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LIVE COACHING CLASSES BOARD OF STUDIES (A), ICAI

CA FINAL PAPER 1: FINANCIAL REPORTING

TOPIC: IND AS 113 - FAIR VALUE MEASUREMENT

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Topics to be Covered

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Need for Ind AS 113



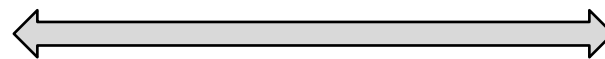
Normally **assets and liabilities** are **exchanged** between parties at their **agreed** terms and conditions based on the prices which might **not be at arm's length prices**.



Entity-specific
Prices



Buyer



Seller

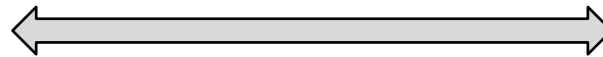


e.g.: reduced prices; reduction in interest rates;
long credit period as compared to market participants

To define fair values, it should be ensured that the values reflect all assumptions/ adjustments to change from transaction specific/ entity specific to normal transaction which is common for all interested parties.



Market-based
Value



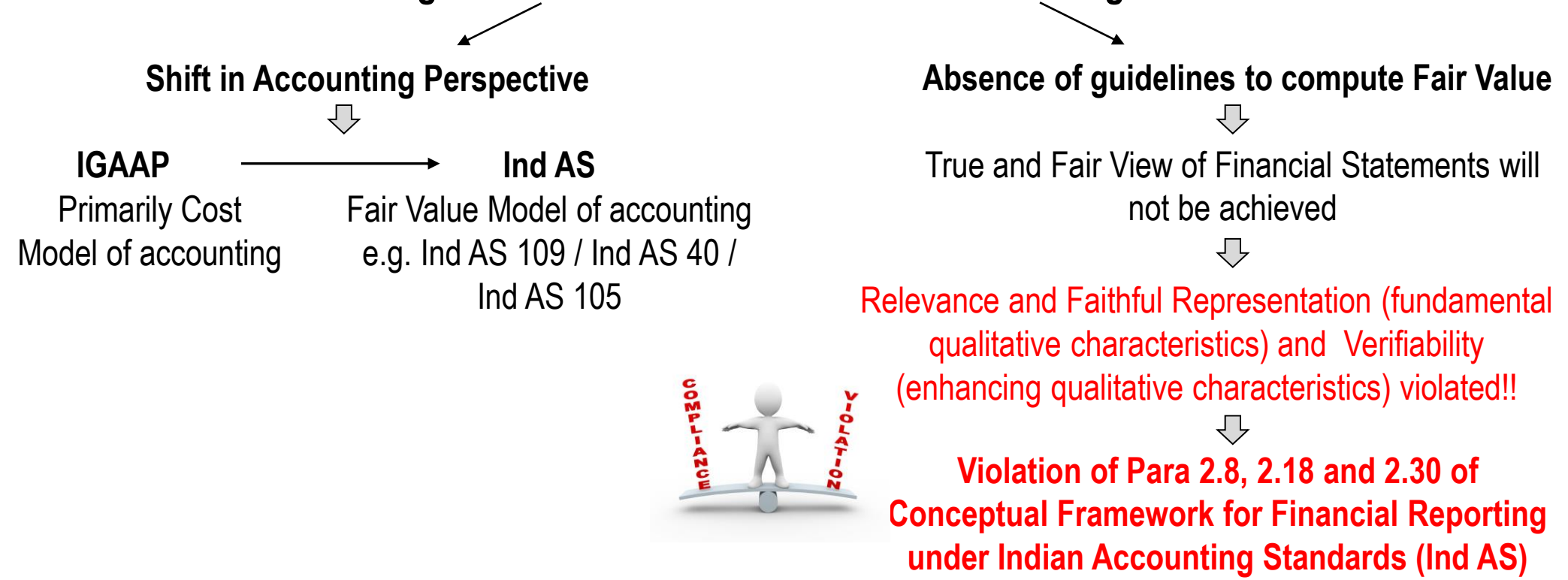
Value should be from the perspective of market participants (i.e. arm's length prices), instead of it being transaction specific / entity specific





What would happen without Ind AS 113?

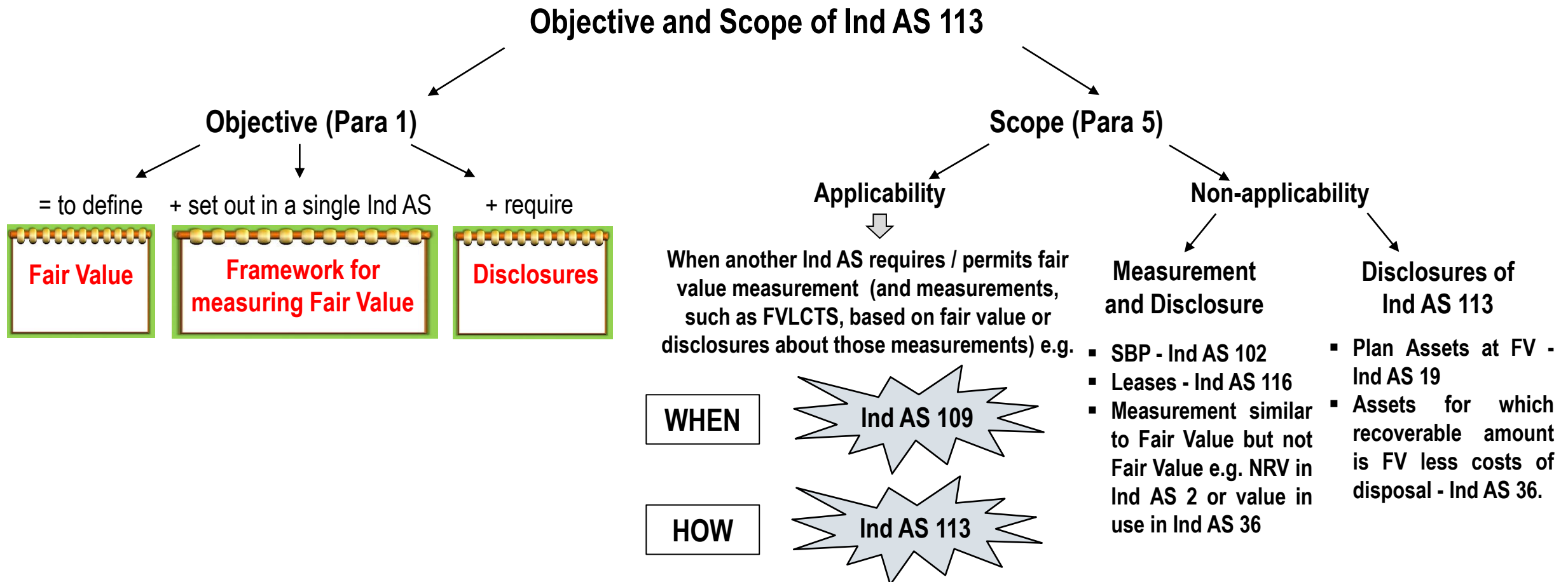
Significance of Fair Value under the Ind AS Regime



Hence Ind AS 113 assumes significance since it ensures compliance with the Framework



Objective and Scope of Ind AS 113





Example 1: Page 4.83

- Fair value less costs to sell as required under Ind AS 105 for assets held for sale.
- Fair value through Profit and Loss or through Other Comprehensive Income as required under Ind AS 109 for Financial Instruments.
- Property, plant & equipment measured using revaluation modal as required under Ind AS 16.
- Biological assets measure at fair value under Ind AS 41 for biological assets.

ICAI Examples



What is Fair Value?

Fair Value (Para 9) = 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**.

Key Aspects in Fair Value Measurement

Price

Appropriate Market

Market Participants

Orderly Transaction

Measurement Date



Key Aspects: Asset or Liability Specific Fair Value

- **FAIR VALUE IS MARKET-SPECIFIC AND NOT ENTITY-SPECIFIC**
- Fair Value Measurement takes into account the characteristics of the asset or liability, e.g. the condition and location of the asset and restrictions, if any, on its sale or use. However, the restrictions or conditions that might be related to a particular entity should not be taken into account because a fair value will be based on market participant assumptions rather to an entity specific conditions or restriction which usually will not affect fair valuation of an asset/ liability.
- An entity shall **measure the fair value** of an asset or a liability **using the assumptions that market participants would use** when pricing the asset or liability, assuming that market participants act in their economic best interest.

RULE

ENTITY-SPECIFIC RESTRICTIONS / CONDITIONS: IGNORED

ASSET / LIABILITY-SPECIFIC RESTRICTION / CONDITIONS TRANSFERRED TO BUYER: CONSIDERED



Example 3: Page 4.85

An entity is having a land which has a restriction to develop into a commercial house because of restricted business objective in which currently the entity operates. The entity wants to sell the land and there would not be any restriction for a buyer of the land to develop a commercial house, since this restriction is entity specific. Hence, it will not be considered while calculating fair value of the land.

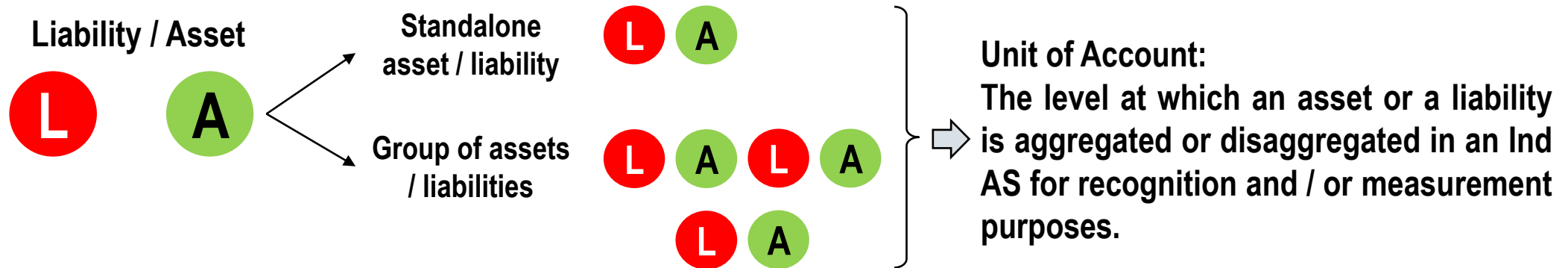
Example 4: Page 4.85

A car has been bought for private use and there is a restriction of not to use the car for any commercial purposes. Commercial vehicle is having more fair value than private vehicle. Since the restriction to use the vehicle is asset specific and market participant will also consider the asset specific restrictions while calculating fair values for such asset and hence this condition will be considered while evaluating fair value of the car.

ICAI Examples



Key Aspects: Unit of Account



- Ind AS 113 describes **how** to measure fair value, **not what** is being measured at fair value. **Other Ind AS** specify **whether** a fair value measurement **considers an individual asset or liability or a group of assets or liabilities** (i.e. the unit of account).
- Whether the asset or liability is a **stand-alone asset or liability**, a **group of assets**, a **group of liabilities** or a **group of assets and liabilities** for recognition or disclosure purposes depends on its unit of account.
- The **unit of account** for the asset or liability shall be **determined in accordance with the Ind AS that requires or permits the fair value measurement**, except as provided in this Ind AS.



Example 5: Page 4.86

An entity having certain securities which are quoted at market and these are recognized at fair value in the balance sheet. Quoted prices at **individual level** will be used in order to find fair values of these investments.

Example 6: Page 4.86

In order to evaluate fair values of assets to identify impairment as per Ind AS 36, which requires to measure such fair value at cash generating units, hence **group of assets** will be used in order to find fair values for the requirement of such standard.

ICAI Examples



Key Aspects: Market Participants

Fair Value is always computed **from the perspective of the market participant** i.e. price that would be received / paid on sale / settlement or transfer of an asset / liability by / to a market player.

What are Market Participants?

The parties which eventually transact the assets/ liabilities either in the **principal market** or **the most advantageous market** in their best economic interest

Characteristics of Market Participants

- They should be **independent** and **not a related party**. However, if **related parties** have done similar transaction **on arm's length price**, then it can be between related parties as well.
- The parties should **not be under any stress or force** to enter into these transactions
- All parties should **have reasonable and sufficient information** about the same.



Example 9: Page 4.89

A land has legal restriction to use it for commercial purposes in next 10 years irrespective of its holder. The fair value of the land will include this restriction about its usage because it is an asset related restriction and any buyer will need to take over with similar restriction to use the land for next 10 years. Now to evaluate its fair value, one has to consider the restriction based on the assumptions which normally would be taking into account by its market participants, mentioned as below

- a) Whether the restriction is commonly imposed on each such type of land?
- b) How useful it will be after the end of 10 years?
- c) Whether there is any alternative use which may be considered normally by a participant for similar kind of deals?
- d) How liquid the sale of land will be with such restrictions?
- e) Comparing the price with similar kind of land without restrictions to arrive at its fair values

ICAI Examples



Key Aspects: Appropriate Market

Principal Market

Market which is normally the place in which the assets / liabilities are being transacted with highest volume with high level of activities comparing with any other market available for similar transactions.

If there is principal market, the price in the market must be used even if the prices in the other market are more advantageous.

Because the principal market is the most liquid market for the asset or liability, that market will provide the most representative input for a fair value measurement.

Most Advantageous Market

This is the market which either maximizes the amount that would be received (Net Proceeds) when an entity sells an asset or minimizes the amount that is to be paid while transferring the liability.

Net Proceeds = Available Price (-)
Transport Costs (-) Transaction Costs

In the absence of principal market, this market is used for Fair Valuation of the Assets/ Liabilities. In many cases Principal market & most advantageous market will be same.



Example 7: Page 4.87

Share of a company which is listed at BSE and NYSE has different closing prices at the year end. The price at BSE has greatest volume and activity whereas at NYSE it is less in terms of volume transacted in the period. Since BSE has got highest volume and significant level of activity comparing to other market although the closing price is higher at NYSE, the closing price at BSE would be taken.

Example 8: Page 4.87

Diamond (a commodity) has got a domestic market where the prices are lesser comparing to the price available for export of similar diamonds. The Government has a policy to cap the export of Diamond, maximum up to 10% of total output by any such manufacturer. The normal activities of diamond are being done at domestic market only i.e. 90% and balance 10% only can be sold via export. The highest level of activities with highest volume is being done at domestic market . Hence, principal market for diamond would be domestic market. Export prices are more than the prices in the principal market and it would give highest return comparing to the domestic market. Therefore, the export market would be considered as most advantageous market. However, if principal market is available, then its prices would be used for fair valuation of assets/ liabilities.

ICAI Examples



Key Aspects: Price

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction **in the principal (or most advantageous) market** at the measurement date **under current market conditions (i.e. an exit price)** regardless of whether that price is **directly observable or estimated** using another valuation technique.

FAIR VALUE (PRICE) = AVAILABLE PRICE (LESS) TRANSPORTATION COST

Transaction costs e.g. brokerage, commission, STT etc. are not a characteristic of an asset or a liability, but a **characteristic of the transaction**. Hence, it would not be appropriate to consider any transaction cost further while assessing fair values. However, they would be considered while ascertaining Net Proceeds for determining the most advantageous market.

NET REALIZABLE VALUE (NRV) = FAIR VALUE (LESS) TRANSACTION COSTS

Transport cost is the cost that would be **incurred to transport the asset from its current location to its principal (or most advantageous) market**. Unlike transaction costs, transport costs arise from an event (transport) that **does change a characteristic of an asset (its location)** and hence, it is deducted from available price to arrive at Fair Value.



Example 10: Page 4.89-90

An entity sells certain commodity which are available actively at location A and which is considered to be its principal market (being significant volume of transactions and activities takes place). However, fair value of the commodity is required to be assessed for location B which is far from location A and requires a transport cost of ₹ 100. Since the transport cost is not a transaction cost and it is not specific to any transaction but it is inherent cost which requires to be incurred while bringing such commodity from location A to location B , it will be considered while evaluating fair value from the principal market.

ICAI Examples



Question 1: Page 4.107

An asset is sold in 2 different active markets at different prices. An entity enters into transactions in both markets and can access the price in those markets for the asset at the measurement date.

In Market A:

The price that would be received is ₹ 26, transaction costs in that market are ₹ 3 and the costs to transport the asset to that market are ₹ 2.

In Market B:

The price that would be received is ₹ 25, transaction costs in that market are ₹ 1 and the costs to transport the asset to that market are ₹ 2.

You are required to calculate:

- (i) The fair value of the asset, if market A is the principal market, and
- (ii) The fair value of the asset, if none of the markets is principal market.

ICAI Test Your Knowledge



Practical Problems

Question 1:

Isha Ltd. operates in the agricultural sector and apart from farming activities, it also has a division retailing agricultural vehicles. It is currently evaluating a proposal involving sale of the retail division, and accordingly wishes to fair value the inventory of vehicles for the purpose of sale. Three markets currently exist for the agricultural vehicles within which Isha Ltd. has transacted regularly. Isha Ltd. wishes to determine the fair value of 250 identical, new vehicles as on 31 March 20X9. The volumes and prices across the three markets are as under:

Market	Sales price per vehicle (₹)	Historical Volume – Vehicles sold by Isha Ltd.	Total Volume of Vehicles sold in the market	Transaction cost per vehicle (₹)	Transport cost to the market per vehicle (₹)
Uttar Pradesh	4,00,000	10,000	1,75,000	5,000	4,000
Punjab	3,80,000	3,750	9,35,000	4,000	7,000
Orissa	3,40,000	1,895	1,45,000	3,000	6,000

Isha Ltd. wishes to value the vehicles at ₹ 3,91,000 per vehicle as these are the highest net proceeds per vehicle (₹ 4,00,000 - ₹ 5,000 - ₹ 4,000), and Uttar Pradesh is the largest market for Isha Ltd.'s vehicles. Isha Ltd. seeks your advice as to whether this valuation would be acceptable under Ind AS 113, Fair Value Measurement.



Valuation of Non-Financial Assets (e.g. land, biological assets)

HIGHEST AND BEST USE CONCEPT

- It is a valuation concept used to value many non- financial assets (e.g. real estate). The highest and best use of a non- financial asset must be **physically possible, legally permissible and financially feasible**.
- The highest and the best use is determined from market participant perspective. **It does not matter whether the entity intends to use the asset differently**.
- To find out the best possible use, one has to identify its market participants and then to find the best legitimate use of this non-financial asset which one would normally do.
- All **restrictions specific to any market participant would not be considered** while finding out fair value of the non-financial asset.
- In absence of potential best use which is not easily available, current use would be considered best use.
- **While considering fair value under any alternative use, deduct the estimated cost to be incurred in order to make the asset ready for alternative use.**



Example 11: Page 4.91

An entity bought some land which is intended to be used for business purposes. However, the entity now wants to sell this piece of land at its fair value. One has to evaluate all possible use of this land before determining its fair value. The land could be used to make a commercial place, which could be more in value as compared to when it is used for business purposes. The commercial place value would be considered its highest and best use if the same is allowed in its near location and conditions.

Example 12: Page 4.91-4.92 Current use as Highest and Best Use

A Ltd acquires a machine in a business combination by acquiring controlling stake in B Ltd. The machine will be held and used in A's operations. The machine was originally purchased by B Ltd from an outside vendor and, before the business combination, was customized by the B Ltd for use in its operations. However, the customization of the machine was not extensive.

A Ltd determines that the asset would provide maximum value to market participants through its use in combination with other assets or with other assets and liabilities (as installed or otherwise configured for use). There is no evidence to suggest that the current use of the machine is not its highest and best use. Therefore, the highest and best use of the machine is its current use in combination with other assets or with other assets and liabilities.

ICAI Examples



Example 13: Page 4.92 Current use as Highest and Best Use

A Ltd owns a property, which comprises land with an old warehouse on it. It has been determined that the land could be redeveloped into a leisure park. The land's market value would be higher if redeveloped than the market value under its current use. A Ltd. is unclear about whether the investment property's fair value should be based on the market value of the property (land and warehouse) under its current use, or the land's potential market value if the leisure park redevelopment occurred.

The property's fair value should be based on the land's market value for its potential use. The 'highest and best use' is the most appropriate model for fair value. Under this approach, the property's existing-use value is not the only basis considered. Fair value is the highest value, determined from market evidence, by considering any other use that is physically possible, legally permissible and financially feasible.

The highest and best use valuation assumes the site's redevelopment. This will involve demolishing the current warehouse and constructing a leisure park in its place. Therefore, none of the market value obtained for the land should be allocated to the building. So the market value of the current building, on the property's highest and best use (as a warehouse), is nil. As a result, the building's current carrying amount should be written down to zero.

ICAI Examples



Question 2: Page 4.107

Company J acquires land in a business combination. The land is currently developed for industrial use as a factory site. Although the land's current use is presumed to be its highest and best use unless market or other factors suggest a different use, Company J considers the fact that nearby sites have recently been developed for residential use as high-rise apartment buildings.

On the basis of that development and recent zoning and other changes to facilitate that development, Company J determines that the land currently used as a factory site could be developed as a residential site (e.g., for high-rise apartment buildings) and that market participants would take into account the potential to develop the site for residential use when pricing the land.

Determine the highest and best use of the land.

ICAI Test Your Knowledge



Question 6(i): Page 4.108-4.109 [Q. 13(i): RTP November 2019]

DS Limited holds some vacant land for which the use is not yet determined. the land is situated in a prominent area of the city where lot of commercial complexes are coming up and there is no legal restriction to convert the land into a commercial land.

The company is not interested in developing the land to a commercial complex as it is not its business objective. Currently the land has been let out as a parking lot for the commercial complexes around.

The Company has classified the above property as investment property. It has approached you, an expert in valuation, to obtain fair value of the land for the purpose of disclosure under Ind AS.

On what basis will the land be fair valued under Ind AS?

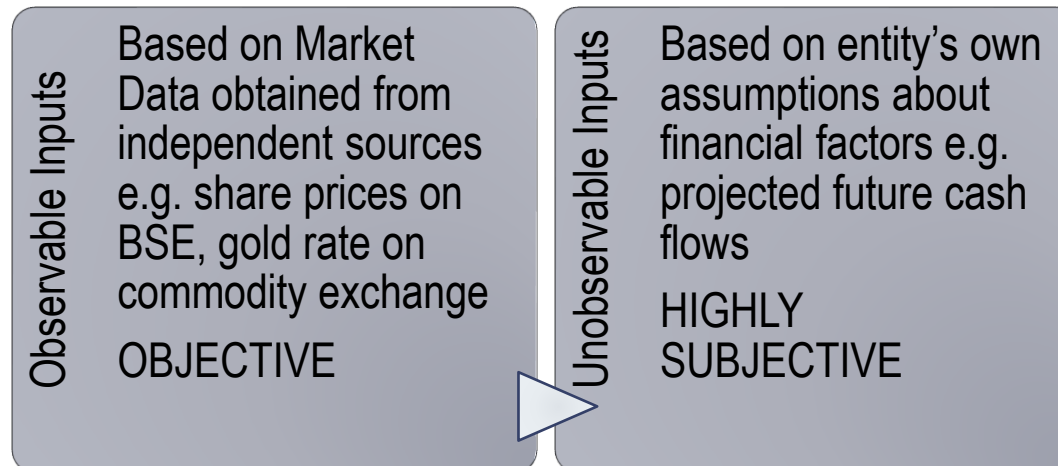
ICAI Test Your Knowledge



Valuation Techniques

- The **objective** of using a valuation technique is to **estimate the price (i.e. quoted prices are not available in the principal / most advantageous market)** at which an orderly transaction would take place between market participants at the measurement date under current market conditions.
- An entity shall **use valuation techniques** that are **appropriate** in the circumstances and for which sufficient data are available to measure fair value, **maximizing the use of relevant observable inputs** and **minimizing the use of unobservable inputs**.

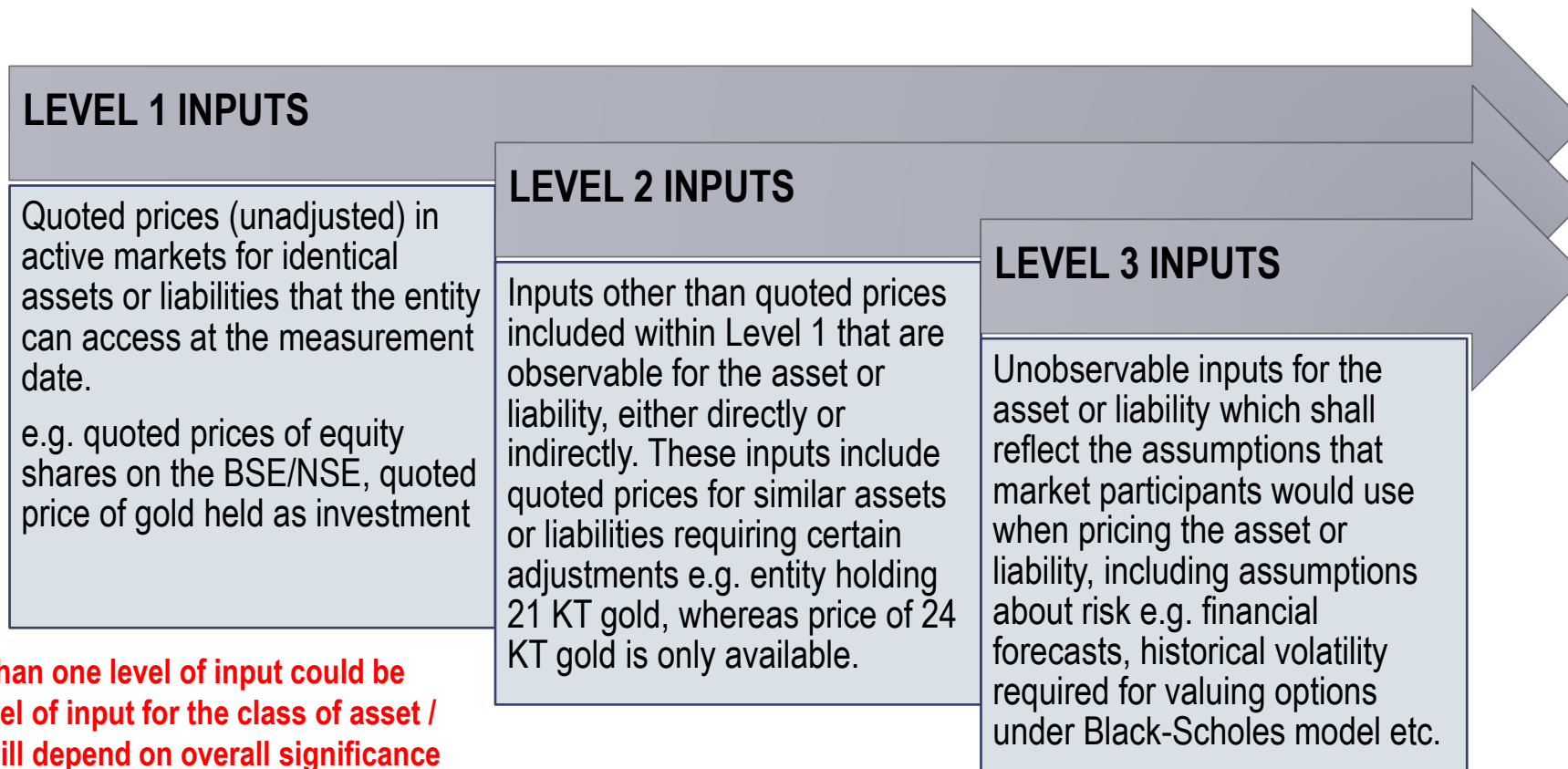
INPUTS TO VALUATION TECHNIQUES





Valuation Techniques

INPUTS TO VALUATION TECHNIQUES: FAIR VALUE HIERARCHY



More than one level of input could be used; level of input for the class of asset / liability will depend on overall significance



Question 6(ii): Page 4.109 [Q. 13(ii): RTP November 2019]

DS Limited holds equity shares of a private company. In order to determine the fair value of the shares, the company used discounted cash flow method as there were no similar shares available in the market.

Under which level of fair value hierarchy will the above inputs be classified?

What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares?

ICAI Test Your Knowledge



Principle: If an observable input requires an adjustment using an unobservable input and that adjustment results in a significantly higher or lower fair value measurement, the resulting measurement would be categorized within Level 3 of the fair value hierarchy.

Example 17: Page 4.101

If a market participant would take into account the effect of a restriction on the sale of an asset when estimating the price for the asset, an entity would adjust the quoted price to reflect the effect of that restriction. If that quoted price is a Level 2 input and the adjustment is an unobservable input that is significant to the entire measurement, the measurement would be categorised within Level 3 of the fair value hierarchy.

ICAI Examples



Example 18: Page 4.102: Level 1 Inputs

An entity is holding investment which is quoted in BSE, India and NYSE, USA. However, significant activities are being done at BSE only. The fair value of the investment would be referenced to the quoted price at BSE India (which is Level 1 fair value- Direct quoted price with no adjustments).

Example 20: Page 4.103: Level 2 Inputs

Receive-fixed, pay-variable interest rate swap based on a yield curve denominated in a foreign currency. It requires rate of swap which is of 11 years. However, normally the rates are available only for the maximum period of 10 years. The rate for 11 years can be established using extrapolation or some other techniques which is based on 10 years' available rates of swap. The fair value of 11 years so derived would be level 2 fair value.

Example 21: Page 4.103: Level 2 Inputs

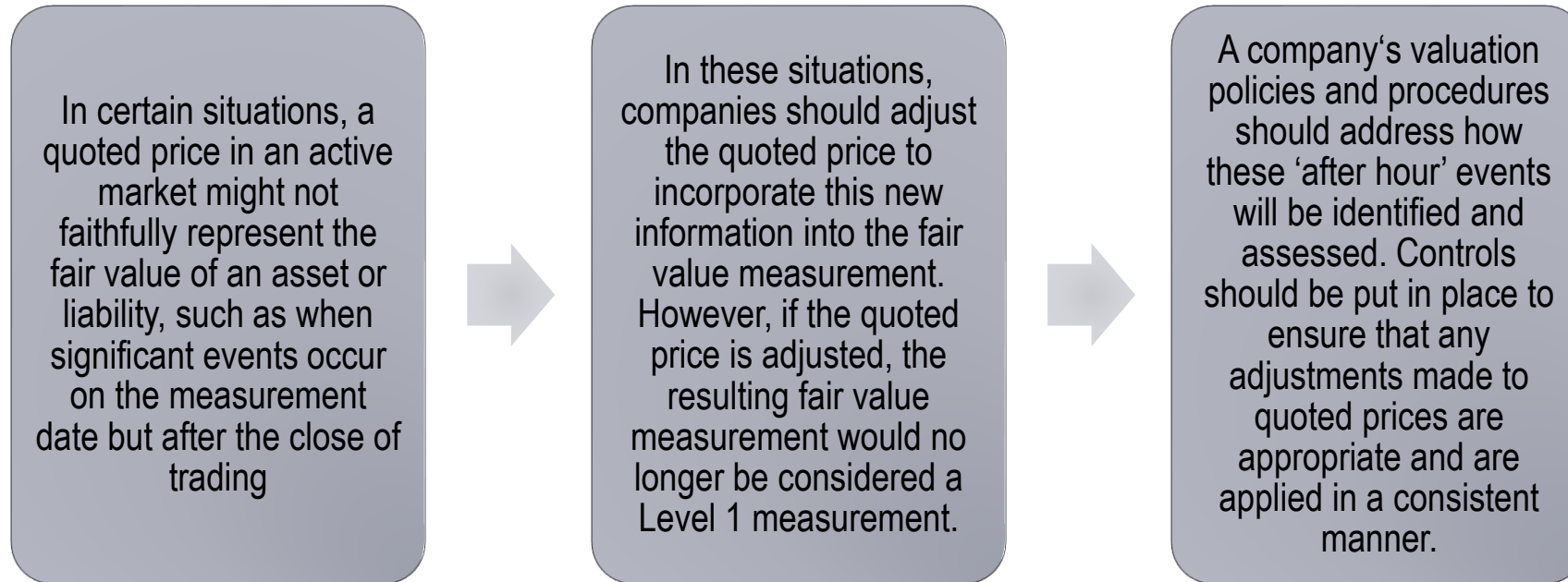
An entity has an investment in another entity which has no active market. However, some similar investment is being traded in an active market. Now, the fair valuation can be done based on either the prices based on the market which is not active or similar traded investment in an active market. This would be considered as level 2 inputs.

ICAI Examples



Valuation Techniques

ADJUSTMENT TO QUOTED PRICE WHEN IT DOES NOT REFLECT THE FAIR PRICE





Example 19: Page 4.102-4.103

A Ltd., a large biotech company with shares traded publicly, has developed a new drug that is in the final phase of clinical trials. B Ltd. has an equity investment in A Ltd.'s shares. B Ltd. determines that the shares have a readily determinable fair value and accounts for the investment at fair value through profit and loss. B Ltd. assesses the fair value as of the measurement date of 31 March 2020. Consider the following:

- (i) On 31 March 2020, the Drug Approval authority notifies A Ltd.'s management that the drug was not approved. A Ltd.'s shares closed at ₹ 36.00 on 31 March 2020.
- (ii) A Ltd. issued a press release after markets closed on 31 March 2020 announcing the failed clinical trial.
- (iii) A Ltd.'s shares opened on next working day at ₹ 22.50.

The drug failure is a condition (or a characteristic of the asset being measured) that existed as of the measurement date. B Ltd. concludes the ₹ 36.00 closing price on the measurement date does not represent fair value of the A Ltd.'s shares at 31 March 2020 because the price does not reflect the effect of the Authority's non-approval. The subsequent transactions that take place when the market opens are relevant to the fair value measurement recorded as of the measurement date. The opening price of ₹ 22.50 indicates how market participants have incorporated the effect of the non-approval on A Ltd.'s stock price. B Ltd. adjusts the 31 March 2020 quoted price for the new information, records the shares at ₹ 22.50 per share at 31 March 2020 and discloses the investment as a Level 2 measurement.

ICAI Examples



Valuation Techniques: Approaches to Valuation

Market Approach

- Uses prices and other relevant information generated by market transactions involving identical or comparable (i.e. similar) assets, liabilities or a group of assets and liabilities, such as a business.
- Using market multiples derived from a set of comparable companies e.g. EV/EBITDA or P/E multiple

Income Approach

- The income approach converts future amounts (e.g. cash flows or income and expenses) to a single current (i.e. discounted) amount i.e. DCF Method e.g. Gordon's formula
- Assumption of future cash flows and appropriate discount rate would be based on market participant's views. Related risks and uncertainty to be considered would be taken in cash flow or discount rate.

Cost / Asset Approach

- This method describes how much cost is required to replace existing asset/ liability in order to make it in a working condition. All related costs will be its fair value. It actually considers replacement cost of the asset/ liability for which we need to find fair value.
- For valuing a business / share, it may be the NAV.

Valuation Approach should be consistently followed. If there is a change in Valuation Approach, it shall be treated as a change in Accounting Estimate as per Ind AS 8 i.e. disclose the reason for such change.



Illustration 1: Page 4.99

Discount Rate assessment to measure present value

Investment 1 is a contractual right to receive ₹ 800 in 1 year. There is an established market for comparable assets, and information about those assets, including price information, is available. Of those comparable assets:

- a. Investment 2 is a contractual right to receive ₹ 1,200 in 1 year and has a market price of ₹ 1,083.
- b. Investment 3 is a contractual right to receive ₹ 700 in 2 years and has a market price of ₹ 566.

All three assets are comparable with respect to risk (that is, dispersion of possible payoffs and credit).

You are required to measure the fair value of Asset 1 basis above information.

ICAI Illustrations



Example 16: Page 4.100

An entity has estimated its next year earning (cash flow) based on certain probability as mentioned below:

Possible cash flow	Probability	Probability weighted cash flows
₹ 700	20%	140
₹ 800	40%	320
₹ 900	40%	360
	Total expected cash flow	820
	Risk free rate	6%
	Present Value of Cash Flow (1 year)	$820 / (1.06) = ₹ 773.58$

ICAI Examples



Question 3: Page 4.107

ABC Ltd. acquired 5% equity shares of XYZ Ltd. for ₹ 10 crore in the year 20X1-X2. The company is in process of preparing the financial statements for the year 20X2-X3 and is assessing the fair value at subsequent measurement of the investment made in XYZ Ltd. Based on the observable input, the ABC Ltd. identified a similar nature of transaction in which PQR Ltd. acquired 20% equity shares in XYZ Ltd. for ₹ 60 crore. The price of such transaction was determined on the basis of Comparable Companies Method (CCM)- Enterprise Value (EV) / EBITDA which was 8. For the current year, the EBITDA of XYZ Ltd. is ₹ 40 crore. At the time of acquisition, the valuation was determined after considering 5% of liquidity discount and 5% of non-controlling stake discount. What will be the fair value of ABC Ltd.'s investment in XYZ Ltd. as on the balance sheet date?

ICAI Test Your Knowledge



Question 4: Page 4.108

UK Ltd. is in the process of acquisition of shares of PT Ltd. as part of business reorganization plan. The projected free cash flow of PT Ltd. for the next 5 years are as follows:

(₹ in crores)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash Flows	187.1	187.6	121.8	269	278.8
Terminal Value					3,965

The weightage average cost of capital of PT Ltd. is 11%. The total debt as on measurement date is ₹ 1,465 crore and the surplus cash & cash equivalent is ₹ 106.14 crore.

The total numbers of shares of PT Ltd. as on the measurement date is 8,52,84,223 shares. Determine the value per share of PT Ltd. as per Income Approach.

ICAI Test Your Knowledge



Question 5: Page 4.108

You are a senior consultant of your firm and are in process of determining the valuation of KK Ltd. You have determined the valuation of the company by two approaches i.e. Market Approach and Income approach and selected the highest as the final value. However, based upon the discussion with your partner you have been requested to assign equal weights to both the approaches and determine a fair value of shares of KK Ltd. The details of the KK Ltd. are as follows:

Particulars	₹ in crores
Valuation as per Market Approach	5,268.20
Valuation as per Income Approach	3,235.20
Debt obligation as on Measurement Date	1,465.90
Surplus cash and cash equivalent	106.14
Fair value of surplus assets and liabilities	312.40
Number of shares of KK Ltd.	8,52,84,223 shares

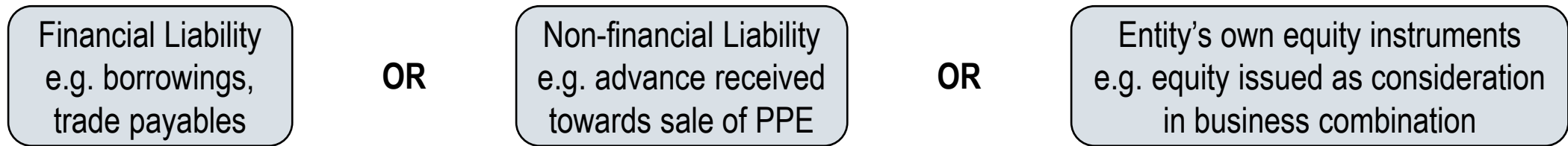
Determine the Equity value of KK Ltd. as on the measurement date on the basis of above details.

ICAI Test Your Knowledge



Applying Fair Value Rules to Liabilities and Own Equity

Assumption made while carrying out fair value measurement:



Transferred to a market participant at the measurement date

↓ Assumption under Ind AS 113

The liabilities and /or equity instruments so transferred will remain outstanding on the date of measurement



Standard prescribes to **use all observable inputs** (if direct quoted prices are not available) and should **minimize any unobservable inputs**. The **transaction** considered to find fair value **should be evaluated** in line with an **orderly transaction (not entity specific)**.

Ind AS 113 **specifically provides guidance** on the respective scenarios while evaluating fair values of the liabilities and own equity instruments in case **direct quoted prices are not available**.



Example 2: Page 4.84

A bank holds a debt obligation with a face value of ₹ 1,00,000 and a market value of ₹ 95,000. Assume that market interest rates are consistent with the amount in the note; however, there is ₹ 5,000 discount due to market concerns about the risk of non-performance by Counterparty I.

Settlement value

Counterparty I would be required to pay the face value of the note to settle the obligation, because the bank might not be willing to discount the note by the market discount or the credit risk adjustment. Therefore, the settlement value would equal the face value of the note.

Transfer value

In order to calculate the transfer value, Counterparty I must construct a hypothetical transaction in which another counterparty (Counterparty II), with a similar credit profile, is seeking financing on terms that are substantially the same as the note. Counterparty II could choose to enter into a new note agreement with the bank or receive the existing note from Counterparty I in a transfer transaction. In this hypothetical transaction, Counterparty II should be equally willing to obtain financing through a new bank note or assumption of the existing note in return for a payment of ₹ 95,000. Therefore, transfer value would be ₹ 95,000, and thus, fair value.

ICAI Examples



Applying Fair Value Rules to Liabilities and Own Equity

Liabilities and / or Equity Instruments of the entity

Held by other parties as assets

When a quoted price for the transfer of an identical or a similar liability or entity's own equity instrument is not available, an entity shall **measure FV of the liability / equity instrument from the perspective of a market participant that holds the identical item as an asset at the measurement date.**

Preference 1:
Use the quoted price in an active market for identical item held by another party as an asset, if available

Preference 2:
If quote price is not available, use other observable inputs such as quoted price in a market that is not active for the identical items held by another party as an asset

Preference 3:
If observable prices in (1) and (2) are not available, use a valuation technique such as income or market approach.

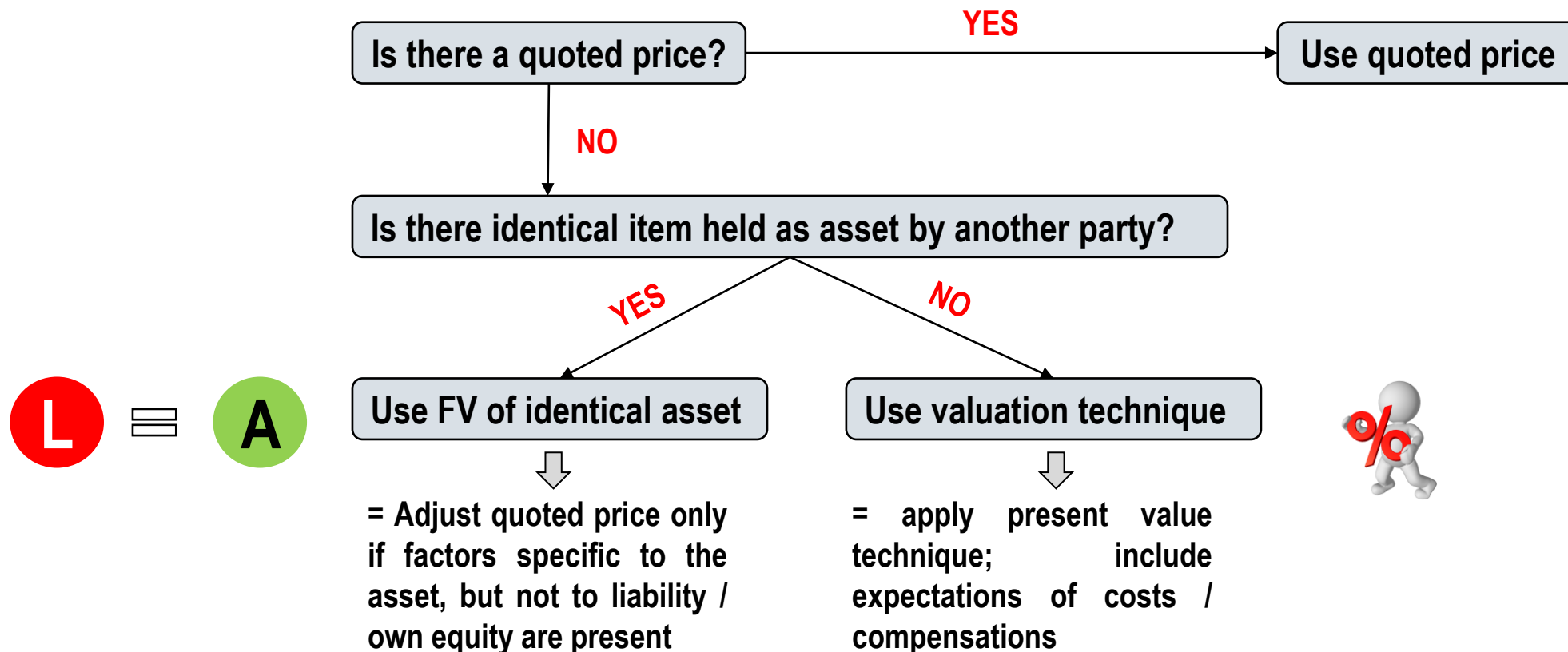
Not held by other parties as assets

When a quoted price for the transfer of an identical or a similar liability or entity's own equity instrument is not available, an entity shall **measure FV of the liability / equity instrument using a valuation technique from the perspective of a market participant that owes the liability or has issued the claim on equity.**



Applying Fair Value Rules to Liabilities and Own Equity

General Principles: \Rightarrow Assume **transfer** and **not settlement** of a liability / own equity instrument



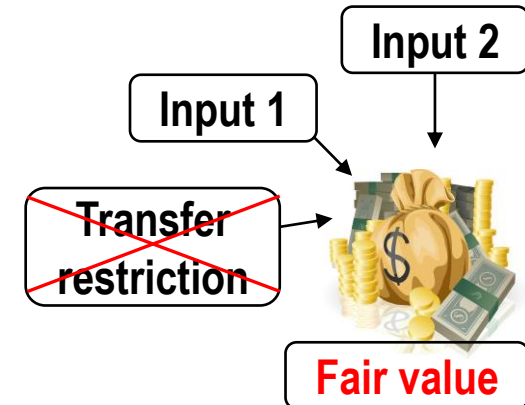
Applying Fair Value Rules to Liabilities and Own Equity

FV of liability reflects \Rightarrow **Non-performance risk**
(includes entity's own credit risk)



Transfer Restrictions

\Rightarrow no separate input / adjustment



FL with demand feature

\Rightarrow FV is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid



Example 22: Page 4.104

X and Y each enter into a contractual obligation to pay ₹ 500 in cash to D in five years. X has an AA credit rating and can borrow at 6%. Y has a BBB credit rating and can borrow at 12%. X will receive about ₹ 374 in exchange for its promise (the present value of ₹ 500 in five years at 6%). Y will receive about ₹ 284 in exchange for its promise (the present value of ₹ 500 in five years at 12%).

The fair value of the liability to each entity (that is, the proceeds) incorporates that entity's credit standing.

ICAI Examples



Applying Fair Value Rules to Financial Assets and Financial Liabilities with Offsetting Positions in Market Risks or Counterparty Credit Risk

Measurement exception



Financial assets and liabilities with offsetting positions

MARKET RISK



Trade Receivables (USD)



FX loss



Liabilities (USD)



FX gain



FV on net basis:

CHOICE

Price receivable to sell net long position

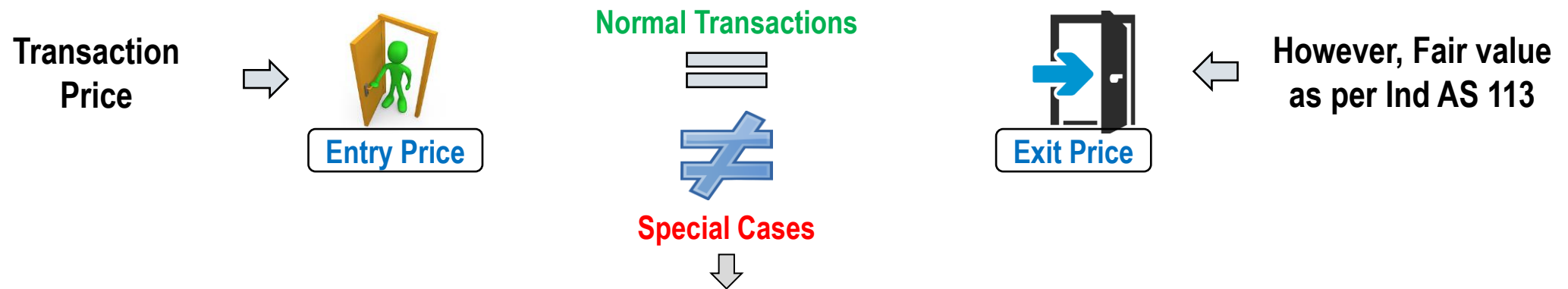
Price payable to transfer net short position

1. Documented risk management / investment strategy
2. Info to key managerial personnel
3. FV at the end of each reporting period



Fair Value at Initial Recognition

- Normal Transaction
- An entity (A Ltd.) acquires an asset or assumes a liability (from B Ltd.) in a normal market transaction
 - A Ltd. enters the transaction, and B Ltd. exits the transaction, and therefore:



I. Related Parties



II. Under duress / seller forced



III. Different unit of account

IV. Not on principal / most advantageous market



Transaction Price – Fair Value = Day 1 PROFIT → Recognize in P/L, if cannot be attributed to Transaction Costs



Practical Problems

Question 2:

Rohini Ltd., a listed company, owns an asset that is traded in different markets, which has to be valued at fair value under Ind AS. Rohini Ltd. currently only buys and sells the asset in the Maharashtra market. The information relating to the asset is as under:

Year to 31 March 20X2	Kerala market	Rajasthan Market	Maharashtra Market
Volume of the market - units	40,00,000	20,00,000	10,00,000
Price	₹ 1,330	₹ 1,120	₹ 1,540
Costs of entering the market	₹ 140	₹ 140	₹ 210
Transaction costs	₹ 70	₹ 140	₹ 140



Practical Problems

Question 2 (continued):

Additionally, Rohini Ltd. acquired an entity on 31 March 20X2 and is required to fair value a decommissioning liability. The entity has to decommission a mine at the end of its useful life, which is in three years' time. Rohini Ltd. has determined that it will use a valuation technique to measure the fair value of the liability. If Rohini Ltd. is allowed to transfer the liability to another market participant, then the following data would be used.

Input	Amount	Input	%
Labour and Material Cost	₹ 14,00,00,000	Annual Inflation Rate	5%
Overheads	30% of labour and material cost	Risk adjustment – cash flow uncertainty	6%
Third-party markup –industry average	20%	Risk-free rate of government bonds	4%
Entity's non-performance risk	2%		

Required:

Discuss, with relevant computations, how Rohini Ltd. should measure the fair value of the above asset and liability under Ind AS 113.



Disclosures

- An entity shall disclose information that helps users of its financial statements assess both of the following:**
- (a) for assets and liabilities that are measured at fair value on a recurring or non-recurring basis in the balance sheet after initial recognition, the valuation techniques and inputs used to develop those measurements.**
 - (b) for recurring fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period.**

REFER TABLE IN STUDY MODULE FOR DETAILED DISCLOSURES



THANK YOU