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Chairman

Mr Hans Hoogervorst

Chairman – IASB

30 Cannon Street

London EC4M 6XH

United Kingdom

PDC N° 76

Post-Implementation Review – IFRS 13 *Fair Value Measurement*

Dear Mr Hoogervorst,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned *Post-Implementation Review – IFRS 13 Fair Value Measurement*. This letter sets out the most important comments raised by interested stakeholders involved in ANC's due process. Our Board has reviewed and approved this letter on the 21st of September 2017. Appendix A fully details ANC's comments on the issues raised by the IASB's PIR on IFRS 13 Fair Value.

ANC's comments on the Post-Implementation Review main issues are presented below.

Disclosures

ANC underlines the fact that ANC's comments presented in this letter, as regard disclosure requirements, are a first step towards enhancing financial statements, and should not be considered as a comprehensive review of IFRS 13 disclosure requirements. In ANC's view, IFRS 13 disclosure requirements should be reviewed in details at standard level in the light of the *Better Communication* project. As a consequence, the comments below are only general orientations for the IASB to start considering IFRS 13 disclosure requirements.

- In practice, difficulties to apply materiality principles to level 3 measurements have been identified with varying degrees of importance depending on the industry. ANC believes that an introductory paragraph should be added to IFRS 13 disclosure requirements, providing a clear description of the disclosures' objectives in order for preparers to be able to analyze materiality to apply judgments. IFRS 13 disclosures should be prepared taking into consideration the materiality concept and the preparers' underlying activity and business model in order to provide relevant, useful and entity-specific information.
- IFRS 13 is a conceptual and pervasive standard that need to focus on definitions and general objectives without proposing detailed disclosure requirements. The detailed disclosures and measurement requirements should remain part of the technical standards (IFRS 7, IFRS 3...). In addition, it must be underlined that the existing disclosure requirements in IFRS 13, IFRS 7, IFRS 3... have been developed separately and need, in ANC's view, to be reviewed in the light of the "*Better Communication*" project to avoid excessive disclosure requirements, overlaps or gaps. Therefore, ANC believes that it may be useful to streamline the different requirements in a way that ensure financial statements provide relevant and entity-specific information and to review the specific fair value disclosure requirements standard by standard in order to better articulate the detailed principles to IFRS 13 and IAS 1 requirements.

Prioritising Level 1 inputs or the unit of account

Apart from investments held by investment entities, applying PxQ measurement is rare in practice.

In ANC's view, the value of an asset is highly dependent upon its use and the parties involved. All these contextual elements determine the unit of account used. As general comment, ANC believes that the standard may unduly promote the use of the PxQ measurement method, even in situations where it has proved less relevant than discounted cash flows.

In addition, ANC considers that disclosures according to the strict hierarchy between levels (1, 2 and 3) may not be sufficient. Another approach to provide relevant information on fair value could also be to take into account the "unit of account" used.

Highest and Best use

ANC considers that the concept of highest and best use should be used in a balanced way since it may be highly theoretical and difficult to implement. In practices, its use is limited to specific assets (real estate, brands...) or transactions (business combinations).

ANC also highlights the fact that most preparers express concerns on the relevance of the use of fair value as a measurement basis, as it does not allow to also take into account management's intent on the use of the asset / liability.

Applying judgment

Two main areas of judgment have been identified by ANC's stakeholders. Those areas are (i) assessing whether a market is active, (ii) categorising unobservable and significant inputs used in the fair value measurement.

- *Active markets* – Although entities in the financial sectors appear, 4 years after the first implementation of IFRS 13, not to find challenging the performance of this assessment, preparers agree on the fact that the definition of an active market is theoretical and that application difficulties arise in certain specific market conditions, in emerging countries or during systemic crisis.
- *Unobservable and significant inputs to the entire measurement* – Entities from the non-financial sectors have experienced difficulties to distinguish level 2 and level 3 inputs as the classification is in some instance highly judgmental. It has also been noted that some level 2 approach (such as market approach) provide sometimes less relevant information than present value techniques considered as level 3.

As regard the underlying overall approach of IFRS 13 and from a general standpoint, ANC is of the opinion that the relevance of the use of fair value in certain level 2 measurements and for level 3 measurements should both, at some point of time, be revisited in terms of concept, relevance and practical consequences.

Please do not hesitate to contact us should you want to discuss any aspect of our comment letter.

Yours sincerely,



Patrick de CAMBOURG

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Question 1A—Your background

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?

The Autorité des Normes Comptables (ANC) sets out in this letter the most important comments raised by interested stakeholders involved in ANC's due process. This comment letter has been reviewed and approved by our Board.

ANC stakeholders involved in the preparation of this letter are preparers, audit firms, regulators applying IFRS 13 in France (quoted companies apply IFRS as adopted by the European Union). The main sectors represented in our working group are banks, insurance, industry and services. ANC underlines the fact that limited input has been provided from IFRS fair valuation experts on biological assets since only few entities are listed in that industry.

Question 1B—Your experience

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 & equipment			X
Intangible assets including goodwill			X
Investment properties			X
Biological assets	X		
Investments in subsidiaries, joint ventures or associates			X
Financial Instruments			X
Other (please specify which)	N/A	N/A	N/A

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 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.

The comments presented below have mostly been raised by preparers, auditors and appraisers, and it must be underlined that few inputs have been obtained from users.

Level 3 disclosures usefulness - ANC highlights the fact that classifying elements in the level 3 fair value category mostly applies to the bank, insurance, real estate, private equity, investments entities sectors. Industrial and services sectors have less elements classified in the level 3 fair value category in their financial statements. For these sectors, level 3's inputs are data that are mostly used for non-consolidated investments in unquoted companies, commodities and non-current assets classified as held for sale (IFRS 5.15).

As a general comment, ANC does not question the importance and necessity of giving information about items classified in the level 3's category. However, ANC believes there is no need to develop disclosure requirements that would constrain preparers to present their level 3's information under a specific format or to define additional specific qualitative disclosures.

ANC believes that the level of disclosures already required by IFRS 13 (qualitative and quantitative) is sufficient and this standard should in our view remain conceptual avoiding developing detailed requirements. However, ANC believes that it is necessary to redefine more clearly the disclosure principles of IFRS 13 in the light of the *better communication* project to stress out that an entity shall consider the level of details necessary satisfy this disclosure principle and how much emphasis to place on each of the various requirements so as to ensure that users will be in a position to understand the key judgments made by the entities when measuring items classified in the level 3's category. In addition, IFRS 13 should be better articulated to the fair value disclosure requirements developed in other standards (IFRS 7, IFRS 3, IAS 40...) as well as to the general disclosure objectives developed in IAS 1.

Examples of qualitative information on which more focus could be placed, depending on their materiality and their relevance to the underlying activities may be: objectives of the valuation models used, explanations on the data used in the valuation models, key methods and assumptions used in

preparing sensitivity analysis... justification of the choice of the valuation model (judgements), explanations on the data used in the valuation model... For example, when one or more of the unobservable inputs change to a reasonable possible alternative assumption significantly modifying the fair value, the effect of changes has to be disclosed. The concept of “reasonable change” is judgmental. In the light of the above mentioned objective, entities should define “reasonably possible alternative assumptions” in order to demonstrate the appropriateness of their qualitative disclosure. However, as mentioned above, this should also be assessed in the light of their activities and the general materiality principles.

Level 3 fair value measurement disclosures costly to prepare

ANC’s stakeholders have identified two costly areas when preparing level 3 disclosures:

- ANC’s stakeholders have concerns about the level 3 reconciliation required by IFRS 13.93.e (iii) and (iv). This disclosure is costly to prepare and of limited value for users. ANC thinks that it could be valuable to replace these requirements by qualitative disclosures to explain the changes in the amount and the type of instruments classified in Level 3 (transfers in and out level 3). Such an approach could allow users to have a better understanding of the Level 3 changes without adding undue costs and complexity for preparers.
- As regard IFRS 13 requirements on the information to be disclosed for each class of assets and liabilities not measured at fair value in the statement of financial position but for which the fair value has to be disclosed concerning financial instruments (as specified in IFRS 13.97 and IFRS 7.25), ANC underlines that providing users with the fair value of instruments accounted for at amortized cost (as for instance loans granted to individuals) is inconsistent with the business model of amortised cost and is of limited usefulness to users.

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 $P \times Q$ 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?

Situations where IFRS 13 is applied in ANC’s jurisdiction

ANC stakeholders have noted that situations where quoted investments in joint ventures and associates as well as quoted CGUs are measured at fair value are relatively rare (apart from investments held by

investment entities). Such information results from the fact that, for this situation to arise, the “value in use” has to be simultaneously lower than book value and lower than fair value.

Conversely, fair value measurement is systematically requested for investments held by investment entities, and may be requested in other companies when a change in ownership interests occurs, notably in step acquisitions.

Identified material differences between fair value amounts measure on the basis of P x Q alone and fair value amounts measured using other valuation techniques

Material differences

ANC’s stakeholders have identified material differences between the P x Q measurement method and other valuation techniques.

To illustrate this assertion, it has been evidenced that values obtained by independent experts in the context of public offerings (based on reports publicly disclosed) differ from quoted prices and that values obtained on a stand-alone basis (meaning excluding synergies) through different approaches (DCF, comparable companies or transactions methods) are significantly different from the fair value obtained using quoted price, in particular when the target company has a low free float and a modest liquidity.

For instance, on the 35 public offers that occurred in France in 2016¹, 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. This example illustrates that market prices rarely represent a fair value.

Strategic interests

For companies having strategic interests in other quoted companies, with a long-term view, the PxQ method may not permit in all instances to accurately measure the fair value. It has to be noted that when an investment has a strategic value it may be better represented by other valuation techniques, and notably relying on a DCF approach (a value in use approach). In that respect, the principles used to measure unquoted investments (for which other valuation techniques are used) would be more relevant.

Other differences arise for companies holding significant blocks of shares with a view to selling them. Entities may incur significant discounts when entering into a sale process for a block of shares (discounts observed in the context of accelerating book building are typically in a range of 5 to 10%) or when an entity holds a large position likely to affect market prices with downward pressures if this position were to be sold.

In ANC’s view, using a market price has the advantage to rely on public data but can sometimes result in irrelevant information, whereas adjusted prices in compliance with valuation principles as considered by market participants may be less observable but can give a more relevant information and can more accurately reflect the price at which the asset or liability would be exchanged in an orderly transaction.

¹ Observatoire des offres publiques – 7^{ème} Edition – 2016 – Author : EY/ Ricol Lasteyrie Corporate Finance (in French)

Furthermore, the adjusted price approach is consistent with the concept of prudence. ANC believes that further research is needed on the “unit of account” definition and its use.

As a conclusion, ANC main concerns are as follows:

- There is a need to clarify IFRS 13 principles and the articulation between unit of account and the measurement.
- The standard unduly restricts the use of discounts, which may seem to go against the objective of fairness of the value
- In ANC’s view, the value of an asset is highly dependent upon the use of the asset, the parties involved in the transaction and the context of the transaction. It means that the fair value measured is highly dependent on the overall context and unit of account correlatively used.

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.

The use of the “highest and best use” concept is limited to specific businesses, notably those dealing with real estates, brands, biological assets... In addition, the “highest and best use” concept is also used when performing a purchase price allocation in a Business Combination.

In practice, ANC has noted that most appraisers have difficulties in applying the “highest and best use” principle as the available information supporting the valuation process is in some instances difficult to access and moderately reliable. The difficulty to apply the “highest and best use principle” has notably been identified in the real estate sector. ANC notes that most appraisers consider the concept to be highly theoretical and difficult to implement.

ANC also highlights the fact that some preparers are not convinced of the relevance of the information obtained when applying fair value as a measurement basis (notably when applying IFRS 3 requirements), as the concept of “highest and best use” does not take into consideration of management intent. In such situation, the resulting measurement outcome is in our view counter-intuitive and of limited relevance.

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 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.

Assessing if the market is active under specific facts and circumstances

According to ANC's stakeholders, entities do not find challenging to perform assessment as to whether financial markets are active or not, unless very specific fact and circumstances arise. Banks have notably underlined the fact that, based on their past practice and local accounting principles, internal efficient processes have been developed in their sector to apply judgments for fair value measurements (for instance, it is since 1990 that the definition of an active market has been developed in the French accounting regulation to be applied by banks, such definition being reintroduced since 2005 by the CNC - 2005-01/ 2008-17 / 2014-07 regulations).

The definition of an active market is rather theoretical. Its application may be source of difficulties for non-financial assets (brands, commodities, biological assets...) or under particular circumstances, as for instance in certain specific markets conditions, in emerging countries or when systemic crisis occur.

Assessing whether an input is unobservable and significant to the entire measurement?

Two considerations raised on non-financial instruments measured at fair value are presented below:

- The frontier between level 2 and level 3 inputs is not clear and is in some instances highly judgmental. In addition, the meaning of such classification is not clearly understood by all users in the non-financial sector and some believe level 3 data is less relevant when it is only less observable.
- The link between the input and the asset or liability to be valued is sometimes faint. Values obtained in application of a market approach (prices obtained using market transactions involving identical/ comparable or similar assets, liabilities or group of assets / liabilities) are often classified as level 2 measurements. It must be underlined that this approach to assess the fair value of an asset or liability don't systematically provide relevant information and that the fair value obtained through present value technique (classified as level 3) often proposes better information.

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?

There exist only few listed French entities with biological assets and therefore biological assets are rarely measured at fair value.

However, it has been noticed that, conceptually, the linkage between the fair value of a biological asset and the market value of an agricultural produce is often theoretical: it is highly dependent on the time horizon and the volatility of commodity markets.

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 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.

The document presents a rather extensive synthesis of commonly-used valuation approaches. Due to the limited IASB's resources, ANC believes that it is not the priority for the IASB to develop valuation guidelines and that the IFRS 13 standard needs to remain principles based.

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.

ANC has noted that its stakeholders remain alert to ensure a level playing field for all companies, whatever their place of quotation. In addition, ANC underlines the fact that US GAAP do not measure

the same assets and liabilities at fair value than IFRS and have their own exceptions, leading to different accounting presentation.

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.

The most controversial issue appears to be the fair value hierarchy between level 2 and level 3 items in the non-financial sector. Such dividing line remains unclear and judgmental for those entities. In addition, ANC's stakeholders doubt this hierarchy to be useful to users for the following reasons:

- In some cases unadjusted quoted prices may not be relevant, and it may be misleading to classify such quoted prices as level 1 inputs.
- Furthermore, a quoted price on an inactive market, which is classified as level 2's measurement, is nevertheless generally less reliable than a DCF measurement, which is classified as level 3.

Another key concept that is debatable in the standard is the one of market participant which definition is very theoretical. As already indicated, market participants are all different and it is very difficult to elaborate a normative behaviour of a market participant.

In addition, as regard the underlying overall approach of IFRS 13 and from a general standpoint, ANC is of the opinion that the relevance of the use of fair value in certain level 2 measurements and for level 3 measurements should both, at some point of time, be revisited in terms of concept, relevance and practical consequences.