

# IFRS Accounting Standards: measurement overview

Date: 29 May 2023  
Addis Ababa



The views expressed in this presentation are my own and not necessarily those of any organization with which I am associated.

1

## Disclaimer and applicable version of IFRS Accounting Standards

- » The sponsors, the authors, the presenters and the publishers do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this PowerPoint presentation, whether such loss is caused by negligence or otherwise.
- » Unless specified otherwise, the accounting requirements that are the subject matter of this presentation are International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) that are applicable for annual period beginning on or after 1 January 2023 without early applying new and amended IFRS Accounting Standards that have a later mandatory application date.

2

2



## Aim

- » The aim of this session is to enhance knowledge and understanding, in the Ethiopian accountancy market, of the range of measurement specified in IFRS Accounting Standards.
- » *[Note: the session that follows after the coffee break is dedicated to enhancing knowledge and understanding, in the Ethiopian accountancy market, of the range of valuation methodologies specified in IVSC valuation standards.]*
- » *[Note: separate sessions in this 5-day workshop are dedicated to enhancing knowledge and skills in particular IFRS measurements, in the Ethiopian context.]*

3

3



## Aims

- » An understanding of:
  1. what IFRS Accounting Standards aim to provide.
  2. the main IFRS measurements: historical cost and fair value.
  3. the main IFRS measurement models for:
    - » non-financial assets;
    - » non-financial liabilities;
    - » financial instruments.

4

4



## Ethiopian context

5



### Ethiopian context 10-year *Economic development plan (2021-2030)*

- » Government of Ethiopia (GOE) 10-year economic development plan (2021-2030) has agriculture as a top priority sector.
- » Plan envisages building a climate resilient green economy:
  - » fight land degradation;
  - » reduce pollution;
  - » reduce GHG emissions;
  - » increase forest protection and development;
  - » increase production of electricity from renewable sources for domestic use and for export; and
  - » focus on modern and energy saving technologies.

Source: [www.trade.gov/country-commercial-guides/ethiopia-agricultural-sector](http://www.trade.gov/country-commercial-guides/ethiopia-agricultural-sector)

6

6

## Ethiopian context

### Ethiopian exports

The top exports from Ethiopia are [Coffee](#) (\$1.16B), [Gold](#) (\$860M), [Other Oily Seeds](#) (\$337M), [Other Vegetables](#) (\$272M), and [Cut Flowers](#) (\$235M), exporting mostly to [United Arab Emirates](#) (\$1.05B), [United States](#) (\$495M), [Somalia](#) (\$361M), [Saudi Arabia](#) (\$248M), and [Germany](#) (\$248M).  
(source: <https://oec.world/en/profile/country/eth>)

**Table:3 Value of coffee export as share of total export (in billions)**

Item	2016/17	2017/18	2018/19	2019/20	2020/21
Total export value	2.9	2.8	2.7	2.67	3.41
Total value of Agricultural export	2.34	2.38	2.3	1.94	3.16
Agricultural exports share out of total exports (%)	81	85	85	73	93
Coffee exports	0.897	0.767	0.789	0.82	1.1
Coffee exports share of total agricultural exports (%)	38	32	34	42	35
Coffee exports share of total exports (%)	31	27	29	31	32

Source: Post calculation

Source: USDA, Ethiopia: Coffee Annual, 09 2022, p4 see [www.fas.usda.gov/data/ethiopia-coffee-annual-7](http://www.fas.usda.gov/data/ethiopia-coffee-annual-7)

7

7

## Ethiopian context

### Ethiopian coffee market: policies and practices

- » **Observed practice:** in the past coffee traders have **distorted the export market** by exporting coffee at a loss to earn foreign currency that is then used to import construction materials and vehicles to sell in Ethiopia at a huge profit.
- » **Export Coffee Contract Administration directive:** On 28/01/2020 Coffee and Tea Authority coordinate with National Bank of Ethiopia (NBE) to create a mechanism that each day fixes a **minimum coffee export price** based on the global weighted average price given to different grades of coffee from various regions.
  - » If sell below the minimum coffee export price, the Administration and Ministry of Trade take legal action.
- » **NBE recently announced Directive:** in response to critical shortage of foreign currency in Ethiopia:
  - » Max. 20% of coffee exporters export earnings may be retained in USD to fund imports.
  - » Min. 80% of coffee exporters export earnings must be converted to Birr for local use.

Source: USDA, Ethiopia: Coffee Annual, 09 2022, p5-p6 see [www.fas.usda.gov/data/ethiopia-coffee-annual-7](http://www.fas.usda.gov/data/ethiopia-coffee-annual-7)

8

8



## IFRS Accounting Standards: What's the aim?

9



### What do IFRS Accounting Standards aim to provide?

- » IFRS financial statements aim to provide **external resource providers** (existing and prospective) with **inputs** for them to use in making their own assessments of:
  - » the reporting entity's **prospects for future net cash inflows** (amount, timing and uncertainty); and
  - » to hold management to account.
- » To achieve this aim, external resource providers need **relevant** information (that is also complete, neutral and free from error) about the reporting entity's:
  - » **assets** and claims against those assets (**liabilities** and equity);
  - » **income, expenses** and other changes in those resources and claims;
  - » the stewardship of management.

Source: Chapter 1 of the Conceptual Framework

10

10

## Structure of a typical IFRS Accounting Standard that specifies accounting and reporting for an asset or a liability

- » **Scope.** Which items does this IFRS Standard apply to?
- » **Recognition.** Does the item meet the specified recognition criteria?
- » **Measurement. How must the recognized item be measured?**
  - » at initial recognition; and
  - » after initial recognition.
- » **Derecognition.** When must the be derecognised?
- » **Disclosure.** What information must be disclosed about: the recognised item; the unrecognised item; and judgements, estimates, risk management etc?

11

11

## Measurement uncertainty

- » “The **use of reasonable estimates** is an **essential part** of the preparation of financial information and **does not undermine the usefulness** of the information **if the estimates are clearly and accurately described and explained.**”
  - » **Reliability** of a highly uncertain estimate **can be achieved through disclosure**, describing the estimate and explaining the uncertainties.
  - » Except in **extremely rare cases**, by determining a range of possible outcomes a **sufficiently reliable estimate** can be made, for example, to recognise a provision in accordance with IAS 37.
  - » Moreover, IAS 1 specifies **overarching disclosures about key sources of estimation uncertainty.**
  - » **Nonetheless**, many IFRS Accounting Standards specify **reliability of measurement recognition thresholds.**

Sources: paragraphs 2.19 and 2.22 of the Conceptual Framework, paragraphs 125-129 of IAS 1 and paragraph 25 of IAS 37. <sup>12</sup>

12



## IFRS Accounting Standards: initial measurements and subsequent measurement models

13



### Many measurements at initial recognition *Summary of class discussion (not intended to be complete!)*

	Asset	Liability
Historical cost	Most non-financial	
Fair value	Financial. Many non-financial when acquired in business combination, exchanges of non-financial, government grant (alternative).	Financial. Cash-settled share-based payment.
Fair value less costs to sell	Biological assets in agricultural activity. Many non-current asset held for sale.	
Best estimate		Provision
Customer consideration		Contract with customer

15

**Many subsequent measurement models (1 of 3 slides)**  
**Summary of class discussion (not intended to be complete!)**

Item	Measurement model + impairment test, if any
PPE (including bearer plants) & intangible assets	Revaluation model (constrained for intangible assets) or cost model. Recoverable amount impairment testing.
Inventory	Lower of cost and net realizable value (NRV) model. However, miners and farmers NRV model (alternative) and commodity broker-traders fair value model (alternative).
Investment property	Cost model with recoverable amount impairment testing (and fair value disclosed) or fair value model
Biological assets in agricultural activity	Fair value (less costs to sell) model.
Non-current assets held for sale (NCAHFS)	Lower of NCAHFS classification-date carrying amount and fair value less costs to sell.

17

17

**Many subsequent measurement models (2 of 3 slides)**  
**Summary of class discussion (not intended to be complete!)**

Item	Measurement model + impairment test, if any
Goodwill asset	Historical cost. Recoverable amount impairment.
Investment in associate	The equity method. Recoverable amount impairment.
Investment in joint venture	The equity method. Recoverable amount impairment.
Short-term employee benefits	Accrual, no discounting.
Termination benefits	Accrual, discounting unless short-term.
Post-employment benefits	If defined benefit, obligation = PUC method. If funded, fund assets = fair value. If defined contribution, accrual method.
Other long-term employee benefits	Projected unity credit (PUC) method.

18

18



## Many subsequent measurement models (3 of 3 slides) Summary of class discussion (not intended to be complete!)

Item	Measurement model + impairment test, if any
Provision liability	Best estimate model.
Onerous contract liability	Onerousness of the contract model.
Income tax asset/liability	Substantively enacted tax rates without discounting model.
Lease: RoU asset	Cost model or revaluation model (or when underlying RoU is investment property and fair value model is elected).
Lease liability	Amortised cost model.
Financial asset	Amortised cost model (ECL impairment), FVOCI debt instrument model (ECL impairment), FVPL model, and FVOCI equity instrument model.
Financial liability	Amortised cost model or FVPL model.

19

19

## IFRS Accounting Standards' mixed measurement model

Assets	IFRS measure	Equity	IFRS measure
Unimpaired land (PPE) & indefinite life intangibles	Historical cost (HC) or fair value (FV) (choice)	<b>Residual (assets minus liabilities)</b>	<b>What does it mean?</b>
Other PPE, intangibles and bearer plants	Modified (M)HC or modified FV (choice)	<b>Liabilities</b>	<b>IFRS measure</b>
Investment property	MHC or FV (choice)	Bank loan	Amortised cost (AC)
Biological assets	FV less costs to sell (except bearer plants)	Trade payable	AC
Investments in associates	Equity method	Derivatives and others when FV option is used	FV
Other financial instruments	MHC or FV (depends on cash flow characteristics and business model)	Provisions	Amount to settle or transfer today
Inventories	Lower of HC and net realisable value; exceptions FV and NRV	Defined benefit employee benefits	Projected unit credit method
<b>TOTAL</b>	<b>What does it mean?</b>	<b>TOTAL</b>	<b>What does it mean?</b>

20

Fair value  
(much of this 5-day workshop is  
dedicated to fair value measurement)

21

## Fair value of an asset *the concept*

» The fair value of an asset is:

- » the price that would be received to sell an asset (exit price)
- » in an orderly transaction (not a forced sale)
- » between market participants (market-based view)
- » at the measurement date (current price) (see IFRS 13 *Fair Value Measurement*)

» **Market participant perspective:** consequently, the entity's intention to hold an asset is not relevant when measuring fair value.

22

22

## Historical cost

23

### Historical cost 'concept': an asset

- » The historical cost of an asset is the consideration given to acquire or to develop it:
  - » the amount of cash or cash equivalents paid; or
  - » the fair value of the consideration given to acquire it at the time of its development or acquisition.
- » Historical cost includes transactions costs incurred to acquire the asset.

24

24



## Historical cost codified conventions include

- » Historical cost includes all costs directly attributable to bringing an asset to the location and condition necessary for it to be capable of operating as intended by management, including:
  - » transactions costs, non-refundable purchase taxes and professional fees
  - » costs of converting raw material into finished goods (including an allocation of fixed production overheads)
  - » qualifying borrowing costs
  - » obligations incurred for dismantling, removing and restoring the site
  - » cost formula (FIFO or weighted-average) for similar items
- » If payment is deferred beyond normal credit terms the interest is computed and cost is net of that interest.

25

25



## Comparing non-financial asset measurement models

26

## Cost model: non-financial assets

- » After initial measurement the historical cost of an asset may be modified to reflect, when relevant:
  - » the **consumption of its service potential** (called **depreciation** or, if an intangible asset, called amortisation); and
  - » that part of the historical cost of the asset is no longer recoverable because of **impairment** due to, for example
    - » deterioration of the asset quality; or
    - » a decline in its economic value.

27

27

## Revaluation model: non-financial assets *reflecting the economics*

- » In presenting **financial position**, the item's carrying amount must not be materially different from its fair value.
- » In presenting financial performance for a period, the revaluation model separates:
  - » **depreciation**, ie the **consumption** of the assets service potential (measured at current economic value); from
  - » **other price change effects**.

28

28

## Revaluation model: non-financial asset the requirements

- » **Accounting policy choice** by class of PPE and intangible asset.
  - » However, revaluation model is available only for items of PPE whose fair value can be measured reliably and intangible assets whose fair value can be measured with reference to an active market.
- » **Carrying amount** of revalued item at the end of a reporting period **cannot differ materially from its fair value.**
- » **Unlike the fair value model**, in reporting **financial performance** the revaluation model presents depreciation separately from impairments/reversals of impairments in profit or loss.
  - » Other revaluation increases/decreases presented in OCI; and
  - » No 'recycling' from OCI to profit or loss.

29

29

## Fair value model: non-financial asset the requirements

- » **Accounting policy choice** for investment property.
  - » If elect cost model, disclose fair value.
- » 'Mark-to-market' consequently **unlike the revaluation model**:
  - » all value changes are reported in profit or loss, ie no OCI; and
  - » depreciation is not presented separately from impairments/reversals of impairments.

30

30

## Comparing cost model, revaluation model and fair value model reporting performance: asset consumed entirely through use

» 1 January 2011 you pay ETB1 million and gain control of a building

» estimated useful life = 40 years

» depreciation method = straight-line

» nil residual value

» 31 December 2018: fair value = ETB1.2 million

» 31 December 2026: fair value (= recoverable amount) = \$300,000

» 31 December 2034 fair value (= recoverable amount) \$800,000.

Plot in a graph the carrying amount of the asset over its useful life using each of the three measurement models for non-financial assets.

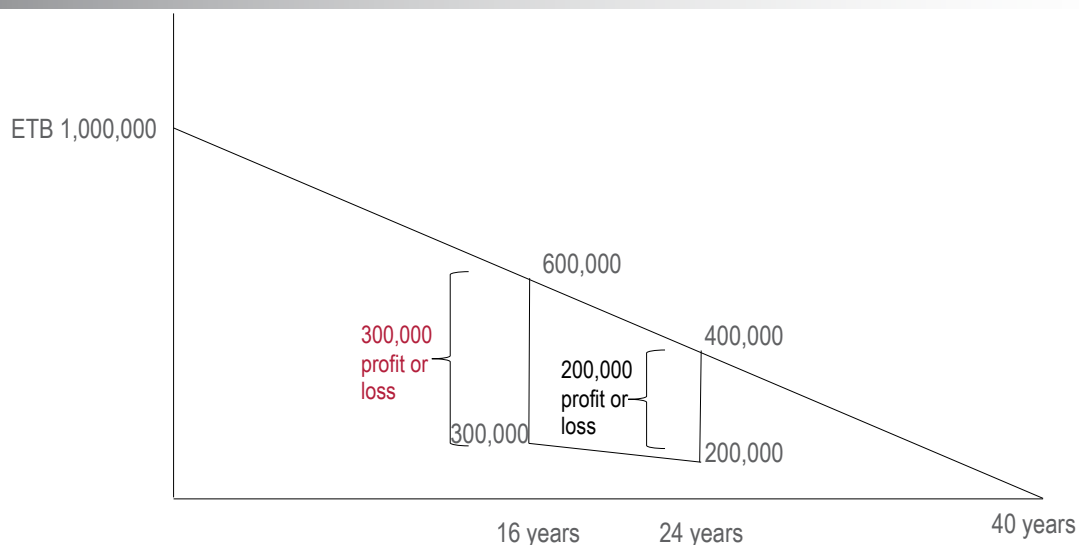
Prepare a table that compares financial performance over the entire life of the asset using each of the three models.

What if you sold the building on 31/12/2022 for ETB1,050,000?

31

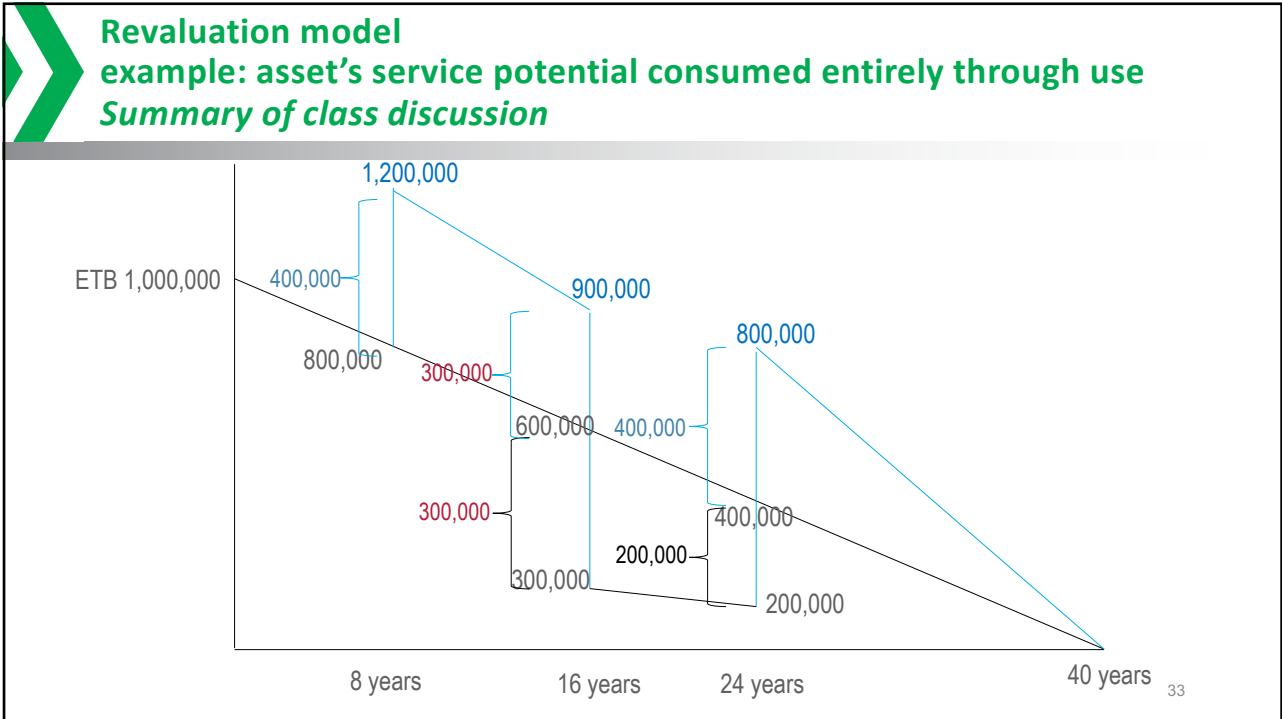
31

## Cost model example: asset's service potential consumed entirely through use *Summary of class discussion*

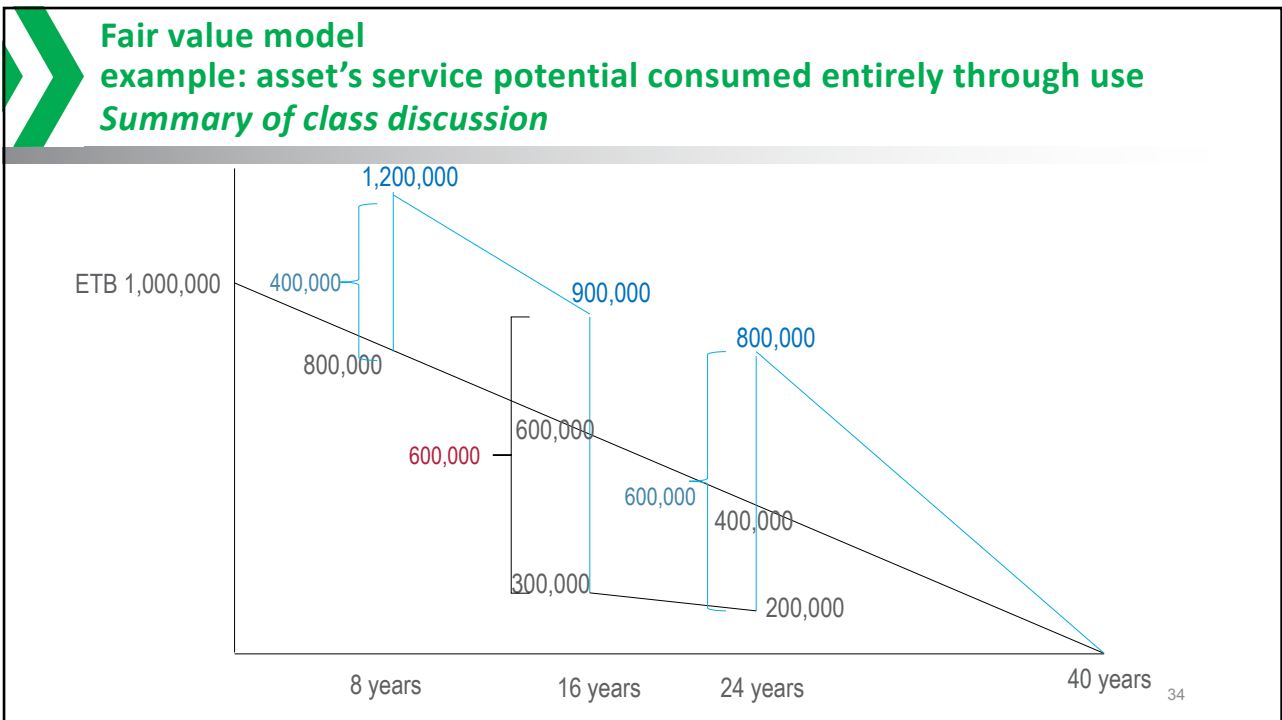


32

32



33



34



## Comparing cost model, revaluation model and fair value model reporting performance: asset consumed entirely through use

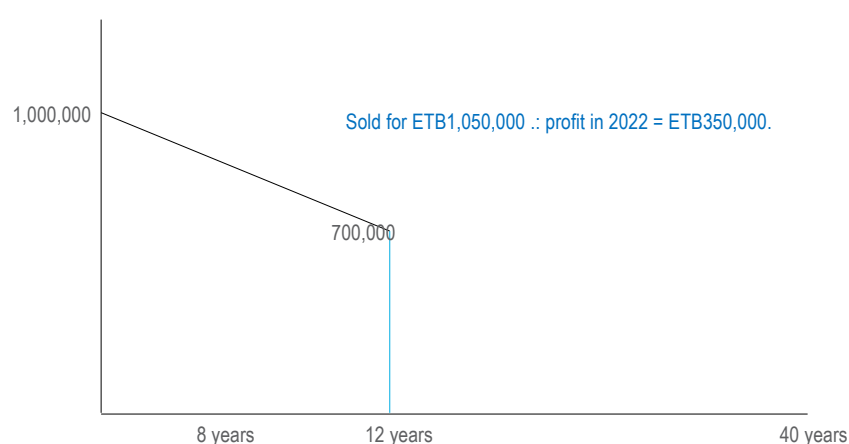
*Summary of class discussion*

2011 to 2050 (40 years)	Cost model	Revaluation model	Fair value model
<b>Profit or loss</b>	<b>(1,000,000)</b>	<b>(1,500,000)</b>	<b>(1,000,000)</b>
- depreciation	(900,000)	(1,400,000)	
- impairment	(300,000)	(300,000)	
- impairment reversal	200,000	200,000	
- fair value change income			1,000,000
- fair value change (expense)			(2,000,000)
<b>Other comprehensive income</b>		<b>500,000</b>	
- revaluation		800,000	
- revaluation decrease		(300,000)	
<b>Comprehensive income</b>	<b>(1,000,000)</b>	<b>(1,000,000)</b>	<b>(1,000,000)</b>

35

35

## Cost model example: asset partly consumed through use and then sold

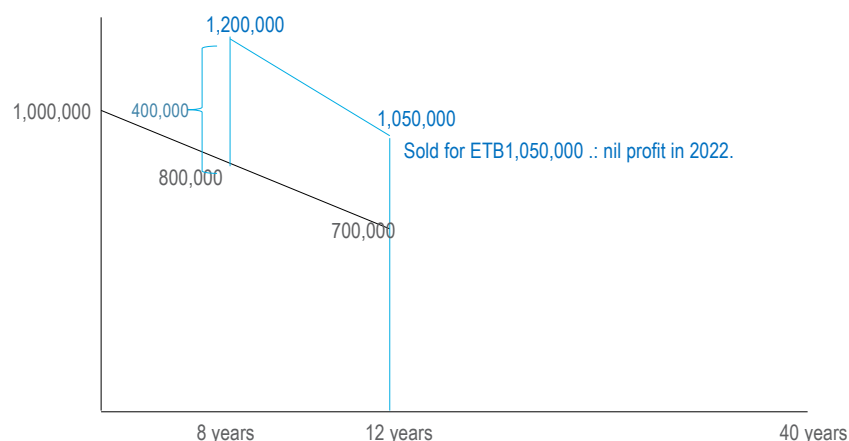


**Assume** Entity sold the building on 31/12/2022 for ETB1,050,000.

36

36

## Revaluation model and fair value model example: asset partly consumed through use and then sold



**Assume** Entity sold the building on 31/12/2022 for ETB1,050,000.

37

37

## Comparing cost model, revaluation model and fair value model reporting performance: asset partly consumed through use and then sold *Summary of class discussion*

2011 to 2022 (12 years)	Cost model	Revaluation model	Fair value model
<b>Profit or loss</b>	<b>50,000</b>	<b>(350,000)</b>	<b>50,000</b>
- depreciation 2011 to 2022	(300,000)	(350,000)	
- profit on sale of PPE <b>in 2022</b>	350,000		
- fair value change income <b>in 2018</b>			400,000
- fair value change (expense)			(350,000)
<b>Other comprehensive income</b>		<b>400,000</b>	
- revaluation <b>in 2018</b>		400,000	
<b>Comprehensive income</b>	<b>50,000</b>	<b>50,000</b>	<b>50,000</b>

38

38

## Comparing cost model, revaluation model and fair value model

### Summary of class discussion

» Which model best reflects the economics of the building over time?

- 1) cost model; or
- 2) revaluation model (Because it separates the consumption of the assets service potential (measured at a real economic value) from the price change effects of the remaining service potential.); or
- 3) fair value model.

» Which model provides the most decision-useful information for primary user resource allocation decision making?

- 1) cost model; or
- 2) revaluation model (Because it provides a more detailed reflection of the underlying economics by separating the consumption of the assets service potential (measured at a real economic value) from the price change effects of the remaining service potential.); or
- 3) fair value model.

40

40

## Comparing cost model, revaluation model and fair value model

### Summary of class discussion

» Which model gives management most flexibility in reporting profit or loss for the period?

- 1) cost model (Because management can use its discretion to determine when price change effects are presented in profit or loss by selling the asset.); or
- 2) revaluation model; or
- 3) fair value model.

» Which model reports least profit over the life of the asset?

- 1) cost model; or
- 2) revaluation model (Because price change effects are presented in other comprehensive income (OCI) without recycling to profit or loss when realised.); or
- 3) fair value model.

42

42



## Which impairment test applies to which assets

43

Measurement model	Which impairment test?
Cost model (non-financial asset)	✓ Recoverable amount
Amortised cost model (financial asset)	✓ ECL impairment model
FVPL model (financial and non-financial assets)	X
FVOCI model debt instrument (financial asset)	✓ ECL impairment model
FVOCI model equity instrument (financial asset)	X
Equity method (financial asset)	✓ Recoverable amount
FV less costs to sell model (non-financial asset)	X
Revaluation model (non-financial asset)	✓ Recoverable amount
Net realisable value model (non-financial asset)	X
Lower of cost and NRV (non-financial asset)	✓ Net realisable value
Lower of reclassification carrying amount and FVLCTS	✓ Fair value less costs to sell

45

## Recoverable amount impairment measurement

### *Which assets?*

#### *Summary of class discussion*

Asset	IAS 36
Property, plant and equipment: cost model and revaluation model	✓
Intangibles assets: revaluation model	✓
Intangibles assets: cost model	✓
Exploration for and evaluation of mineral resources	✓
Investment property: cost model only	✓
Investment in associates, joint ventures and subsidiaries accounted for using the cost model or the equity method	✓

46

46

## Other impairment measurement

### *which measure / which assets?*

#### *Summary of class discussion*

Net realisable value (NRV)	IFRS
Inventory	✓ IAS 2
Fair value less costs of disposal	IFRS
Non-current assets held for sale	✓ IFRS 5

47

47



## When to test non-financial assets for impairment

48



### When to test for impairment?

- » Inventory (IAS 2)
  - » at the end of each reporting period
- » Other non-financial assets (IAS 36)
  - » at reporting date assess whether there is any **indication** that an asset may be impaired
  - » if any such indication exists perform **impairment test**
- » Irrespective of whether there is any indication of impairment: (paragraph 10 of **IAS 36**) test for impairment:
  - » at the same time each year (and whenever impairment is indicated) **goodwill**, **indefinite life intangible asset** or **an intangible asset not yet available for use**; and
  - » such assets must be tested for impairment in the year of their acquisition.

49

49



## IAS 36 *Impairment of Assets* *impairment indicators*

Consider, as a minimum: external and internal sources of information

### » External sources of information

- » asset's market value declined significantly > expected
- » significant changes in the technological, market, economic or legal environment
- » market rates increased (for example, effect on discount rate)
- » carrying amount of the net assets > estimated fair value of the entity

50

50



## IAS 36 *Impairment of Assets* *impairment indicators*

### » Internal sources of information

- » obsolete or physical damaged asset
- » significant changes in the extent or manner in which, an asset is (or is expected to be) used
  - » for example, idle assets, plans to discontinue or restructure operation, plans to dispose before expected, and reassessing the useful life from indefinite to finite
- » internal reporting indicates that the economic performance of an asset is, or will be, worse than expected

51

51



## IFRS 6 *Exploration for and Evaluation of Mineral Resources* impairment indicators

### » Impairment indicators (paragraph 20 of IFRS 6)

- (a) the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed.
- (b) substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned.
- (c) exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources and the entity has decided to discontinue such activities in the specific area.
- (d) sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

52

52



## Recoverable amount

53



## Impairment testing level

- » **Principle**—test for impairment at the individual asset level (ie item-by-item)
- » **Application guidance** is necessary for cash-generating units (CGU) and corporate assets etc
  - » CGU is the the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.
- » Goodwill **exception** from the principle (a rule)
  - » Goodwill is tested for impairment at the lowest level at which it is monitored for internal management (ie CODM) purposes provided that level is not larger than an operating segment as defined in IFRS 8 (before aggregation) (paragraph 80 of IAS 36)

54

54

## What is recoverable amount?

- » The recoverable amount of an asset is the greater of:
  - » its **fair value less costs to sell**; and
  - » its **value in use**.

*[Most of this 5-day workshop is dedicated to fair value measurement. The next few slides focus on value in use.]*

55

55

## Value in use of an asset

- » To measure value in use
  - » estimate future cash flows (in and out) from continuing use of the asset
  - » estimate future cash flows (in and out) from ultimate disposal of the asset
  - » apply appropriate discount rate to future cash flows
- » Cash flow estimates do **not include** cash flows from
  - » improving or enhancing the asset's performance (measuring the existing asset in its current condition, not a possible future asset)
  - » cash flows from financing activities (a separate liability)
  - » income tax receipts and payments (a separate asset or liability)

56

56

## Value in use of an asset

- » Reflect in the calculation of value in use
  - » expectations about possible variations in the amount or timing of the estimated future cash flows the entity expects
  - » time value of money (current market risk-free rate of interest)
  - » price for uncertainty inherent in the asset
  - » other factors (for example, illiquidity) that market participants would adjust for
- » Avoid double-counting effects in future cash flows and in the discount rate.

57

57

## Value in use: estimating cash flows

- » Base cash flow projections **on reasonable and supportable assumptions** that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.
  - » use recent budgets/forecasts to est. cash flows;
  - » extrapolate beyond forecast period using steady or declining growth rate, unless another is justified;
  - » **Give greater weight to external evidence.** For example, published spot prices for commodities.

58

58

## Value in use *judgements and estimates*

- » Identifying internal and external indicators of impairment
- » Identifying cash-generating units (CGUs)
- » Allocating assets (eg goodwill) to CGUs
- » Measuring VIU:
  - » estimate future cash flows (in and out) from continuing use of the asset and its ultimate disposal, and
  - » determine appropriate discount rate to apply to future cash flows
  - » etc

59

59



## Contrasting inputs to DCF models when measuring value in use and fair value (Level 3)

60



### Contrasting value in use and fair value measurement objective, perspective, valuation model and inputs *What do you think?*

	Value in Use	Fair Value
Measurement objective	?	?
Measurement perspective	?	?
Assumed use of the asset	?	?
Market conditions	?	?
Valuation technique	?	?
Discount rate	?	?
Discrete projection period	?	?
Future improving/enhancing asset's performance	?	?
Possible future restructurings	?	?
Growth rate	?	?
Growth rate beyond discrete projection period	?	?
Use of observable data	?	?
Tax assumption	?	?

61

61

**Contrasting value in use and fair value measurement objective, perspective, valuation model and inputs**  
*Summary of class discussion*

	Value in Use	Fair Value
Measurement objective	Estimate PV of future net cash inflows	Estimate selling price in market
Measurement perspective	Entity-specific	Market participant
Assumed use of the asset	Current use	Highest and best use
Market conditions	Management's expectations (but constrained)	Market participant views of current market conditions
Valuation technique	Discounted cash flows	Whatever market participants use
Discount rate	'Market based'	Market rates
Discrete projection period	5 years	Market participant expectations

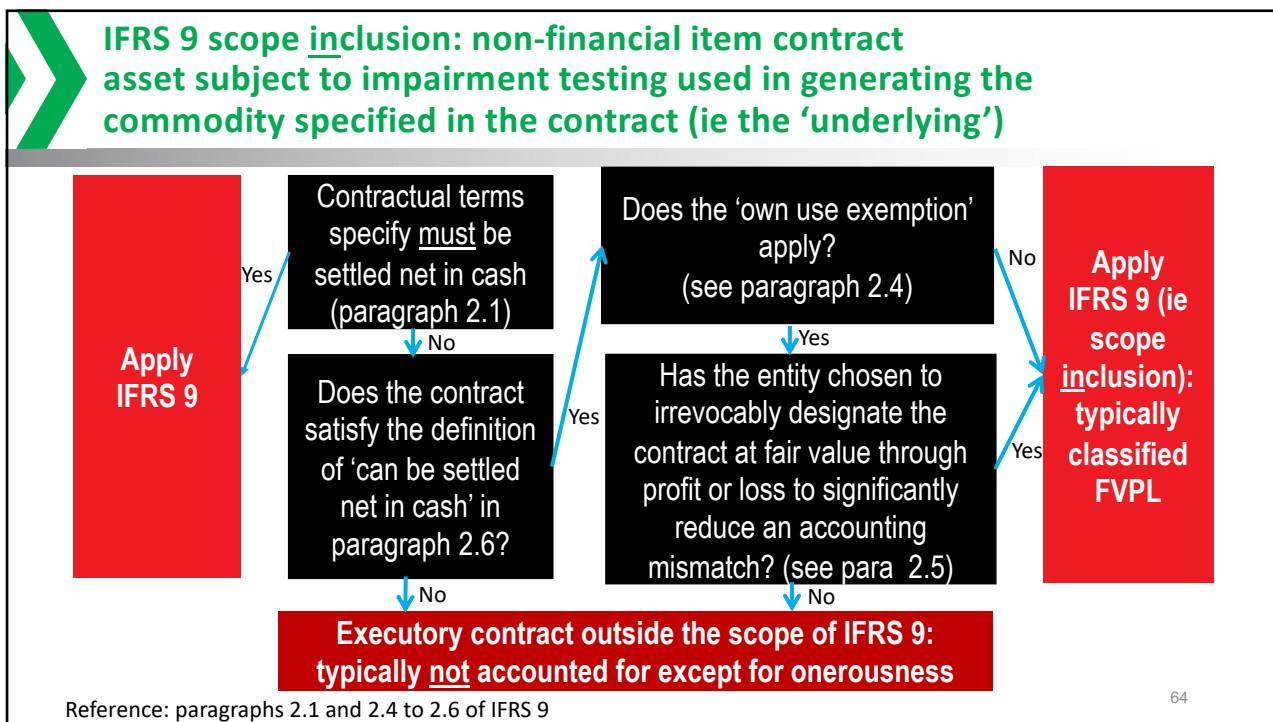
62

**Contrasting value in use and fair value measurement objective, perspective, valuation model and inputs**  
*Summary of class discussion*

	Value in Use	Fair Value
Future improving/enhancing asset's performance	Ignore	Market participant expectations
Possible future restructurings	Ignore	Market participant expectations
Growth rate	Usually average historical growth rates (but constrained)	Market participant expectations
Growth rate beyond discrete projection period	Steady or declining (unless convincing evidence)	Market participant expectations
Use of observable data	Reasonable and supportable assumptions	Maximise observable inputs the 'fair value hierarchy'
Tax assumption	Pre-tax: cash flows and discount rates	Silent (must be internally consistent)

63

63



64

### Contrasting value in use and fair value 'forward' contracts: asset subject to impairment testing used in generating the commodity specified in the contract (ie the 'underlying')

The contract is...	Value in Use	Fair Value
...in the scope of IFRS 9 (see decision tree on previous slide)	Is the price in the contract relevant to measuring ViU?	Is the price in the contract relevant to measuring fair value?
...out the scope of IFRS 9 (see decision tree on previous slide) and 'in the money'	Is the price in the contract relevant to measuring ViU?	Is the price in the contract relevant to measuring fair value?
...out the scope of IFRS 9 (see decision tree on previous slide) and 'out of the money'	Is the price in the contract relevant to measuring ViU?	Is the price in the contract relevant to measuring fair value?

65

## Contrasting value in use and fair value

'forward' contracts: asset subject to impairment testing used in generating the commodity specified in the contract (ie the 'underlying')

Summary of class discussion

The contract is...	Value in Use	Fair Value
...in the scope of IFRS 9 (see decision tree on previous slide)	The contract is recognised as a separate asset/liability that is measured at its fair value. Consequently, the contract is <b>irrelevant</b> to calculating the VIU of the asset that produced it.	Irrespective of whether it is recognised separately, the value of the 'fixed-price contract to sell the commodity' is <b>not necessarily relevant</b> to measuring the fair value of the asset that produced it "because fair value reflects the current market conditions in which market participant buyer and sellers would enter into a transaction." (paragraph 16 of IAS 41 <i>Agriculture</i> ) However, if entered into at the reporting date in an arm's length transaction then the price specified in the contract could inform the input 'commodity price' for the coterminous delivery date.
...out the scope of IFRS 9 (see decision tree on previous slide) and 'in the money'	The contract is <b>relevant</b> to calculating VIU of the asset that produced it only to the extent that the contract: (i) has not been recognised as a separate asset; <u>and</u> (ii) is not used to 'protect' another asset from impairment (eg inventory).	
...out the scope of IFRS 9 (see decision tree on previous slide) and 'out of the money'	The contract is <b>relevant</b> to calculating VIU of the asset that produced it only to the extent that the contract: (i) has not been recognised as a separate liability (eg when the contract is onerous); and (ii) is not taken account of in measuring the impairment of another asset (eg, inventory).	

66

66

## Comparing financial instrument measurement models

67

## IFRS 9: measurement and presentation of financial performance

Measurement model	Interest or dividends	Impairment	Foreign exchange	Change in FV	Recycling OCI to PL?
Amortise cost	PL: effective interest rate	PL	PL		
Fair value (FV) profit or loss (PL)	PL	PL	PL	PL (incl. forex and 'impairment')	
FVOCI: basic debt model	PL: effective interest rate	PL (on basis of amortised cost)	PL (on basis of amortised cost)	OCI (FV change adjusted for AC accounting)	Yes
FVOCI: equity	PL: dividends	OCI	OCI	OCI (incl. forex and 'impairment')	No

68

68

## IFRS 9: presentation of financial performance example 1: debt instrument

- » 01/01/2022: Entity (functional currency ETB) pays ETB1 million to purchase a F\$1 million (foreign currency denominated) debt instrument at its fair value (when 1ETB = 1F\$).
  - » The counterparty is contractually obliged to pay F\$100,000 interest on 31 December each year 2022 to 2031 (10 years) and F\$1million redemption on 31/12/2025.
  - » Entity determines that the asset is not purchased or originated credit-impaired.
- » 31/12/2022: the fair of the instrument decreased to FTB880,000 (FTB100,000 decrease as as a result of changes in currency exchange rates (assume: exchange rate change occurred on 02/01/2022) and FTB20,000 decrease as a result of changes in market interest rates). Entity:
  - » receives F\$100,000 (which its immediately exchanges for FTB90,000)
  - » determines that there has not been a significant increase in credit risk since initial recognition and that expected credit losses should be measured at an amount equal to 12-month expected credit losses (ECL), which amounts to F\$10,000 (ie FTB9,000).
- » 01/01/2023: Entity sells the instrument for F\$977,778 million (ie FTB880,000).

69

69



## IFRS 9: presentation of financial performance

### example 1: debt instrument continued

#### summary of class discussion

#### Which classification of financial asset must Entity apply in accounting for the debt instrument?

Choose one of:

- 1) subsequently measured at amortised cost
- 2) subsequently measured at fair value through profit or loss (FVPL)
- 3) subsequently measured at fair value through other comprehensive income (FVOCI)
- 4) the classification 1), 2) or 3) depends on Entity's business model
- 5) the classification 1), 2) or 3) depends on Entity's business model and whether the entity has invoked the fair value option to avoid 'an accounting mismatch'

Reference: paragraphs 4.1.1 to 4.1.5

71

71

## IFRS 9 accounting for debt instrument (basic entries)

### Summary of class discussion

	Amortised cost		Fair value PL		Fair value OCI	
<b>1 January 2022</b>						
Financial asset	1,000,000		1,000,000		1,000,000	
Cash		1,000,000		1,000,000		1,000,000
<i>Purchase of the financial asset</i>						
<b>31 December 2022</b>						
Cash	90,000		90,000		90,000	
Profit or loss: finance income		90,000		90,000		90,000
<i>Finance income earned and received in 2022</i>						

73

## IFRS 9 accounting for debt instrument (basic entries)

### Summary of class discussion

	Amortised cost		Fair value PL		Fair value OCI	
<b>31 December 2022</b>						
Profit or loss: forex loss	100,000				100,000	
Profit or loss: impairment	9,000				9,000	
Profit or loss: FV change			120,000			
OCI: FV change					11,000	
Financial asset		109,000		120,000		120,000
<i>To recognise part (amortised cost) or all (fair value PL and fair value OCI) of the change in fair value of the debt instrument that occurred in 2022</i>						

74

74

## IFRS 9 accounting for debt instrument (basic entries)

### Summary of class discussion

	Amortised cost		Fair value PL		Fair value OCI	
<b>1 January 2023</b>						
Cash	880,000		880,000		880,000	
Profit or loss: loss on disposal	11,000					
Financial asset		891,000		880,000		880,000
Profit or loss: 'recycling' prior period FV losses					11,000	
OCI: 'recycling' FV losses						11,000
<i>To derecognise the debt instrument on its disposal by sale (and amortised cost: recognising previously unrecognised prior period unrealised losses) (and fair value OCI: reclassifying prior period losses that were presented in prior period OCI to profit or loss for 2023)</i>						

75

75

## IFRS 9 accounting for equity instrument Example

- » 01/01/2022: Entity (functional currency FTB) pays FTB1 million to purchase a F\$1 million (foreign currency denominated) equity instrument at its fair value (when 1FTB = 1F\$).
- » 31/12/2022:
  - » receives F\$100,000 dividend (which it immediately exchanges for FTB90,000)
  - » the fair of the instrument decreased to FTB880,000 (ie F\$977,778, assume the exchange rate change occurred on 02/01/2022).
- » 01/01/2023: Entity sells the instrument for F\$977,778 (which it immediately exchanges for FTB880,000).

76

76

## IFRS 9 accounting for equity instrument *summary of class discussion*

### Which classification of financial asset must Entity apply in accounting for the equity instrument?

Choose one of:

- 1) subsequently measured at amortised cost
- 2) subsequently measured at fair value through profit or loss (FVPL)
- 3) subsequently measured at fair value through other comprehensive income (FVOCI)
- 4) the classification 2) or 3) depends on Entity's business model
- 5) the classification 2) or 3) depends on Entity's business model (for example, if held for trading cannot designate FVOCI) and whether the entity has invoked the fair value OCI option

References: paragraphs 4.1.1 to 4.1.5 and B4.1.1 to B4.1.36 of IFRS 9

78

78

## IFRS 9 accounting for equity instrument (basic entries)

### Summary of class discussion

	Fair value PL		Fair value OCI	
<b>1 January 2022</b>				
Financial asset	1,000,000		1,000,000	
Cash		1,000,000		1,000,000
<i>Purchase of the financial asset</i>				
<b>31 December 2022</b>				
Cash	90,000		90,000	
Profit or loss: dividend income		90,000		90,000
<i>Dividend income earned and received in 2022</i>				

80

## IFRS 9 accounting for equity instrument (basic entries)

### Summary of class discussion

	Fair value PL		Fair value OCI	
<b>31 December 2022</b>				
Profit or loss: FV change	120,000			
OCI: FV change			120,000	
Financial asset		120,000		120,000
<i>To recognise the change in fair value of the equity instrument that occurred in 2022</i>				
	Fair value PL		Fair value OCI	
<b>1 January 2023</b>				
Cash	880,000		880,000	
Financial asset		880,000		880,000
<i>To derecognise the debt instrument on its disposal by sale (note: no 'recycling' for FVOCI equity)</i>				

81