

## **Comparison of IFRS 13 *Fair Value Measurement* with the AASB’s submissions on selected issues in the related Exposure Drafts**

This document summarises selected issues raised by the AASB in its submissions to the IASB on ED/2009/5 *Fair Value Measurement* and ED/2010/7 *Measurement Uncertainty Analysis Disclosure for Fair Value Measurement* and how its comments have been addressed in IFRS 13 *Fair Value Measurement*.

AASB staff have included below only those issues in the related Exposure Drafts that the AASB disagreed with. The issues that staff think have not been sufficiently addressed in IFRS 13 appear first (Questions 1, 5, 9 and 11), followed by the remaining issues (Questions 6, 8, 13 and a general issue on ED/2010/7) that we think have been sufficiently addressed in IFRS 13.

### **Comparison of IFRS 13 *Fair Value Measurement* with ED/2009/5 *Fair Value Measurement***

<b>Proposals in ED/2009/5 <i>Fair Value Measurement</i></b>	<b>AASB views in submissions to IASB on ED/2009/5</b>	<b>Has IFRS 13 dealt with AASB’s concerns?</b>	<b>Staff comments and recommendations</b>
<p><b>Question 1</b>  <b><i>Definition of fair value and related guidance</i></b></p> <p>The exposure draft proposes defining fair value as ‘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’ (an exit price) (see paragraph 1 of the draft IFRS and paragraphs BC15 – BC18 of the Basis for Conclusions). This is relevant only when fair value is used in IFRSs.</p> <p>Is the definition appropriate? Why or why not? If not, what would be a better definition and why?</p>	<p>The AASB requested clarification of the implications of the definition for the references to fair value in, for example, IAS 16 <i>Property, Plant and Equipment</i> and IFRS 3 <i>Business Combinations</i>. In particular, the AASB sought clarification of whether market buying prices could continue to be used to measure particular items of revalued property, plant and equipment under IAS 16 and individual assets that are part of a group of assets under IFRS 3. The ED accommodates various valuation approaches in determining fair value, including the use of a cost approach (such as depreciated replacement cost), which is an entry price notion. The AASB considered that, if the IASB regards the cost approach as consistent with an exit price notion of fair value, it would be useful for the Fair Value Measurement Standard (or its Basis for Conclusions) to explain more fully the IASB’s reasons for that conclusion. As a matter of practicality, the AASB could not see how the IASB can avoid using</p>	<p>No. The definition of fair value in IFRS 13 is the same as ED/2009/5 and the cost approach is retained in IFRS 13 as one of the valuation techniques.</p> <p>The IASB noted that an entity’s cost to replace an asset would equal the amount that a market participant buyer of that asset would pay to acquire it. Therefore, the IASB concluded that the cost approach is consistent with an exit price notion. (refer to paragraph BC141 of IFRS 13).</p>	<p>AASB staff note the apparent inconsistency between the overall exit price notion explicit in the fair value definition and the entry price notion implied in using the cost approach to calculate fair value is concerning, however, AASB staff do not think this is a fatal flaw in IFRS 13.</p> <p>No action required.</p>

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**Agenda Paper 3.2**  
**AASB Meeting – 8-9 June 2011**

<b>Proposals in ED/2009/5 Fair Value Measurement</b>	<b>AASB views in submissions to IASB on ED/2009/5</b>	<b>Has IFRS 13 dealt with AASB's concerns?</b>	<b>Staff comments and recommendations</b>
	current input values for many non-financial assets. For example, purchase price allocations for business combinations and revaluations of fixed assets under IAS 16 normally use such values.		
<p><b>Question 5</b>  <i>Application to assets: highest and best use and valuation premise</i></p> <p>The ED proposes that:</p> <p>(a) the fair value of an asset should consider a market participant's ability to generate economic benefit by using the asset or by selling it to another market participant who will use the asset in its highest and best use (see paragraphs 17-19 of the draft IFRS and paragraph BC60 of the Basis for Conclusions).</p> <p>(b) the highest and best use of an asset establishes the valuation premise, which may be either 'in use' or 'in exchange' (see paragraphs 22 and 23 of the draft IFRS and paragraphs BC56 and BC57 of the Basis for Conclusions).</p> <p>(c) the notions of highest and best use and valuation premise are not used for financial assets and are not relevant for liabilities (see paragraph 24 of the draft IFRS and paragraphs BC51 and BC52 of the Basis for Conclusions).</p> <p>Are these proposals appropriate? Why or why not?</p>	<p>The AASB considered there to be a tension between the IASB's decision to apply the highest and best use notion to assets, but not to liabilities, when measuring fair value. Entity-specific efficiencies or inefficiencies would appear to be taken into account in estimating the fair value of specialised assets but not the fair value of performance obligations. The AASB considered that this issue should be clarified in the proposed Fair Value Measurement Standard and in its Basis for Conclusions.</p>	<p>No. IFRS 13 does not provide any additional clarification on this issue in either the Standard or Basis for Conclusions (see paragraph BC63 of IFRS 13).</p>	<p>Although staff think that this issue has not been adequately addressed, we do not think this is a fatal flaw in IFRS 13.</p> <p>No action required.</p>

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<p><b>Question 9</b>  <b>Fair value at initial recognition</b></p> <p>The exposure draft lists four cases in which the fair value of an asset or liability at initial recognition might differ from the transaction price. An entity would recognise any resulting gain or loss unless the relevant IFRS for the asset or liability requires otherwise. For example, as already required by IAS 39, on initial recognition of a financial instrument, an entity would recognise the difference between the transaction price and the fair value as a gain or loss only if that fair value is evidenced by observable market prices or, when using a valuation technique, solely by observable market data (see paragraph 36 and 37 of the draft IFRS, paragraphs D27 and D32 of Appendix D and paragraphs BC76-BC79 of the Basis for Conclusions).</p> <p>Is this proposal appropriate? In which situation(s) would it not be appropriate and why?</p>	<p>With respect to the consequential amendments to paragraph AG76 of IAS 39, the AASB disagreed with the proposal to defer the recognition of any gain or loss that results from initially measuring the fair value of a financial asset or financial liability at an amount different from the transaction price, if that initial fair value is determined other than by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets (that is, it is based on a level three measurement). The AASB considered that, if the evidence supporting an estimate of the fair value of a financial asset or financial liability is sufficient to enable reliable measurement of the fair value of that asset or liability, it is sufficient to enable reliable measurement of any resulting gain or loss at the same time. Therefore, the recognition of such gains and losses in profit or loss should not be deferred.</p> <p>The AASB also recommended that the IASB clarifies whether the proposed consequential amendments will also apply to unquoted equity instruments, given the proposed removal of the cost exemption in the IASB's Exposure Draft ED/2009/7 <i>Financial Instruments: Classification and Measurement</i>. (Subsequent to this, AASB staff note that IFRS 9 <i>Financial Instruments</i> requires investments in unquoted equity instruments to be measured at fair value. However, in limited circumstances, cost may be an appropriate estimate of fair value).</p>	<p>No. The AASB's concerns and recommendations have not been addressed in IFRS 13.</p>	<p>Although AASB staff note this as an issue, we do not think it is sufficient to warrant the Board rejecting IFRS 13 in Australia. The benefits of adopting IFRS compliant standards outweigh the costs of accepting a less than optimal technical solution.</p> <p>No action required.</p>
<p><b>Question 11</b>  <b>Disclosures</b></p> <p>The ED proposes disclosure requirements to enable users of financial statements to assess the methods and inputs used to develop fair</p>	<p>In addition to the comments on Question 6, the AASB disagreed with the proposed amendment to IAS 34 <i>Interim Financial Reporting</i> to require all the disclosures in paragraphs 56-59 and paragraph 61 of the ED for an interim reporting period, because it</p>	<p>No. The AASB's concern is not addressed in IFRS 13.</p>	<p>AASB staff agree that imposing these disclosure requirements on entities would be excessive and inconsistent with the underlying disclosure principle of IAS 34.</p>

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<b>Proposals in ED/2009/5 Fair Value Measurement</b>	<b>AASB views in submissions to IASB on ED/2009/5</b>	<b>Has IFRS 13 dealt with AASB's concerns?</b>	<b>Staff comments and recommendations</b>
<p>value measurements and, for fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period (see paragraphs 56-61 of the draft IFRS and paragraphs BC98-BC106 of the Basis for Conclusions).</p> <p>Are the proposals appropriate? Why or why not?</p>	<p>considered the proposed disclosures referred to in that amendment would be excessive and inconsistent with the underlying disclosure principle of IAS 34 (that is, that significant changes be shown). For example, the AASB considered that, unless there is a significant change in the valuation technique applied since the prior annual reporting period, the disclosure of the methods and inputs used in the fair value measurement of assets and liabilities under paragraph 57(d) would be unduly onerous.</p>		<p>However, we do not think this is a fatal flaw in IFRS 13. AASB staff think that this issue could be addressed in part, for Tier 2 entities, when the RDR Subcommittee consider the Tier 2 Disclosure Requirements for the consequential amendments to IAS 34 that result from IFRS 13.</p> <p>No action required.</p>
<p><b>Question 6</b>  <b>Separate disclosure of 'incremental value'</b></p> <p>When an entity uses an asset together with other assets in a way that differs from the highest and best use of the asset, the exposure draft proposes that the entity should separate the fair value of the asset group into two components: (a) the value of the assets assuming their current use and (b) the amount by which that value differs from the fair value of the assets (ie their incremental value). The entity should recognise the incremental value together with the asset to which it relates (see paragraphs 20 and 21 of the draft IFRS and paragraphs BC54 and BC55 of the Basis for conclusions).</p> <p>Is the proposed guidance sufficient and appropriate? If not, why?</p>	<p>The AASB disagreed with requiring separate disclosure of the 'incremental value' and existing-use value in those circumstances, because it considered that such disclosure requirements would:</p> <ul style="list-style-type: none"> <li>(a) be piecemeal in only applying to assets measured at fair value. If disclosures about assets deployed for uses other than their highest and best use provide useful information for resource allocation decisions and assessing the accountability of the entity's management, and if the benefits of that information exceed the related costs, those disclosures should not be limited to assets measured at fair value;</li> <li>(b) require the underlying assets of investments in subsidiaries to be bifurcated into existing use market value and incremental value; and</li> <li>(c) involve significant costs to obtain dual valuations of an entity's assets as well as the assets of investments in subsidiaries (as mentioned in (b) above). Valuers do not generally provide separate valuations for assets at their current use and highest and best use (where that use differs from current use).</li> </ul>	<p>Yes. The following proposed disclosure requirements in ED/2009/5 have not been retained in IFRS 13:</p> <ul style="list-style-type: none"> <li>(a) the value of the assets assuming their current use; and</li> <li>(b) the amount by which the fair value of the assets differ from their value in their current use.</li> </ul> <p>Paragraph 93(i) of IFRS 13 requires that when an entity uses a non-financial asset in a way that differs from its highest and best use (and that asset is measured at fair value), the entity must disclose that fact and why the asset is being used in a manner that differs from its highest and best use (refer to paragraphs BC72-BC73 of IFRS 13).</p>	<p>No action required.</p>

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<b>Proposals in ED/2009/5 Fair Value Measurement</b>	<b>AASB views in submissions to IASB on ED/2009/5</b>	<b>Has IFRS 13 dealt with AASB's concerns?</b>	<b>Staff comments and recommendations</b>
<p><b>Question 8</b>  <b>Application to liabilities: restrictions</b></p> <p>The exposure draft proposes that:</p> <p>(a) the fair value of a liability reflects non-performance risk, ie the risk that an entity will not fulfil the obligation (see paragraph 29 and 30 of the draft IFRS and paragraphs BC73 and BC74 of the Basis for Conclusions).</p> <p>(b) The fair value of a liability is not affected by a restriction on an entity's ability to transfer the liability (see paragraph 31 of the draft IFRS and paragraph BC75 of the Basis for Conclusions).</p> <p>Are these proposals appropriate? Why or why not?</p>	<p>Whilst the AASB supported the proposal that the fair value of a liability is not affected by a restriction on an entity's ability to transfer the liability, it considered that the characteristics of the participants in the relevant market for the liability would reflect any restrictions on who may participate in that market. For example, a regulator (such as a financial services regulator) may require that transactions to transfer a particular liability can only take place with entities of equivalent or higher credit standing, which in turn would affect the particular liability's exit price. Accordingly, the AASB considered that any restrictions on who may participate in the relevant market for a liability should be taken into account in determining the relevant market for estimating the 'price that would be paid to transfer the liability in an orderly transaction between market participants at the measurement date'.</p>	<p>Yes. The revised wording in IFRS 13 requires restrictions to be included in inputs of the fair value measurement. (refer to paragraphs 45-46 and BC99-BC100 of IFRS 13).</p>	<p>No action required.</p>
<p><b>Question 13</b>  <b>Other comments</b></p> <p>Do you have any other comments?</p>	<p>The AASB disagreed with the discussion of deprival value in paragraphs BC65-BC66 of the ED because:</p> <p>(a) the context in which deprival value is introduced (in the first sentence of paragraph BC65) is as an alternative to fair value: this seems inappropriate for an IFRS on <i>how</i> to measure fair value;</p> <p>(b) its comparison with fair value is superficial and therefore not very informative; and</p> <p>(c) it mis-describes deprival value as being based on entity-specific information. Therefore, the AASB considered that a comparison of fair value with deprival value should occur in the <i>Conceptual Framework</i> instead.</p>	<p>Yes. IFRS 13 does not discuss deprival value.</p>	<p>No action required.</p>

**Comparison of IFRS 13 Fair Value Measurement with ED/2010/7 Measurement Uncertainty Analysis Disclosure for Fair Value Measurement**

<b>Proposals in ED/2010/7 Measurement Uncertainty Analysis Disclosure for Fair Value Measurement</b>	<b>AASB views in submissions to IASB on ED/2010/7</b>	<b>Has IFRS 13 dealt with AASB's concerns?</b>	<b>Staff comments and recommendations</b>
<p>An entity shall disclose, at a minimum, the following information for each class of assets and liabilities measured at fair value in the statement of financial position after initial recognition:</p> <p>(a) a measurement uncertainty analysis for fair value measurements categorised within Level 3 of the fair value hierarchy. If changing one or more of the unobservable inputs used in a fair value measurement to a different amount that could have reasonably been used in the circumstances would have resulted in a significantly higher or lower fair value measurement, an entity shall disclose the effect of using those different amounts and how it calculated that effect. When preparing a measurement uncertainty analysis, an entity shall not take into account unobservable inputs that are associated with remote scenarios. An entity shall take into account the effect of correlation between unobservable inputs if such correlation is relevant when estimating the effect on the fair value measurement of using those different amounts. For that purpose, significance shall be judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised</p>	<p>The proposed disclosure appears to require consideration of a range of many and varied alternatives in recalculating estimates of fair value, rather than alerting users to the specific areas of uncertainty that could change fair value significantly. Focusing on discrete ranges of uncertainty may erroneously imply that any amount within that range would be an acceptable measure of fair value. The AASB does not consider it the role of financial statements to disclose recalculated estimates of fair value.</p> <p>The proposed disclosures in the ED are likely to be costly to make, particularly because a dynamic model for incorporating the effects of correlation would seem necessary. The cost involved in preparing the proposed disclosures may discourage entities from applying fair value options available in IFRSs.</p> <p>The AASB sought clarification about how to apply the proposals to non-financial assets measured, for example, at DRC as an estimate of fair value, when DRC incorporates significant unobservable inputs.</p>	<p>Yes. Paragraph 93(h) of IFRS 13 only requires an entity to provide a <b>narrative description</b> of the sensitivity of a recurring fair value measurement categorised within Level 3 of the fair value hierarchy to changes in the unobservable inputs used in the measurement if a change in those inputs to a different amount would result in a significantly higher or lower fair value measurement. If there are interrelationships between those inputs and other unobservable inputs, an entity shall <b>provide a description of those interrelationships</b> and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement.</p>	<p>Consistent with the AASB's views, AASB staff note that in paragraph BC205 of IFRS 13 respondents to ED/2010/7 did not consider the proposals to be operational and the costs associated with preparing the disclosures would outweigh the benefits to users. Therefore the IASB and FASB decided to only require qualitative disclosures. However, the Boards noted that they will continue to assess whether a quantitative measurement uncertainty analysis disclosure would be practical after issuing IFRS 13, with the aim of reaching a conclusion about whether to require such a disclosure at a later date.</p> <p>No action required at this stage.</p>

<p>in other comprehensive income, with respect to total equity.</p> <p>(b) for fair value measurements categorised within Level 3 of the fair value hierarchy, a description of the valuation technique(s) and the inputs used in the fair value measurement.</p>			
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