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26 August 2010   By email: commentletters@hkicpa.org.hk & by post

Mr. Steve Ong
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Hong Kong Institute of Certified Public Accountants
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Dear Steve

Exposure Draft –Measurement Uncertainty Analysis Disclosure for Fair Value Instruments

We refer to your letter dated 5 July 2010 and would like to set out below our comments on the above ED for your consideration.

Question 1

Are there circumstances in which taking into account the effect of the correlation between unobservable inputs (a) would not be operational (eg for cost-benefit reasons) or (b) would not be appropriate? If so, please describe those circumstances.

In some cases, the valuation of a particular asset may be based upon numerous unobservable inputs. For example, a private equity investment may be valued using a method such as PE benchmarking for which the unobservable discount factor, used to discount the observable input (i.e. industry PE of listed companies), may be further distinguished into various sub-discount factors such as discount on operational scale, discount on liquidity, discount on management quality, etc. In such cases, we do not believe that it is operational to identify all relevant unobservable inputs that may have some level of correlation. In addition, the proposed requirements state that correlation should be taken into account when it is relevant but does not provide guidance on how to determine whether the relationship between two or more variables is reliably correlated, other than to make clear that a statistical analysis (e.g., regression) is not required. We believe that existing practice already incorporates correlation when it clearly exists and it is reasonable to do so. Specifically requiring that correlation be incorporated could impose a level of due diligence to identify potential correlation that is not operational.

We recommend that correlation be identified as a factor to be considered in identifying the unobservable inputs that could have been used in the circumstances. In addition, this guidance should be reflected as application guidance rather than as a requirement within the body of the standard.

Question 2

If the effect of correlation between unobservable inputs were not required, would the measurement uncertainty analysis provide meaningful information? Why or why not?

We believe that a measurement uncertainty analysis that does not reflect correlation among unobservable inputs is of limited value. The resulting disclosures could reflect scenarios that are not possible of occurring because the unobservable inputs cannot coexist in reality the way they are portrayed in the analysis.

Question 3

Are there alternative disclosures that you believe might provide users of financial statements with information about the measurement uncertainty inherent in fair value measurements categorized within Level 3 of the fair value hierarchy that the Board should consider instead? If so, please provide a description of those disclosures and the reasons why you think that information would be more useful and more cost-beneficial.

While we do not have a proposal for an alternative disclosure, we believe that there are clarifications that should be made to the proposal. The Board should clarify that the disclosure for each category of Level 3 assets and liabilities is a single range reflecting the optimal combination of unobservable inputs that could have reasonably been used resulting in one amount for a "higher" valuation and one amount for a "lower" valuation. In addition, it should be clarified that the correlation to be considered is among unobservable inputs for a single asset rather than among the various assets in a class.

Yours sincerely,

Rita Liu
Secretary