

# Pricing Sources Task Force

Greg Scates

*Deputy Chief Auditor, Office of the Chief Auditor*

Greg Fletcher

*Associate Chief Auditor, Office of the Chief Auditor*

# Discussion Agenda

---

- Background
- Task Force Members
- Meeting Highlights
- Key Themes and Audit Considerations
- Next Steps
- SAG Discussion

# Background

- The Board, as announced at the SAG meeting on March 24, 2011, formed a Pricing Sources Task Force
- The Board's 4010 report on the economic crisis indicated auditors did not always comply with standards when they used pricing services; current inspection findings indicate this condition continues to exist
- The Pricing Sources Task Force is comprised of several members of the SAG, as well as other investors, preparers, and auditors, representatives from pricing services and brokers ("pricing sources"), and observers from FASB, the SEC, and the Federal Reserve
  - Three meetings held to date

# Task Force Members

Matthew Berry	Markit
Glenn Booraem	The Vanguard Group
Matthew Brodin	IDC
Neri Bukspan*	S&P
Timothy Chatting	Lexmark International
Theresa Cooper	General Electric
James Cowden	State Street Corporation
Brian Doyle	Goldman, Sachs & Co.
Susan DuRoss	Harvest Investments
John Fogarty	D&T
Michael Gallagher*	PwC
Gaylen Hansen*	Ehrhardt Keefe Steiner & Hottman

\*SAG Member

# Task Force Members (Cont'd)

John Hebble	Fidelity
Mark Heckert	IDC
Gregory Hinkle	T. Rowe Price Group
Nigel Hyde	Markit
John Keyser	McGladrey & Pullen
Jeffrey Mahoney*	Council of Institutional Investors
Mark Niswonger	KPMG
Michael Santay	Grant Thornton
Verne Scazzarro	Harvest Investments
Robert Schirling	E&Y
Heather Slavkin	AFL-CIO
Lynn Turner*	Former SEC Chief Accountant
David Weiskittel	BDO

\*SAG Member

# Meeting Highlights

The Task Force discussed:

- ❑ Issues pertaining to fair value measurements of financial instruments and the use of third-party pricing sources
- ❑ Overview of issuers' processes and controls over information obtained from pricing sources
- ❑ Nature and extent of information pricing sources provide (or are willing to provide) to issuers and auditors
- ❑ Pricing sources' processes and controls over the data used in valuation of financial instruments
- ❑ Auditor's procedures in connection with the use of information produced by pricing sources in a financial statement audit

# Meeting Highlights

- A sample of financial instruments within different asset classes were priced by the pricing source representatives on the Task Force. For each financial instrument, the Task Force discussed:
  - How the pricing sources determined the prices for individual instruments
  - The valuation technique, the proprietary nature of the models, and the assumptive data used by the pricing sources
  - Why the valuations were similar or different

# Key Themes

- There are different types of pricing sources providing a variety of services to issuers and auditors
- Issuers' use of third-party pricing information to value financial instruments varies
  - Some issuers use information from pricing sources as a data point to corroborate their internal models
  - Other issuers rely on information obtained from pricing sources for their fair value measurements
  - Issuers also may use a combination of the above methods for different financial instruments held by the issuer



# Key Audit Considerations

- It is important for the issuer's portfolio to be classified into separate categories with similar risks and characteristics so that the auditor can:
  - Understand the risks within each category
  - Focus attention on those instruments with higher risks of material misstatement
- A SAS 70 report could provide some assurance over the controls at a pricing service. However, from an audit standpoint, it would not provide sufficient appropriate audit evidence to support the fair value measurements of financial instruments.

# Next Steps

---

- OCA is considering additional guidance or a new standard which would build on the principles in AU sec. 328, *Auditing Fair Value Measurements and Disclosures*

# **Pricing Sources Task Force – Discussion**