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Fair value once more in focus

The July meeting of the IASB included another entertaining debate on the use of fair value, and a first look at the staff draft of an exposure draft on consolidation. The Board had a first look at the Management Commentary project and continued to re-deliberate the *IFRS for private entities*.

Having issued the FASB's fair value standard (SFAS 157) as a discussion paper, the IASB staff attempted to move forward at the July meeting towards an exposure draft. The key issue was whether the IASB should converge with the FASB and describe an exit value as fair value, or abandon the term and just talk about entry and exit values.

Sir David Tweedie preferred abandoning fair value and using current exit and current entry price. He described the FASB standard as 'convoluted' and later 'cryptic'. Mary Barth, however, thought SFAS 157 was a very helpful document that had clarified a lot.

The IASB chairman said that people thought of the transaction price as the entry value, and when they looked at exit value, they thought this involved recording a loss. Ms Barth summed up the FASB position as being that the entry and exit price were the same in the same market. The issue was that someone seeking to sell a used asset was in a different market from someone buying a new asset. The important issue was which market, not which price.

She added that SFAS 157 also allowed of fair value being based on an 'in-use premise'. Fair value, for example as used in a business combination, was the highest and best value that could be obtained from the future economic exploitation of the asset, not necessarily its price on the market for used assets. Jan Engtsröm commented that 80% of industrial assets were unsaleable anyway.

Both Bob Garnett and Philippe Danjou felt this way of explaining current values did not achieve the required clarity. Mr Danjou thought that 'fair value' had an emotional baggage and should be replaced by neutral technical terms. What was 'fair' about it anyway?

However, Steve Cooper and Warren McGregor said that the publication of SFAS 157 and the spotlight put on fair value in the credit crunch had encouraged people to get to grips with the concept. They should not throw out a term people had just started getting used to. The Board decided to let the staff go to the next paper using transaction price as the entry value and fair value for subsequent measurement. That is unlikely to be the end of the debate.

Alan Teixeira, the new director of technical activities, introduced a staff draft of an exposure draft on consolidation. Normally the staff bring papers addressing topics within the scope of the exposure draft and the first the world sees of it is when it is officially published.

He remarked that enough fundamental issues had been discussed by the Board over the life of the project to make it possible to prepare a draft. He hoped that this would speed the process.

The exposure draft is for a standard that will replace both IAS 27 on consolidation and SIC 12 on special purpose entities (SPEs). This is one of the projects to which the G8 finance ministers at their April meeting asked the IASB to give priority. The staff draft can be downloaded from the project page on the IASB website (www.iasb.org).

Board reactions to the draft were that it was too much oriented towards SPES and Special Investment Vehicles (SIVs). The staff countered that the basic notion of control of a subsidiary was simple, it was the grey areas between clear control and clear absence of control that were difficult to regulate. Jim Leisenring also thought the wording was too subtle.

The Board is hoping to publish a discussion paper on revenue recognition shortly. In May they took the decision to abandon one of the two competing models they had been working on. At the July meeting they acknowledged that while this meant they could proceed more rapidly, in effect what they will publish is not much more than an updated approach to IAS 18 and IAS 11.

In addition, while the alternative model (based on fair value) might have had wide application - as well as being very controversial - the ‘customer consideration’ model has narrower application. It would therefore be necessary to discuss what scope limitations should be placed on it. Board members thought that commodities, leases, financial instruments and insurance were all obvious candidates.

The customer consideration model is based on allocating the contract price over each stage where a deliverable is provided to the client. It therefore requires that there should be a contract and individually recognisable deliverables. Jim Leisenring reported that a FASB member had described the draft paper as a paper on cost allocation.

The Board continued to re-deliberate the proposed standard for private entities. Many comments were looking for further relief, leading to Jim Leisenring commenting in exasperation: ‘Why don’t we just accept that drawing up accounts is too difficult?’ The Board was not in giving mood this month.