

An Overview of Asset Valuation

CPA. Dr Elizabeth Kalunda

Presentation Overview

- Definition of assets
- Structure of IFRS
- Why value assets
- Asset Valuation models
- Types of assets and relevant standards
- Selection criteria of Standard to apply
- Examples IAS 16 and 2

Objectives

- Appreciate the discourse in definition of assets
- Recall the structure of IFRS
- Justify the need to value assets
- Discuss the different types of assets and relevant standards
- Apply the selection criteria of applicable standard
- Differentiate the asset valuation models
- Apply the criteria in valuation on selected standards IAS 16,2, 40

Definition



Existing definitions of an Asset

- A resource controlled by the entity as a result of past events from which future economic benefits are expected to flow to the entity



Suggested revised definition

- A present economic resource controlled by the entity as a result of past events
- An economic resource = a right, or other source of value, that is capable of producing economic benefits

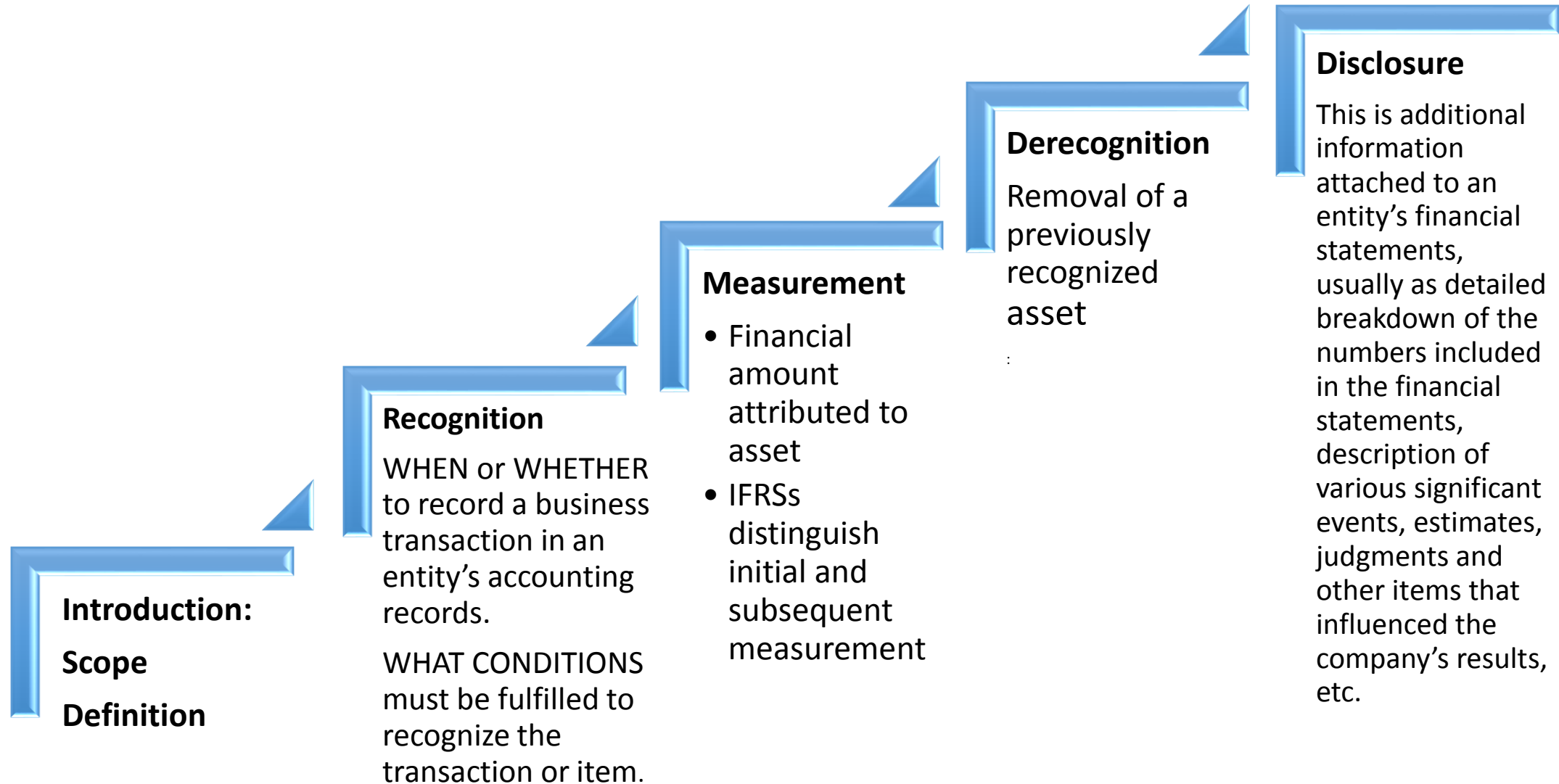
Why value assets ?



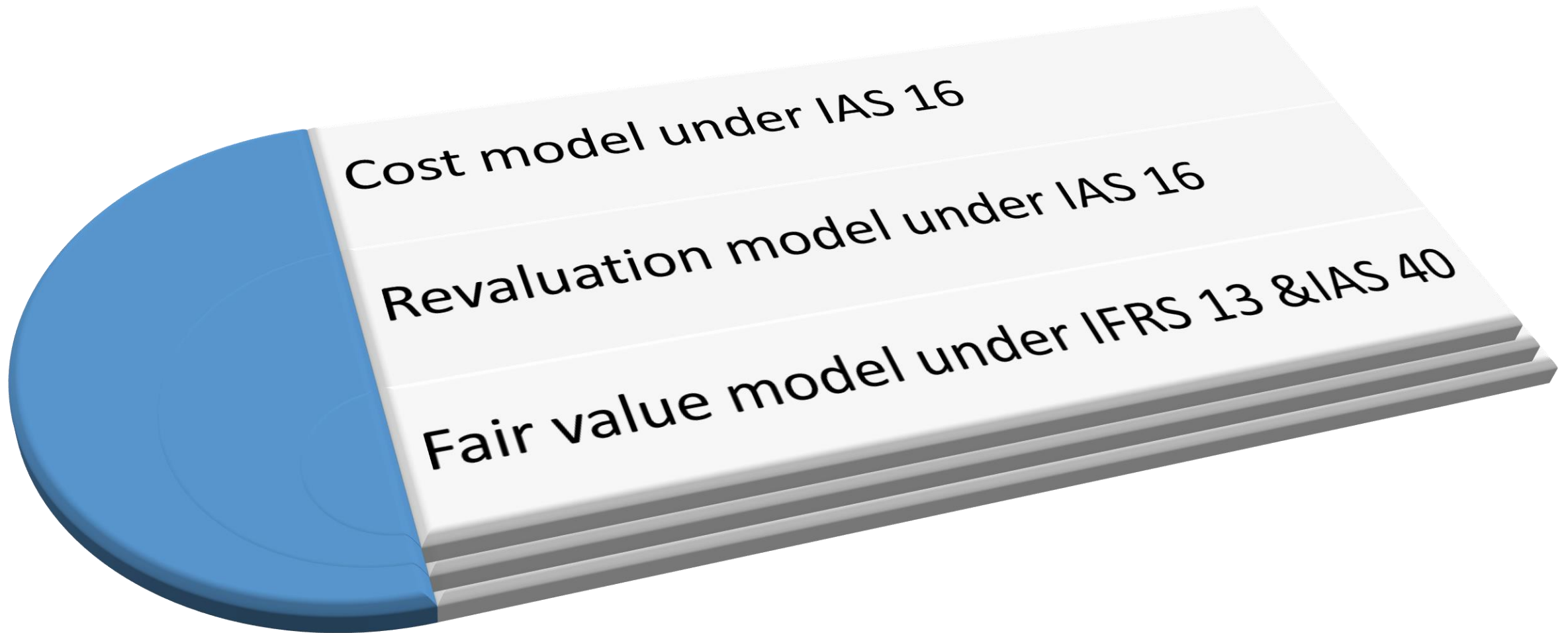
Reasons

- Buying or Selling Property
- Taxation
- Rent Function
- Security of loans or Mortgage
- Compulsory acquisition
- Insurance
- ★ Financial Reporting ★

Structure of the IFRS



Summary Measurements Models

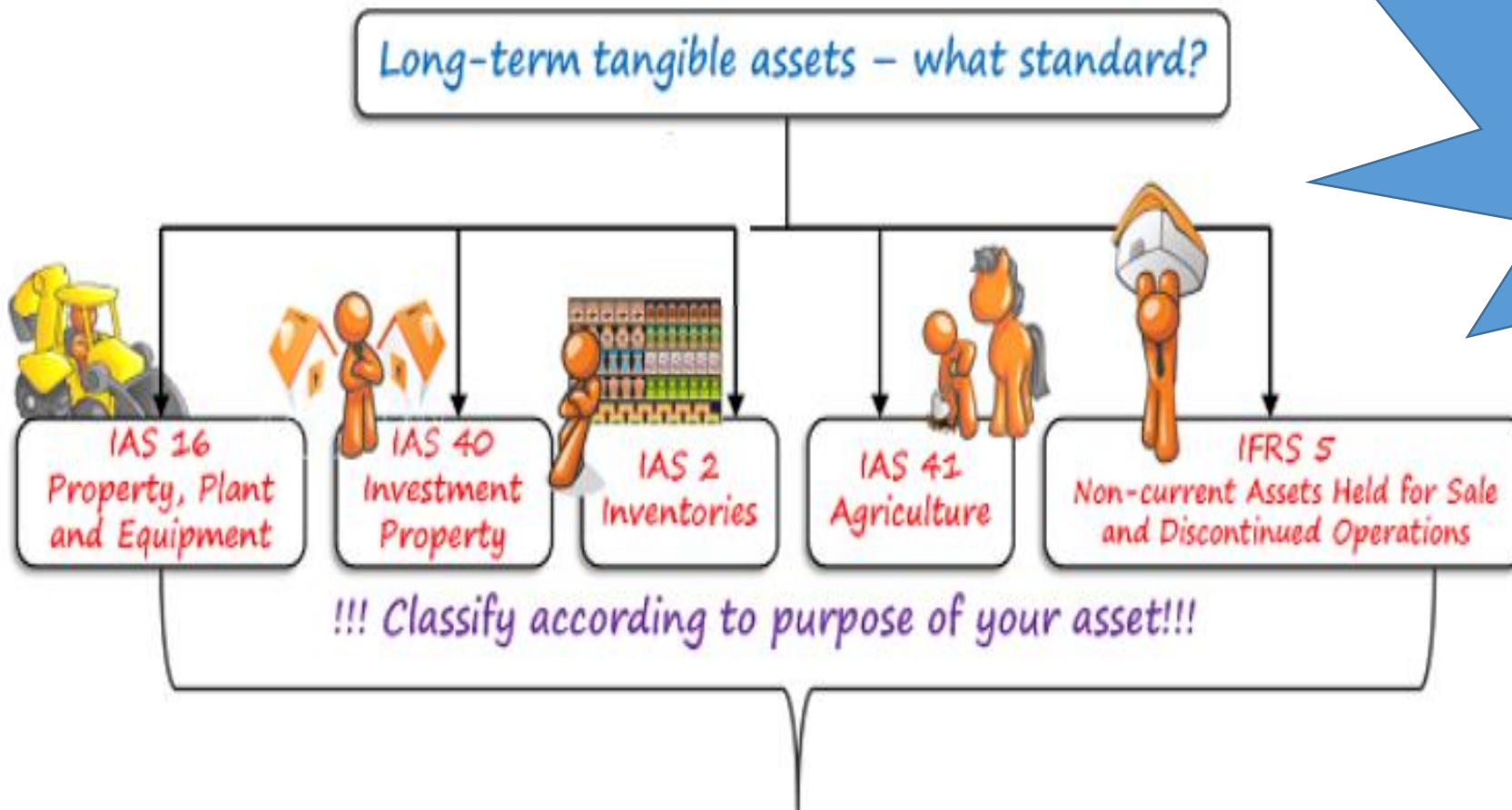


Types of Assets & Relevant Standards

- Inventory IAS 2
- Property plant and equipment IAS 16
- Investment Property IAS 40
- Agricultural Asset IAS 41
- Financial Assets IFRS 9
- Deferred Tax IAS 12
- Non-current Assets Held for Sale and Discontinued Operations IFRS 5

Selection of Standard to apply

- Why do you hold an asset: purpose or reason???



This classification is NOT that easy and obvious and you need to make judgment in order to pick the right standard

Why do you hold an asset: purpose or reason

Examples

- Land or building, or part of a building or both held by an entity to earn rentals and/or for capital appreciation: IAS 40-Investment property.

Any other properties are accounted for as PPE or inventory.

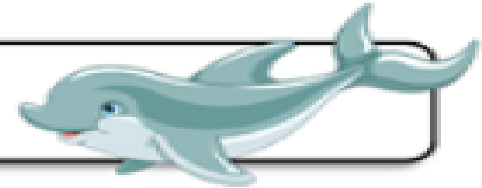
- If they are held for use in the production or supply of goods or services (IAS 16, PPE)
- If they are held for sale in the ordinary course of business (IAS 2, Inventories)

Selection of Standard to apply

- Example –The Indianapolis dolphin show has exciting water adventures where dolphins dance in the water.
- Under which standards are the dolphins accounted for?
- The fact it's a living animal might suggest that it's automatically biological asset under IAS 41, but is it really?
- Well, no. Here, the dolphins were used primarily for being shown to people and they generated income from fees paid by these people – this is NOT an agricultural activity and as a result, IAS 41 does NOT apply. Yes, you guessed that – here, IAS 16 applies.
- But, if the company would have bred the dolphins in order to get their offspring (children) and sell young dolphins, then yes, this would have been an agricultural activity and IAS 41 applies here.

Selection of Standard to apply...contd

Example: How to classify dolphins?



How do you generate income from dolphins?

To get fees from clients observing dolphin show



IAS 16
Property, Plant and Equipment

To breed an offspring (children) and sell it



IAS 41
Agriculture

IAS 16: Property, Plant and Equipment

- Prescribes the accounting treatment for PPE
- One of the most important and commonly applied standards.
- The main issues in IAS 16 are
 - ❖ Recognition of PPE
 - ❖ Measurement at and after recognition
 - ❖ Impairment of PPE (IAS 36 deals with impairment in more detail)
 - ❖ Derecognition

IAS 16: Property, Plant and Equipment

Recognition

- a) It is probable that future economic benefits associated with the item will flow to the entity
- b) The cost of the item can be measured reliably.

IAS 16: PPE

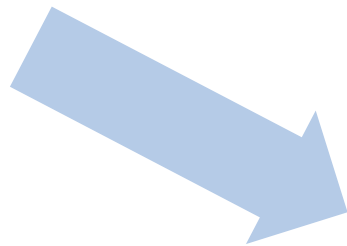


Definition

- PPE are tangible items
- a) held for use in production/supply of goods/services
 - b) rental to others
 - c) administrative purposes during more than one period.

Application of recognition criteria

When incurred initially.
subsequently on replacement or servicing



IAS 16...contd

Issues:

- The cost of an item of PPE is the cash price equivalent at the recognition date.
- If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognized as interest over the period of credit (unless such interest is capitalized in accordance with IAS 23).
- If an asset is acquired in exchange for another non-monetary asset, the cost will be measured at the fair value unless
 - (a) the exchange transaction lacks commercial substance or
 - (b) the fair value of neither the asset received nor the asset given up is reliably measurable.
 - (c) If the acquired item is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

IAS 16...contd

Initial Measurement

Cost

Subsequent Measurement

An entity may choose 2 accounting models for its property plant and equipment:

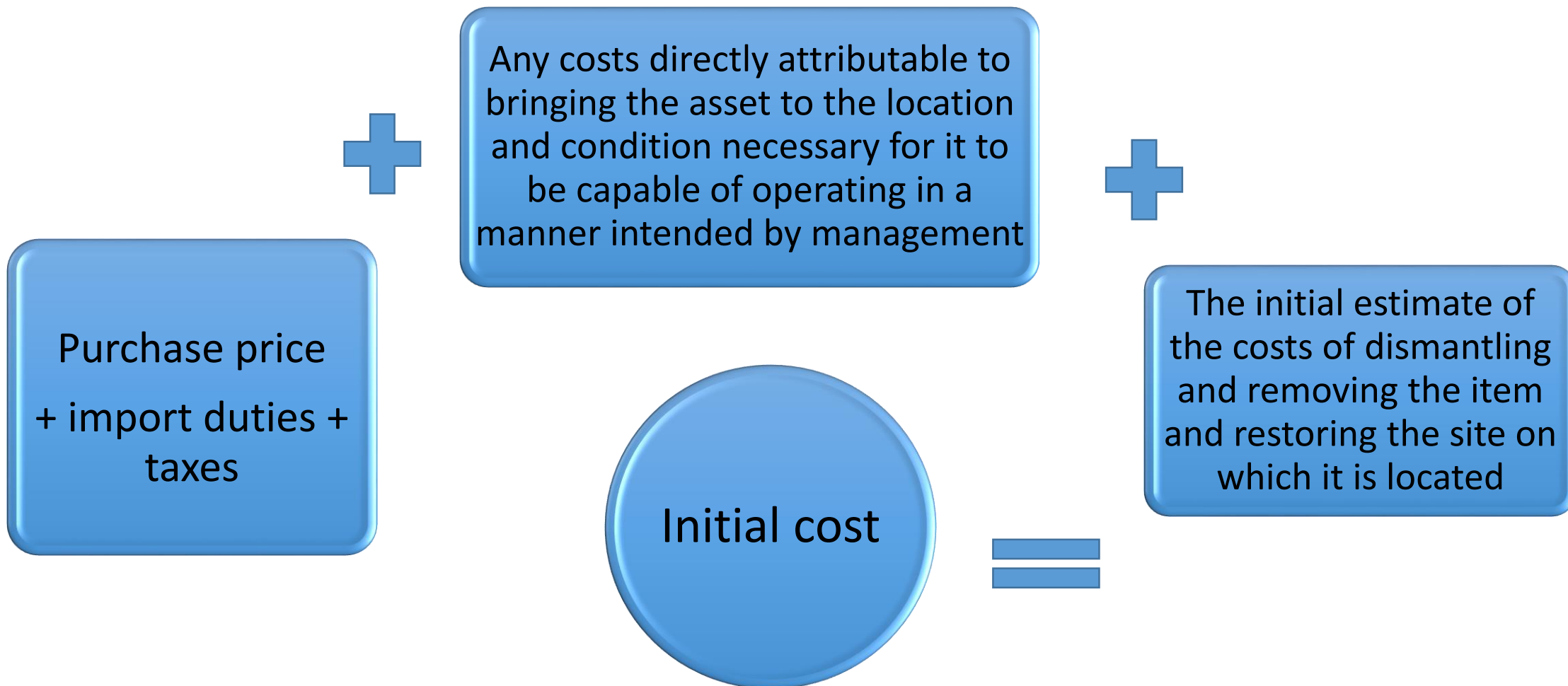
❖ Cost model

An entity shall carry an asset at its cost less any accumulated depreciation and any accumulated impairment losses.

❖ Revaluation model

An entity shall carry an asset at a revalued amount. Revalued amount is its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

Initial cost-IAS 16



Subsequent measurement-Cost model

Initial Cost

Depreciation:
systematic basis
over the asset's
useful life

Any change changes
are accounted for
prospectively(IAS 8)

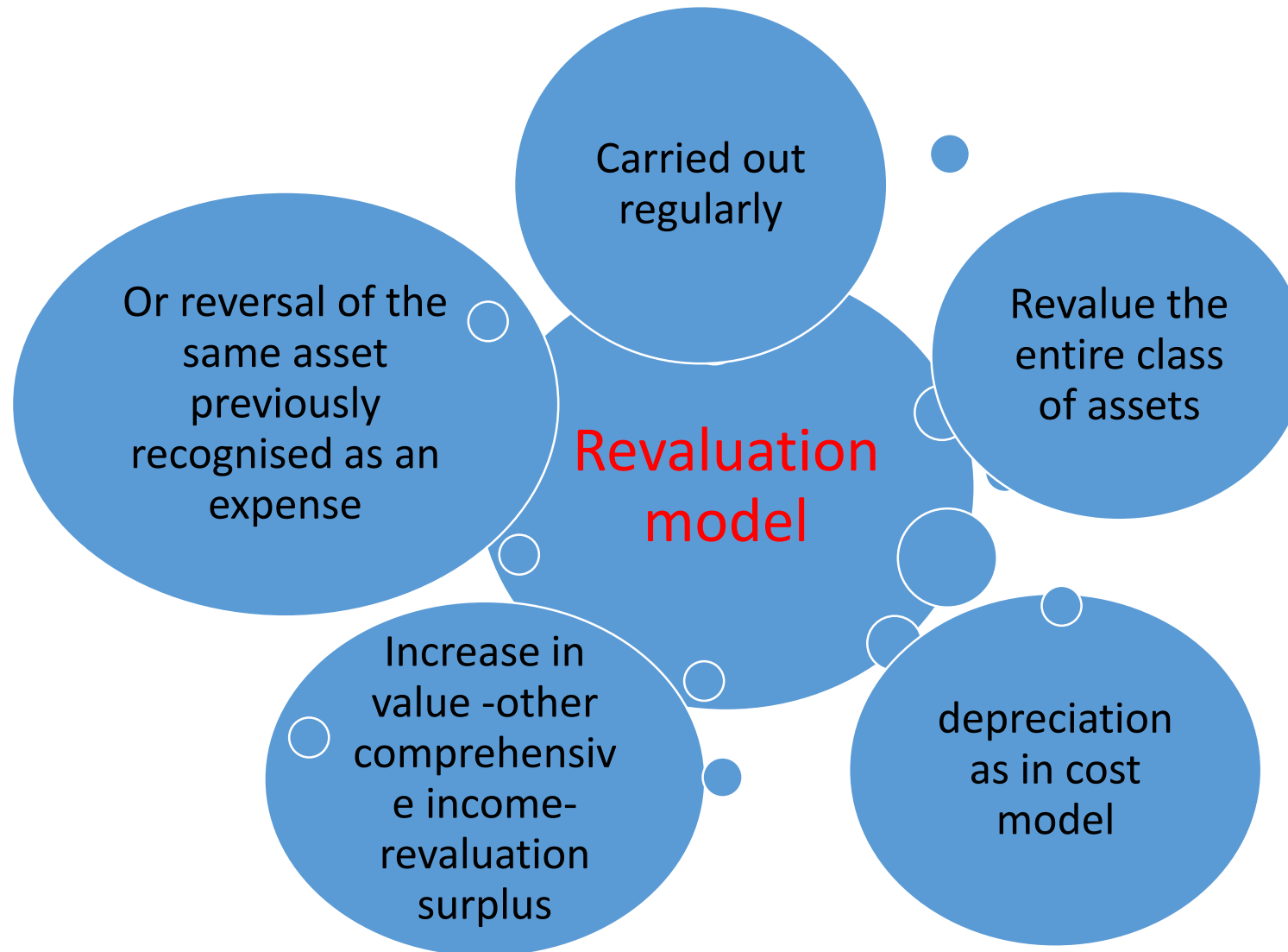
less acc.
depreciation

Residual value,
useful life & dep
method are
reviewed annually

Cost model

Less impairment losses

Revaluation model



IAS 16 (Bearer Plants) and IAS 41



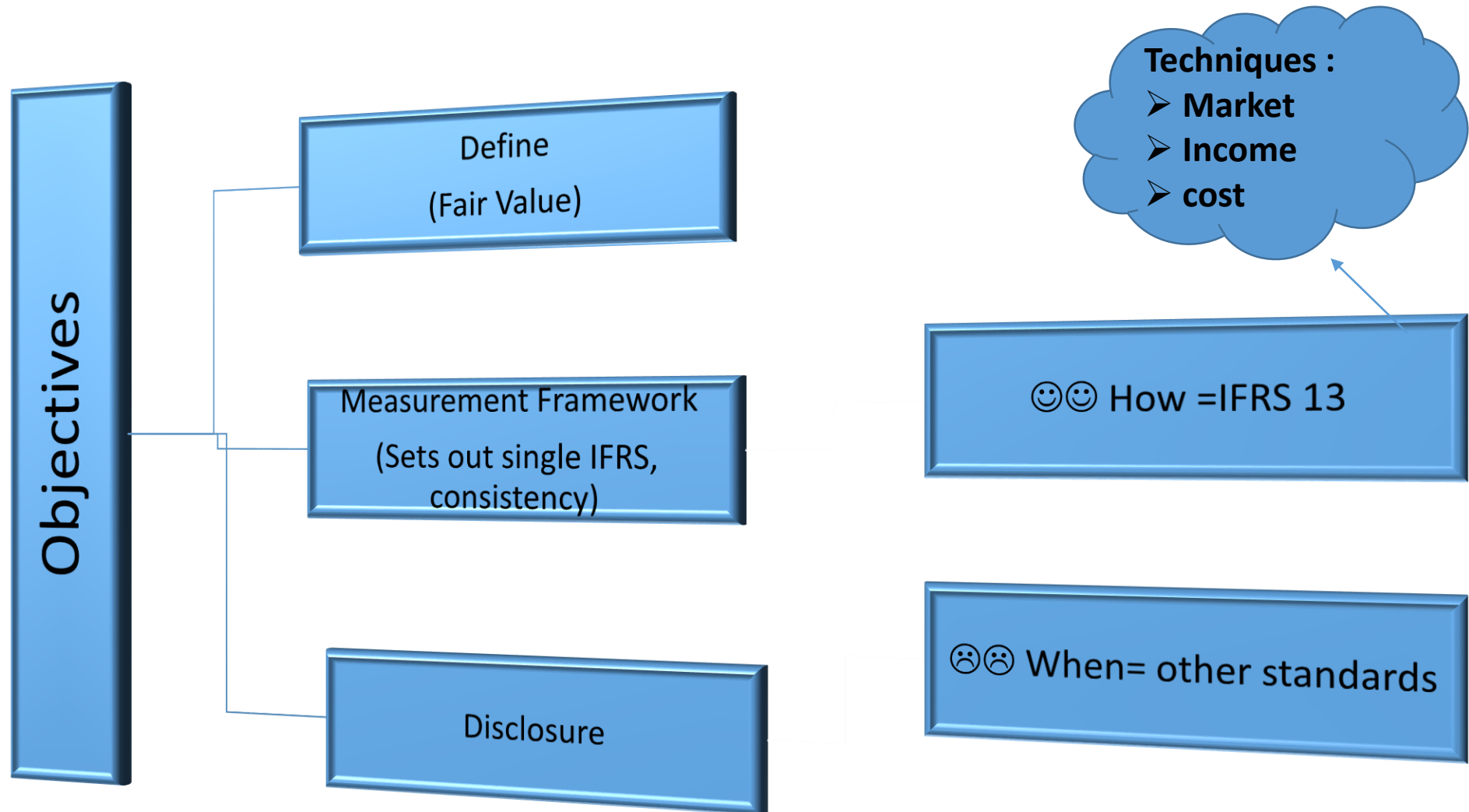
IAS 16 (Bearer Plants)
Cost Model
or
Revaluation Model



Produce IAS 41
Fair Value Model

Effective
1.1.2016

IFRS 13 Fair Value Measurement



Definition of 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*”

- This price is an



exit price

and

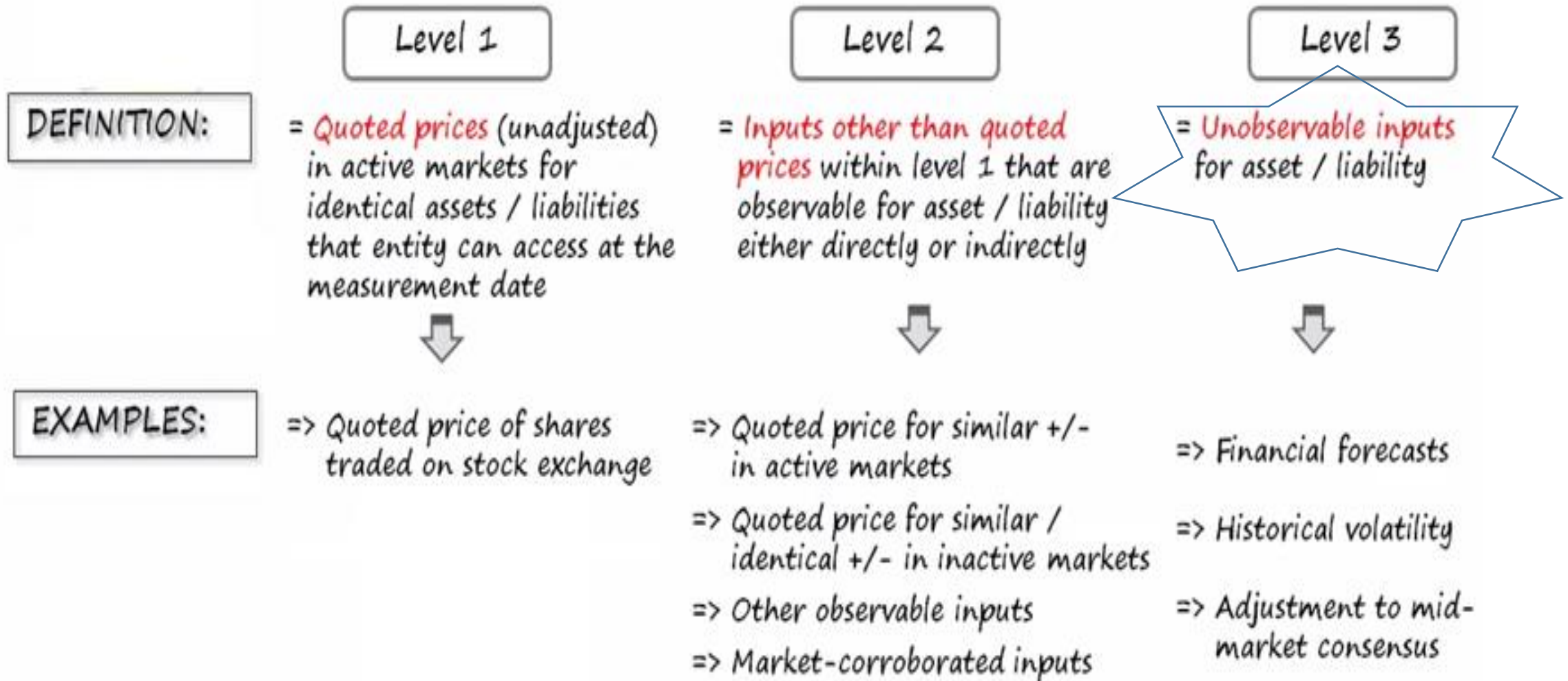


market and not
entity based



Fair Value

- A fair value measurement requires an entity to determine all of the following:
 - ❖ The particular asset that is the subject of the measurement (consistently with its unit of account)
 - ❖ for a non-financial asset, the valuation premise that is appropriate for the measurement (consistently with its highest and best use)
 - ❖ The principal or most advantageous market for the asset
 - ❖ The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.

Fair Value Hierarchy



Difference between Fair Value and Revaluation Model

	Fair value model	vs.	Revaluation model
Which standard?	 IAS 40 Investment Property		IAS 16 Property, Plant and Equipment 
What assets?	<ul style="list-style-type: none">✓ For capital appreciation✓ To earn rentals✓ Buildings and lands only		<ul style="list-style-type: none">✓ For production of goods/rendering services✓ For rentals to others✓ For administrative purposes
How to apply?	<ul style="list-style-type: none">✓ Keep at fair value✓ Fair value changes in P/L		<ul style="list-style-type: none">✓ Revalue regularly to fair value✓ Revaluation changes in equity
Depreciation?	***NO***		***YES***



