IFRS

STAFF PAPER

January 2018

IASB Meeting

Project	**Post-implementation Review of IFRS 13 *Fair Value Measurement***		
Paper topic	Detailed analysis of feedback received		
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Purpose of the paper

1. This paper provides a detailed analysis of comment letters and other feedback on the Request for Information (RFI) on Post-implementation Review (PIR) of IFRS 13 *Fair Value Measurement* (IFRS 13).

Structure

2. The agenda paper is structured as follows:

   (a) Analysis of the respondents and outreach (paragraphs 4–7 and Appendix A);

   (b) Focus areas in phase 2 of the PIR (paragraphs 8–10);

   (c) Feedback on fair value measurement disclosures (paragraphs 11–93);

   (d) Feedback on the unit of account and fair value measurement (paragraphs 94–116);

   (e) Feedback on the application of highest and best use (paragraphs 117–142);

   (f) Feedback on the use of judgements (paragraphs 143–156);

   (g) Feedback on fair value measurement of biological assets and unquoted equity instruments (paragraphs 157–187);

(h) Feedback on effects and convergence (paragraphs 188–204); and

(i) Feedback on other matters (paragraphs 205–218).

3. The paper does not ask the Board any questions and is intended for discussion only.

Analysis of the respondents and outreach

4. The RFI on the PIR of IFRS 13 was issued on 25 May 2017 and the deadline for responses was 22 September 2017. The Board received 67 comment letters.

5. Staff held 24 meetings with various stakeholders, including:

   (a) a conference session at the IFRS Conference in Amsterdam in May 2017;

   (b) a joint public meeting with the members of the Capital Markets Advisory Committee (CMAC) and Global Preparers Forum (GPF) in June 2017;

   (c) a public meeting with members of the GPF in October 2017,

   (d) a public meeting with members of the Accounting Standards Advisory Forum in December 2017;

   (e) two meetings with securities regulators;

   (f) three meetings with standard-setters; and

   (g) fifteen meetings with users of financial statements, including a public meeting with members of the CMAC in October 2017.

6. Responses received in comment letters and during meetings were often a combination or collections of responses from various groups of individuals or organisations. Where feedback included in comment letters was from different stakeholders' groups, or was divergent, we considered each type of feedback separately in our qualitative analysis.

7. Appendix A provides detailed analysis of respondents and outreach conducted.

Areas of focus in the phase 2 of the PIR

8. The RFI focussed on the following areas of IFRS 13:

   (a) disclosures about fair value measurements (in order to gain a deeper understanding of both users' and preparers' perspectives on the usefulness of fair value measurement disclosures).

   (b) whether to prioritise Level 1 inputs or the unit of account (in order to further assess the extent and effect of the issue as well as current practice).

   (c) application of the concept of the highest and best use when measuring the fair value of non-financial assets, (in order to better understand the challenges when applying this concept and whether further support could be helpful).

   (d) application of judgement in specific areas (in order to assess the challenges and whether further support could be helpful).

9. In addition, this RFI explored whether there is a need for further guidance, such as education material, on measuring the fair value of biological assets and unquoted equity instruments.The RFI also included questions on the effects of IFRS 13 and on any other matters not covered by questions.

10. The rest of the paper provides analysis of the feedback by each of topics covered in the RFI.

Feedback on fair value measurement disclosures

Background and questions in the RFI

11. IFRS 13 requires entities to categorise fair value measurements within one of three levels of a fair value measurement hierarchy, according to the type of inputs used in the measurement.[1] During the development of the Standard, users asked the Board to require preparers to provide more information about Level 3 fair

[1] The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to significant unobservable inputs (Level 3 inputs).

value measurements than is required for Level 1 and Level 2.[2] The following is the main information required to be disclosed for Level 3 fair value measurements:[3]

(a) quantitative information about the significant unobservable inputs used in the valuation technique(s);

(b) reconciliations from opening to closing balances;

(c) descriptions of valuation processes used by the entity; and

(d) sensitivity to changes in significant unobservable inputs—a narrative description for all fair value measurements and a quantitative analysis for financial instruments measured at fair value.

12. During phase 1 of the PIR, users confirmed that information about Level 3 fair value measurements is important. Nevertheless, they and other stakeholders questioned the usefulness of information disclosed to comply with requirements in IFRS 13 for disclosure relating to Level 3 fair value measurements.

13. The RFI included the following questions on IFRS 13 disclosures:

Question 2—Fair value measurement disclosures

(a) How useful do you find the information provided about Level 3 fair value measurements? Please comment on what specific information is useful, and why.

(b) In your experience of Level 3 fair value measurements:

  (i) how do aggregation and generic disclosures affect the usefulness of the resulting information? Please provide examples to illustrate your response.

  (ii) are you aware of any other factors (either within or outside IFRS requirements) affecting the usefulness of the information? Please provide examples to illustrate your response.

  (iii) do you have suggestions on how to prevent such factors from reducing the usefulness of the information provided?

(c) Which Level 3 fair value measurement disclosures are the most costly to prepare? Please explain.

(d) Is there information about fair value measurements that you think would be useful and that IFRS 13 does not explicitly require entities to disclose?

[2] See paragraph BC187 of IFRS 13.

[3] IFRS 13 requires information to be disclosed by classes of assets and liabilities, with guidance provided on how to determine appropriate classes.

If yes, please explain what that information is and why you think it would be useful. Please provide any examples of disclosure of such information.

Usefulness of disclosures feedback

14. The question on the usefulness of fair value measurement disclosures was discussed by almost all respondents to the RFI. Most respondents considered the information provided about Level 3 measurement disclosures to be useful although some disclosures were seen as more useful than others and different views were expressed on the usefulness of quantitative sensitivity analysis and on the reconciliation from the opening balance to the closing balance, with the views split between users and preparers.

15. Most respondents indicated that the most useful disclosures were about Level 3 valuation techniques and inputs, quantitative significant unobservable inputs and the fair value hierarchy. For example, Singapore Accounting Standards Council commented:

> In particular, our constituents commented that the disclosures relating to the valuation techniques and inputs (including quantitative information about significant unobservable inputs), together with the valuation policies and procedures, provide insights into complex measurements and the judgements made in those measurements. In addition, such information could be useful for explaining fluctuations in fair value measurements over time and for benchmarking within particular industries.

16. Respondents said that assets and liabilities classified within Level 3 of the fair value hierarchy were mostly found in banks, insurance, real estate, private equity and investment entities.

What specific information is useful and why?

Disclosure of the level of the fair value hierarchy within which the fair value measurements are categorised

17. Many respondents indicated that the disclosure of the level of the fair value hierarchy, which includes disclosure of the fair value of assets and liabilities

measured within Level 3 of the fair value hierarchy, was useful. These respondents were a mix of preparers, professional accounting bodies, a valuation specialist and an academic. The respondents indicated that this disclosure was useful because it can help users of financial statements understand the extent of risks and the inherent subjectivity and uncertainty of the measurement of assets and liabilities.

18. During outreach, users often referred to this disclosure as being the first (and sometime the only) piece of information about fair value measurement they look at in order to assess significance of Level 3 measurements.

Description of the valuation technique(s) and the inputs used in the fair value measurement

19. The disclosure of the valuation technique(s) and the inputs used in the fair value measurement is required for both Level 2 and Level 3 measurement but the RFI question and responses related to Level 3 measurements. Some respondents found disclosures of valuation techniques and inputs useful. These respondents included preparers, standard-setters, users, a valuation specialist and an auditor. In outreach, most users said these disclosures were useful.

20. The respondents gave the following reasons for this disclosure being useful:

    (a) helps understand how fair value measurement was derived;

    (b) provides insight in assumptions underlying fair value measurements;

    (c) enables evaluation of the reasonableness of techniques and assumptions used by management; and

    (d) provides insight into potential impact on the measurement under stress.

21. A few respondents did not think the disclosure of valuation techniques was useful if the information provided is only generic. See more discussion on factors affecting usefulness of fair value disclosures in paragraphs 52-56.

Quantitative information about the significant unobservable inputs used in the fair value measurement

22. Some respondents found disclosures of significant unobservable inputs useful. These respondents included standard-setters, preparers, auditors and users. In outreach, most users said these disclosures were useful.

23. Of the respondents that found the quantitative disclosure of significant unobservable inputs useful, most stated this is because it allows users to understand the judgements made by the management, which would otherwise not be publicly available. Some also provided similar reasons for usefulness as for description of valuation techniques and the inputs outlined in the previous section.

24. A few respondents did not think the disclosure of significant unobservable inputs is useful, mainly due to aggregation of information. See more discussion on factors affecting usefulness of fair value disclosures in paragraphs 46-51.

Sensitivity analysis

25. Many respondents commented on the Level 3 sensitivity analysis disclosure. They expressed mixed views about its usefulness. Some of the comment letter respondents did not make it clear whether their comments related to the:

    (a) narrative description of sensitivity of fair value measurement to changes in unobservable inputs (required for all Level 3 instruments); or

    (b) quantitative disclosure of the effect of a change to reflect reasonably possible alternative assumption (required only for financial instruments measured within Level 3).

26. In outreach, most users said the quantitative disclosure was useful, when presented appropriately, and some users said narrative disclosure was useful too. The staff thought there was some misunderstanding of quantitative disclosure by the users, some of which seemed to see it as a stress-test, and not a reflection of reasonably possible alternatives. To alleviate this some suggested using the term uncertainty analysis.

27. Specific comments relating to narrative disclosures mostly said it was not useful unless accompanied with quantitative information and users provided the same feedback in outreach meetings.

28. The rest of the analysis relates to the quantitative disclosure.

Useful

29. Some respondents indicated that the quantitative disclosure of sensitivity analysis is useful. These respondents were a mix of regulators, users and an auditor.

30. The respondents gave the following reasons for this disclosure being useful:

(a) helps understand uncertainty of measurement;

(b) allows users to understand the measurement without having to be valuation specialists; and

(c) ensures measurements are scrutinised.

31. The European Banking Authority commented:

> The disclosures about Level 3 positions outlined in IFRS 13, when made well and with thoughtful consideration, are crucial to the understanding of banks' balance sheets, particularly disclosures in paragraph 93 that quantify the impact of reasonably possible alternative assumptions. The ability to quantify and fully understand the valuation uncertainty arising from illiquid positions within the balance sheet promotes sound decision making and ensures that the valuations, and the assumptions underlying them, receive an appropriate level of scrutiny both externally and internally within the bank.

Not useful

32. Several preparers and two valuation specialists found the Level 3 sensitivity analysis not useful. They said that it:

(a) is difficult to compare across reporting entities; and

(b) provides only limited decision-useful information, in particular when presented in aggregate for non-homogeneous assets (see more discussion on factors affecting usefulness of fair value disclosures in paragraphs 46-51).

33. For example, Duff & Phelps commented:

> Two specific types of disclosures, quantitative information about significant unobservable inputs and sensitivity to reasonably possible changes in inputs, provide very limited decision useful information, with the possible exception of disclosures of Level 3 inputs for a single asset or for a group of homogeneous assets. However, for non-homogeneous assets, such as those held by investment entities, the required disclosures are not meaningful.

Description of valuation processes used by the entity

34. Some respondents also thought that the disclosure of Level 3 valuation processes were useful. These respondents include standard-setters, a user and a valuation specialist. In outreach, most users said the disclosure was useful.

35. The respondents gave the following reasons for this disclosure being useful:
    - (a) gives insight into complex measurement processes;
    - (b) helps assess reliability of conclusions; and
    - (c) provides information on involvement of qualified experts indicating that professional judgement is applied.

36. A few respondents said this disclosure was not useful, for the following reasons:
    - (a) it is not a role of financial statements to provide such information;
    - (b) the information provided is generic (see more discussion on factors affecting usefulness of disclosures in paragraphs 52-56); and
    - (c) the information does not help users to assess uncertainty.

Reconciliation of changes from opening to closing balances

37. Some respondents commented on the Level 3 reconciliation disclosure. They had split views about its usefulness. In outreach, most users said this disclosure was useful, although some thought it was not.

Useful

38. The respondents that found the disclosure useful include users and a preparer. The respondents gave the following reasons for this disclosure being useful:
    - (a) explains movements and the level of activity in the period;

(b) provides information about allocation of investments and risks; and

(c) improves confidence in fair value measurement.

39. Some of these respondents stated that the usefulness of disclosure can be affected by aggregation and by descriptions of categories, issues which are discussed in paragraphs 46-51.

40. Users that provided feedback during outreach meetings mostly said this disclosure was useful for the above reasons although a few did not think a full reconciliation was needed.

Not useful

41. The respondents that questioned the usefulness of the reconciliation disclosure were a mix of standard-setters, a preparer group, a professional accounting body and a valuation specialist. Most of them said that the information was not used by management and is provided solely for compliance with disclosure requirements. Some users the staff spoke to during outreach said they did not use this disclosure in their analysis of financial statements.

Transfers between levels of hierarchy

42. IFRS 13 requires disclosure of the amounts of any transfers into or out of Level 3 of the fair value hierarchy, the reasons for those transfers and the entity's policy for determining when transfers between levels have occurred. In outreach, most users said this disclosure was useful.

43. A few respondents, including a preparer, a valuation specialist and a standard-setter, said that the disclosure of transfers between levels of fair value hierarchy was useful because it helps users of financial statements to understand an entity's portfolios and is essential to knowing the instrument's history. Respondents found information about transfers between Level 2 and Level 3 most useful, along with the reasoning for such movements.

Unrealised gains and losses

44. A few respondents stated that disclosure of unrealised gains and losses relating to Level 3 instruments was useful because it provides users with information about the effects on profit or loss and other comprehensive income, and about earnings quality, as well as information about uncertainty. Some referred to this

information being more useful in jurisdictions that determine distributable profits on the basis of realised gains. In outreach, many users said this disclosure was useful.

45. A few respondents, however, did not think that this disclosure provides useful information. The respondents did not provide explanation for this view in their comment letters. However during outreach meetings with users they provided this view:

    (a) information about liquidity is more useful than about what is not realised because liquid assets can be realised quickly; and

    (b) providing information about unrealised gains and losses only for Level 3 assets and liabilities limits the usefulness of that information, particularly for instruments that can move between levels of fair value hierarchy.

Aggregation and generic disclosure

46. Most respondents commented on the effect of aggregation and of providing only generic information. They said that both these practices reduced the usefulness of disclosures. Almost all of those respondents discussed aggregation; some provided comments on generic information. In outreach, users were mostly concerned about inappropriate aggregation and thought generic information can be useful.

Feedback on aggregation

47. Responses on aggregation are grouped as follows:

When and why is aggregation useful?

48. Preparers and standard-setters provided the following examples of when aggregation of information is useful:

    (a) it is usually impractical to provide information by individual instruments and some aggregation is required;

(b) aggregation is useful when the information is structured and presented according to class of asset or liability, indicating the inputs used and the related technique applied; and

(c) aggregation is useful when instruments have a similar nature or are individually immaterial.

When and why is disaggregation not useful?

49. Respondents representing all stakeholder groups provided the following examples of when aggregation of information is not useful:

(a) disaggregation by measurement basis only, which combines instruments from different asset classes, does not provide useful information;

(b) disaggregation by asset classes may not be sufficient when the asset class includes instruments with different characteristics. Erste Group included the following example:

> … a bond issued by an emerging economy government could be classified as Level 3 due to illiquid market and missing observable valuation inputs, however its characteristics are different to, for example, structured CLO also classified as Level 3. These instruments may be disclosed in the same class of Level 3 instruments such as fixed rate income (debt) instruments class. The complex CLO may expose the investor to larger fair value changes.

(c) a wide range of measurement inputs can be disclosed for a single line item (eg yields of 3% to 10%). Weighted averages could be provided, but with such wide ranges, none of the information disclosed is very useful; and

(d) the category labelled 'other', with no explanation of inclusions, is often large, and sometimes can be the largest line item in a group. This was a particular concern for users in outreach.

Consequences of the issues raised

50. Respondents discussed consequences of inappropriate aggregation, including

(a) users are unable to assess whether the entity's assumptions, for example, on significant unobservable inputs, differ from users' own views/expectations; and

(b) the disclosures are not comparable between entities.

Reasons for today's practice

51. Respondents typically referred to these reasons for current practice with disaggregation:

(a) consideration of the level of detail practically needed by users (as defined in the *Conceptual Framework for Financial Reporting*)to avoid disclosure overload. Some commented that, if each item is immaterial, it is difficult to see how aggregation can be avoided without undue expansion of the disclosures and without burying useful information;

(b) the entity's intention to protect commercially sensitive information, for example, when an asset is marketed for sale or is the subject of price negotiation; and

(c) lack of guidance on disaggregation in IFRS Standards. Some commented that preparers may lack experience of applying principle-based requirements.

Feedback on generic information

52. Respondents provided comments on when generic information is useful and when it is not, as follows.

When is generic information useful?

53. Users provided the following examples of when generic information is useful:

(a) a user of general purpose financial statements should not be expected to be familiar with valuation techniques, even if they are commonly used within an industry;

(b) a more educated user may want confirmation that a valuation has been performed in an expected manner; and

(c) if any entity reports similar information every period, that suggests that it uses the same techniques and types of inputs in each period. An expectation of varied language in such circumstances is not warranted and varying the language might even be misleading.

When is generic information not useful?

54. Respondents that found generic information not useful included standard-setters, preparers, an auditor and a user, and have provided the following examples:

(a) generic disclosures may include standard text not relevant, or adjusted, to what an entity does.

(b) Generic information may include no description of how it relates to the particular instruments held by an entity. The Canadian Bankers Association includes the following example illustrating the issue:

> For instance, a portfolio of private equity holdings may use a number of valuation techniques, such as earnings multiple and discounted cash flows; however these techniques are described in general terms. It is therefore difficult for a reader to infer how much of the portfolio is valued using each method.

55. Some respondents suggested that disclosure of generic information about sensitivity to unobservable inputs undermines the usefulness of that information.

56. Some respondents commented that disclosures about valuation policies and procedures, together with information about significant unobservable inputs, tend to be more generic when external specialists do the valuation, for example, in the case of property valuations.

Other factors affecting usefulness

57. Almost all respondents who commented on aggregation and disclosure of generic information, and from all stakeholder groups, also discussed other factors affecting usefulness.

58. The single most-discussed factor was the tick-box approach to providing disclosures, resulting in disclosure of immaterial information. Several respondents stated that this is due to strict interpretation by enforcers and the way IFRS 13 requirements are drafted, using the expression ‘at a minimum’. Another aspect of this issue is that little guidance is available regarding the assessment of

whether information to be disclosed is material, although some noted the Board's newly issued Practice Statement 2: *Making Materiality Judgements* is expected to help.

59. A few respondents said that tabular presentation might be misleading because it might imply no judgement is involved in classification in particular rows or columns, whereas in fact often a great deal of judgement is involved.

60. Several respondents discussed factors which they thought make information about sensitivity analysis less useful:

(a) there are not enough tools to guide judgements on structuring the disclosure;

(b) there is diversity in practice in how information used to produce sensitivity analysis is prepared; and

(c) related items subject to risk management may not be in the scope of a required disclosure. Thus, the disclosure may not provide the whole picture.

61. A valuation specialist commented that differences in methodology make disclosures of inputs used less comparable and potentially misleading, unless information about methodology accompanies those disclosure. They provided an example: when using present value measurement techniques for fair value measurement, an entity can reflect risk either by adjusting discount rate or by adjusting the cash flows. In this example, they said that the disclosure of discount rates may not be useful, and potentially even misleading, if it not clear to the reader which method was used.

Suggestions to prevent factors from reducing usefulness of disclosures

62. Many respondents provided suggestions on how to prevent the factors discussed above from reducing the usefulness of disclosures about fair value measurements, including:

(a) providing more guidance and examples to ensure appropriate aggregation, make sure only material information is disclosed, and help with some of the individual disclosures relating to Level 3 assets and liabilities;

(b) leveraging the work on the Disclosure Initiative, in particular the Principles of Disclosures project; and

(c) removing some of the more onerous requirements around sensitivity analysis and reconciliation.

Additional guidance or examples that would be useful

63. Some respondents provided suggestions on how to improve aggregation of information about fair value measurements. Most of these suggestions were to add guidance to help in applying judgment to determine the appropriate level of aggregation. Their suggestions included adding guidance on factors to consider and to add illustrative examples. A few respondents suggested considering developing non-authoritative full-length case studies or excerpts of best practices.

64. Some respondents provided suggestions on how to address some of the materiality concerns, including:

(a) provide education material on the background, significance, and effects of the disclosures; and

(b) guidance on ways to restrict the size of range disclosed, for example for inputs used in valuation. A suggestion was made to remove extreme examples at the top and bottom of the range, if they relate to only a small proportion of the assets/liabilities in the class.

65. Some respondents provided suggestions for guidance to improve specific disclosures, including:

(a) expand on examples in paragraph B36 of IFRS 13 and include examples of key assumptions/inputs to disclose for common types of investments, with a few respondents suggesting adding an illustration of useful inputs commonly used in international valuation guidelines;

(b) provide implementation guidance on disclosure for various methods of valuation;

(c) provide disclosure templates by asset classes, eg property. Some preparer associations suggested that the Board works with the International Valuation Standards Council (IVSC) to provide such examples;

(d) provide more guidance on what gains are 'realised'; and

(e) develop application guidance on how to perform and disclose a sensitivity analysis in situations where an entity has a large portfolio of equity instruments, contrasted with situations where an entity holds few equity instruments.

Suggestions relating to the Principles of Disclosure project

66. Many respondents expressed their support for the Board's work on the Disclosure Initiative, and the Principles of Disclosures project in particular. They thought that this project would help entities apply judgement when deciding which disclosures to provide, and to ensure that the disclosures are relevant and thus improve the usefulness of information provided. Specific suggestions included:

(a) redefine disclosure principles in the light of the Better Communication initiative;

(b) in line with the changes contemplated in the Disclosure Initiative, the checklist of disclosures should be only suggested disclosures;

(c) to encourage changes in behaviour, use less prescriptive language, including avoiding phrases such as "an entity shall disclose" or "as a minimum";

(d) describe clearly the objective pursued by the specific disclosure requirements of IFRS 13;

(e) require entities to provide all fair value information in a single note to the financial statements; and

(f) keep IFRS 13 principle-based as valuation techniques will continue to evolve.

Remove disclosure requirements

67. Some respondents suggested removing or reducing some of the disclosure requirements, including:

(a) remove quantitative sensitivity analysis, which is not required by US GAAP; and

(b) replace the reconciliation of changes from opening to closing balances with either:

   (i) disclosure of specific information, including gains or losses recognised in profit or loss or other comprehensive income; or

   (ii) narrative description of changes in period.

68. Standard-setters in Australia and New Zealand shared their experience with reducing fair value disclosure requirements for some entities and suggested that the Board should consider the impact of that reduction.

The costs of Level 3 fair value disclosures

69. Most of the respondents to the RFI had experience with Level 3 fair value disclosures, most of whom said the disclosures were costly to prepare. Many of those listed disclosures that were costly to prepare, but did not explain why these disclosures were the most costly.

70. However, a few respondents indicated the additional fees incurred when procuring and auditing information from external valuation specialists as the reason for the Level 3 disclosures being costly.

71. A few respondents also indicated that the disclosures for Level 3 fair value measurements in interim financial statements were very costly because of the limited time available to prepare them, and questioned its cost-benefit due to the limited time-frame for which they provide information (see more discussion in the section on Other matters in paragraph 210).

Which specific disclosures are most costly and why?

72. Some respondents highlighted the following disclosures relating to Level 3 fair value measurements as being the most costly to prepare:

   (a) reconciliation of changes in Level 3 fair value measurements (reconciliation);

   (b) quantitative analysis of the sensitivity of Level 3 measurement to reasonably possible changes in significant unobservable inputs (sensitivity analysis);

(c) quantitative information about significant unobservable inputs; and

(d) unrealised gains and losses.

Reconciliation

73. Most respondents stated that the reconciliation of changes in Level 3 measurements was the most costly disclosure. The respondents were a mix of preparers, standard-setters, professional accounting bodies, auditors and a regulator.

74. Most of the respondents stated that this disclosure was the most costly because preparing it is a manual and complex task. Some respondents further explained why its preparation cannot be automated, and detailed the work needed to be completed at end of a reporting period:

(a) inputs are collected from various information systems;

(b) transaction data is not managed by levels in the fair value hierarchy; and

(c) categorisation of measurements within the fair value hierarchy is done only at the end of reporting period.

75. Some respondents indicated that the complexity of preparing this disclosure also makes it difficult to prepare it in a consistent way over time.

76. Some respondents stated that the part of the reconciliation relating to purchases and sales is particularly costly.

Sensitivity analysis

77. Of the respondents who stated that the sensitivity analysis disclosure was costly to prepare, some did not make a distinction between the narrative and quantitative sensitivity analysis and referred to both, for example, to 'IFRS 13 paragraph 93(h)' or 'sensitivity analysis'. Respondents were again a mix of preparers, standard-setters, auditors and professional accounting bodies and a valuation specialist.

78. Of the respondents who did make such a distinction, most indicated that the quantitative portion of the sensitivity analysis for financial instruments is the most costly to prepare due to time required and additional cost incurred.

79. For example, the International Association of Consultants, Valuators and Analysts commented:

> Valuators select the most likely set of assumptions. There can be others but to determine all that are “reasonably possible” would be onerous and therefore expensive. The valuator has to convince the auditor that those selected are the most appropriate.

Quantitative information about significant unobservable inputs

80. A few preparers stated that the disclosures of significant unobservable inputs are costly to prepare and some provided comments on the costs incurred to provide the disclosure. For example, *Comitê de Pronunciamentos Contábeis* commented ‘the disclosure … is the most costly …, because some of the unobservable inputs used in the valuation are very confidential and ….. can affect futures negotiation’.

Unrealised gains and losses

81. A few respondents stated that preparing the amount of Level 3 total gains or losses for the period was costly. The Norwegian Accounting Standards Board commented:

> Especially for non-financial contracts (e.g. commodity contracts that fails the own use exception) the required information may be burdensome to provide, as settlement for these types of contracts in many cases is done on a continuous basis. Accordingly, calculating realised gains or losses must also be done on a continuous / daily basis to provide the required information.

Information not required by IFRS 13 that would be useful

82. Most respondents commented on this question but expressed mixed views as to whether additional disclosures would be useful. Many respondents stated that the current disclosure requirements were comprehensive, sufficient and gave useful information.

83. Many other respondents, however, said that additional disclosures would be useful. Their suggestions are outlined in the following paragraphs and cover:

(a) explanation of assumptions;

(b) improvements to disclosures about inputs and sensitivity analysis;

(c) more information about Level 2 measurements;

(d) use of valuation specialists and valuation standards;

(e) expanding scope of disclosures to initial measurement for non-recurring measurements;

(f) policy for determining whether a market is active; and

(g) primary valuation technique.

84. Users were most interested in additional disclosures for Level 2 measurements.

85. Some respondents also asked for additional disclosures relating to risks of assets and liabilities measured at fair value. However, this is outside the scope of IFRS 13 and is not discussed in this paper.

Explanation of assumptions

86. Some respondents indicated that disclosure of more explanation of the assumptions made in calculating Level 2 or Level 3 fair value measurements would be useful. The respondents included standard-setters, an auditor, a regulator and a preparer. Some respondents indicated that this disclosure could include a description of how an entity chose an assumption or valuation technique.

Improvements to disclosures about inputs to valuation techniques and sensitivity analysis

87. Some respondents suggested that requiring a disclosure of an average or mean of inputs used in the measurements, in particular when the range disclosed is wide, would provide more useful information; and

88. A few respondents asked for the quantitative sensitivity analysis to reflect interrelationships between inputs to avoid providing potentially misleading information.

Level 2 measurements

89. Some respondents stated that expanding some Level 3 disclosures to also cover Level 2 measurements would be useful. The respondents included regulators, a

standard-setter as well as users in outreach meetings. They made the following suggestions:

(a) a few respondents (users and regulators) stated that expanding the Level 3 sensitivity analysis disclosure to Level 2 would be useful.

(b) a few respondents (users and a standard-setter) stated that disclosure that distinguishes realised and unrealised gains and losses for Level 2 (and possibly also for Level 1) would be useful.

Valuation specialists and valuation standards used

90. Some respondents said the disclosure of an entity's use of external valuation specialists or an entity's internal qualifications for valuation would be useful. The respondents included valuation specialists, an auditor and a standard-setter. The respondents stated that the disclosure of the name, location and accreditation details of an entity's valuation specialists would allow users to assess the quality of the measurements. Another respondent indicated that disclosure of valuation standards used would be useful.

Initial measurement for non-recurring fair value measurements

91. A few respondents said that the scope of IFRS 13 disclosure requirements should be extended so that they also apply at initial recognition for non-recurring fair value measurements, for example when non-financial assets are acquired in a business combination. The respondents included a standard-setter and regulator.

Description of policy on determining when a market is active

92. A few respondents indicated that a disclosure describing the entity's policy for determining whether a market is active would be useful. The respondents included a preparer and regulator. See more discussion on 'active market' in the section on judgements (paragraphs 146–150).

Disclosure of primary valuation technique

93. A few respondents stated that disclosure of which valuation technique was the primary technique used would be useful. The respondents included users and a preparer group. The European Public Real Estate Association commented:

Some valuations are performed using a primary method with valuation results subsequently being cross-checked by reference to another method. When this is the case, it would assist the reader if this were explicitly stated, i.e. which method is the primary method and what the valuation inputs (with the additional detail listed above) were and the same information for supporting cross-check methods.

For instance, when information such as fair market values per square meter estimated from 'actual market transactions' is disclosed, it is not always clear whether this was used in the primary or a supporting valuation method.

Feedback on unit of account and fair value measurement

Background and questions in the RFI

94. IFRS 13 requires that:

    (a) the fair value measurement of an asset or a liability or a group of assets and/or liabilities takes into consideration the unit of account for the item being measured (for example a financial instrument or a cash-generating unit or a business). The unit of account itself is determined applying other IFRS Standards.[4]

    (b) an entity selects inputs that are consistent with the asset or liability characteristics that market participants would take into account in a transaction for the asset or liability.[5]

    (c) to measure fair value, Level 1 inputs should be used without adjustment whenever those inputs are available.[6]

95. After IFRS 13 came into effect, some stakeholders raised questions about how to measure fair value when Level 1 inputs exist but do not correspond to the unit of account (the unit of the account issue). Those stakeholders asked whether the use

[4] See paragraphs 13 and 14 of IFRS 13.
[5] See paragraph 69 of IFRS 13.
[6] See paragraphs 77 and 80 of IFRS 13.

of Level 1 inputs or the unit of account should be prioritised in arriving at the measurement.

96. The Board has sought to clarify which of these requirements to prioritise. In September 2014, the Board proposed in the Exposure Draft *Measuring Quoted Investments in Subsidiaries, Joint Ventures and Associates at Fair Value*[7] (the 2014 Exposure Draft) that the unit of account for an investment in a subsidiary, joint venture or associate is the investment as a whole. In that 2014 Exposure Draft, the Board also proposed that the product of the quoted price (P) for the individual financial instruments that make up the entity's investments and the quantity of financial instruments (Q), or P×Q, should be used, without adjustment, to measure:

(a) the fair value of an investment in a subsidiary, joint venture or associate when the investment is quoted in an active market; and

(b) the fair value less costs of disposal of a cash-generating unit that is an entity quoted in an active market, when determining the recoverable amount of that cash-generating unit.

97. Many respondents to the 2014 Exposure Draft agreed with the proposal that the unit of account is the investment as a whole but disagreed with the proposed measurement on the basis of P×Q, because, in their opinion, it resulted in an irrelevant measurement. In contrast, many users of financial statements who responded to the 2014 Exposure Draft preferred measurement on the basis of P×Q because, in their opinion, such measurement is objective and verifiable. The Board decided to consider this issue during the IFRS 13 PIR and stopped work on the project that led to the 2014 Exposure Draft.

98. The RFI included the following questions relating to unit of account:

Question 3—Prioritising Level 1 inputs or the unit of account
(a) Please share your experience to help us assess:

[7] The 2014 Exposure Draft can be found at: http://www.ifrs.org/Current-Projects/IASB-Projects/FVM-unit-ofaccount/Exposure-Draft-September-2014/Documents/Exposure-Draft-Measuring-Quoted-Investments-September-2014.pdf

(i) how common it is for quoted investments in subsidiaries, joint ventures and associates, and quoted cash-generating units to be measured at fair value (please support your comments with examples).

(ii) whether there are material differences between fair value amounts measured on the basis of P×Q alone (when P is the quoted price for an individual instrument and Q is the quantity of financial instruments held) and fair value amounts measured using other valuation techniques. Please provide any examples, including quantitative information about the differences and reasons for the differences.

(iii) if there are material differences between different measurements, which techniques are used in practice and why.

Please note whether your experience is specific to a jurisdiction, a region or a type of investment.

(b) The Board has undertaken work on this area in the past (see Appendix 3 [of the RFI]). Is there anything else relating to this area that you think the Board should consider?

Feedback received

99. Most respondents to the RFI commented on this question. However, the majority also said the unit of account issue as described in paragraphs above was not applicable to them. That was either:

(a) because there are no Level 1 inputs that could be used in the measurement (for example shares of subsidiaries tested for impairment as a single asset, or as a part of a cash-generating unit, are usually not quoted in an active market); or

(b) because the investments, even if quoted, are not measured at fair value (for example investments in associates and joint ventures were measured using the equity method).

100. Most stakeholders in outreach meetings also wanted to discuss this question, although they provided similar feedback in regards to applicability of the issue.

How commonly are these items measured at fair value?

101. Most respondents, from all stakeholder groups except for users, said the fair value measurements of these instruments was not common. For example, RSM International commented:

> In practice, measuring investments in subsidiaries, joint ventures and associates at fair value proves not to be very common. In fact, it is very rare for non-investment entities to fair value such investments; they are usually measured at cost at company level (ie in separate financial statements).

102. This is not to say that respondents said these instruments were never measured at fair value. For example, ESMA found in their review of a sample of 78 European issuers:

> For 18% of the issuers in the sample the issue of the unit of account was relevant, the reasons for the fair value measurement included the following: (i) measurement of a subsidiary for impairment test purposes, (ii) classification as held for sale according to IFRS 5, (iii) loss of control while retaining a minority stake in a disposal, (iv) step acquisition and (v) application of the investment entity consolidation exemption in IFRS 10.

103. Most respondents noted fair value measurement of investments held by **investment entities** is common, because IFRS Standards require investment entities to measure their investments at fair value.

104. Some respondents also said fair value measurement takes place during **impairment testing** of cash generating units, when they are or include listed subsidiaries, or in impairment testing of listed associates accounted for under the equity method. However, there was some mixed feedback on whether the unit of account issue arises in these circumstances:

    (a) some respondents' feedback (eg ESMA's study of European issuers, standard-setters in Korea, Singapore and a preparer in Brazil) suggested that, in impairment testing, the recoverable amount tends to be value in use as that is higher than fair value less cost of disposal, so the unit of account question is not applicable, even if the subsidiary or associate is listed in an active market.

    (b) feedback received from valuation professionals in Canada and some preparers in South America said that the recoverable amount tends to be fair value less cost of disposal, as it was usually higher than value in use and that the unit of account is therefore an issue when these investments are listed in an active market.

105. For example, ESMA found in their review that:

> Although 17% of the issuers in the sample indicated that they had CGUs that were or included quoted issuers, 69% of those indicated that the recoverable amount was measured using the value-in-use and not the fair value less cost of disposal. The remaining issuers indicated that the CGU was measured by reference to the quoted price of the listed entity.

106. A few respondents mentioned other situations where the unit of account issue may be applicable, including when:

(a) a **business combination** is achieved **in stages**, in which case IFRS Standards require previously held interest to be measured at fair value;

(b) sale of ownership interest results in **loss of control** and recognition of new ownership interest (e.g. associates) measured at fair value; or

(c) a subsidiary or investments in joint ventures and associates are classified as **held for sale** in accordance with IFRS 5 *Assets held for Sale*.

107. The frequency of the fair value measurements mentioned above also depends on business practices and laws in a particular jurisdiction. For example, Duff and Phelps said 'situations involving Cash Generating Units ("CGUs") with a listed price tend to arise in jurisdictions where cross-holdings between companies and complicated ownership structures are common'.

Are there material differences in the PxQ and fair value amounts measured using other valuation techniques?

108. Some respondents, from all stakeholder groups except for users, provided a response to this question and all of them said that material differences may arise between fair value amounts measured on the basis of P×Q alone and amounts measured using other valuation techniques, although they did not provide quantitative information.

109. Those respondents provided reasons for the difference between amount measured on the basis of P×Q alone and amount measured using other valuation techniques as follows:

(a) most respondents said that share prices do not reflect the liquidity of the market for the shares.

(b) some respondents said that share prices do not reflect the value of control and the value of synergies. For example, ANC commented:

> For instance, on the 35 public offers that occurred in France in 2016, the median premium granted by the offer prices was 22% over quoted prices when that median premium offered was only 8% over experts' DCF values, meaning that the DCF values were closer to the offered price than the quoted prices were. The offer prices may in fact integrate control premium and synergies explaining premiums paid, when experts' values do not.

(c) a few respondents said that some markets lack depth and are susceptible to speculative trading, information asymmetry and other factors.

110. Some respondents said this question was not applicable to them as they measured these investments on the basis of PxQ alone and thus did not perform a comparison with other measurement techniques.

Which techniques are used in practice

111. Only a few respondents provided an answer to this question. They referred to the discounted cash flow method being used in the case of differences between different measurement approaches, with some also referring to the market approach reflecting expected future performance and potential synergies (ie adjusted PxQ). Some referred to performing a reasonableness check against control premiums for similar companies.

Anything else to consider?

112. Some respondents, representing all stakeholder groups, commented on this question and most of them:

(a) referred to the Board's 2014 Exposure Draft on this issue and their comment letter;

(b) stated that the measurement should be for the investment as a whole, adjusting PxQ for the value of control, value of synergies, market liquidity as applicable; and

(c) urged the Board to clarify the Standard in this regard and provide application guidance to ensure consistency of application.

113. A few respondents asked the Board to clarify the standard, without stating their preference for the accounting treatment.

114. This feedback differs from the feedback received in outreach meetings with users of financial statements, most of whom supported the measurement on the basis of PxQ, because it is verifiable and in the view of some, better represents fair value of the investment in question.

115. A few users said during outreach meetings that they were supportive of measuring the fair value for the unit of account as a whole, provided an explanation is given of any difference between the resulting measurement and the amount based on PxQ.

116. A few respondents made additional comments:

(a) the Board should consider further research of relevant literature, including the work by the US Appraisal Foundation working group on "The Measurement and Application of Market Participant Acquisition Premiums"[8]; and

(b) the Board should consider day one gain/loss accounting for instruments in the scope of IFRS 9 *Financial Instruments* (IFRS 9) when considering this issue (day one gains/losses are also discussed in the section on Other matters, in paragraph 215).

[8] The voluntary guidance developed by that working group can be found here: https://appraisalfoundation.sharefile.com/app/#/share/view/sf6c518cbd8a41df9

Feedback on the application of highest and best use

Background and questions in the RFI

117. IFRS 13 requires the highest and best use (HBU) of a non-financial asset to be considered when measuring its fair value, even if that use is different from the asset's current use. The Standard stipulates that the HBU of a non-financial asset must be physically possible, legally permissible and financially feasible. The Standard further presumes that an entity's current use of a non-financial asset is its HBU unless market or other factors suggest that a different use by market participants would maximise the value of the asset.

118. The Board sought feedback from stakeholders to better understand the challenges in applying the HBU concept, the pervasiveness of these challenges and the support that might be helpful to address those challenges.

119. The RFI included the following questions on the concept of HBU:

Question 4—Application of the concept of highest and best use for non-financial assets
Please share your experience to help us assess: (a) whether the assessment of an asset's highest and best use is challenging, and why. Please provide examples to illustrate your response. (b) whether the current uses of many assets are different from their highest and best use, and in which specific circumstances the two uses vary. (c) whether, when applying highest and best use to a group of assets and using the residual valuation method, the resulting measurement of individual assets in the group may be counter-intuitive. If so, please explain how this happens, and in which circumstances. (d) whether there is diversity in practice relating to the application of the concept of highest and best use, and when and why this arises. Please note whether your experience is specific to a jurisdiction, a region or a type of asset.

Feedback received

120. Many respondents commented on the questions on the application of HBU, with most saying they had experience with it and found it challenging to apply. They said that most challenges arise when assessing whether an alternative use is

legally permissible. Many respondents also commented that they disagreed with the concept of HBU because it did not reflect the business model of the entity.

121. Some respondents commented that the application of the concept was not challenging because, in their experience, the current use of an asset is also its HBU. A few respondents indicated circumstances when the HBU of an asset differs from its current use, mostly noting this is not a common occurrence.

122. A few respondents discussed the use of the residual method and said they found its outcome counter-intuitive because it can result in understatement of the cost of inventories.

123. The respondents had mixed views on whether there is diversity in the application of the HBU.

124. The users that provided feedback during outreach meetings said they were generally satisfied with the concept of the HBU.

Challenges in applying the HBU concept

125. Most respondents who had experience with HBU stated that they found the application of the concept challenging, with challenges mostly arising in business combinations. These respondents included preparers, standard-setters, auditors, valuation specialists, professional accounting bodies, a regulator, an academic and a user. The specific challenges the respondents discussed are described in the following subsections.

Assessing whether an alternative use is 'legally permissible'

126. Some respondents stated that a particular challenge was assessing whether a use was 'legally permissible' and that there is diversity in interpretations of the requirement that a potential alternative use must be legally permissible. Examples of challenges identified by respondents include:

(a) impact of restrictions on assessment eg:

(i) government-imposed restrictions, particularly land;

(ii) restrictions because an asset is subject to a contract to sell it for a nominal amount at a distant date; and

(b) differences in thresholds used in assessing whether an alternative use is legally permissible. For example, property valuation specialists may reflect an alternative use in their measurement only if there is evidence both of probable future approval that is specific to the subject of valuation, and that the alternative use is 'reasonably permissible' which may be different to how preparers interpret IFRS 13 requirements.

Determining the amount of evidence

127. Some respondents stated that another challenge in applying the HBU concept is determining how much evidence is needed when looking for an alternative use. The Singapore Accounting Standards Council provided the following example:

> ...a prospective buyer of a building could offer a price that is higher than the value derived from current use under an income approach, but the entity might not have information about whether the offer price is derived based on a different use.

128. A few respondents said that the use of the term 'suggest' in paragraph 29 of IFRS 13[9] creates challenges in assessing the amount of evidence needed, because 'suggest' could be read as meaning anything between an indication that an alternative use exists and clear evidence that an alternative use would generate higher returns. A few respondents recognised that paragraph 71 of the Basis for Conclusions on IFRS 13[10] provides some reassurance that an exhaustive search for alternative uses is not required.

[9] Paragraph 29 of IFRS 13: '… However, an entity's current use of a non-financial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximise the value of the asset.'

[10] Paragraph BC71 of IFRS 13: IFRS 13 does not require an entity to perform an exhaustive search for other potential uses of a non-financial asset if there is no evidence to suggest that the current use of an asset is not its highest and best use. The IASB concluded that an entity that seeks to maximise the value of its assets would use those assets at their highest and best use and that it would be necessary for an entity to consider alternative uses of those assets only if there was evidence that the current use of the assets is not their highest and best use (ie an alternative use would maximise their fair value). Furthermore, after discussions with valuation professionals, the IASB concluded that in many cases it would be unlikely for an asset's current use not to be its highest and best use after taking into account the costs to convert the asset to the alternative use.

Identifying characteristics of market participants

129. Some respondents stated that a challenging part of assessing the HBU of a non-financial asset was in identifying characteristics of market participants for possible asset uses that were not the current use. The respondents indicated that the concept of ‘market participants’ is well understood but the notion of identifying their ‘characteristics’, as opposed to identifying specific market participants, was difficult. A few respondents provided examples of when this challenge arises:

    (a) when assets or liabilities are not sold or transferred: it is not clear whether the reporting entity itself should in those circumstances be viewed as a (or perhaps the only) market participant.

    (b) when assets can be used for many different purposes (eg an out-of-town prime retail site could be of interest to a lessor, a housing developer, retail competitors, etc).

Identifying alternative use

130. Some respondents stated that another challenge when applying the HBU concept was determining the alternative uses for an asset. Respondents indicated that this occurs when the asset is unique or new, for example technology or software.

Other challenges

131. Valuation specialist Duff &Phelps said there might be differences in practice in accounting for economic obsolescence when the valuation premise is ‘in combination’ with other assets and asked for guidance on the topic. They described circumstances in which this arises

> This issue may arise in situations in which it is concluded that market participants would continue operating a business or a group of assets in combination with each other while economic obsolescence is present in the group (business). Economic obsolescence (EO) arises when structural changes in an industry or shifts in demand permanently constrain the cash flow generating capacity of a business.

Disagree with the concept of highest and best use

132. Many respondents stated that they disagreed with the concept of HBU. These respondents included preparers, standard-setters, auditors, a user and an academic. Many of the respondents questioned whether the HBU method gives relevant information to users of financial statements. Some respondents thought that the method is too theoretical because its application could be based on hypothetical transactions.

133. Many respondents also said they disagree with the concept of highest and best use because it does not take into account an entity's business model or its management's intent with regard to a particular asset and it causes additional costs.

Circumstances in which current use differs from HBU

134. Of the respondents who have experience with the concept of HBU, a few said they have experienced circumstances where an asset's HBU differed from its current use. These respondents included standard-setters, valuation specialists, regulators, a preparer and a professional accounting body. However, most of those respondents noted that it is uncommon for the current use of an asset to be different from its HBU.

135. In providing examples of circumstances in which current use is different from HBU, respondents mostly referred to property carried at fair value; and property, brands and technology acquired in business combinations, and also one example provided relating to biological assets. The Malaysian Accounting Standards Board gave the following example for property:

> The current use of houses located along a main road could be maximized in view of its location along a busy road by changing its use from residential use to commercial use.

136. Examples of brand or technology provided by respondents related to acquisition made for defensive purposes, where assets are acquired but not used.

137. A valuation professional commented that HBU can sometimes be different than current use due to economic obsolescence, with obsolescence becoming prevalent in industries with large capital investment undergoing structural shifts.

Application of the residual method

138. A few respondents commented on this question, most of them expressing the view that applying the HBU concept to a group of assets using the residual valuation method resulted in a counter-intuitive outcome. The respondents included standard-setters, preparers, valuation specialists, auditors and professional accounting bodies. Most of the respondents stated that the method was counter-intuitive because the method can result in an individual asset valued at nil. A few said that if factory is measured at nil, no depreciation would be included in the cost of items produced in factory, distorting presentation of financial performance when those items are sold.

Diversity in practice in applying the HBU concept

139. The respondents had mixed views on whether there is diversity in the application of the HBU. The respondents included standard-setters, valuation specialists, preparers, an auditor and a professional accounting body. Most respondents who had seen diversity in practice thought that the diversity arose in the judgements and in interpretations of concepts. Examples provided included:

(a) a few auditors indicated that the amount of work done to assess HBU varied between preparers. For example, they saw diversity in the extent of evidence sought to rebut the presumption that the highest and best use is the current use.

(b) whether and how the probability of future regulatory approval for an alternative use could swing the conclusion between ‘legally prohibited’ and ‘not legal at the measurement date’.

(c) valuation specialists’ understanding of the concept might differ because of divergent valuation guidance or customary practice across various jurisdictions. For example, some valuation specialists accept an alternative use as being the HBU if it is ‘reasonably probable’, which may be a different threshold than IFRS 13 requires.[11]

[11] It is unclear whether and how a ‘reasonably probable’ criterion in this example relates to a ‘reasonably permissible’ criterion assessment when assessing whether a use is legally permissible, because these examples were provided by different respondents.

(d) whether economic obsolescence leads to assessment of highest and best use being different from current use.

Recommendations from respondents

140. Although the RFI did not ask respondents for recommendations, some respondents provided suggestions to the Board in this area.

141. Some recommended that the Board consider providing practical guidance in the following areas:

(a) assessing whether an alternative use is the HBU (including the concept of 'legally permissible'); and

(b) determining when it is possible to rebut the presumption that current use is also the HBU.

142. A few provided recommendations to move paragraphs from the Basis for Conclusions on IFRS 13 to the Standard:

(a) paragraph BC69[12] to assist preparers to make better sense of what is meant by 'legally permissible'.

(b) paragraph BC71 to assist preparers to determine the amount of evidence that is needed to assess an asset's HBU.

Feedback on the application of judgement

Background and questions in the RFI

143. IFRS 13 requires the use of judgement when measuring the fair value of an asset or a liability. During phase 1 of the PIR, some stakeholders stated that making these judgements is challenging. The areas in which applying judgement is

[12] Paragraph BC69 of IFRS 13: Some respondents asked for further guidance about whether a use that is legally permissible must be legal at the measurement date, or if, for example, future changes in legislation can be taken into account. The IASB concluded that a use of an asset does not need to be legal at the measurement date, but must not be legally prohibited in the jurisdiction (eg if the government of a particular country has prohibited building or development in a protected area, the highest and best use of the land in that area could not be to develop it for industrial use).

considered most challenging were assessing whether a market is active and assessing whether an input is a significant unobservable input.

144. The RFI included the following questions about the use of judgements:

Question 5—Applying judgements required for fair value measurements
Please share your experience to help us assess the challenges in applying judgements when measuring fair value: (a) is it challenging to assess whether a market for a asset or liability is active? Why, or why not? (b) is it challenging to assess whether an input is unobservable and significant to the entire measurement? Why, or why not? Please provide specific examples to illustrate your response and note whether your experience is specific to a jurisdiction or a region or a type of asset or liability.

Feedback received

145. Many respondents discussed application of judgement. Most of those respondents found challenging the assessments of both whether a market is active and whether an unobservable input is significant.

Assessment of whether a market is active

146. Most respondents that discussed assessment of market activity said it was challenging, and most of them asked the Board to provide further guidance on assessment. A few respondents said that, although the assessment is challenging, additional guidance would not be helpful and that the Standard should remain principle-based. The respondents included preparers, standard-setters, auditors, valuation specialists, regulators and a professional accounting body.

147. A large majority of those who said the assessment of active market was not challenging stated this was because they either had developed internal guidance or used industry level guidance for assessment. A few said the guidance in paragraph B37 of IFRS 13 is sufficient.

148. Respondents identified areas and circumstances in which there are challenges with assessment of market activity:

(a) developing countries and smaller developed economies with generally lower volume and frequency of trading;

(b) over the counter markets;

(c) debt instruments in developed markets; and

(d) financial markets under stress conditions.

149. Respondents said there is inconsistency in the assessment in practice, and identified some specific areas of assessment that cause challenges and the support needed:

(a) assessment of whether there is both sufficient frequency and volume, and relationship between these. Many respondents asked for further guidance on what constitutes sufficient frequency and volume. A securities regulator suggested the Board should provide additional examples to explain the additional analysis that should be carried out under paragraphs B38 of IFRS 13[13] when an entity concludes that there has been a significant decrease in the volume or level of activity for the asset or liability in relation to normal market activities.

(b) assessment of whether there are recent or relevant comparable transactions. A few respondents asked for guidance on how the assessment is affected by a temporary closure of the market or by a low level of transactions.

150. A few respondents noted the link between the assessment of the market activity and the PxQ issue and said the PxQ issue puts additional pressure on the assessment.

[13] Paragraph B38 in IFRS 13: This IFRS does not prescribe a methodology for making significant adjustments to transactions or quoted prices. See paragraphs 61–66 and B5–B11 for a discussion of the use of valuation techniques when measuring fair value. Regardless of the valuation technique used, an entity shall include appropriate risk adjustments, including a risk premium reflecting the amount that market participants would demand as compensation for the uncertainty inherent in the cash flows of an asset or a liability (see paragraph B17). Otherwise, the measurement does not faithfully represent fair value. In some cases determining the appropriate risk adjustment might be difficult. However, the degree of difficulty alone is not a sufficient basis on which to exclude a risk adjustment. The risk adjustment shall be reflective of an orderly transaction between market participants at the measurement date under current market conditions.

Assessment of whether an input is unobservable and significant

151. Many respondents commented on this and most of them said they found the assessment challenging, in particular the assessment of whether an unobservable input is significant. The respondents mostly referred to assessments relating to financial instruments, with a few comments relating to property. The respondents included preparers, standard-setters, auditors, valuation specialists and a regulator.

152. As with assessment of active market, most of those who said the assessment of whether an input is significant and unobservable was not challenging stated this was because they either had developed internal guidance or used industry level guidance. Respondents provided the following examples of guidance they used:

    (a) Bloomberg Valuation Service (BVAL) score on a security, which gives an indication of whether there is limited availability of pricing data in the market;

    (b) assessment of significance using information systems, for example using the ratio of the risk measure of the unobservable input to the present value of the instrument; and

    (c) industry inputs, such as aircraft blue book.

153. Some respondents said there is a bias towards classification within Level 2 of the hierarchy because disclosure requirements are more extensive for Level 3 measurements. A few respondents said that early adopters of new market practices may be deterred from introducing new inputs (such as funding valuation adjustments) because this would take the measurement within Level 3 of the hierarchy, even though in their view such measurements may be superior to those derived using current techniques.

The challenges with the assessment

154. Respondents provided examples of specific challenges arising during the assessment of whether inputs are unobservable and significant as well as of diversity in practice:

(a) the assessment is more difficult when using third party pricing and brokers without sufficient visibility into the valuation techniques and inputs used;

(b) it is not clear to some respondents whether the assessment is qualitative or quantitative. Some other respondents said they understood the assessment to be quantitative but struggled with how to incorporate qualitative factors in a quantitative assessment;

(c) is the assessment made over time or at a point in time, which can make a difference for inputs that may vary over time (such as own credit risk)?

(d) use of market multiples: should measurements that involve significant judgment be classified within Level 3 when an observable market data point is used as a starting point;

(e) some respondents said they observed diversity in practice as follows:

  (i) differences in thresholds. Some respondents said that, although the majority of banks apply a criterion that the valuation uncertainty range exceeds a certain percentage of the position value, there are some differences in the threshold across banks;

  (ii) variation in whether portfolio level adjustments are considered during assessment (eg credit valuation adjustment (CVA) on an uncollateralised OTC derivative may have been a key unobservable when pricing the deal but some banks do not consider it as an input for the Level 2 / Level 3 determination because CVA is calculated on a portfolio basis);

  (iii) differences in how the size of the unobservable input is considered. The European Banking Authority provided the following example: suppose the fair value of an instrument is being estimated by taking the observable quoted price of a similar instrument (for example, 10) and adjusting for differences between the two instruments (for example, adjustment of 2) to take into consideration unobservable inputs. Some banks interpret IFRS 13 as requiring them to treat only the 2 as unobservable and some interpret it as requiring them to treat the whole of the 8 as unobservable.

(iv) some respondents said that some preparers believe that classification within the hierarchy should be made at an asset class level, instead of at the individual instrument level.

Guidance sought

155. Most respondents who found the assessment challenging sought further guidance or examples on what constitutes unobservable inputs, and on when such an input is significant. Some suggested that such guidance should consider how such assessment needs to be performed, and the interaction of quantitative and qualitative information in making such assessment.

156. A few respondents also raised a question about the definition of Level 1 inputs—they asked whether net asset value, comprised of investments in quoted shares only, can be considered a Level 1 input.

Feedback on fair value measurement of biological assets and unquoted equity instruments

Biological assets

Background and questions in the RFI

157. IAS 41 *Agriculture* (IAS 41) requires biological assets to be measured at fair value. The bearer plants on which some biological assets grow are in the scope of IAS 16 *Property, Plant and Equipment* (IAS 16) and are measured on either a cost basis or at fair value.

158. During phase 1 of the PIR, some stakeholders said that measuring biological assets at fair value is challenging in inactive markets or in the absence of a market. Some of those stakeholders also said that additional guidance (such as education material) could help entities measure such items at fair value.

159. With the RFI, the Board aimed to explore whether there is a need for further guidance, such as education material, on measuring the fair value of biological assets.

160. The RFI included the following questions relating to fair value measurement of biological assets:

> **Question 6A—Education on measuring biological assets at fair value**
>
> Please describe your experience of measuring the fair value of biological assets:
>
> (a) are any aspects of the measurement challenging? Why, or why not? Please provide examples to illustrate your response.
>
> (b) what, if any, additional help would be useful in applying IFRS 13? In which areas?

Feedback received

161. Some respondents had experience with biological assets. Most of them said the fair value measurement of biological assets was challenging, and many asked for additional guidance and/or changes to IAS 41.

Challenging aspects of the measurement

162. Most respondents to this question said measuring biological assets at fair value was challenging when there is no active market, with growing produce often mentioned as an example. Respondents included standard-setters, preparers, accounting firms, and valuation specialists. Some specific growing produce mentioned in the letters included: fruit, fish, palm oil, tea leaves and crops such as wheat or corn.

163. These respondents mentioned several aspects of such measurements as being challenging:

    (a) determining the point at which to recognise growing produce as distinct from a bearer plant, for example whether from the pollination date, from when the produce is first visible or some other point. Mazars gave example of diversity in practice ‘We have noted that some appear to not be valuing growing produce until harvest point, whilst others use a prorata temporis calculation based on the estimated yield and market value’.

(b) selecting inputs such as discount rates. Sometimes the valuation is very sensitive to those inputs due to long periods to maturity, for example for forests.

(c) deciding which costs to allocate in income based valuation methods. Some noted that there is often confusion about whether an entity can consider future replanting or replacement of plants, as it would in a business valuation. Some pointed to diversity in whether maintenance costs are included in valuation. For example KPMG commented:

> Some entities consider that these maintenance costs are not material and need not be factored into the valuation (based on the view that fertilizers applied currently will only benefit future fruit) while others factor the full maintenance costs into the valuation model.

(d) determining how much of the estimated total profit to allocate to various stages prior to harvest or maturity. EY commented ‘entities may misunderstand the allocation of profit margin through the period to maturity, either believing all margin is earned at maturity or harvest, or attributing too much margin in early stages of development’.

(e) assessing whether the measurement is reliable (if fair value measurement is determined to be unreliable, paragraph 30 of IAS 41 requires measurement at cost). Mazars indicated there is diversity in practice in this area as well:

> In an outreach carried out by the IFRS IC, we have performed a desktop review and found that some entities within the same type of business have rebutted the presumption, others have not but do not use the information internally, whilst others having not rebutted the presumption provide such wide ranges in the assumptions of a Level 3 measurement that this raises a question in terms of reliability/uncertainties.

Measurement is not challenging

164. Several preparers noted examples of biological assets, such as grains, for which they stated that there are active markets and for which it was easy to determine fair value. Similarly, pricing information may be published for some biological assets, such as sugarcane. The respondents did not find the measurement of biological assets in these circumstances challenging.

165. Valuation specialists Duff & Phelps said the measurement of biological assets is generally not challenging, because there are established measurement methods for various biological assets, depending on what inputs are available.

> …value is determined through a contract between grower and buyer (eg vineyard and orchard assets) or when market pricing is available, such as for some timber assets; or based on the use of multi-period excess earnings method such as for sugarcane assets

166. They further noted that in some cases specialist expertise and education might be required.

Would additional help be useful?

167. Of the respondents who said the fair value measurement of biological asset was challenging, many asked for additional help. These respondents included standard-setters, preparers, accounting firms, and valuation specialists. However, different views were expressed about what that help should entail. Some questioned whether providing that help is a job for the Board or for the valuation profession.

168. A few also noted that they expect divergence in practice to decline as valuation practice develops.

In which areas was guidance sought?

169. Of the respondents who asked for more guidance in IFRS 13, nearly all sought guidance on measuring the fair value of growing produce. Respondents included preparers, a standard-setters, an auditor and a professional accounting body. Specific suggestions of areas in which guidance would be most useful included:

(a) alternative approaches to measuring the fair value of biological assets when there is no market for particular stages of the process of growth of the biological assets;

(b) the allocation of costs between produce and bearer plants;

(c) the allocation of profit margin through the period to maturity;

(d) taking into account data from a similar market (eg neighbouring market) that is active; and

(e) application of valuation methods, such as the multi-period excess earnings method.

What form of guidance was sought?

170. Respondents suggested various forms of guidance including:

(a) adding illustrative examples to accompany IFRS 13;

(b) education material similar to that for unquoted equity instruments within the scope of IFRS 9; and

(c) including application guidance in IFRS 13 itself.

Why some think no more guidance is needed?

171. Some respondents said they expect that the application of Practice Statement 2: *Making Materiality Judgements* will lead to a conclusion that some of these biological assets, in particular immature produce, are immaterial and thus not required to be recognised in the financial statements.

172. Other respondents said there is no need for more guidance as there are no major issues today that could be solved by guidance.

173. Some said they think entities need to use valuation specialists, because it is difficult for the standard to provide guidance for specific circumstances.

174. Some respondents suggested that the Board engages with the valuation community to work on achieving better comparability of measurement of biological assets.

Suggestions for changes to IAS 41

175. Although outside the scope of the IFRS 13 PIR and the RFI, some respondents suggested changes to, or further guidance in, IAS 41. Most of those respondents asked for guidance on how to determine whether a measurement is 'clearly unreliable' and the biological asset must therefore be measured at cost, as per paragraph 30 of IAS 41. They asked that any such guidance includes clarification of the meaning of 'significant practical difficulties'.

176. A few respondents suggested changes to the scope of IAS 41, with the following suggestions:

    (a) account for produce growing on bearer plants under IAS 2 *Inventories* (IAS 2);

    (b) account for bearer livestock under IAS 16; and

    (c) measure immature fish at cost or at fair value through other comprehensive income.

177. One respondent suggested replacing fair value measurement with disclosure requirements only, for example 'disclosures of volumes and sizes combined with information on forward prices'.

Relevant work by other standard-setters

178. There is currently no authoritative guidance for accounting for biological assets by private entities in Canada. The Accounting Standards Board of Canada is undertaking a project to develop authoritative guidance in this area for private enterprises and not entities that apply IFRS Standards. The project[14] will address:

    (a) when a biological asset should be recognized;

    (b) how it should be measured on initial recognition and in subsequent periods;

    (c) how agricultural produce should be accounted for; and

    (d) what disclosures should be required.

[14] For more details see project website: http://www.frascanada.ca/standards-for-private-enterprises/projects/active/item55805.aspx

179. The IVSC is considering adding to its agenda a project[15] on valuation of biological assets. The project would cover all assets within the scope of IAS 41.

Unquoted equity instruments

Background and questions in the RFI

180. To assist entities with measuring fair value when limited information is available, in 2012, the IFRS Foundation Education Initiative published Illustrative Examples to accompany IFRS 13 *Unquoted equity instruments within the scope of IFRS 9*.[16] The education material describes the thought process, as well as a range of the most commonly used valuation techniques for measuring the fair value of unquoted equity instruments within the scope of IFRS 9. The material also includes examples that illustrate how the fair value of an unquoted equity instrument could be measured, even with limited information.

181. During phase 1, some stakeholders stated that measuring the fair value of unquoted equity instruments is challenging because:

(a) the values are not readily available; and

(b) the range of valuation techniques available to use and there is perceived to be high subjectivity surrounding some of the assumptions and inputs used. These factors make the resulting measurements contentious.

182. The RFI included the following questions relating to fair value measurement of unquoted equities:

Question 6B—Education on measuring unquoted equity instruments at fair value

Please describe your experience of measuring the fair value of unquoted equity instruments:

(a) in 2012, the IFRS Foundation Education Initiative published *Unquoted equity instruments within the scope of IFRS 9 Financial Instruments*. Have you used this educational material? If so, how did this material help you to measure the fair value of unquoted equity instruments?

(b) do you have questions not covered in *Unquoted equity instruments within the scope of IFRS 9 Financial Instruments?* Do you think that additional help

[15] The IVSC agenda consultation document can be found: https://www.ivsc.org/files/file/view/id/861
[16] The education material can be found at: http://www.ifrs.org/Use-around-the-world/Education/FVM/Documents/Education-guidance-FVM.pdf

would be useful in applying the requirements? Why, or why not? Please provide examples to illustrate your response.

Feedback received

183. Most respondents to the RFI did not respond to this question or said they had no experience in this area. Of those that did respond, most said they were familiar with the education material. Some of those respondents noted they were also using guidance prepared by industry groups, with most quoting the International Private Equity and Venture Capital Valuation Guidelines[17].

184. Many of those who responded to the questions said additional guidance was needed. Those respondents included several accounting firms, preparers, standard-setters and a user. Some respondents, including several standard-setters and preparers, said additional guidance was not needed. Some respondents, including standard-setters and preparers, said that the valuation profession should develop any additional guidance, and not the Board.

Questions not covered in the education material, additional guidance requested

185. The respondents who said that additional guidance was needed requested guidance for the following examples:

(a) how to reconcile valuations using two different methods, if differences are significant. For example is the weighted average method appropriate? If not, how should a method be selected and what weights should be placed on different valuation techniques and inputs?

(b) how to measure fair value of investments in early-stage, emerging private entities.

(c) how to determine the cost of equity capital in view of problems with the Capital Assets Pricing Model (CAPM). Respondents said alternative models used in practice include a build-up rate based on US sources such as Ibbotson or Duff & Phelps, adjusted for local conditions; or the Risk Rate Component Model.

[17] The IPEVC valuation guidelines can be found at: http://www.privateequityvaluation.com/valuation-guidelines/4588034291

(d) how to determine the size of discount for a lack of liquidity.

(e) how to determine whether a restriction on transfer is a characteristic of the equity instrument or is specific to the holder of the instrument.

186. Some respondents referred to additional guidance in specific sections of the education material as follows:

(a) risk-free rate and equity market discussion - update the discussion on discount rates given the current environment of major central bank intervention in financial markets (and corresponding impact on cost of capital inputs).

(b) country risk premium discussion - mention that there are now other models also used by practitioners to quantify country risks (eg Erv-Harvey Viskanta Country Credit Ratings model).

(c) transaction price paid for a similar instrument of an investee - more guidance on valuation of equity securities in complex capital structures that include more than one class of securities.

187. Some respondents made further points:

(a) recommended that the Board makes reference to detailed valuation guidance already developed by industry, for example International Private Equity and Venture Capital Valuation Guidelines.

(b) IFRS 9 requires fair value measurement of unquoted instruments that were carried at cost under IAS 39 *Financial Instrument: Recognition and Measurement* (IAS 39). Some expressed concern that these measurements would be of poor quality and asked the Board to consider reintroducing the exception that was in paragraph 46(c) of IAS 39 requiring cost-based measurement in some cases.

Feedback on effects and convergence

Background and questions in the RFI

188. One objective of the PIR is to assess the effects of the Standard since its implementation. IFRS 13 is also a converged with Topic 820 *Fair Value*

*Measurement (*Topic 820) in US Generally Accepted Accounting Principles issued by the Financial Accounting Standards Board (FASB).

189. These two matters were included in the RFI with the following questions:

Question 7—Effects and convergence
(a) Please share your experience of the overall effect of IFRS 13: (i) what effect did IFRS 13 have on users' ability to assess future cash flows? If you are a user of financial statements, please provide us with examples of how you use information provided by entities about their fair value measurements and any adjustments you make to the measurements. (ii) what effect did IFRS 13 have on comparability of fair value measurements between different reporting periods for an individual entity and between different entities in the same reporting period? (iii) what effect did IFRS 13 have on compliance costs; specifically, has the application of any area of IFRS 13 caused considerable costs to stakeholders and why? (b) Please comment on how you are affected by the fact that the requirements for fair value measurement in IFRS 13 are converged with US GAAP; and please comment on how important it is to maintain that convergence.

Feedback received

190. Most respondents commented on the effects of IFRS 13 and on convergence. Most respondents stated that the ability to assess future cash flows as well as the comparability of financial statements had increased since IFRS 13 came into effect. Some respondents indicated that the comparability increased only for individual entities over time but not across industries. Many respondents stated that IFRS 13 had increased compliance costs but some respondents indicated that the benefits outweighed the cost. Almost all respondents stated that maintaining convergence was important to them and that this convergence is a main driver of the increased comparability globally.

Ability to assess future cash flows

191. Most respondents discussed the effect of IFRS 13 on users' ability to assess future cash flows and many of those thought IFRS 13 had improved users' ability to assess future cash flows. These respondents included preparers, valuation

specialists, a user, a regulator, a standard-setter and an auditor. The respondents indicated that the disclosures in IFRS 13, specifically the sensitivity analysis for Level 3 fair value measurements, unrealised gains or losses and valuation techniques and inputs, are useful for assessing future cash flows.

192. However, some other respondents had mixed views due to factors in practice affecting the usefulness of the information. These respondents indicated that the level of aggregation in the IFRS 13 disclosures takes away from usefulness and from the ability to assess cash flows. Some thought fair value measurement overall (and therefore IFRS 13) has limited effect on users' ability to assess future cash flows, for example Duff & Phelps commented:

> Fair value measurements and the related disclosures do not necessarily directly predict future cash flows (i.e., the emphasis here is misplaced); rather, they go beyond cash flows. It is true that a fair value measurement today reflects expected future benefits. However, in addition to cash flows, the other significant determinants of value are the timing and risk of the cash flows; together, these main elements combine to produce a fair value estimate. In that sense, fair value is useful in that it boils down market participant expectations to a single concluded amount that would be reported in the financial statements (or otherwise considered for financial reporting purposes).

193. A few respondents thought that IFRS 13 did not improve users' ability to assess future cash flows. These respondents included standard-setters, preparers, a valuation specialist, an auditor and a professional accounting body.

194. A few respondents further thought that enabling users of financial statements to assess future cash flows should not be an objective of fair value information. One respondent stated that IFRS disclosures cannot help users assess an entity's future cash flows because the objective of financial reporting is to reflect the financial position as at a balance sheet date only.

Comparability

195. Of those respondents who commented on comparability, most stated that the issuance of IFRS 13 has improved comparability between different reporting periods for an individual entity and between different entities in the same reporting period. These respondents included preparers, standard-setters, valuation specialists, a regulator, a professional accounting body, an auditor, a user and a regulator. Some respondents commented that the consistent definition of fair value provided in IFRS 13 has improved consistency in financial reporting and created a single framework for applying it. Business Europe commented 'One experience shared by some of our members is that the internal valuation processes have been further formalised and (made) transparent as a consequence of the standard'.

196. A few respondents stated that comparability had improved because of the disclosure of the fair value hierarchy and because overall guidance in paragraph 36[18] had helped to make accounting practice more uniform. Another respondent indicated that the increase in comparability stems from convergence between IFRS 13 and its US equivalent.

197. Some respondents stated that comparability has improved over time only within individual entities, because entities have assets and liabilities at different levels of the hierarchy and use different valuation techniques and inputs. The Korea Accounting Standards Board commented:

> …the result of the survey indicates that our stakeholders believe that there is high comparability of fair value measurements and disclosures between different reporting periods for an individual entity, but low comparability between different entities in the same reporting period.

198. A few respondents reported that there was no significant improvement in comparability because of IFRS 13.

[18] IFRS 13 paragraph 36 In all cases, an entity shall maximise the use of relevant observable inputs and minimise the use of unobservable inputs to meet the objective of a fair value measurement, which is to estimate the price at which an orderly transaction to transfer the liability or equity instrument would take place between market participants at the measurement date under current market conditions.

Compliance costs

Considerable costs

199. Of respondents that commented on the costs of IFRS 13, many indicated that the costs were considerable. The respondents include preparers, standard-setters, professional accounting bodies, auditors, a valuation specialist and a user. These respondents indicated that large quantities of Level 3 fair value measurement valuations and disclosures created considerable costs. These respondents also indicated that the cost to prepare the Level 3 reconciliation disclosure was considerable. Some respondents stated that additional costs were considerable due to external audit fees and valuation specialist fees. A few respondents stated that, specifically, considerable costs are incurred when determining fair value for items that do not have an active market; unquoted equity instruments were also mentioned. Die Deutsche Kreditwirtschaft commented '…costs for internal projects and process implementation were considerable. Current measurement process does not create significant cost, but disclosure requirements do'.

Costs not considerable

200. Some respondents indicated they did not experience considerable costs when applying IFRS 13. These respondents included several preparers and one valuation specialist. One respondent stated that the costs decreased due to the decreased time spent in searching for suitable fair value measurements. Another respondent indicated that they did not experience increased costs but increased time spent preparing the fair value information.

Convergence with US GAAP

201. Most respondents commented on convergence between IFRS 13 and Topic 820 and almost all respondents stated that it was important that IFRS 13 remained converged with Topic 820. The respondents included preparers, standard-setters, auditors, regulators, professional accounting bodies and valuation specialists. Most respondents gave a general statement that the convergence was important.

202. Many respondents indicated that the convergence leads to increased comparability for financial statements globally. The respondents also indicated that the

increased convergence is facilitating efficient capital markets, increased user confidence and reduced compliance costs. A few respondents also indicated that the convergence has led to more material to be available for stakeholders around fair value measurements.

203. A few respondents stated that the Board should not let a desire for convergence prevent the Board from clarifying the Standard or from providing guidance to improve the quality of disclosures. A few other respondents, however, stated that the Board should work with the FASB on any further areas of consideration for the converged Standards.

204. A few respondents also indicated that maintaining convergence was not important in their view. These respondents included standard-setters and a user. However, these respondents stated that convergence in this area had increased comparability.

Other matters

205. The RFI included the following question regarding other matters not covered by the RFI:

Question 8—Other matters
Should the Board be aware of any other matters as it performs the PIR of IFRS 13? If so, please explain why and provide examples to illustrate your response.

Feedback received

206. Other matters mentioned by respondents, and not covered in focus areas in the RFI, included:

(a) as mentioned in the feedback on disclosures, some respondents reported a perception that the fair value hierarchy implies that information about items on Level 1 or Level 2 is more relevant than information about Level 3. They indicated that this perception puts pressure on classification. They also said that this perception is mistaken.

(b) some respondents stated that the requirements for fair value disclosures for financial instruments in interim reports are challenging and they questioned the usefulness of this information.

(c) a few respondents discussed blockage factors.

(d) a few respondents referred to diversity in practice with respect to valuation adjustments in measurement of financial instruments.

(e) a few respondents indicated issues in practice with assessment of whether transaction price equals fair value and whether any day one gains or losses are to be recognised in profit or loss.

(f) a few respondents had challenges with the following:

  (i) the lack of a practical expedient to use net asset value for measuring the fair value of an investment in an investment company;

  (ii) how to consider tax in fair value measurement; and

  (iii) how to measure fair value of liabilities.

Fair value hierarchy

207. Some respondents stated that they disagreed with the perception that the fair value hierarchies implying Level 1 fair value measurements provide more relevant information than Level 2 or Level 3. The respondents included preparers, valuation specialists, a standard-setter, a regulator and a user. The respondents indicated that the hierarchy appears to suggest that measurements classified within Level 3 are of lower quality than measurements classified within other levels. The respondents stated that there is a pressure to classify items within Level 1 or Level 2 to avoid the additional disclosures required for Level 3 and because of the perception that Level 3 items are more risky. One respondent indicated this pressure could lead to inconsistent application of the hierarchy for the same assets (ie one entity classifying an asset as Level 2 another entity classifying the same asset within Level 3 of the hierarchy).

208. A few respondents said that Level 3 measurement based on discounted cash flows could be more reliable than a Level 2 measurement based on market multiples.

209. A few respondents recommended that the Board consider renaming the levels to remove the perception that Level 1 and Level 2 are more relevant than Level 3 (for example using terminology such as ‘listed and active’ and ‘unlisted and/ or inactive’).

Interim disclosures

210. A few respondents stated that the requirement in IAS 34 *Interim Financial Reporting* for full fair value disclosures for financial instruments in interim reports is burdensome and challenging. These respondents included standard-setters, users, valuation specialists, a professional accounting body, a preparer and a user. The Canadian Bankers Association commented:

> The fair value disclosures are point-in-time disclosures, which may not be representative of the entire reporting period. Further, from quarter to quarter, we generally do not see significant changes in our fair value disclosures and they are not an area of focus for our financial statement users, including investors and analysts. The fair value disclosures are costly to prepare and voluminous.

Blockage factors

211. A few respondents, preparers in financial service industry, asked the Board to reconsider reflecting premiums or discounts that reflect size of holding in the fair value measurement, which is currently prohibited. Those respondents said they disagreed with this ‘blockage’ factor being considered like a transaction cost.

212. A regulator said it observes diversity in practice today in distinguishing between blockage factors (not included in fair value measurement) and liquidity discounts (included in fair value measurement) for Level 2 and 3 instruments and asked the Board to clarify the distinction.

Valuation adjustments

213. A few respondents indicated that there is diversity in the use of valuation adjustments when measuring fair value of financial instruments. These respondents included standard-setters and regulators.

214. The respondents recommend that the Board should monitor developments in practice for valuation adjustments. Some respondents stated that this is not an area for the Board to produce guidance on but that Board should work with relevant valuation bodies to help develop specific guidance and ensure consistency is improved.

When transaction price does not equal fair value

215. A few respondents, including a professional accounting body, a regulator and an auditor, indicated issues with the application of guidance in para B5.1.2A of IFRS 13 on assessing whether transaction price differs from fair value and with accounting for any difference between transaction price and fair value for financial instruments at initial recognition, specifically:

(a) a requirement to recognise only some day 1 gains and losses in profit or loss diverges from US GAAP, which requires all day 1 gains and losses to be recognised in P&L; and

(b) inappropriate recognition of day 1 gains or losses in profit or loss. European Banking Authority commented 'pervasive and material issue in the banking industry and can mislead users' and explained two causes of this:

> Dealers using paragraph B4(d) to refer to a 'dealer market' but where there is no active dealer market and where it is optimistic to assume that another dealer would not price the transaction like a 'retail' customer.
>
> Other valuation adjustments (XVAs) are generally calculated at a portfolio level and we have seen practice of banks determining that they are therefore not an unobservable input …. This exploits exception B4(c): unit of account for the transaction price is not the same as the unit of account for fair value, in a way which we believe is against the spirit of IFRS 13.

(c) illustrative example 7 in IFRS 13 can be misleading. KPMG commented:

> …by stating that the transaction price (an entry price) of zero represents the fair value (an exit price) of the swap to Entity A, Example 7 seems to suggest that it is appropriate to mark to the opposite side of the bid-ask spread (i.e. a long position at ask, a short position at bid) than that explicitly permitted by IFRS 13.70 and to regard the whole of the bid-ask spread as a transaction cost that would be incurred on exiting the position.

Other topics

Net asset value

216. A few respondents asked the Board to introduce a practical expedient to allow the application of net asset value (NAV)[19]. The respondents indicated that since this is an area of divergence between IFRS 13 and US GAAP, the same instruments are valued using different techniques and this decreases comparability.

Tax considerations

217. KPMG said it was not clear how a market perspective should factor in tax considerations and suggested that additional guidance is provided on this issue.

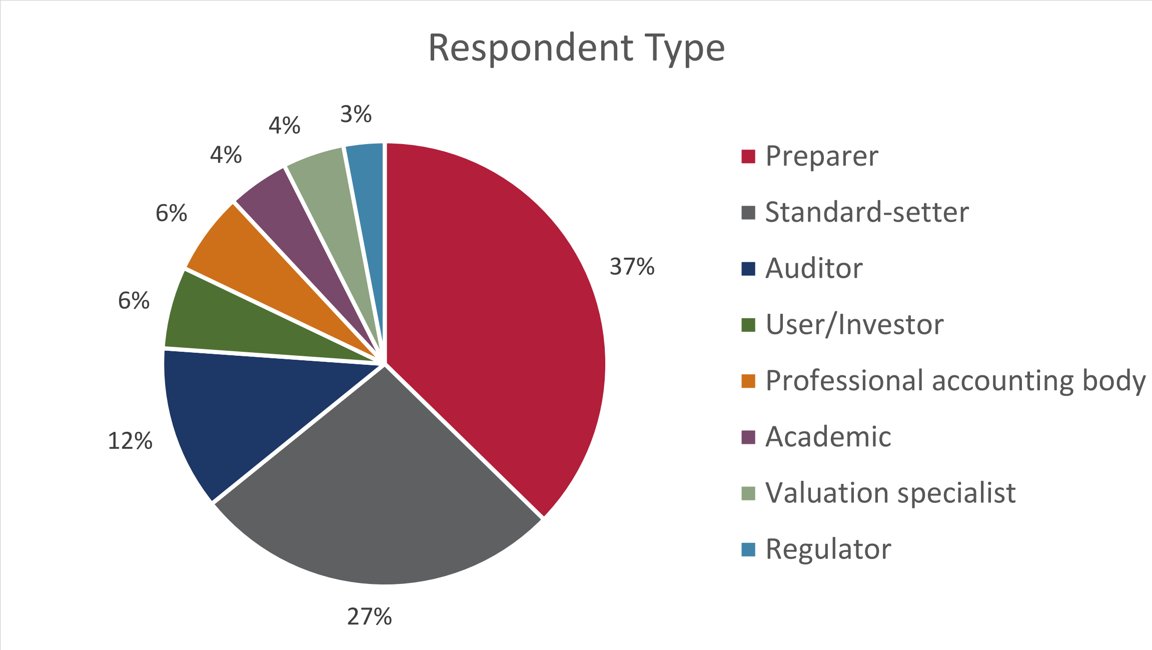
How to measure fair value of liabilities

218. The Norwegian standard-setter said there is a lack of guidance on measuring the fair value of liabilities. They provided examples of questions that sometimes arise, including reflecting tax amortisation benefit and adjusting for risk.

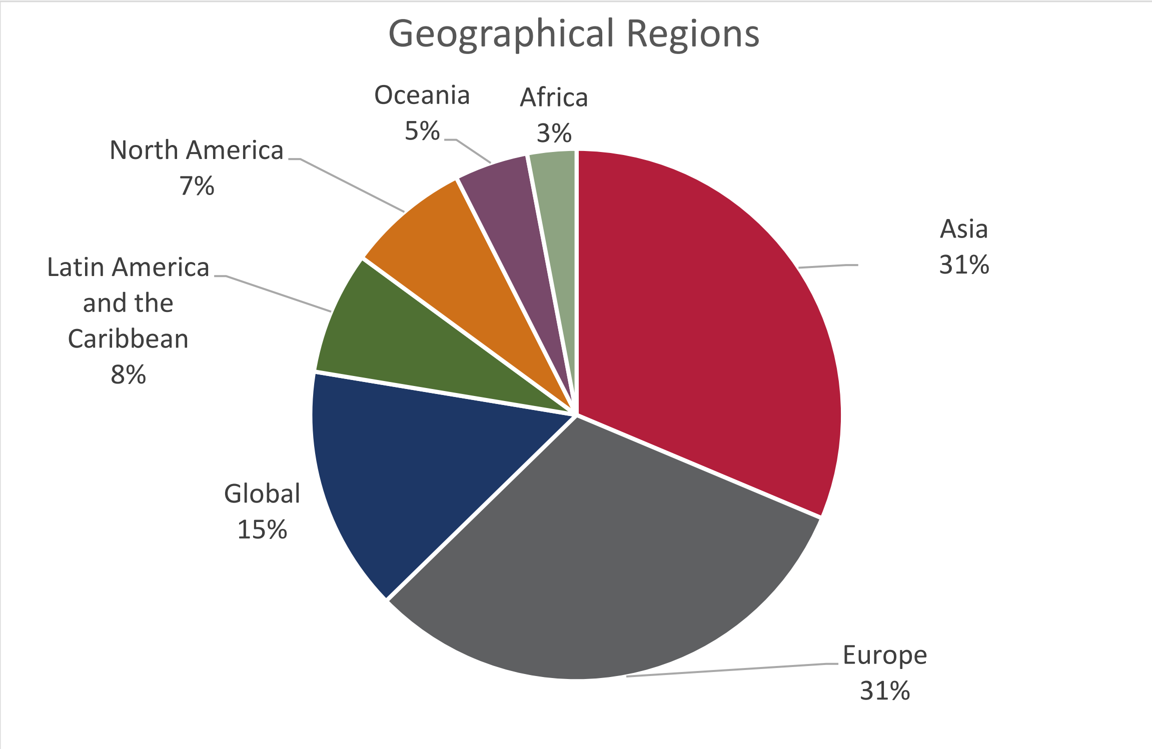
[19] Topic 820 in US GAAP provides a practical expedient that permits an entity with an investment in an investment company to use as a measure of fair value in specific circumstances the reported net asset value without adjustment. IFRS 13 does not provide this expedient.

Appendix A—Overview of the comment letter respondents and outreach conducted

A1. This chart demonstrates which types of respondents provided their feedback through comment letters:



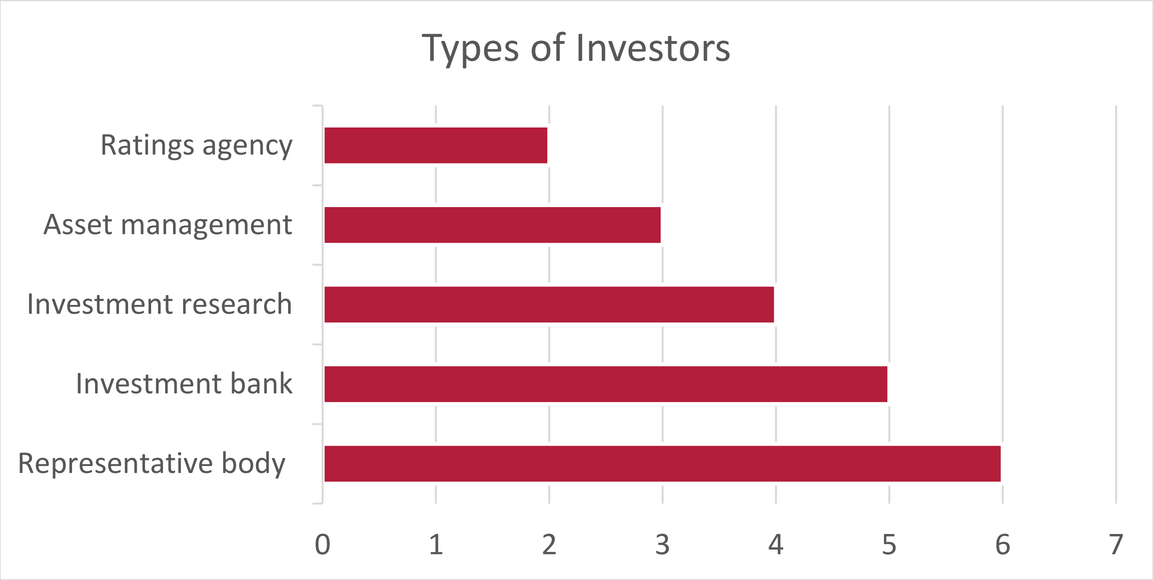
A2. This chart demonstrates geographical regions of respondents who provided feedback through comment letters:



A3. Of the total of 67, 17 respondents (one regulator and 16 standard-setters) carried out outreach in their jurisdictions. The type of research completed by the respondents include organisational committee meetings, outreach meetings, surveys and literature reviews.

A4. The various types of research that respondents undertook included users. For instance, many respondents held meetings of internal committees that included a user member. Some respondents also held outreach meetings with users to obtain their feedback. One respondent issued a user survey and submitted the results in the comment letter.

A5. Staff held 15 meetings with 20 investor organisations and representative bodies. The chart demonstrates the types of investors that the staff met with during phase 2 of the RFI:



A6. In these outreach meetings held with investor organisations and representative bodies the staff prepared slides with examples of disclosures to focus the discussion on the usefulness of Level 3 fair value measurement disclosures. The fair value measurement disclosures included examples of disclosures about financial instruments and about investment property.[20]

[20] An example of the material used for the meetings can be found at: http://www.ifrs.org/-/media/feature/meetings/2017/october/cmac/ap5a-appendices-fair-value-measurement-pir.pdf