

Post-implementation Review of IFRS 13 *Fair Value Measurement* *Feedback from investor outreach*

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Agenda Paper 5

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- Purpose
- Questions for CMAC
- Introduction
- Project status
- Investor feedback received
- Appendices (for reference only) in separate presentation:
 - feedback on IFRS 13 from CMAC/GPF June 2017 meeting;
 - information IFRS 13 requires to be disclosed; and
 - examples of most discussed fair value disclosures.

Purpose of the session

- Share **preliminary** feedback from **investors*** on Post-implementation Review (PIR) of IFRS 13
- Obtain your comments on the feedback received
- Discuss investors' suggestions for improvements and their potential benefits to the users of financial statements

* feedback from other stakeholders is still being analysed and is not included in this presentation

Questions for CMAC members

Disclosures

Q1a What are your thoughts on investor feedback on fair value measurement disclosures (slides 14 -16)?

Q1b Would any of the suggested improvements to the four disclosures bring significant benefits to the users of financial statements (slides 17-18)?

If so, what are those benefits? Please discuss suggestions for each of the disclosures:

- reconciliation of changes to Level 3 measurements;
- P&L impact of Level 1 and Level 2 fair value measurements;
- valuation techniques and inputs; and
- sensitivity analysis.

Other areas

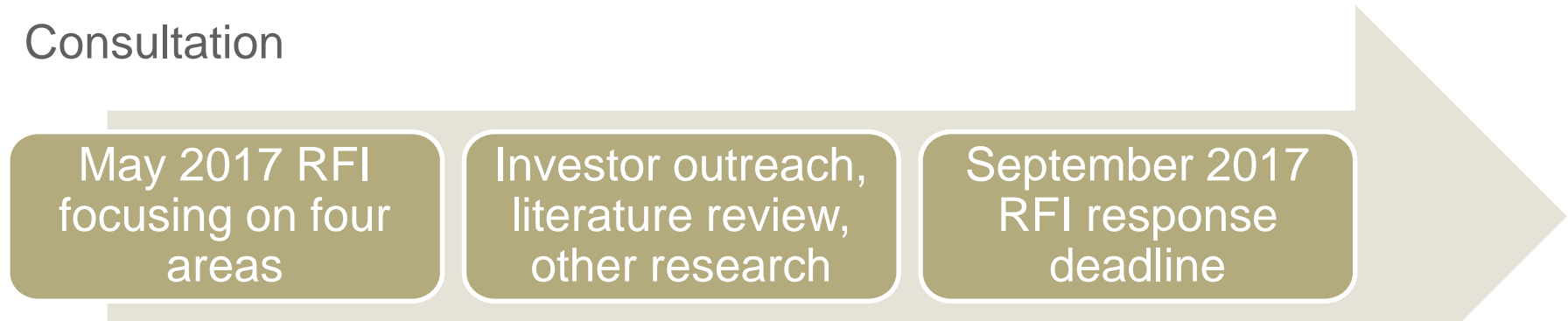
- Q2 What are your thoughts on the unit of account and other investor feedback (slides 19-20)?
- Q3 Do you have any other thoughts in relation to the Board's PIR of IFRS 13?

- Post-implementation Reviews serve an important role, helping the Board assess whether a Standard is:
 - working as intended; and
 - providing useful information to users of financial statements.
- The Board sought feedback through a Request for Information (RFI).
- Currently processing the feedback and preparing for Board discussions.
- The Board can take several steps following the PIR, not necessarily involving standard-setting.

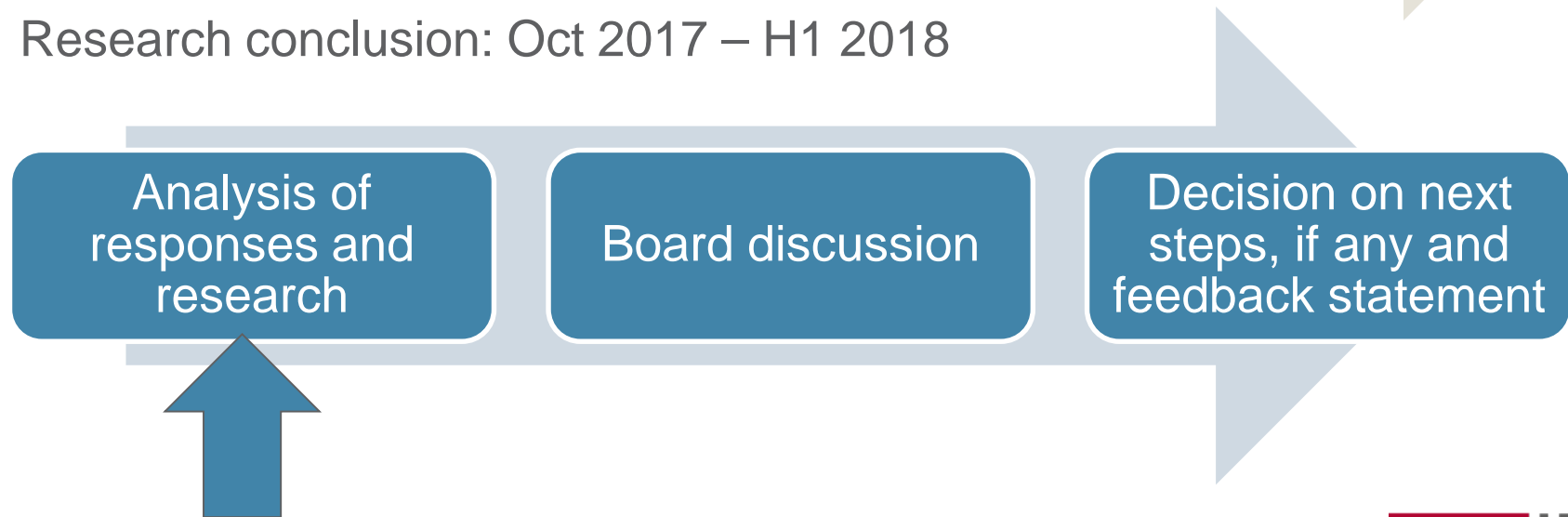
Status of the PIR of IFRS 13

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Consultation



Research conclusion: Oct 2017 – H1 2018



When is the guidance in IFRS 13 for fair value measurement guidance used?

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IFRS 13 applies when another IFRS Standard...

requires fair value measurement for some or all items within its scope, with or without IFRS 13 disclosures

permits fair value measurement, with IFRS 13 disclosures required

requires fair value information for items measured at cost

IFRS 3 *Business Combinations**

IFRS 9 *Financial Instruments***

IAS 19 *Employee Benefits**, **

IAS 41 *Agriculture*

IAS 36 *Impairment**, **

IFRS 5 *Assets Held for Sale***

IAS 16 *Property, Plant and Equipment*

IAS 38 *Intangible Assets*

IAS 40 *Investment Property*

IFRS 9 *Financial Instruments*

IAS 40 *Investment Property*

* IFRS 13 disclosures are not required.

** Applied to some items in the scope of the Standard or to items in specific circumstances.

Particular focus on usefulness of disclosures

Specific measurement aspects:

The unit of account and fair value of quoted investments - PxQ

Application of judgements

Application of highest and best use of non-financial assets

Also researching the challenges with measuring the fair value of biological assets and unquoted equities

- 14 meetings with 20 investor organisations and representative bodies:

Type of Investor	Number of organisations met
Asset management	3
Investment bank	5
Investment research	4
Representative Body	6
Ratings agency	2
Total	20

- Around 60 comment letters received (not analysed at the time of preparing this presentation) - including the results from European standard-setters survey of about 25 users of financial statements, as well as input from several users submitted by themselves or via other standard-setters.

- Feedback was consistent with initial assessment prior to the RFI publication. There are persistent differences in views between preparers* and users on the unit of account issue (often referred to as PxQ) and some disclosures.
- Relatively stable economic environment along with regulatory developments which may indicate there is less investor interest in level 3 disclosures today.

*Detailed feedback from preparers not presented in these slides.

What did we find out about use of fair value in practice*

- Fair value measurement mostly used in accounting for financial instruments and business combinations; as well as impairment testing.
- Little use of fair value option for property, plant and equipment and intangibles.
- Regional trends in accounting for investment properties with some areas, for example, Japan and South America tending to choose cost method.
- Since changes to IAS 41 took effect in 2016, bearer plants are typically carried at cost, reducing use of fair value measurement for biological assets.

* These are anecdotal findings based on discussions and examples of financial statements.

What did we find out about fair value in practice - fair value hierarchy*

- Investment property and biological assets measured at fair value tend to be measured at Level 3 (L3) of fair value hierarchy.
- Financial instruments-a significant decrease of proportion of L3 measurements compared to a decade ago (attributed to the global financial crisis and changes to regulatory requirements).
- Smaller, simpler banks may have nothing in L3.
- However, there may have been an increase in private equity investments - L3 measurements.

* These are anecdotal findings based on discussions and examples of financial statements.

Investor feedback - useful disclosures

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- Fair value measurement **hierarchy** is the single most useful disclosure.
 - First step: identify L3 assets as proportion of total assets.
 - Several investors do not look at L3 disclosures if L3 insignificant part of total, unless aware of assets in stress.
- Description of **valuation processes, techniques** and disclosure of **significant unobservable inputs** very useful.
 - Disclosures presented in a table cross-referenced to measurements most useful.
 - Help understand the approach and build confidence in model used.
- Also useful:
 - Information about **transfers between levels**, in particular between L2 and L3; useful to track instruments moving between levels; and
 - Effects of **L3 measurements on P&L**; interested in relationship to overall profit or loss.

Investor feedback - mixed views on usefulness

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- **Reconciliation** of changes in Level 3 measurements:
 - Useful because the volume of changes in the period is useful to understand significance of level 3 measurements to business model;
 - Not useful because only a few items are relevant and used in analysis (P&L impact and transfers).
 - Not useful because the grouping and description of changes can be hard to understand and analyse.
- **Sensitivity analysis:**
 - Quantitative disclosure is useful because it helps to understand the room to manoeuvre and which point did management choose.
 - Not useful unless disaggregated to instruments with similar risks which is not practicable in many cases.
 - Not useful as considered a preserve of valuation profession and not an item for analysis.
 - Narrative sensitivity disclosure generally not considered useful.

Investor feedback- factors affecting usefulness

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- **Aggregation** of dissimilar instruments or instruments subject to different risks makes disclosures about them hard to use.
- Some information is **unavoidably generic** - for example when describing a valuation technique, but it still provides useful information.
- **Materiality** - if L3 assets are a small proportion of an entity's balance sheet, detailed L3 disclosures are just clutter.
- **Presentation** - fair value disclosures dispersed across notes and not clearly linked, makes them hard to use.
- **Tabular** presentation most useful - for example for significant unobservable inputs and sensitivity analysis.
- Differences in **level of detail** provided hinders comparisons, for example on valuation techniques used.

Fair value disclosures - suggestions from investors

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- **Remove** requirement for **reconciliation of Level 3 instruments**, only requiring information on P&L effect and transfers between levels (but some wanted full disclosure to remain).
- **Expand** disclosures for **L1 and L2 assets** to include unrealised gains/losses recognised in P&L (but some more interested in liquidity rather than what is realised).
- **Valuation techniques and inputs:**
 - Include **weighted averages** in the disclosure of ranges of unobservable inputs and/or remove outliers in the range; and
 - Promote consistency of disclosure by providing **examples** of information expected to be disclosed in relation to valuation techniques and significant unobservable inputs.

Fair value disclosures - suggestions from investors, continued

- **Sensitivity analysis** - various suggestions:
 - remove requirement for narrative and require numerical sensitivity for non-financial instruments; and/or
 - reflect correlations between inputs; or
 - remove requirement for numerical analysis altogether.

Suggestions outside scope of IFRS 13

- Entity specific information:
 - intention about timing of liquidation of assets measured at fair value; and
 - difference between highest and best use and value in use, and intentions on crystallising highest and best use.
- Scope of IFRS 13:
 - disclosure requirements for fair value in business combinations to be more consistent with IFRS 13; and
 - abolish equity method of accounting and require fair value.

- Investors mostly commented on their preferred accounting outcome:
 - Most investors would want the measurement to be based on PxQ; it is seen as unbiased and some investors think control premiums often do not exist in practice anyway.
 - Some investors would permit the measurement to depart from PxQ, and would want disclosure of the difference compared to PxQ with an explanation of the reasons for it.

- Investors had little experience/feedback on:
 - highest and best use; and
 - measurement of biological assets.
- Investors do not think disclosures about measurement of unquoted equities provide much insight into management assumptions. Would like to see more – but comprehend this is not disclosed for commercial reasons.

What is happening in the US

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- Standards substantially converged.
- 2015 Exposure Draft with proposals for public companies to:
 - Remove:
 - the amounts of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy; and
 - the policy for the timing of transfers between levels, valuation policies and procedures for Level 3 fair value measurements.
 - Clarify ‘narrative description of the sensitivity of fair value measurement to changes in unobservable inputs’ should be a ‘narrative description of the **uncertainty of the fair value measurement as of the reporting date**’.
 - Add:
 - unrealised gains or losses for Levels 1 and 2 in hierarchy; and
 - the range, weighted average and time period used to develop significant unobservable inputs for Level 3 fair value measurements.
- Project on hold pending completion of work on the Disclosure Framework.

Contact us

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IFRS 13 PIR project



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