

International Valuation Standards Board
41 Moorgate
London
EC2R 6PP

24 December 2010

Discussion Paper on Valuation Uncertainty

Dear Sirs

UBS AG appreciates the opportunity to submit comments on the International Valuation Standards Board's Discussion Paper on the topic of Valuation Uncertainty. As an organization that is required to provide information in its general purpose financial statements on the fair value of financial instruments, UBS strongly supports the development of consistent standards on how to identify and report valuation uncertainty.

The financial crisis highlighted that for financial instruments which are complex and not traded in an active market, establishing fair value often requires reporting entities to apply assumptions which are selected using judgement. For such instruments, using alternative assumptions that could reasonably have been chosen may result in a different valuation. The resulting fair values may contain an element of valuation uncertainty.

There is presently no established methodology applied consistently by banks for identifying, measuring and reporting valuation uncertainty for financial instruments. This is despite the increase in recent years in the nature and extent of valuation related disclosures under IFRS and US GAAP, and interest in the topic from financial regulators. For a number of years UBS has provided in its financial statements a measure of valuation uncertainty for level three instruments as required by IFRS 7. However following discussions with other banks, we understand that they apply different methodologies for their equivalent disclosures. The lack of a single methodology applied consistently challenges the ability to reliably compare the level of valuation uncertainty between banks.

For many financial instruments, fair value provides the most appropriate means to report their performance. Establishing a clear standard for the consistent reporting and measurement of valuation uncertainty will significantly enhance the usefulness of fair value information provided and make cross comparison between banks more meaningful. It will also potentially highlight the levels of fair value uncertainty that banks are prepared to be exposed to.

We have included responses to the specific questions raised in the valuation uncertainty paper in the appendix to this letter. If you would like to discuss any comments that we have made, please do not hesitate to contact Paul Hawkes at +41 44 236 5929 or David Bradbery at +44 207 568 0457.

Regards,

UBS AG

Paul Hawkes
Managing Director
Head of Group Valuation Governance

David Bradbery
Managing Director
Group Valuation Governance

APPENDIX

Question 1: Do you agree that it is only when material, or abnormal, uncertainty attaches to a valuation on a specific time or date that that specific disclosure is necessary when the valuation is reported? If not please explain why you consider that an uncertainty statement should be provided in all cases.

Specific disclosure should be provided for valuation topics that are material or for where the level of valuation uncertainty is significant. This is consistent with the approach that UBS follows for the disclosures in its financial statements. We provide detailed information for specific valuation topics that UBS identifies would be of interest to users of our financial statements. In addition UBS provide an indicator of the overall level of valuation uncertainty for level three items, in line with the requirements of IFRS 7.

Question 2: Do you believe that the Board has identified all major sources and types of material valuation uncertainty? If not please identify what additional causes of uncertainty exist and how often you encounter these in practice.

Yes, the major sources of valuation uncertainty have been identified by the IVSB. However we consider that it would be useful to further distinguish within "Scope of Work" the specific uncertainty in relation to operational risk. This arises for example where existing reporting and valuation tools could be improved to better address the complexity of the instruments being reported. This may be relevant for complex new financial instruments that are developed in response to a pressing current market need or economic circumstance. In such cases the reporting and control infrastructure put in place when they first come into existence whilst adequate, may offer scope for future improvement. The resulting operational risk contributes to the overall level of valuation uncertainty and may need to be separately captured and monitored.

Question 3: Do you agree with the Board's conclusion that an explanation of any abnormal uncertainty identified and an explanation of the impact this has on the valuation (a qualitative statement) is more helpful to users in understanding the valuation than a purely numeric expression of the range of possible values created by the uncertainty (a quantitative statement)?

Yes, we agree that disclosures with respect to valuation uncertainty are most useful when they combine qualitative and quantitative information. The qualitative information provided must be of a high standard and communicate the salient facts of the issue to ensure that it complements and fully explains the critical elements of the quantitative data.

Question 4: Do you think the IVSB should include an explicit requirement in the proposed IVS 105, Valuation Reporting, to disclose any material uncertainty or is the principle that requires valuation reports not to be ambiguous or misleading sufficient?

Yes, we agree that valuation reports should disclose the source and nature of any material valuation uncertainty. It is not sufficient to only require that valuation statements should not be ambiguous or misleading. In UBS's external reports this requirement is already substantially met with respect to financial instruments, since IFRS 7 requires disclosure of significant valuation uncertainty for level three items and a description of the valuation techniques applied for material items.

Question 5: Do you consider that there are cases where a qualitative statement of the causes and impact of uncertainty on the valuation is inadequate and should be either augmented or replaced by a quantitative statement? If so please

- state the circumstances and assets classes where you believe that quantitative statements are more helpful to users and,
- provide a brief explanation or example of the type of quantitative statement that you believe would be useful.

Consistent with our answer above to question 3, we believe that a combination of qualitative and quantitative information is the most effective way to disclose valuation uncertainty. This is the approach favoured by UBS for its external reporting. When providing the disclosure it is critical that it is clear, relevant and contains an appropriate level of detail for the issue to be understood.

Question 6: Do you consider that it would be helpful if IVSC developed guidance on methods for making a quantitative disclosure of uncertainty under specific circumstances? If so please indicate the circumstances and any methods that you either use or encounter in your market.

Yes. There is currently no established industry practice for calculating and disclosing valuation uncertainty. It would therefore be very helpful if the IVSB were able to facilitate the discussion of potential approaches and the development of suitable market practice that would enable this disclosure to be provided consistently by different organizations.

The IASB published in June 2010 an Exposure Draft, Measurement Uncertainty Analysis Disclosure for Fair Value Measurements. The proposal was identical to the FASB's suggested amendments to Topic 820. They propose that additional information is provided for the level of valuation uncertainty that relates to level three instruments and to factor in the effect of correlation between unobservable inputs. UBS's comment letter on the proposals emphasised that the current absence of an industry wide methodology for calculating valuation uncertainty, will result in the additional disclosures contributing little or no additional decision useful information to the financial statements.

UBS is currently looking at how best to capture and calculate valuation uncertainty for financial instruments and plans to further develop its approach during 2011. We are looking at various possible approaches, which may include using the results of independent price verification work performed by the valuation controllers and/or the results obtained from consensus pricing services. Our work on this topic is in progress. We strongly support the development of a consistent industry response and would therefore be interested to contribute to the IVSC's work in this area.