# Issue Assets − 10: Fair Value Measurement

## Issue

* What are the new disclosures required by the Australian accounting standard AASB 13 Fair Value Measurement?

## Intent

* This Policy Brief aims to complement AASB 13 *Fair Value Measurement* by interpreting elements of the Standard within the Territory context. The interpretation and examples are meant as a guide only and do not replace an entity’s own assessment of its individual circumstances.

## Background

* The Australian accounting standard AASB *13 Fair Value Measurement* sets out a revised definition of fair value based on exit price, as well as the principles to be applied when determining the fair value of assets and liabilities. The Standard prescribes additional disclosure requirements, most significantly concerning the inputs to the valuation techniques used to measure fair value.
* The Standard outlines how to measure fair value, not when to use fair value and what to measure at fair value. It provides a single source of guidance on fair value, which was previously distributed across a number of standards.
* The Standard applies when another Standard requires or permits fair value measurements or disclosures about fair value measurements, and does not expand the application of fair value measurements to any new items. Therefore it applies to land, buildings, infrastructure, plant and equipment, heritage and cultural assets, biological assets, investment property, assets held for sale, intangibles at fair value and financial instruments at fair value. The Standard does not apply to leases and inventory.
* The Standard applies for the first time to the 2013-14 annual reporting period for entities with a 30 June year end.
* The Standard is to be applied prospectively as of the beginning of the annual reporting period in which it is initially applied. Consequently, the disclosure requirements of the Standard need not apply to the comparative prior year period.

## Policy

* The Standard defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Therefore, fair value is not an entity-specific value, but is based on a market participant’s perspective.
* No material impact on the fair value of assets and liabilities is expected in most cases.
* Valuation techniques used to calculate fair value fall into one of the following approaches:
* Market approach – uses prices and other relevant information generated by market transactions involving identical or similar assets or liabilities;
* Income approach – converts future cash flows to a single current discounted amount. This approach will not apply to not-for-profit government entities; and
* Cost approach – reflects the amount that would be required currently to replace the service capacity of an asset (e.g. depreciated replacement cost).
* Inputs to valuation techniques – valuation techniques used to measure fair value shall maximise the use of relevant observable inputs and minimise the use of unobservable inputs. Unobservable inputs are used to the extent that sufficient relevant and reliable observable inputs are not available for similar assets or liabilities.

Observable inputs are publicly available data that are relevant to the characteristics of the assets/liabilities being valued, for example, published sales data for land and general office buildings.

Unobservable inputs are data, assumptions and judgements that are not available publicly, but are relevant to the characteristics of the assets/liabilities being valued. Such inputs include an entity’s internal adjustments to observable data to take account of particular and potentially unique characteristics/functionality of assets/liabilities and assessments of physical condition and remaining useful life.

Inputs are categorised into three levels based on their observability to a market participant:

* Level 1 inputs – are quoted prices (unadjusted) in active markets for identical assets or liabilities;
* 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. These inputs include quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active, and inputs other than quoted prices that are observable, for e.g. interest rates and yield curves at commonly quoted intervals. Adjustments to Level 2 inputs will vary depending on factors specific to the asset or liability, e.g. the condition or location of the asset. Adjustments using unobservable inputs that are significant to the entire fair value measurement may result in the entire fair value measurement being categorised as Level 3; and
* Level 3 inputs – are unobservable inputs for the asset or liability. This is expected to be the case for specialised assets such as hospitals and prisons.
* Determining fair value with reference to values of identical assets would be rare for non‑current physical assets. Therefore it is unlikely that any agency non-current physical assets will have Level 1 fair values.
* Appendix 1 presents a flowchart to assist with determining the level of input used in measuring fair value. Appendix 2 presents the potential valuation techniques and input levels for some common non-financial assets.

## References

AASB 13 Fair Value Measurement

## Appendix 1: Determination of Input Levels Used in Measuring Fair Value

Is there a quoted price in an active market for an identical asset?

**Level 1**

(unlikely for non-current physical assets)

Is there a quoted price in an active market for a similar asset?

Is there other data available from a publically accessible source that can be used to determine fair value?

Is a significant adjustment required, using data that is not publically accessible?

**Level 2**

**Level 3**

Yes

Yes

Yes

Yes

No

No

No

No

## Appendix 2: Valuation Techniques and Input Levels for Non-Financial Assets

| **Asset Class** | **Example** | **Valuation Technique** | **Input Level** |
| --- | --- | --- | --- |
| Land | In areas where there is an active market, and not subject to restrictions as to use or sale | Market approach | Level 2 |
|  | In areas where there is no active market or subject to restrictions as to use or sale | Cost approach | Level 3 |
| Buildings | General office or commercial building  Social/public or employee housing for which there is an active market | Market approach | Level 2 or 3, depending on significance of adjustments using unobservable data |
|  | Specialised building with limited alternative uses and/or substantial customisation, e.g. prisons, hospitals  Social/public or employee housing for which there is no active market | Cost approach | Level 3 |
| Infrastructure | Any type | Cost approach | Level 3 |
| Plant and Equipment | Any type | Cost approach | Level 3 |
| Heritage and Cultural Assets | Item for which there is an active market | Market approach | Level 2 or 3, depending on significance of adjustments using unobservable data |
|  | Item for which there is no active market | Cost approach | Level 3 |
| Intangibles | Only where there is an active market for that intangible and it has a long useful life (otherwise intangible not revalued) | Market approach | Level 2 |