AcSB
Accounting Standards Board

COVID-19 Resource

Fair Value Measurement

What you need to know (April 2020)

What's the issue?

1. COVID-19 began as a health crisis but has expanded into a global economic event, creating a profound degree of uncertainty and volatility in financial markets. This unprecedented situation is evolving rapidly and market-based measures, like fair value, are likely to change significantly and perhaps in unpredictable ways.

2. IFRS 13 *Fair Value Measurement* applies when another IFRS® Standard requires or permits fair value measurements or disclosures about fair value measurements. Market volatility and uncertainty can affect the determination of fair value either directly, using observable market prices, or indirectly, using market inputs in valuation techniques.

How will the uncertainty and volatility in financial markets impact the fair value measurement of my assets and liabilities?

3. COVID-19 is having an unprecedented impact on financial markets globally, across all industries and sectors. Companies need to immediately take a fresh look at the decisions, assumptions and inputs they use to measure the fair values of assets and liabilities to ensure that fair value measurements accurately reflect current market conditions. Companies also need to revisit these decisions, assumptions and inputs at each interim and annual reporting date as new or different information becomes available. This process may require a considerable amount of professional judgment, using information that may change significantly from one measurement date to the next, and strong controls to ensure that any estimates are updated with late information that was known or knowable at the measurement date.

4. Companies should begin by confirming an asset's or liability's principal market (i.e., the one with the greatest volume and level of activity, and determine fair value using the assumptions that market participants would use when pricing the asset or liability. In the absence of a principal market, the most advantageous market may be used. (IFRS 13.16)

5. Some companies with non-financial assets, such as investment property, may need to revisit their decisions made regarding an asset's highest and best use. They should do this according to a market participant's ability to generate economic benefits in the current environment, regardless of the asset's current or intended use. (IFRS 13.27)

6. Companies may need to reassess valuation techniques if they rely on information that is no longer available, such as when markets become inactive, or if current market conditions indicate that a different technique would maximize the use of observable inputs versus unobservable inputs. (IFRS 13.61). If a company determines that a current valuation technique for a particular asset or liability is no longer appropriate under the current circumstances, the valuation technique should be changed. Such a change is treated as a change in estimate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. (IFRS 13.66)

7. Many companies use a discounted cash flow model to determine fair value. The discount rate used includes several market inputs, including a risk-free rate and cost of debt. The discount rate also needs to be commensurate with the risks inherent in the expected cash flows, all of which is likely to change as a result of the current environment.

How do I determine if there is still an active market for an asset or liability and what do I do if it becomes inactive?

8. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. A quoted price in an active market provides the most reliable evidence of fair value and if one is available then it must be used to measure fair value. Companies may not use hindsight or adjust for what may be viewed as depressed pricing at the measurement date due to volatility in market prices. (IFRS 13.77, 79). Quoted, unadjusted prices from active markets are considered Level 1 inputs in the fair value hierarchy.

9. The fair value of an asset or a liability might be affected when there has been a significant decrease in the volume or level of activity for that asset or liability in relation to normal market activity for the asset or liability. Companies must use judgment to determine whether, based on current market conditions, there has been a significant decrease in the volume or level of activity for the asset or liability.

10. If there has been a significant decrease in the volume or level of activity for the asset or liability, it may still be possible to determine what is observable in the marketplace and weigh it accordingly. The objective is to determine the point within the range that most represents fair value under current market conditions. A wide range of fair value measurements may indicate that further analysis is needed. Prices other than unadjusted quoted prices that are, instead, derived from observable market activity, are considered Level 2 inputs. (IFRS 13.81-82)

11. Finally, unobservable inputs may be used in valuations but may require significant adjustment to reflect the risks and uncertain market conditions at the measurement date. (IFRS 13.86). Companies should be mindful that all adjustments to inputs are known or knowable at the measurement date. Unobservable inputs, such as cash flow forecasts developed using a company's own data, are Level 3 inputs.

How will this affect my fair value hierarchy and financial statement disclosures?

12. Once companies have concluded on the level of each of the inputs used in determining fair value, they should consider how significant each input is to the entire measurement of the asset or liability. Fair value measurements must be categorized as the lowest level input that is significant to the entire measurement of an asset or liability. (IFRS 13.73). Accordingly, instruments may need to be reclassified and the number of instruments classified as Level 3 might increase.

13. On both an interim and annual basis, a change in fair value measurement affects the disclosures required by IFRS 13, of the valuation techniques and the inputs used in the fair value measurement of assets and liabilities, as well as the sensitivity of the valuation to changes in assumptions. It might also affect the sensitivity analysis required for recurring fair value measurements categorized within Level 3 of the fair value hierarchy. (IFRS 13.93(e)(iv), (h), IAS 1.125, 129, IAS 34.15, 16A(j))

Has the IFRS® Discussion Group talked about this topic?

14. The Group has had several conversations on fair value measurement. The discussions listed below may be helpful as you think about how COVID-19 could affect the measurement of your assets and liabilities at fair value:

Meeting Date	Topic	Meeting Report
June 21, 2018	Cannabis Accounting – Recognition and Determining Fair Value	View Document
May 31, 2016	Definition of an Active Market	View Document
December 9, 2014	Subsequent Measurement of Fair Value	View Document
December 9, 2014	Fair Value Measurement of Government Loans	View Document
September 5, 2013	Fair Value Measurement Unit of Account	View Document
June 13, 2013	Interplay between Fair Value Measurement and Impairment	View Document
June 13, 2013	Fair Value Measurement Disclosure Challenges	View Document
January 11, 2013	Disclosures in Interim Financial Statements	View Document

What other resources are available?

15. Do you need more information? The following publication may provide more insight:

PwC, Podcast, "COVID-19: Fair value questions, answered," March 26, 2020.

Extracts from Relevant IFRS® Standards

Standard	IFRS Guidance
IAS 1	125 An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of: (a) their nature, and (b) their carrying amount as at the end of the reporting period. 129 An entity presents the disclosures in paragraph 125 in a manner that helps users of financial statements to understand the judgements that management makes about the future and about other sources of estimation uncertainty. The nature and extent of the information provided vary according to the nature of the assumption and other circumstances. Examples of the types of disclosures an entity makes are: (a) the nature of the assumption or other estimation uncertainty; (b) the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity; (c) the expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected; and (d) an explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.
IAS 34	15 An entity shall include in its interim financial report an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period. Information disclosed in relation to those events and transactions shall update the relevant information presented in the most recent annual financial report. 16A 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 or elsewhere in the interim financial report. The following disclosures shall be given either in the interim financial

Standard	IFRS Guidance
	statements or incorporated by cross-reference from the interim financial statements to some other statement (such as management commentary or risk report) that is available to users of the financial statements on the same terms as the interim financial statements and at the same time. If users of the financial statements do not have access to the information incorporated by cross-reference on the same terms and at the same time, the interim financial report is incomplete. The information shall normally be reported on a financial year-to-date basis. (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*.
IFRS 13	16 A fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place either: (a) in the principal market for the asset or liability; or (b) in the absence of a principal market, in the most advantageous market for the asset or liability. 27 A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use. 61 An entity shall use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. 66 Revisions resulting from a change in the valuation technique or its application shall be accounted for as a change in accounting estimate in accordance with IAS 8. However, the disclosures in IAS 8 for a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application. 73 In some cases, the inputs used to measure the fair value of an asset or a liability might be categorised within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorised in its entirety in the

Standard	IFRS Guidance
	same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgement, taking into account factors specific to the asset or liability. Adjustments to arrive at measurements based on fair value, such as costs to sell when measuring fair value less costs to sell, shall not be taken into account when determining the level of the fair value hierarchy within which a fair value measurement is categorised. 77 A quoted price in an active market provides the most reliable evidence of fair value and shall be used without adjustment to measure fair value whenever available, except as specified in paragraph 79. 79 An entity shall not make an adjustment to a Level 1 input except in the following circumstances: (a) when an entity holds a large number of similar (but not identical) assets or liabilities (eg debt securities) that are measured at fair value and a quoted price in an active market is available but not readily accessible for each of those assets or liabilities individually (ie given the large number of similar assets or liabilities held by the entity, it would be difficult to obtain pricing information for each individual asset or liability at the measurement date). In that case, as a practical expedient, an entity may measure fair value using an alternative pricing method that does not rely exclusively on quoted prices (eg matrix pricing). However, the use of an alternative pricing method results in a fair value measurement categorised within a lower level of the fair value hierarchy. (b) when a quoted price in an active market does not represent fair value at the measurement date. That might be the case if, for example, significant events (such as transactions in a principal-to-principal market, trades in a brokered market or announcements) take place after the close of a market but before the measurement date. An entity shall establish and consistently apply a policy for identifying those events that might affect fair value measurements. However, if the quoted price is adjusted for new information, the adjustment results in a fair value measurement categorised within a lower level of the fair value hierarchy. (c) when measuring the fair value of a liability or an entity's own equity instrument using the quoted price for the identical item traded as an asset

Standard	IFRS Guidance
	in an active market and that price needs to be adjusted for factors specific to the item or the asset (see paragraph 39). If no adjustment to the quoted price of the asset is required, the result is a fair value measurement categorised within Level 1 of the fair value hierarchy. However, any adjustment to the quoted price of the asset results in a fair value measurement categorised within a lower level of the fair value hierarchy. 81 Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. 82 If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Level 2 inputs include the following: (a) quoted prices for similar assets or liabilities in active markets. (b) quoted prices for identical or similar assets or liabilities in markets that are not active. (c) inputs other than quoted prices that are observable for the asset or liability, for example: (i) interest rates and yield curves observable at commonly quoted intervals; (ii) implied volatilities; and (iii) credit spreads. (d) *market-corroborated inputs*. 86 Level 3 inputs are unobservable inputs for the asset or liability. 93 To meet the objectives in paragraph 91, an entity shall disclose, at a minimum, the following information for each class of assets and liabilities (see paragraph 94 for information on determining appropriate classes of assets and liabilities) measured at fair value (including measurements based on fair value within the scope of this IFRS) in the statement of financial position after initial recognition: (e) for recurring fair value measurements categorised within Level 3 of the fair value hierarchy, a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:

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	(iv) 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 are deemed to have occurred (see paragraph 95). Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3. (h) for recurring fair value measurements categorised within Level 3 of the fair value hierarchy: (i) for all such measurements, a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement. If there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, an entity shall also provide a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement. To comply with that disclosure requirement, the narrative description of the sensitivity to changes in unobservable inputs shall include, at a minimum, the unobservable inputs disclosed when complying with (d). (ii) for financial assets and financial liabilities, if changing one or more of the unobservable inputs to reflect reasonably possible alternative assumptions would change fair value significantly, an entity shall state that fact and disclose the effect of those changes. The entity shall disclose how the effect of a change to reflect a reasonably possible alternative assumption was calculated. For that purpose, significance shall be judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised in other comprehensive income, total equity