41 of the exposure draft should also clearly state that the disclosure requirements apply to assets and liabilities, as well as to equity.

Yours faithfully,

Kiyoshi Ichimura
Executive Board Member－Accounting Standards
The Japanese Institute of Certified Public Accountants