IFRS 13: Fair Value Measurement Disclosure Challenges

Extract, IFRS Discussion Group Report on Meeting – June 13, 2013

IFRS 13 *Fair Value Measurement* requires disclosure of information that helps users of financial statements assess the following:

- For assets and liabilities measured at fair value on a recurring and non-recurring basis in the statement of financial position after initial recognition, the valuation techniques and inputs used to develop those measurements.
- For fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period.

The illustrative examples that accompany IFRS 13 include five examples to illustrate these disclosures (Examples 15-19 in paragraphs IE 60-IE66).

IAS 34 *Interim Financial Reporting* was amended as a consequence of issuing IFRS 13 to require additional disclosures about fair value of financial instruments in interim financial statements. Paragraph 16A(j) of IAS 34 requires entities to make in the interim financial statements the majority of the disclosure requirements about the fair value of financial instruments that will be required in their 2013 annual financial statements.

Paragraph 16A in IAS 34 states, in part:

> "In addition to disclosing significant events and transactions in accordance with paragraphs 15–15C, an entity shall include the following information in the notes to its interim financial statements, if not disclosed elsewhere in the interim financial report. The information shall normally be reported on a financial year-to-date basis.
>
> (a) …
>
> (j) for financial instruments, the disclosures about fair value required by paragraphs 91–93(h), 94–96, 98 and 99 of IFRS 13 Fair Value Measurement and paragraphs 25, 26 and 28–30 of IFRS 7 Financial Instruments: Disclosures."

Although these disclosure requirements for interim financial statements relate only to financial instruments, fair value disclosures related to non-financial assets and liabilities may be necessary in interim financial statements in some limited circumstances when required under paragraph 15 of IAS 34.

The Group considered the major changes to fair value financial instruments disclosures for interim periods beginning on or after January 1, 2013.

The Group's Discussion

Group members noted that the new requirements are a relatively long list of disclosures. Most of these disclosures fit into four categories:

- overarching disclosure objectives (paragraphs 91, 92 and 94 of IFRS 13);
- financial assets and financial liabilities measured at fair value (paragraphs 93 and 98 of IFRS 13);
- fair value measurements categorized within Level 3 of the fair value hierarchy for financial assets and financial liabilities (paragraph 93 of IFRS 13);
- financial instruments not measured at fair value but for which fair value is disclosed (paragraphs 25, 26 and 28-30 of IFRS 7).

Group members observed that one of the most challenging aspects of the new disclosures required for Level 3 fair value measurements relate to the quantitative information about significant unobservable inputs.

Although IFRS 13 does not provide specific guidance on what information is required, example 17 in paragraph IE63 of the illustrative examples for IFRS 13 may be helpful. The additional disclosure requirements for Level 3 measurements include:

(a) For recurring fair value measurements (paragraph 93(h)(i) of IFRS 13):

  - a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in the inputs would result in significantly higher or lower fair value measurements; and
  - a description of the interrelationships between unobservable inputs and how the interrelationship affects the sensitivity analysis.

(b) Quantitative information about the significant unobservable inputs used in the fair value measurement, unless the inputs were not developed by the entity. However, an entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the entity (paragraph 93(d) of IFRS 13).

(c) A reconciliation of movements in fair value of opening to closing balances for recurring fair value measurements (paragraph 93(e) of IFRS 13). Reconciling items are required for:

  - amounts in profit or loss (and the line item in which they are recognized);
  - amounts in other comprehensive income;
  - amounts of purchases, sales, issues and settlements (separately by type); and
  - amounts of transfers in or out of Level 3, including the reasons for the transfers and the entity's policy for determining when the transfers are deemed to have occurred).

(d) For fair value measurements categorized within Level 3 of the fair value hierarchy, a description of the valuation processes used by the entity for both recurring and non-recurring fair value measurements (Paragraph 93(g) of IFRS 13). Paragraph IE65 of the illustrative examples for IFRS 13 indicates an entity might disclose the following to comply with paragraph 93(g):

- for the group within the entity that decides the entity's valuation policies and procedures:
    - its description;
    - to whom the group reports; and
    - the internal reporting procedures in place;
- the frequency and methods used for calibration, back testing and other testing procedures of pricing models;
- the process for analyzing changes in fair value measurements from period to period;
- how the entity-determined third party information used in the fair value measurement was developed in accordance with IFRSs; and
- the methods used to develop and substantiate the unobservable inputs used in a fair value measurement.

A description of the valuation processes used and whether there has been any change to the process for fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy (paragraph 93(d) of IFRS 13).

Group members observed that this relatively long list represents only one of the four categories of new disclosures noted above. The above list of disclosures would be longer if it included all of the new interim financial statement disclosures that paragraph 16A(j) in IAS 34 requires.

Cameron McInnis, Chief Accountant of the Ontario Securities Commission, noted that entities should remember when looking at a long list of disclosure requirements to avoid a checklist mentality. Entities should consider materiality and provide thoughtful, informative disclosures that are useful to investors.

The Group did not recommend any further action be taken.