



INTERNATIONAL VALUATION STANDARDS COUNCIL

# IVS 500 *Financial Instruments*

## Exposure Draft

**Issued:** 11 December 2020  
**Comments Due:** 19 April 2021



# IVS 500 *Financial Instruments* Feedback Form Questions for Respondents

<b>IVS 500 <i>Financial Instruments</i> Exposure Draft: Objective</b>	
The objective of IVS 500 <i>Financial Instruments</i> is to establish principles that will enable entities to derive fit-for-purpose valuations of financial instruments in all market conditions and circumstances, and for whatever purpose it is required, including for financial, tax and regulatory reporting.	
<p><b>Question 1:</b> Do you agree with the proposed objective? Why or why not? If you agree with only parts of the proposed objectives, please specify what you agree and disagree with. If you disagree with the proposal, please explain what you propose instead and why.</p>	<div style="border: 1px solid #ccc; padding: 5px;"> <p>[Q1] Yes, we agree with the objective.</p> </div>
<p><b>Question 2:</b> The Exposure Draft is focused on the requirements that have to be met for two elements, Governance and Data, of the proposed standard in order for an entity to arrive at a fit-for-purpose valuation of financial instruments. Do you agree that the requirements are clear, complete and provide adequate guidance to ensure compliance? Why or why not? If you agree with only parts of the requirements, please specify what you agree and disagree with. If you disagree with the requirements, please explain what you propose instead and why. If you think the requirements are incomplete, please explain what you propose should be included and why.</p>	<div style="border: 1px solid #ccc; padding: 5px;"> <p>[Q2]</p> <ul style="list-style-type: none"> <li>• We believe that there are areas in which the requirements and guidance could be improved.</li> <li>• Although it does not remove valuation risk entirely, a robust Independent Price Verification (IPV) process can help to identify valuations which are at risk of being inaccurate. Independent validation of the final valuation to some extent removes the need to validate the underlying input data and / or model assumptions.</li> <li>• Without seeing the Methods and Models and Controls and Reporting sections it is a little difficult to make comprehensive feedback.</li> <li>• Although valuation uncertainty is referenced several times, there is no specific description of how it should be measured or how such uncertainty should be utilised in the determination of the final fit-for-purpose valuations.</li> </ul> </div>



**IVS 500 *Financial Instruments* Exposure Draft: Scope**

Para 20.1 outlines the scope of application of IVS 500 *Financial Instruments*. In arriving at the proposed scope the FI Board focused on limiting the application of IVS 500 to only those instruments intended by the Board and on ensuring, as far as possible, that all definitions are clear to avoid ambiguity in practice.

In addition, in order to avoid overlaps with extant IVS requirements and the inclusion of instruments that could potentially meet the definition of a financial instrument but are not valued as such within the scope of IVS 500, the FI Board has proposed a number of exceptions to the scope requirements in IVS 500 as outlined in para 20.1 of this Exposure Draft.

**Question 3:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

[Q3] We consider the scope to be appropriate and have no further comment.



**IVS 500 *Financial Instruments* Exposure Draft: Definitions**

Paras 30.1 to 30.5 provide definitions for the purpose of applying IVS 500 *Financial Instruments*. More specifically they define:

- fit-for-purpose valuations
- financial assets
- financial liabilities; and
- equity instruments

**Question 4:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

[Q4]

The use of both "entity" and "third-party" is confusing. Perhaps "counterparty" would be clearer?

The definitions are regarding "financial instruments". The current definitions all exclude physically (rather than financially) settled contracts. Physically settled contracts are prevalent throughout the industry.

In paras 30.6 to 30.8, valuation uncertainty and valuation risk are defined for the purposes of IVS 500 *Financial Instruments*. This Exposure Draft uses valuation risk to set proportionality parameters (para 30.9) that determine the level of effort and the nature and extent of processes and controls needed in order to arrive at a fit-for-purpose valuation of a financial instrument. The objective of the FI Board in outlining the above concept is to enable constituents to evaluate in a consistent manner the extent and rigour of the processes necessary to ensure a fit-for-purpose valuation of financial instruments given the requirement for which it is needed, market conditions and other circumstances prevailing at the valuation date.

**Question 5:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

[Q5] We are comfortable with this section and have no comments.



### IVS 500 *Financial Instruments* Exposure Draft: Governance

The Exposure Draft provides guidance on the processes that entities should follow to ensure proper governance around financial instrument valuations.

The guidance requires that a valuation process should be:

- systematic
- consistently applied
- economically sound; and
- controlled

In order for the valuation process to meet the above objectives it should require:

- ownership
- accountability
- transparency
- consistency
- review and challenge
- diversity; and
- documentation

**Question 6:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

**[Q6]**

- For Ownership we feel that while Valuation is dependent on the trading desk, IPV must be independent, including control of an appropriate budget. If Valuations are to be transparent and consistent then there needs to be an audit trail of parameters, methods and results.
- Three layers of diversity; initial valuation, validation of results, validation of valuation. This is a Control aspect.
- 50.4.2 What is a Pricing Service? Presumably this includes both consensus / IPV and Valuation services, these should be differentiated more. We recommend changing the last sentence to "There should, however, be individuals within the organisation who are ultimately responsible for the satisfactory execution and assessment of the valuation process". This makes clear that the vendors are external and that the organisation does not outsource oversight.
- 'Developer' already has a well-established meaning within organisations relating to software. Given the definition here requires the identification of data, methods, models and systems, this is a role that requires extensive product knowledge and extends further to the process, controls and vendor assessment. We suggest using something like 'Process Owner'.



### IVS 500 Financial Instruments Exposure Draft: Data

For the purposes of this Exposure Draft, data is considered to be any input to a process undertaken to arrive at a fit-for-purpose valuation. Firstly, the section on data outlines the principles for creating a data taxonomy or dictionary to categorise, assess and control all data that is used in valuations. Secondly, the specific requirements that need to be met for the following data types are outlined:

- internally sourced data
- market data
- transaction data
- model-based/indicative market data
- judgement-based data;
- historical data; and
- performance data

The section further describes the controls necessary for aggregating and managing data in an organisation and how the concept of proportionality applies in determining the requirements concerning the use of data.

**Question 7:** Do you agree with the principles outlined in paras 60.5.1 to 60.5.3 regarding the development of a data taxonomy? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

[Q7]

We agree with the data taxonomy, although we would make the following comments;

- 60.4 – This item contains a reference to “Section 6.5”; this should be to 60.5
- 60.5.1 Specific and Indicative are not opposite ends of the same continuum, which makes the first item confusing.
- 60.5.2. We feel that the word “active” should be added to “many market participants”.



<p><b>Question 8:</b> Paras 60.6.2 to 60.6.8 outline the specific requirements for the data-types listed above. Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.</p>	<p>[Q8] 60.6 We feel that it should be made clear where Consensus Prices fit into the hierarchy.          60.6.3.1 iii: We feel that changing the wording to "...reflect the market conditions on the valuation date and time as appropriate for the market." would be better.          60.6.5.2 Note that this is actually labeled as 6.6.5.2.Consensus Pricing services are included here with (in fact ranking below) broker indicative data. Clearly, if internal data is at the top of the list (as presented here) an independent assessment of that internal data through comparison to other active market participants' internal data should surely be as strong or stronger than the internal data alone. Combine that already strong consensus comparison with active trades and market quotes and you have the single best source of information available with published metrics on uncertainty.          60.6.6.14 "Challenges are essential". This is true on all data types, not just Judgement-based.          60.6.7: Frequency of the valuation (and valuation review) process is key to ensuring reliable historic data calculations.</p>
<p><b>Question 9:</b> Paragraphs 60.7.1 to 60.7.6 outline the principles for controlling and aggregating data across an organisation. Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.</p>	<p>[Q9] 60.7 There is no mention of relationships with external entities, although perhaps this would be found in Controls &amp; Reporting. If it is needed here then something on engagement and procedures would be useful. In 60.7.1 there could also be a role for compliance.          60.7.5 60.5.5.1 is wrong number, should be 60.7.5.1.</p>

PLEASE PROVIDE THE FOLLOWING INFORMATION:

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