RSM

RSM International Limited
50 Cannon St
London
EC4N 6JJ
UK

T +44 (0)207 6011080

www.rsm.global

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom
Email: commentletters@ifrs.org

22 September 2017

Re: Request for Information – Post-implementation Review IFRS 13 *Fair Value Measurement*

Dear Mr Hoogervorst

On behalf of RSM International Limited, a worldwide network of independent audit, tax and consulting firms, we are pleased to comment on the IASB's Request for Information *Post-implementation Review IFRS 13 Fair Value Measurement* ('the RFI').

Our comments and detailed responses to the questions set out in the RFI are detailed hereafter.

We would be pleased to respond to any questions the Board or its staff may have about any of our comments.

Please do not hesitate to contact me or Joelle Moughanni at +44 207 601 1080.

Sincerely,

Robert Dohrer
Global Leader - Quality and Risk
RSM International

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<u>Question 1A—Your background</u>
Please tell us:

(a) your principal role in relation to fair value measurement. For example, are you a preparer of financial statements, an auditor, a valuation specialist, a user of financial statements, a regulator, a standard-setter, an academic, or a professional accounting body? If you are a user of financial statements, what kind of user are you (for example, buy-side analyst, sell-side analyst, credit rating analyst, creditor/lender, asset or portfolio manager)?

(b) your principal jurisdiction and industry. If you are a user of financial statements, which geographical regions and industries do you follow or invest in?

We are a worldwide network of independent audit, tax and consulting firms. The information in this comment letter is a consensus reflecting the experience of member firms from around the world – in jurisdictions where IFRS Standards have been adopted or allowed - in relation to measuring fair value, in their capacity as auditors mostly (in a few cases as valuation specialists or providers of accounting assistance) of a large range of clients operating in various industries.

<u>Question 1B—Your experience</u>
How extensive is your experience in relation to the measurement of the following items at fair value (including the measurement of their recoverable amount on the basis of fair value less costs of disposal)?

Type of item	The extent of your experience with fair value measurements		
	Little	Some	Much
Property, plant and equipment			X
Intangible assets including goodwill			X
Investment properties			X
Biological assets		X	
Investments in subsidiaries, joint ventures or associates			X
Financial instruments		X	

<u>Question 2—Fair value measurement disclosures</u>

(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 disclosure 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 require entities to disclose? 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.

Overall, the principle of providing information about Level 3 fair value measurements is perceived as useful. However, it appears that information provided in practice is most often generic and aggregated, thus not providing sufficient information on the nature and impact of unobservable inputs, and on the reasons why preparers consider them unobservable.

Aggregation and generic disclosure limit the usefulness of the resulting information in that disclosures are often boilerplate and not entity-specific (eg on sensitivity analysis of inputs). Sometimes, it is unclear and almost impossible to understand what inputs were used, or to which extent observable inputs were used in priority to unobservable inputs. Therefore, we recommend that additional disclosures are included to assist users in better

understanding the Level 3 fair value measurements. These may include why the entity chose a particular valuation technique, the basis supporting the more subjective inputs and assumptions adopted, the significant risk factors that could impact the measurement, the name and accreditation details of the entity's valuation expert, etc.

While we would also recommend more guidance/examples on determining which types of assets and liabilities can be aggregated for disclosure purposes, and additional examples (to the existing ones in paragraph B36 of IFRS 13) on key assumptions or inputs that should be disclosed, other disclosures have been identified as excessive and unnecessary, such as the detailed reconciliation from the opening balances to the closing balances required under paragraph 93(e) of IFRS 13 - the cost of preparing the reconciliation can often be high, whereas it does not provide information that is useful to either management or users.
Also, the disclosures required by paragraph 93(h) prove to be (amongst) the most costly to prepare. For many, the disclosure requirement of a quantitative sensitivity analysis for financial instruments is considered one of the most costly, in particular where it involves complex financial modelling.

Question 3—Prioritising Level 1 inputs or the unit of account

(a) Please share your experience to help us assess:
- **(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 in this area in the past (see Appendix 3). Is there anything else relating to this area that you think the Board should consider?

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).

Many users, auditors and valuation experts are by far in favour of measuring the investment as a whole instead of on the basis of PxQ. From a control, joint control or significant influence perspective (ie not a mere financial investment), the quoted price of a share (ie P) does not always reflect its real value. For example, P may not reflect the liquidity of the market for the shares, or P may be affected by a recent transaction (eg major acquisition or disposal).

In our submission to the 2014 Exposure Draft ('the ED'), we agreed with the Board's conclusion that the unit of account of investments in subsidiaries, joint ventures and associates within the scope of IFRS 10, IAS 27 and IAS 28 respectively is the investment as a whole, and not the individual financial instruments that make up the investment. However, we disagreed with the proposal that the fair value measurement of quoted investments in subsidiaries, joint ventures and associates should be PxQ without adjustments as, in our opinion, the proposal contradicts the Board's conclusion.

In addition, this is consistent with neither initial recognition of such investments (ie the investment as a whole), nor Levels 2 or 3 fair value measurement (PxQ being proposed only for Level 1).
In particular, the proposals do not appear to be in line with the guidance in paragraph B45 of IFRS 3, which acknowledges that market participants would take into account a control premium in the per-share fair value of the acquirer's interest in the acquiree (or a non-control discount in the per-share fair value of the non-controlling interest).

In the absence of a Level 1 input for the investment as a whole (being the unit of account), we reiterate the view that the investment's fair value should be measured using a valuation technique, or by adjusting the Level 1 price to reflect differences between the investment and the underlying individual financial instruments. In fact, the asset measured at fair value is the whole investment and not a group or a position made up of a number of financial instruments.

The ED proposals would result in information that may not be the most relevant in that it ignores market price adjustments that take into account the nature of the investment as a whole. The price paid for an investment at acquisition includes premiums or discounts and consequently differs from the mathematical product P×Q, resulting in day two gains or losses (assuming that the day one transaction price is the fair value according to paragraph 58 of IFRS 13 and the day two carrying amount is measured according to the mathematical product P×Q). Alternatively, a day one gain or loss would need to be recognised if the acquisition was measured at P×Q on acquisition date. In such cases, the mathematical product P×Q may not represent fair value for the investment as a whole. The resulting financial information lacks relevance and does not represent the substance of the transaction because of the recognition of a day one or day two gain or loss irrespective of the existence of underlying economic reasons that led to the payment of a premium.

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.

Not only is the assessment of an asset's highest and best use challenging, but also the application of the concept of highest and best use in itself often raises practical issues when measuring fair value of non-financial assets. Other than property (where 'open market value' generally represents highest and best use) there are likely to be no observable inputs, and entities find it difficult to generate unobservable inputs, for a use other than the current one.

Highest and best use can be difficult for land and property, in terms of determining the use by market participants that would maximise the value in some circumstances. This is because market participants can be broad (eg an 'out-of-town' prime retail site could be of interest to a lessor, a housing developer, retail competitors, etc.) and there may not be more activity for one particular participant.

Difficulties might be more significant in specific jurisdictions. For example, in China the assessment of the highest and best use for a land-use-right is quite challenging from a physically possible, legally permissible and financially feasible perspective. This is primarily due to uncertainty over government policy about land-use-rights and the difficulties of obtaining finance for development.

In a few cases, application of the highest and best use concept and the valuation premise might produce counter-intuitive results, in particular where a residual valuation method is used. For example, where the redevelopment value of land is higher than its current use, a building situated on that land may be determined to have no value.

There appears to be diversity in practice in the application of the highest and best use concept and how much work is done by preparers in making the assessment.

<u>Question 5—Applying judgements required for fair value measurements</u>

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 an asset or a 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.

Our understanding is that assessing whether a market for an asset or a liability is active is challenging in particular in emerging and unstable economies. There is limited guidance available in IFRS 13 to assist with determining whether there is sufficient frequency and volume of transactions to provide pricing information on an ongoing basis.

Assessing whether an input is unobservable and significant to the entire measurement also comes with its practical challenges. For example, independent professional valuers might be reluctant to provide evidence on the use of observable data. Another example is where an entity uses its own interest rates (set by its Asset-Liability Committee) as inputs into fair value measurement of loans which correspond to the range of publicly available market interest rates: should they be considered as observable?

<u>Question 6A—Education on measuring biological assets at fair value</u>

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?

Almost all aspects of the measurement of the fair value of biological assets are challenging – even, in some cases, establishing physical quantities (eg for growing produce). Allowing bearer plants to be measured at cost less depreciation has helped, but that has been largely negated by the need to measure growing produce at fair value. For some crops for example, such as sugar cane and sisal, there is now a challenge in distinguishing the bearer plant from the growing produce – essentially the plant is just the root, and everything above the ground is growing produce – but how does one decide what costs should be capitalised as growing the root separately from growing the produce? Another example is forestry (the trees are not bearer plants) which presents challenges due to the long period to maturity: the valuation then becomes very sensitive to the discount rate applied. Also, separating the value of a biological asset from land to which the asset is physically attached can be challenging.

As this is a relatively new area, we currently see divergence in practice, but expected to decline as generally accepted approaches are being developed by valuation experts. However, more guidance in IFRS 13 on measuring the fair value of growing produce would be helpful.

<u>Question 6B—Education on measuring unquoted equity instruments at fair value</u>

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

We have no comments.

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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.

Generally, we do not believe IFRS 13 has enhanced users' ability to assess future cash flows, and our view is that assessment of future cash flows is not and should not be an objective of financial statements; otherwise, management should be required to disclose their own projections of future cash flows.

IFRS 13 did not fundamentally change the way fair values were measured, but did add disclosure requirements. In this respect, it has improved comparability between different entities, as well as between different reporting periods for an individual entity.

The main effect on compliance costs has been the increased disclosure requirements in IFRS 13, particularly in respect of Level 3 valuations, but in our experience the increased costs have not been unreasonably significant.

Although we are supportive of maintaining convergence with US GAAP, it should never be to the detriment of understandable and principles-based IFRS Standards. In the particular case of fair value measurements, valuation experts consider it to be critical to maintain such convergence.

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.

We have no further comments.

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