

STAFF PAPER

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IASB Meeting

Project	Post-implementation Review of IFRS 13 <i>Fair Value Measurement</i>		
Paper topic	Next steps in the PIR		
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Introduction

1. Agenda Paper 7C summarises the activities and the feedback received from stakeholders during the first phase of the PIR. This paper should be read in conjunction with that paper, in particular the matrix of areas highlighted by stakeholders.
2. This paper discusses the next steps in the PIR and asks the Board to make the following decisions:
 - (a) Whether to proceed with the PIR at this time and issue a RFI seeking feedback on topics you wish to examine; and, if you agree;
 - (b) Which matters to examine? and
 - (c) For each of the matters to examine, in addition to issuing a RFI and conducting a literature review, which, if any, additional activities to conduct?

Summary of staff's recommendation

3. The staff recommend that the Board:

- (a) proceeds with the PIR and issues a Request for Information (RFI) with questions focussed on topics the Board wants to examine further;
- (b) focuses the scope of the PIR on four topics identified by many stakeholders during Phase 1 as follows:
 - (i) effectiveness of disclosures on fair value measurements;
 - (ii) unit of account and fair value measurement of investments that are quoted in an active market;
 - (iii) applying judgements in specific areas when measuring fair value; and
 - (iv) applying highest and best use (HBU) when measuring the fair value of non-financial assets.

The staff proposes objectives for each of these areas when considering them further in the second phase of this PIR (see paragraphs 10 to 28).

- (c) complements the findings from the RFI with additional activities in order to fully meet the objectives for each of the areas in the scope of the PIR. Proposed additional activities are as follows:
 - (i) outreach with investors and preparers focussing on fair value disclosures; and
 - (ii) assessment (to the extent possible) of how widespread are some of the matters in the scope of the PIR, in particular the 'P × Q' and HBU topics.

4. The paper includes the following sections:

- (a) proceeding with the PIR;
- (b) matters to examine further and the objectives of the examination;
- (c) additional activities; and
- (d) questions for the Board.

Proceeding with the PIR

5. The Due Process Handbook envisages that, following the initial assessment, the Board proceeds with the PIR by issuing a RFI seeking feedback on the matters it wants to examine further, providing that the Board is satisfied that:
 - (a) it has enough information to establish scope of the PIR; and
 - (b) the initial assessment indicates that there are parts of the Standard requiring further examination.
6. The Handbook also envisages that the Board may decide that, on the basis of its initial assessment, it would be premature to proceed with the PIR at this point. In that case, the Handbook stipulates that the Board has to inform the Due Process Oversight Committee and explain why it has taken this decision.
7. The staff recommend the Board proceeds with the PIR for the following reasons:
 - (a) according to the feedback gathered from stakeholders during Phase 1, there was a consistency in messages on the need for some items to be considered further by the PIR;
 - (b) The Standard has been applied since 2013 by IFRS preparers and since 2008 by US GAAP¹ preparers which has contributed to cumulative experience with its requirements.

Matters to examine further and the objectives of the examination

8. Several stakeholders noted the Standard was working well and most thought that a wide-scope review of the Standard was not needed. Overall, the stakeholders gave highest priority to five matters which they wanted to be considered further. These matters were assigned either high or medium priority in the matrix of matters included the Agenda Paper 7C and are as follows:
 - (a) effectiveness of disclosures on fair value measurements;

¹ The original US GAAP guidance on fair value issued in 2006 had some differences to the revised Standard issued in 2011, which was mostly converged. Also, the scope of use of fair value in US GAAP is different from IFRS. For more details, see Agenda Paper 7B.

- (b) unit of account and fair value measurement of investments that are quoted in an active market;
 - (c) applying judgements in specific areas when measuring fair value;
 - (d) applying HBU when measuring the fair value of non-financial assets;
 - (e) measuring fair value when markets are inactive or when there are no markets, especially for biological assets.
9. The staff recommend that the first four matters are included in the scope of the PIR. The following subsections discuss the reasons for the recommendations and proposed objectives of the PIR in each of the recommended areas.

Effectiveness of disclosures

10. IFRS 13 requires disclosures about fair value measurements with greater requirements for measurements classified within Level 3 of the fair value hierarchy (an overview of the disclosure requirements in IFRS 13 is included as an appendix to Agenda Paper 7A).
11. Almost all stakeholders raised the need to review the effectiveness of disclosures about fair value measurements. As such, the staff recommend the Board to seek feedback on this area in the RFI.
12. Preparers and users had different views on the reasons for the lack of, and remedies to improve, effectiveness of disclosures. Some preparers saw some of the disclosure requirements as too onerous and questioned their relevance to investors. Some investors found the disclosures provided as being often boilerplate and needed more granularity.
13. The staff recommend that the objective of the review in this area is to gain deeper understanding of both users' and preparers' perspectives on the effectiveness of fair value measurement disclosures, especially in relation to Level 3 fair value measurements and how their different views could be reconciled.

Unit of account and fair value measurement of investments that are quoted in an active market ('P x Q')

14. IFRS 13 requires that Level 1 inputs are used whenever available. The Standard also requires that the measurement considers the unit of account of the item being measured at fair value. Some stakeholders reported lack of clarity on whether the use of Level 1 inputs (for example individual share prices) prevails over the principle of considering the unit of account of the item measured at fair value.
15. Many stakeholders questioned the relevance of measuring quoted investments in subsidiaries, joint ventures or associates or the recoverable amount of quoted cash generating units (CGUs) on the basis of fair value less costs of disposal by using unadjusted Level 1 inputs in all circumstances.
16. Overall the feedback received in Phase 1 of the PIR was very similar to the feedback received on the 2014 Exposure Draft and during the research undertaken in 2015 on this topic (see Agenda Paper 7A). The Board had stopped work on this project and decided to consider the topic as part of this PIR.
17. The staff research done at the time the project was active as well as the stakeholder feedback during Phase 1 of the PIR indicated that this issue is not pervasive however it can have a material impact when it occurs. Furthermore, the research done at the time of the project only covered some of the circumstances in which this matter may arise (quoted investments held by investment entities).
18. The staff think the most useful work that could be done in next stage of the PIR is to research and update evidence on the pervasiveness of the issue in order to help the Board decide whether and if so how to take it forward.
19. The staff are proposing the objective of the review in this area to be to further assess current practice and understand how widespread are the issues relating to these measurements together with any circumstances in which current practice does not seem to provide relevant information to investors.

Applying judgements in specific areas

20. IFRS 13 requires entities to apply judgement when measuring fair value. Some stakeholders stated entities face challenges when applying judgement in some circumstances. Areas for which judgements are particularly difficult to apply are:

- (a) categorisation of measurements within the fair value hierarchy; and
 - (b) assessing whether a market is active.
21. For example, stakeholders often raised questions on how to assess the volume and frequency of transactions in a particular market when determining if that market is active, also noting that the 'P × Q' issue increases the pressure on the definition of active market (if markets are considered inactive, entities are less inclined to use unadjusted market prices when measuring quoted investments). In relation to the level within the fair value hierarchy, many stakeholders raised questions on how to assess whether an input is 'significant' and when it is 'unobservable'.
22. The staff recommend further review of these two specific areas of judgement in which the questions were often raised.
23. The staff recommend that the objective of the PIR in this area is to assess why there are difficulties in applying judgement and identify any relevant support that may be required.

Applying HBU when measuring the fair value of non-financial assets

24. For non-financial assets, IFRS 13 requires that the HBU of an asset is considered when measuring its fair value, even if that is different from the asset's current use.
25. Some stakeholders (mainly national standard-setters and preparers in Asia) have stated that, when the valuation premise of a non-financial asset is to use it in combination with other assets and liabilities and the HBU of any of the assets within that group is different from its current use, the measurement for the non-financial asset is not clear and may result in counter-intuitive outcomes (for example, the fair value of the non-financial asset may be nil). Examples given were of groups of assets including biological assets or factories on land for which the HBU is different from its current use.
26. Several stakeholders we spoke to during Phase 1 of the PIR noted they had no issues with applying the HBU although they commented that this was a much-discussed issue at the time the Standard was being developed. In particular stakeholders from America and several in Europe stated they did not think this was an issue that warranted to be considered.

27. Given that this was a relevant issue for the stakeholders that did raise it and was common across a particular region, the staff think it requires further consideration and therefore recommend to include it in the scope of the PIR.
28. The staff recommend that the objective of the review in this area is to better understand the issues with applying this concept and how widespread it is.

Determining fair value when markets are inactive or when there are no markets, especially for biological assets

29. IFRS 13 sets out requirements for measuring the fair value of assets and liabilities regardless of whether observable market prices exist for them. Several stakeholders (mostly in emerging markets and in Asia) reported difficulties with measuring fair value when markets are not active or when there are no observable market prices that can be used. The most common examples given were unquoted equity instruments and biological assets (in particular immature produce on bearer plants).
30. The staff think that considering these matters is outside the scope of the PIR and should therefore not be included for two reasons:
- (a) the issue is principally about how to apply FVM framework in IFRS 13 and not about requirements in IFRS 13 itself;
 - (b) consideration of what should be measured at fair value is not in the scope of IFRS 13.
31. The staff do not recommend including any other specific areas for further consideration. The staff however propose to include an overarching question in the RFI which would allow respondents to comment on any other specific experience with IFRS 13 they may deem important, including their overall experience of the effects of the Standard.

Proposed activities during Phase 2 of the PIR

32. The Due Process Handbook (the Handbook) envisages using the RFI as the main tool to gather evidence in the Review. The RFI should explain why the Board is seeking feedback on the matters specified and include its initial assessment, if

any. The RFI would include a set of questions for respondents on the topics identified by the Board.

33. The Handbook gives some examples of additional activities the Board may conduct to supplement information received from the RFI which are:
- (a) an analysis of financial statements or of other financial information;
 - (b) a review of academic and other research related to the implementation of the Standard being reviewed; and
 - (c) surveys, interviews and other consultations with relevant parties.
34. The staff think that all three types of additional activities mentioned in the Handbook will provide useful evidence for some of the matters staff recommends to be examined further in the PIR. We propose to conduct these activities in a targeted manner as follows.
- (a) a review of academic and non-academic literature for evidence relevant to each of the areas being examined, as available (Agenda Paper 7D discusses scoping of academic research);
 - (b) consultations with preparers and investors to better understand effectiveness of disclosures; and
 - (c) analysis of financial statements in order to:
 - (i) assess how wide spread are the issues relating to the 'PxQ'; and
 - (ii) assess how wide spread are the issues relating to the HBU.
35. The reasons for proposals for the additional activities are discussed in the following sub-sections. These are organised by the areas the staff have proposed to include in the PIR.

Disclosure effectiveness

36. The staff propose the following objective of the this assessment
- gain deeper understanding of both user and preparer perspectives on effectiveness of fair value measurement disclosures and how their different views reconcile?

37. Discussions on disclosures during the initial assessment revealed a tension between views of preparers and auditors with the views of investors. A significant portion of time of most outreach meetings, especially with investors, was spent discussing disclosures. We found those discussions very useful yet it was hard to use those to delve deeper on specific requirements or issues. To help us to do this, we are proposing to hold more targeted discussions during next stage of the Review. Our aim is to understand from preparers and investors what information is costly to prepare and what information is most useful/decision-relevant. The staff think that discussing examples from published financial statements may be helpful.
38. The IFRS Taxonomy team are currently conducting a common practice review for disclosures about fair value measurement which will also be useful evidence for the PIR.
39. We will also continue to monitor the progress of the work on Disclosure Initiative project as well as work of our FASB colleagues in their Disclosure Framework project.

Unit of account and fair value measurement of quoted investments (PXQ)

40. The staff propose the following objective of this assessment:
- further assess current practice and pervasiveness of the fair value measurement of quoted investments, together with any circumstances in which current practice does not seem to provide relevant information to investors
41. The staff are proposing to research databases of financial statements as well as selected individual financial statements to help us assess the population of entities/assets affected by this issue. Although this is not likely to give us complete insight as sometimes entities that have issues with this concept do not disclose that, this will complement the findings from the RFI and related outreach activities.
42. The staff think this additional activity will help provide an overall perspective on the issue given that outreach and previous work done by the Board seemed to indicate the issue may not be pervasive.

Applying specific judgements required by IFRS 13

43. The staff propose the following objective of this assessment:
- to assess why there are difficulties in applying specific judgements in the Standard and identify support that may be required.
44. The staff think the responses to the RFI along with related outreach activities will provide the Board with sufficient information in this area. The staff therefore do not propose any specific additional activities.

Highest and best use for non-financial assets

45. The staff propose the following objective for review in this area:
- to better understand the issues with applying the HBU concept and their pervasiveness
46. The staff are proposing to research databases of financial statements as well as selected individual financial statements to help us assess the population of entities/assets affected by this issue. Although this is not likely to give us complete insight as sometimes entities that have issues with this concept do not disclose it, this will complement the findings from the RFI and related outreach activities.
47. The staff think this additional activity will help provide an overall perspective on the issue given that outreach seemed to indicate the issue is limited to some regions/industries.
48. This concludes the staff suggestions for additional activities during the next stage of the PIR.

Questions for the Board**Question 1 – Proceeding with the Review**

Does the Board agree to proceed at this time with the Post-Implementation Review of IFRS 13?
If not, why not?

Question 2 - Areas to examine further in Phase 2 of the PIR

a) Does the Board agree to focus the scope of the PIR on the following areas:

- Effectiveness of disclosures about fair value measurements – in order to gain deeper understanding of both user and preparer perspectives on effectiveness of fair value measurement disclosures and how their different views reconcile?;
- Fair value measurements of quoted investments – in order to further assess current practice and pervasiveness of these measurements, together with any circumstances in which current practice does not seem to provide relevant information to investors?;
- Applying judgements in specific areas– in order to assess difficulties in applying relevant judgements in the Standard and support that may be required?; and
- Applying HBU when measuring the fair value of non-financial assets – in order to better understand the issues with applying this concept and their pervasiveness?

If you agree, do you have any comments or suggestions on the objectives of the Review for each of the areas?

If you do not agree, why not?

b) Does the Board want to further consider any other specific issues identified by stakeholders during initial assessment? If so which ones and what would be the objective of the examination?

Question 3 – Activities during Phase 2 of the PIR

Does the Board agree to conduct the following activities during phase 2 of the Review:

- Issue an RFI with questions in areas the Board has decided to conduct further examination as well as an overarching question on other areas and the overall effects of the Standard;
- Conduct consultations with preparers and investors to assess effectiveness of disclosures;
- Review academic and non-academic literature for evidence relevant to the areas the Board has decided to conduct further examination; and

- Research financial statements to assess population of entities affected by issues surrounding measurement of quoted investment and application of highest and best use valuation premise for non-financial assets?

If you agree, do you have any specific comments or suggestions on these activities?

If you do not agree, why not and what do you propose instead?