Project **Fair Value Measurement**

Topic **Measuring own equity instruments at fair value**

Purpose of this paper

1. This paper addresses the guidance for measuring the fair value of an entity's own equity instruments. This is an issue for business combinations in which an acquirer issues equity as consideration for the acquiree.

2. This paper asks the boards to decide whether to include guidance for measuring the fair value of an entity's own equity instruments in a converged fair value measurement standard.

Summary of differences between the IASB's exposure draft and Topic 820

3. The IASB's exposure draft *Fair Value Measurement* explicitly addresses the fair value of an entity's own equity instruments. Although FASB Accounting Standards Codification Topic 820 (Fair Value Measurements and Disclosures) does not provide measurement guidance for own equity, it states that the definition of fair value also shall be applied to instruments measured at fair value that are classified in stockholders' equity (paragraph 820-10-35-20).

4. The IASB's exposure draft contains a similar statement to Topic 820 in its footnote to paragraph 1, which states that the core principle (ie the definition of fair value) shall also be applied when measuring the fair value of equity instruments.

5. Paragraphs 32 and 33 of the IASB's exposure draft state the following:

> As with assets and liabilities, the objective of a fair value measurement of an equity instrument is to estimate an exit price at the measurement date.
>
> However, although the objective is the same, the issuer of an equity instrument can exit from that instrument only if the instrument ceases to exist or if the entity repurchases the instrument from the holder. For this reason, an entity shall measure the fair value of its equity instrument from the perspective of a market participant who holds the instrument as an asset.

Overview of comments received on the IASB's exposure draft

6. The invitation to comment for the IASB's exposure draft did not ask a specific question about the appropriateness of the proposed guidance for measuring the fair value of an entity's own equity instruments, although this was noted as a difference between the exposure draft proposals and Topic 820 in paragraph BC110 of the basis for conclusions.

7. Some respondents did comment on the proposal to include guidance on the measurement of an entity's own equity instruments. Those respondents find the proposal in the IASB's exposure draft to be helpful because it clarifies the measurement objective for the issuer of an equity instrument measured at fair value. They suggest that the boards work together to provide consistent guidance.

Staff analysis

8. The IASB included this proposal in the exposure draft because the exit price notion does not seem applicable to an entity's own equity instruments. An entity cannot 'exit' its own ownership interests unless those interests cease to exist (eg if an entity is acquired by another entity). This is because equity instruments represent a residual interest in the entity, irrespective of who holds them. As a result, the statement that the definition of fair value also shall be applied to an entity's own equity instruments measured at fair value does not seem to 'fit'.

9. Furthermore, equity instruments are not the same as liabilities. Non-performance risk does not apply to most equity instruments, unless there is an obligation for the entity to pay or perform (eg puttable instruments).

10. The IASB concluded that the best possible approach to addressing this issue is to deem that the exit price of an equity instrument to the issuer is the same as the exit price for the holder of that instrument (as a market participant). This reflects the fact that a transaction assumes an equal exchange and seemed to be the most practical solution.

Staff recommendation

11. The staff recommends that a converged fair value measurement standard include guidance for measuring the fair value of an entity's own equity instruments.

12. If the boards agree with the staff recommendation, we recommend that the guidance reflect the proposal in the IASB's exposure draft (see paragraph 5 above).

Question 1 – Measuring the fair value of own equity
Do you agree with the staff recommendation to include guidance for measuring the fair value of an entity's own equity instruments in the converged fair value measurement standard? If not, what do you propose and why?