

August 30, 2017

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 043 (Proposed Auditing Standards - *Auditing Accounting Estimates, Including Fair Value Measurement*)

To the Board:

ICE Data Services appreciates the opportunity to comment on the proposed auditing standards, *Auditing Accounting Estimates, Including Fair Value Measurements* (“the Proposal”), published on June 1, 2017 by the Public Company Accounting Oversight Board (“the Board”).

ICE Data Services’ company, Interactive Data Pricing and Reference Data LLC, provides independent evaluations to both auditors and end clients as an input in their valuation process for assets and liabilities required to be measured at fair value. We believe our extensive experience as a third party evaluations provider serving more than 5,000 global organizations can give rise to useful insights concerning the practices and processes that result in high quality evaluations. We believe that this experience closely aligns us with the auditing objectives of understanding information provided by third-party pricing sources and evaluating whether the company has used such information appropriately.

We have focused our comments regarding the proposed requirements specifically on the questions relating to the use of information from third-party pricing sources. In summary, ICE Data Services believes:

- The industry would likely benefit from allowing additional time for pricing services to develop and test new vehicles designed to support implementation of the Proposal, and for the audit community to be trained in using new data and tools for evaluating the relevance and reliability of pricing service information. This could be accomplished by extending the Proposal’s effective date to audits of fiscal years beginning two (2) years following the year of SEC approval, or three (3) years after the year of SEC approval if such approval occurs in the fourth quarter.
- Differences in approach toward valuation of financial instruments can create differing levels of bias risk among pricing services. The Board’s objective of heightening auditors’ awareness of potential management bias and the need for professional skepticism could be advanced if auditors were directed to consider a pricing service’s procedures for

assessing market information when assessing the reliability and relevance of pricing service information.

- The Proposal’s guidance for assessing a pricing service’s experience and expertise could be reinforced by encouraging auditors to consider, among other things: (i) the size and experience levels of the pricing service’s evaluation staff; (ii) the amount and quality of informational resources the pricing service makes available to help both auditors and clients understand the pricing service’s information and methodologies; and (iii) the pricing service’s evaluation quality controls and price challenge process(es).
- The Proposal’s guidance for assessing the relevance of pricing information provided by a pricing service appropriately emphasizes that audit responses should be risk-based, focusing attention on estimates with the greatest risk of material misstatement. We believe that a selective, risk-driven approach is likely to be both more effective and efficient than an effort to validate every security price reflected in a company’s financial statements. Further, considerations of cost and potential unintended consequences make it desirable to avoid materially broadening the scope of market data required to conduct an audit. The risk of unintended reduction in market data availability could arise if originators of quote and trade data such as securities dealers and investment firms perceived that confidential information they currently share with pricing services might be released to other parties beyond the scope of existing agreements.
- When pricing information from third parties is based on transactions of similar instruments, we believe the additional audit procedures to be performed could include consideration of the relative roles played by evaluators employed by (i) the applicable pricing service; (ii) regular and consistent contacts with market participants; and (iii) algorithms, in the applicable pricing service’s determinations of comparable transactions.
- Viewing bond comparability as a point along a continuum instead of a simple binary variable permits rank-ordering bonds according to their degree of similarity to the bond being valued. An ability to rank potentially comparable bonds using objective criteria can contribute to the relevance of pricing service information by tying estimations to the most closely comparable instruments while limiting the influence of data for instruments relatively less similar to the bond being evaluated.

Background on ICE Data Services

As an independent pricing vendor, ICE Data Services provides evaluated pricing and calculated pricing across a wide spectrum of instruments for more than 40 years. ICE Data Services is the marketing name for multiple entities in the pricing business described below. Interactive Data Pricing and Reference Data LLC (“Interactive Data”) is a Registered Investment Adviser with the

SEC under the Investment Advisers Act of 1940. The company provides global security evaluations designed to support financial institutions' and investment funds' pricing activities, research and portfolio management. Interactive Data offers evaluations for approximately 2.7 million fixed income instruments (including loan products), as well as Fair Value Information Services for international equities, options and futures, and valuations for complex structured products.

ICE Data Services has invested considerable resources to expand our coverage and provide our clients with greater transparency and insight into the inputs utilized to derive our evaluated and calculated prices, as well as to help automate and streamline key valuations processes.

ICE Data Services maintains active collaboration with both auditors and reporting entities through working groups, client sessions and regular meetings to discuss valuation and price validation topics. Members of our staff also have participated on the Pricing Sources task Force within the PCAOB's Standing Advisory Group.

Effective date

The Board seeks comment on the amount of time auditors would need before the proposed new auditing standard and amendments become effective.

ICE Data Services believes that if the proposed standard and amendments are adopted by the Board and approved by the SEC, auditing firms and their clients will seek additional information from third party pricing providers to assist with compliance. The audit community will require a period of learning and training in using new data and tools that are expected to become available to assist them with evaluating the relevance and reliability of pricing information provided by a pricing service. In addition, pricing services would require time to develop and test new vehicles meant to enhance transparency of pricing information as the proposed standard contemplates. Consequently, we believe that the industry as a whole would benefit from extending the effective date to audits of fiscal years beginning two years after the year of the SEC approval, or three years after the year of SEC approval if that approval occurs in the fourth quarter.

Avoiding bias in fair value estimates

The Proposal's stated objectives include "*emphasizing that accounting estimates should be free from bias that results in material misstatement,*" (page 16-17) and prompting auditors "*to devote greater attention to addressing potential management bias in accounting estimates, while reinforcing the need for professional skepticism.*" (page 3)

When discussing third-party pricing information, the Proposal distinguishes among different types of third parties and cites common characteristics of pricing services that reduce the risk of bias, unless a relationship exists by which company management can directly or indirectly control or significantly influence the pricing service (page 36-37).

Although the Proposal recognizes that pricing services may need to be treated differently from other third party pricing sources under some circumstances, we observe that levels of bias risk can vary across different pricing services, due to differences in approach toward valuation of financial instruments. We believe that a focused awareness of such distinctions could strengthen the audit process.

For any security or category of securities, market quotations available in the marketplace may be biased, and even reported trades, may not all be equally representative of fair value. A valuation approach that entails automatically combining or averaging market information received from a variety of sources without human oversight may be susceptible to bias, or even manipulation, by certain market participants submitting raw data to the third party. Additionally, approaches that systemically adjust to client price challenges without relying on human oversight to confirm the validity and context of the challenge data can equally create a bias, or even manipulation.

Accordingly, we believe that:

- The diversity of market data creates an important role for human oversight in the analysis, weighting, and synthesis of such data for the creation of pricing information.
- A valuation approach that treats each piece of incoming information as a distinct input that must be validated and its significance determined by a combination of sophisticated technology and evaluator oversight, may reduce the risk that unrepresentative data submitted by an interested party could influence the pricing information.
- The Board's objective of heightening the need for professional skepticism could be advanced if auditors were directed to consider a pricing service's procedures for assessing market information when assessing the reliability and relevance of pricing service information.

When filtering market data for potential use in our pricing models, ICE Data Services applies an approach akin to the concept of "professional skepticism" that auditors are expected to practice toward data provided by their clients. ICE Data Services performs a security and/or sector review that helps us determine whether or not trade or bid information is consistent with other recent information available to use or derived by us. Trade and bid information will be reflected in our

evaluations for comparable bonds, to the extent the information impacts our opinion of what a holder would receive for those securities. If we determine that trade or bid information is not consistent with other information available to us, the trade or bid will not be reflected in that day's evaluation.

Our evaluated pricing process also includes intra-day, weekly, and/or monthly quality controls in support of our evaluations.

Reliability of pricing service information

On pages A1-15 and pages A3-35-37, the Proposal mentions three factors that affect the reliability of pricing information provided by a pricing service:

- a) The experience and expertise of the pricing service relative to the types of financial instruments being valued, including whether the financial instruments being valued are routinely priced by the pricing service;
- b) Whether the methodology used by the pricing service to evaluate or value the financial instrument being tested is in conformity with the applicable financial reporting framework; and
- c) Whether the pricing service has a relationship with the company by which company management has the ability to directly or indirectly control or significantly influence the pricing service.

We agree that the above factors affect reliability, and that a pricing service's experience and expertise should be gauged in context of the types of financial instruments being valued and whether those instruments are "routinely priced" by the pricing service.

We suggest the Board consider augmenting the above with wording such as:

When assessing a pricing service's experience and expertise, auditors may consider (among other things):

- The number of evaluators employed by the service, and the length and nature of the evaluators' financial industry experience.
- The degree to which the informational resources that the pricing service makes available to assist auditors and clients in fulfilling their responsibility to:
 - understand information provided by third-party pricing sources; and

- determine whether the methodology used by the pricing service to evaluate/value the financial instrument being tested is in conformity with the applicable financial reporting framework.
- The evaluation quality controls practiced by the pricing service.
- Evidence that the pricing service maintains a rule-governed price challenge process supported by appropriate technology resources. This should be supported by suitable record keeping policies and providing controls around these processes.

In addition, we note that the Board used terminology such as fair value estimates, fair values and determining fair value when describing the role of pricing services (page A1-15). As indicated in guidance previously issued by the Securities and Exchange Commission¹, and consistent with the industry view of the role of a pricing services, pricing services provide evaluated pricing or other pricing information designed to assist the users in determining the fair value of their portfolio securities. Pricing services do not engage in determining fair value for clients. As such we suggest that the terminology used in the standard to describe the role of a pricing service will be revised to be more consistent with the SEC and industry view on the role of a pricing service.

Relevance of pricing service information

On pages A1-16-17 and A3-35-37, the Proposal enumerates factors that affect the relevance of pricing information provided by a pricing service and provides direction on audit procedures for evaluating the relevance of pricing service information, depending on the inputs used by the pricing service:

- a) quoted prices in active markets for identical financial instruments
- b) transactions of similar financial instruments, or
- c) information other than recent transactions for the same or similar financial instruments.

The Proposal further states:

- For pricing information based on transactions of similar financial instruments, the auditor should perform additional audit procedures to evaluate the process used by the pricing service.
- When there are no recent transactions for the same or similar financial instruments, the auditor should perform additional audit procedures, including evaluating the

¹ See Money Market Fund Reform; Amendments to Form PF; Release No. 33-9616, IA-3879; IC-31166; FR-84; File No. S7-03-13 and corresponding Valuation Guidance Frequently Asked Questions.

appropriateness of the valuation method and the reasonableness of observable and unobservable inputs used by the pricing service.

ICE Data Services agrees with the overall spirit of the above passages, which is consistent with the principles set forth in ASC 820. In particular, we believe that the most effective approach for testing the reasonableness of pricing service's estimates is to compare estimated values with observable market data, where possible: trades, dealer quotes, and other relevant observable information including comparable securities.

We also agree with the Proposal's emphasis that audit responses should be risk-based, enabling the auditor to focus attention on estimates with the greatest risk of material misstatement. Citing AS 2301, the Proposal notes that as the assessed risk of material misstatement increases, the evidence from substantive procedures that the auditor should obtain also increases. On page A1-14, the Proposal outlines matters the auditor should take into account to identify and assess risks of material misstatement related to the fair value of financial instruments.

Close tying of audit responses for financial instruments to risks of material misstatement has the benefit of limiting the need for auditors to sharply expand their demands for market data. ICE Data Services has long argued for a selective approach to validating third-party pricing information. Rather than examining prices for all securities or a randomly drawn sample of portfolio assets, we believe that both asset owners and auditors benefit when they concentrate their price verification efforts on selected samples of assets drawn from asset types associated with relatively high valuation risks. We believe the three-part division set out in the Proposal provides useful guidance for a selective and risk-based approach for auditing information from pricing services.²

Numerous fixed-income instruments are neither actively traded nor actively quoted. Such instruments may be valued based on comparable securities for which current market data is available. Pricing service's methodologies for such securities require making judgments regarding the criteria for identifying comparable instruments and the appropriate price or yield spread to apply between a comparable and the security in question. In such instances, it is impractical for an auditor to test exhaustively each individual evaluation and assess all associated input data. Consequently, a selective, risk-driven approach is likely to be both more effective and more efficient than an effort to validate every fair value determination in a company's financial

² As stated in our comment letter on the 2014 Staff Consultation Paper: *"We believe the goals of Auditing Standard 12, "Auditing Standard No. 12: Identifying and Assessing Risks of Material Misstatement," would be best served by directing auditors to focus their attention on those areas of financial reporting that pose the highest risks to reliable financial reporting. With regard to fair value measurements, the highest risk areas might include complex securities, thinly traded securities, and instruments for which no current market data is available."*

statements. The selective approach requires that the auditor develop an understanding of the assets, liabilities, and third-party data in order to assess which data is most relevant for assessing accounting risk. This spares both auditors and third parties the unnecessary effort of processing large amounts of data that may have little value for assessing the risk of material misstatements.

In addition, we believe that considerations of cost and potential unintended consequences make it desirable for a standard to guide auditors toward a risk-based sampling approach and, conversely, to avoid materially broadening the scope of market data required to conduct an audit.

Enlarging the scope of market data required by auditors will impose economic costs on both auditors and reporting entities. Pricing services can be expected to pass through any costs they incur for providing additional data and developing additional services to their direct clients, who include auditors. In addition, auditors can be expected to pass along to clients any costs they incur to obtain and examine a larger universe of transaction-related data. In a recent speech Jay Clayton, the chairman of the Securities and Exchange Commission, signaled increased attention to costs of compliance, including indirect costs, when the SEC formulates and implements rules.³

The risk of unintended consequences could arise if originators of market data, such as securities dealers and investment firms, perceived that quote and trade data they currently share with third parties on a confidential basis might be released to other parties beyond the scope of existing agreements. If data originators pulled back from sharing such data, the amount of market data available to both auditors and market participants could shrink -- an unintended consequence that would run directly counter to the auditing standard's desired effect.

Some market data is subject to confidentiality agreements

Despite recent advances toward greater transparency into market inputs, institutional arrangements often impede pricing services from releasing all relevant inputs used in their evaluation process. In practice, even inputs that may be judged "observable" under ASC 820 may have limited visibility outside a narrow circle of market participants due to various constraints on redistribution. For example, many agreements between ICE Data Services and its market data sources include confidentiality provisions that permit us to utilize their trade or quote data to produce evaluations, but bar us from displaying or sharing their data beyond our organization. We are also barred from sharing information from trade confirmations that clients submit to us through our challenge process.

³ Remarks at the Economic Club of New York, July 12, 2017, <https://www.sec.gov/news/speech/remarks-economic-club-new-york>

Identifying Comparable Transactions and Quantifying Their Relevance

On pages A3-35 through 37, the Proposal states that when the pricing information is based on transactions of similar instruments, additional audit procedures would be required to evaluate the process used by the pricing service. The additional audit procedures may include, for example, evaluating how comparable transactions are selected and monitored or how matrix pricing is developed.

We believe the following observations about similar financial instruments can be pertinent to the audit process.

- Selection of comparable transactions is a dynamic process whose outcome can be enhanced by the addition of human judgment alongside of algorithms that seek to identify financial instruments with common features. A list of specific instruments considered comparable to the instrument being valued constitutes one of the assumptions that market participants would use when pricing the financial instrument. Therefore, we believe that the additional audit procedures to be performed to evaluate the process used by a pricing service when pricing information is based on transactions of similar instruments could include consideration of the relative roles played by evaluators employed by the pricing service, regular contracts with market participants, and algorithms, in the pricing service's determinations of comparable transactions.
- Comparability among financial instruments need not be a binary variable. Viewing bond comparability as a point along a continuum allows for ranking a list of similar bonds according to their degree of similarity to the bond being valued. An ability to rank potentially comparable bonds using objective criteria can contribute to the relevance of pricing service information in two ways:
 - Providing a higher level of confidence that the most relevant instruments were used to produce evaluations based on transactions of similar instruments.
 - Making it possible for other relevant market data, such as firm quotes for instruments most similar to the bond being valued but have no recent transactions, to influence the pricing information along with transactions in a bond that might have relatively less similarity to the bond being valued. We believe that situations arise in which market participants would consider a firm quote for a closely similar bond to be a more reflective data point than a recent transaction in a distantly similar bond.

Summary

ICE Data Services appreciates the opportunity to present our views on the Proposed Auditing Standard, *Auditing Accounting Estimates, Including Fair Value Measurements* and Proposed Amendments to PCAOB Auditing Standards. We support the proposal to develop a new standard that would consolidate and augment provisions from a number of existing audit standards that address this subject. We strongly believe that the goals of reinforcing best practices in auditing fair value estimates and evidence obtained from third party pricing sources, updating existing standards to remove perceived inconsistencies, and further integrating the requirements of the existing standards with those of the risk-assessment standards, which would be best served by adopting the proposal subject to the following added considerations:

- Extend the effective date to audits of fiscal years beginning two years after the year of SEC approval, or three years after the year of SEC approval if that approval occurs in the fourth quarter.
- To further reduce the risk of manipulation of third party pricing services, incorporate language encouraging auditors to consider a pricing service's procedures for assessing market information when assessing the reliability and relevance of pricing service information.
- Augment the guidance regarding reliability of pricing service information by encouraging auditors to consider: the number and financial industry experience levels of evaluators employed by the service; the extent of informational resources that the pricing service provides to assist users in understanding its data and evaluation methodologies; and the service's evaluation quality controls and price challenge processes.
- Guide auditors to practice a risk-based sampling approach toward assessing the relevance of pricing service information. Focusing audit attention on estimates with the greatest risk of material misstatement aligns with existing auditor standards and can help to ensure that the standard will not materially broaden the scope of market data required to conduct an audit. Expanding data requirements would impose economic costs on auditors and reporting entities, and may also induce market data originators such as securities dealers and investment firms to stop sharing their confidential market data with pricing services.
- When pricing information is based on transactions of similar instruments, the additional audit procedures to be performed could usefully include consideration of the relative roles played by the pricing service's evaluators, regular contacts with market participants, and algorithms, in the pricing service's determinations of comparable transactions. We believe audit quality also could benefit from viewing bond comparability as a point along a continuum with many possible values, and from considering the pricing service's ability to rank potentially comparable bonds using objective criteria.

We look forward to working with the Staff, the PCAOB and the audit community on this important issue.

Kind regards,



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