



IFRS 13 Fair Value Measurement

Credibility

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Professionalism

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AccountAbility

Agenda



- ❖ Objective
- ❖ Scope
- ❖ Definitions
- ❖ Measurement
- ❖ Disclosure

Objective of IFRS 13



- ❖ The IFRS applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements except in specified circumstances;
- ❖ The IFRS is to be applied for periods beginning on or after 1 January 2013;
- ❖ Some IFRSs require or permit entities to measure or disclose the fair value of assets, liabilities or their own equity instruments;
- ❖ The requirements for measuring fair value were dispersed and in many cases did not articulate a clear measurement objective; and
- ❖ Part of the work between IASB and FASB to develop common requirements for measuring fair value measurements

Objective of IFRS 13



- ❖ Fair value is **a market based measurement**, not an entity specific measurement;
- ❖ For some assets and liabilities, observable market transactions or market information might be available while for others it might not be available;
- ❖ Regardless the objective of a fair value measurement in both cases is the same i.e. **to estimate the price at which an orderly transaction to sell the asset or transfer a liability would take place between market participants at the measurement date under current market conditions.**
- ❖ When a price for an identical asset or liability is not observable, an entity measures fair value using another valuation technique that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs.

Scope



- ❖ The IFRS explains how to measure fair value for financial reporting;
- ❖ It does not require fair value measurements in addition to those already required or permitted by other IFRSs and is not intended to establish valuation standards or affect valuation practices outside financial reporting;
- ❖ IFRS 13 applies when another IFRS requires or permits fair value **measurement** or **disclosures** about fair value measurements;
- ❖ It does not apply to the following;
 - ✓ Share based payment transactions under IFRS2
 - ✓ Leasing transactions within the scope of IAS 17
 - ✓ measurements that have similarities to fair value but are not fair value such as net realisable value in IAS 2 or value in use under IAS 36.

Definitions



- ❖ **Fair value** – the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date;
- ❖ **Level 1 inputs** – quoted (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- ❖ **Level 2 inputs** – inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly or indirectly;

Definitions



- ❖ **Level 3 inputs** – unobservable inputs for the asset or liability;
- ❖ **Principal market** – the market with the greatest volume and level of activity for the asset or liability.
- ❖ A fair value measurement assumes that the transaction to sell the asset or to transfer the liability takes place in the principal market for the asset or liability.
- ❖ **Most advantageous market** – the market that maximizes the amount that would be received to sell the asset or minimize the amount that would be paid to transfer the liability.
- ❖ In the absence of a principal market, the transaction is assumed to take place in the most advantageous market for the asset or liability.

Measurement



- ❖ A fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between **market participants** to sell the asset or transfer the liability under current market conditions;
- ❖ This assumes that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability or the absence of a principal market in the most advantageous market;
- ❖ The market in which the entity would normally enter into a transaction to sell the asset is presumed to be the principal market;
- ❖ The price should not be adjusted for transaction costs and these should be accounted for in accordance with other IFRSs.

Measurement



❖ Application to a non financial asset – a fair value measurement of a non financial asset takes into account a market participant’s ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use;

Valuation approaches and techniques



- ❖ An entity shall use valuation approaches and techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs;
- ❖ IFRS 13 refers to a “valuation approach” as a broad category of techniques, whereas a “valuation technique” refers to a specific technique such as a particular option pricing model.

Valuation approaches and techniques



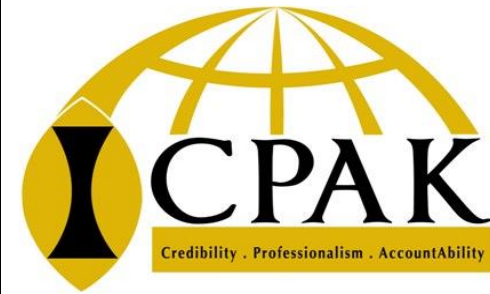
- ❖ Valuation techniques used to measure fair value fall under three approaches
 - ❖ Market approach
 - ❖ Cost approach
 - ❖ Income approach
- ❖ IFRS 13 does not establish requirements for specific valuation techniques to be used.
- ❖ In some cases a single technique will be appropriate, in other cases multiple valuation techniques will be appropriate.
- ❖ Valuation techniques used to measure fair value shall be applied consistently.
- ❖ However a change is appropriate if it results in a measurement that is more representative of fair value.

Valuation techniques



- ❖ **Market approach** – uses prices and other relevant information generated by market transactions involving identical or comparable assets;
- ❖ **Cost approach** – reflects the amount that would be required currently to replace the service capacity of an asset.
- ❖ A market participant buyer would not pay more for an asset than the amount for which it could replace the service capacity of that asset;
- ❖ **Income approach** – converts future amounts e.g. cash flows or income and expense to a single current (discounted) amount. When the income approach is used, the fair value measurement reflects current market expectation about those future amounts.
- ❖ Examples valuation techniques include present value techniques and option pricing models.

Inputs to valuation techniques



- ❖ **Inputs** to valuation techniques are the assumptions that market participants would use in pricing the asset or liability.
- ❖ These inputs include assumptions about risk, such as the risk inherent in a particular valuation technique used to measure fair value and the risk inherent in the inputs to the valuation technique
- ❖ An entity selects the valuation techniques
 - ❖ That are appropriate in the circumstances
 - ❖ For which sufficient data is available
 - ❖ That maximizes the use of relevant observable inputs and minimize the use of unobservable inputs

Fair value hierarchy



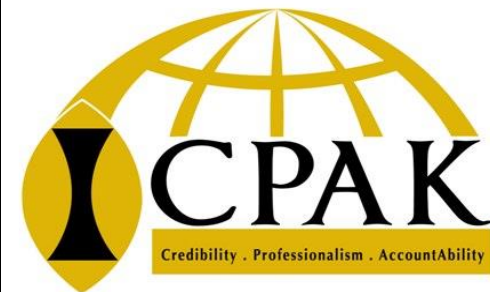
- ❖ To increase consistency and comparability in fair value measurement, IFRS 13 establishes a fair value hierarchy that categorizes into three levels the inputs to valuation techniques used to measure fair value.
- ❖ This gives highest priority to quoted prices in active markets and the lowest priority to unobservable inputs.
- ❖ Fair value hierarchy **prioritizes the inputs to valuation** techniques, not the valuation techniques used to measure fair value.

Fair value hierarchy



- ❖ **level 1 inputs** - These are quoted prices (unadjusted) in active market for identical assets or liabilities;
- ❖ A quoted price in an active market provides the most reliable evidence of fair value;
- ❖ A level 1 input will be available for many financial assets and liabilities, some of which might be exchanged in multiple active markets.
- ❖ The emphasis within level 1 is determining the principal market for the asset or liability or in the absence the most advantageous market.

Fair value hierarchy



- ❖ **Level 2 inputs** – these are inputs other than the quoted prices included within level 1 that are observable for the asset or liability either directly or indirectly;
- ❖ Level 2 inputs include;
 - ❖ Quoted prices for similar assets or liabilities in active markets
 - ❖ Quoted prices for identical or similar assets in markets that are not active
 - ❖ Inputs other than quoted prices that are observable for the asset or liability e.g. Interest rates and yield curves observable at commonly quoted intervals
 - ❖ Market corroborated inputs

Fair value hierarchy



- ❖ Adjustments to level 2 inputs will vary depending on factors specific to the asset such as condition or location of the asset, extent to which inputs relate to items that are comparable to the asset and the volume or level of activity in the market within which the inputs are observed;
- ❖ An adjustment to a level 2 input that is significant to the entire measurement might result in a fair value measurement categorised within level 3 of the fair value hierarchy if the adjustment uses significant unobservable inputs.

Fair value hierarchy



- ❖ Level 3 inputs – these are unobservable inputs for the asset or liability
- ❖ Unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little if any market activity for the asset or liability at the measurement date;
- ❖ An entity shall develop unobservable inputs using the best information available in the circumstances which might include the entity's own data.
- ❖ Own data shall be adjusted if reasonable available information indicates that other market participants would use different data .
- ❖ An entity need not make exhaustive efforts to obtain information about market participants assumptions.

Disclosures



- ❖ An entity shall disclose information that helps users of its financial statements assess for assets and liabilities measured at fair value, the valuation techniques used to develop those measurements
- ❖ For recurring fair value measurements using significant unobservable inputs (level 3) the effects of the measurement on the profit or loss or other comprehensive income

Disclosures



- ❖ For recurring and non recurring fair value measurements, the fair value at the end of the reporting period and for non recurring fair value measurements, the reasons for the measurement.
- ❖ Recurring fair value measurements are those that other IFRSs require or permit at the end of the period;
- ❖ Non recurring fair value measurements are those that other IFRSs require in particular circumstances e.g. under IFRS 5 non current assets held for sale;

Disclosures



- ❖ The level of fair value hierarchy within which the fair value measurements are categorized
- ❖ A description of the valuation techniques and the inputs used in the fair value measurement
- ❖ For recurring fair value measurements a reconciliation from the opening balance to the closing balance disclosing separately the total gains for the period recognized in profit or loss, under other comprehensive income, purchases sales and settlements;
- ❖ The amounts of any transfers into and out of level 3 of the fair value hierarchy

Summary of measurement basis

Standard	Measurement Basis
IAS 2 – Inventories	Inventories shall be measured at the lower of cost and net realizable value.
IAS 16 –Property, Plant and Equipment	An entity shall choose either the cost model or the revaluation model as its accounting policy
IAS 40 – Investment Property	Cost or fair value model
IFRS 5 – Non current assets held for sale and discontinued operations	Lower of carrying amount and fair value less costs to sell
IAS 41 – Agriculture	Fair value

Measurement basis

- ❖ **Net realisable value** - Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
- ❖ **Cost model** - cost less any accumulated depreciation and any accumulated impairment losses.
- ❖ **Revaluation model** - After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses.