PSAK 68: MEASUREMENT OF FAIR VALUE IFRS CONVERGENCE Fair Value Concept

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Abstract

Purpose - This study aims to find out about the concept of fair value in PSAK 68: IFRS Convergence Fair Value Measurement, as a substitute for book value. The convergence of the application of new accounting standards is oriented towards the International Financial Reporting Standard (IFRS) issued by the International Accounting Standard Boards (IASB). In this new accounting standard, the concept of fair value is emphasized more than the concept of book value. This is what makes the difference and triggers this convergence to change the simpler book value model

Design/methodology/approach - This study uses a descriptive qualitative method with a literature study approach on fair value measurement.

Finding - The result of this study is the concept of fair value (fair value) that is currently considered to have an advantage over book value is a concept that is widely applied all over the world, as well as with accounting in Indonesia should be ready to apply the concepts of reasonable value in its accounting standards

Originality -

Keyword - IFRS, PSAK 68, Fair Value

Paper Type – Research Paper

Introduction

Accounting is a business language agreed upon by all parties as a tool for measuring the financial performance of a business organization and used as a basis for making business decisions by all related parties (stakeholders), so that the financial reports presented must be impartial, reliable and timely. As time goes by, accountants find many gaps in existing financial reporting approaches to commit fraud. This is one of the causes of the emergence of new principal based accounting regulations, namely IFRS (International Financial Reporting Standard).

In Indonesia, the IFRS convergence plan was first declared by the Indonesian Accountants Association (IAI) in 2008. IAI plans to fully converge PSAK to IFRS in 2012. It is targeted that in 2012, all PSAK will have no material differences with IFRS in effect as of January 1 2009 (Farida and Sirajudin, 2011). The fair value concept was then adopted into international accounting standards and came into effect for the first time in 2003.

IFRS convergence can increase the information power of the financial reports of companies in Indonesia. Adoption of international standards is also very important for economic stability. Basically, the adoption of international accounting standards into domestic accounting standards aims to produce financial reports that have a high level of accountability in running the company. Apart from that, company financial reports are also expected to produce more relevant and accurate information, so that financial reports will be more comparable and produce valid information for company assets, debt, equity, income and expenses (Petreski, 2005).

In accounting terms, fair value is described as the estimated value of various assets and liabilities that must be recorded in the books. Fair value refers to the amount for which an asset such as a product, stock, security, or property can be sold or a liability settled at a price that is fair to the buyer and seller. Fair value is the highest price an asset will sell on the free market based on its current market value. This means the buyer and seller know each other, are motivated to sell, and there is no pressure to sell (as in the case of company liquidation). The fair value of an asset or liability is ideally derived from observable market prices of similar transactions.

The Indonesian Statement of Financial Accounting Standards (PSAK) emphasizes that asset valuation must use fair value, so entities must follow this from the previous implementation. Financial reports present financial conditions using a historical cost approach. However, the presence of PSAK 68, which is the result of the adoption of IFRS 13, means that several financial statement items must be measured using the fair value approach.

According to the general chairman of the Indonesian Appraisal Professional Society (MAPPI) Hamid Yusuf, quoted from the third edition of the Indonesian Accountant Magazine, No. 16, the first to introduce the concept of fair value were Australia, England and countries that were former British colonies. This concept was first used to calculate biological assets in plantation and livestock companies in Australia and England.

Before the use of International Financial Reporting Standards (IFRS), accounting in Indonesia used historical costs to measure transactions. As time goes by, the use of historical costs is no longer relevant because the credibility and usefulness of financial reports has been hampered by serious challenges. And many people think and believe that accounting standards that use historical costs play an important role in causing economic damage, this was expressed by

Shanklin, Hunter and Ehlen (2011), especially savings and loan institutions in the 1980s and banking problems in the 1990s. In conditions of global money and capital markets which are increasingly dynamic and developing very quickly, the concept of historical cost is no longer considered suitable, because it does not reflect market value. Instead, the fair value concept set by the International Accounting Standard Board (IASB) is used as the basis for measuring assets.

Research methodology

In this research, the methodology used is descriptive qualitative research with a literature study approach regarding fair value measurement.

Findings

Statement of Financial Accounting Standards (PSAK)

In accounting, there are rules or standards that are enforced to ensure that all financial reports comply with applicable standards and make it easier for users of financial reports. This standard is known as PSAK or Statement of Financial Accounting Standards. PSAK is a guideline used to prepare financial reports based on applicable accounting standards. Indonesian Financial Accounting Standards (PSAK) is a framework of accounting procedures for presenting accounting financial reports which consists of standards for recording, preparing, treating and providing financial reports. This statement was made and compiled by the Indonesian Accountants Association (IAI). The aim of PSAK is to create financial reports that can be presented clearly, understandably and similarly. Its use is to help users of financial reports understand it more easily and financial reports will be easier compared to previous reports because the writing and recording standards are the same.

IFRS Convergence

According to Warren, et al (2014) International Financial Reporting Standard (IFRS) is a set of global accounting standards developed by the International Accounting Standards Board (IASB) for the preparation of company financial reports. The IASB is an independent body that makes accounting regulations. The IASB does not make accounting regulations for a particular country but rather makes accounting regulations that can be used by various countries with the aim of developing a set of global accounting standards. IFRS is used for companies that issue trade debt and securities for equity to the public, which are called public companies.

The convergence of PSAK to IFRS is one of the regulations regarding accounting standards in Indonesia. The aim of IFRS convergence is to increase transparency and accountability in financial reports and to increase global investment flows through comparison of financial reports between one country and another. According to Warren, et al (2014) Since 2005, 27 countries in Europe (EU) have been required to present financial reports using IFRS. In addition, more than 100 other countries have adopted IFRS for their public companies. In advanced economies, Japan is considering mandatory

adoption in 2016, India is allowing limited use of IFRS, and China is converging its standards with IFRS over time. In Australia, local government entities showed a significant increase in liabilities after the implementation of IFRS (Ahmed and Alam, 2012) in (Kristanti, 2013). The same thing happened in New Zealand, the average total assets, total liabilities and net profit were higher after adoption (Kabir et el, 2010) in (Kristanti, 2013).

Indonesia, which was previously more inclined towards accounting standards issued by the FASB, since 1994 has begun to harmonize and move closer to IFRS. According to Warren, et al (2014) Indonesia officially adopted IFRS for Indonesian companies since 2008 and was effectively implemented in 2012. The wide acceptance that IFRS has gained throughout the world, however, has put great pressure on Indonesia to align SAK with IFRS. Therefore, Indonesia needs to achieve convergence of SAK and IFRS. However, the application of IFRS must be carried out carefully because it does not rule out the possibility that it will cause conflicts with various aspects. In IFRS new approaches are developed in making financial reports. For example, increased disclosure of qualitative transaction information, regulations for financial reporting using principal based, namely principles that emphasize professional judgment rather than rule based where accountants prepare financial reports based on principles that are regulated in detail, as well as the elimination of certain items, presentation the financial statements are changed to reflect the nature of the financial statements, and the use of a fair value measurement approach. With this global standard, universal comparability and exchange of information is possible. IFRS convergence can increase the information power of financial reports companies in Indonesia. Adoption of international standards is very important for economic stability. The benefits of the IFRS convergence program are expected to reduce investment barriers, increase company transparency, reduce costs associated with preparing financial reports, and reduce the cost of capital. This convergence process will bring major changes in financial reporting practices in Indonesia from previously referring to historical cost accounting to referring to fair value accounting. This change occurs because several IFRS/IAS standards use a fair value measurement basis.

PSAK 68: Fair Value Measurement
Fair Value (Fair Value)
According to (IAI, 2014) in the explanation of PSAK 68, fair value is the price that will be received to sell an asset or the price that will be paid to transfer a liability in an orderly transaction between market participants on the measurement date. This fair value is used to measure such as one asset, a group of assets, one liability, a group of liabilities, the net consideration of one or more assets less one or more related liabilities, one segment or division of an entity, one location or region of an entity, one the entire entity. The IFRS International Financial Standards Board has stated that fair value is the only concept that is relevant in the business world. Their opinion in IFRS–Wiley 2010 is that

fair value accounting can increase transparency of information conveyed to the public, fair value information is the main information in the current economic situation, and fair value will provide more current information to creditors and investors.

The scope of PSAK 68 is that this statement is applied when other statements require or permit measurements or disclosures regarding fair value (and measurements such as fair value after deducting costs to sell), based on fair value or disclosures regarding measurements. The except as described in paragraphs 06 and 07.

The scope of the exception is as explained in Book 2 of SAK 2015, namely: Measurement and disclosure:

1. Share-based payment transactions within the scope of PSAK 53: Share-Based Payment;
2. Rental transactions within the scope of PSAK 30: Leases
3. Measurements that have some similarities to fair value but are not fair value, such as net realisable value in PSAK 14: Inventory or value in use in PSAK 48: Impairment of Asset Value.

   Disclosure:
1. Program assets measured at fair value in accordance with PSAK 24.
2. Investment in retirement benefit programs measured at fair value in accordance with PSAK 18.
3. Assets whose recoverable amount is the fair value after deducting disposal costs in accordance with PSAK 48.

Fair value is the price that would be received to sell an asset or the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Assets or Liabilities
Fair value measurements are for specific assets or liabilities. Therefore, when measuring fair value an entity takes into account the characteristics of the asset or liability if market participants will take those characteristics into account when determining the price of the asset or liability at the measurement date. These characteristics include:

1. Based on the location of the asset in a strategic location and the condition of the asset
2. Use of the asset or sale of the asset itself.

The measurement impact arising from a particular characteristic will differ depending on how that characteristic is taken into account by market participants. Assets or liabilities measured at fair value may consist of any of the following, namely, stand-alone assets or liabilities and a group of assets, a group of liabilities or a group of assets and liabilities.

Transaction

Fair value measurements assume that the asset or liability was exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions.

Fair value measurement assumes that a transaction to sell an asset or transfer a liability occurs:

    a. In the primary market for the asset or liability; or

    b. If there is no primary market, the most profitable market for the asset or liability.

If there is a primary market for the asset or liability, then the fair value measurement represents the price in that market, even if the price in a different market is potentially more favorable at the measurement date.

Market players

An entity measures the fair value of an asset or liability using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants are acting in its best economic interests.

In developing these assumptions, an entity does not need to identify specific market participants. Instead, it identifies characteristics that differentiate market participants generally, considering factors specific to all of the following:

    a. Assets or liabilities

    b. The main market or most profitable market for the asset or liability

    c. Market players who will carry out transactions with entities in that market.

Price

Fair value is the price that would be received to sell an asset or the price that would be paid to transfer a liability in an orderly transaction in the primary or most profitable market at the measurement date under current market conditions, that is, the exit price regardless of whether the price is directly observable. or estimated using other valuation techniques.

Assessment Techniques

As explained in PSAK 68, the valuation technique in reducing fair value is that an entity uses production techniques that are appropriate to the circumstances and adequate data to measure fair value, maximizing the use of observable and relevant inputs and using unobservable inputs. The aim is to estimate the price at the time of transaction or transfer of liabilities that will occur between market participants on the measurement date under current market conditions. Apart from that, there are three approaches that can be used, namely the market, cost and income approaches.

The techniques used to measure fair value are applied consistently. However, a change may occur if the change results in a measurement that is the same or shows a better fair

value. The valuation technique used to measure fair value uses observable inputs and uses unobservable inputs.

In some relevant cases the entity may provide a premium or discount. However, fair value measurements do not include premiums or discounts that are inconsistent with the unit of account in the requiring or recommending statements

fair value measurement. In all cases, if there is a quoted price in an active market for the asset or liability, the entity uses that price unmeasured when measuring fair value.

If there is a bid price and an ask price, then the price in the bid-ask spread that represents fair value in that situation is used to measure fair value, regardless of where the input is categorized in the fair value hierarchy. This Statement does not prescribe mid-market pricing (mid-market pricing) or pricing conventions that market participants use as a practical guide to measuring fair value in bid-ask spreads.

Fair Value Hierarchy

To increase consistency and comparability in fair value measurements and related statements, the fair value hierarchy categorizes into three levels of input for techniques used in fair value measurements, namely input level 1, input level 2, and input level 3.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity has access to at the measurement date. Quoted prices in active markets provide the best evidence of fair value and are used without measuring the available fair value.

Level 1 inputs will be available for most financial assets and financial liabilities, some of which are fungible in some active markets. Therefore, the settings at level 1 are to determine two things, namely, the primary market for the asset or liability and whether the entity can carry out transactions for the asset or liability.

An entity does not make adjustments to level 1 inputs except in the following circumstances:

1. When an entity has a large number of similar assets or liabilities measured at fair value and a reasonable price in an active market is available but not accessible for each such asset or liability individually.
2. When quotations in an active market do not represent fair value at the measurement date.
3. When measuring the fair value of an entity's own equity instruments.

If there is a sequence of assets or liabilities in an active market then the fair value of the asset or liability is measured at level 1 as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This applies when the normal daily trading volume in the market is unable to absorb the quantity held, and placing an order to sell in a single transaction can affect the quote.

Level 2 input , namely input other than quoted prices included in level 1 that can be observed for assets or liabilities, either directly or indirectly. If an asset or liability has

specific (contractual) terms, then level 2 inputs must be observable for a substantial total period of the asset or liability. Input Level 2 includes the following

1. Quoted prices for similar assets or liabilities in active markets.
2. Quoted prices for identical or similar assets or liabilities in an inactive market.
3. Inputs other than observable quoted prices for assets or liabilities.
4. Inputs that take the market (market-boosted inputs).

Adjustments to level 2 inputs will vary depending on factors specific to the asset or liability. Such factors include things such as the condition or location of the asset, the degree to which the asset or liability is related, and the volume or level of activity at which the input can be observed.

Level 3 inputs are unobservable inputs for assets or liabilities. It is used to measure the fair value of relevant observable inputs that are not available. Fair value measurements remain the same. Therefore, unobservable inputs reflect the assumptions that market participants would use when pricing an asset or liability, including assumptions regarding risk.

Risk assumptions include inherited risks in measurement techniques used to measure fair value and inherited risks in inputs to the techniques. Measurements that do not account for risk will not represent fair value assessments if market participants were to calculate tables that determine prices or valuations.

An entity may develop unobservable inputs using information available in the circumstances, which may include the entity's own data. In developing unobservable inputs, an entity may start with its own data, but will need to adjust that data if information is generally available that other market participants would use different data or there is something specific about the entity that is not available to other market participants.

An entity determines the appropriate asset and liability classes according to the nature, factors and risks of the asset or liability and the level of the fair value hierarchy at which the fair value measurement is categorized. An entity consistently discloses and follows its policies in determining when movements between levels of the fair value hierarchy are deemed to have occurred.

The policy regarding when to acknowledge a move is the same for moves into the level and for moves out of the level.

For each class of assets and liabilities that are not assessed at fair value in the statement of financial position, for these assets and liabilities, the entity does not need to provide other required disclosures as stated in PSAK 68 regarding fair value measurements. For liabilities measured at fair value and issued with an inherent improvement in third party credit quality, the issuer discloses the existence of the credit quality improvement and whether it has been reflected in the fair value measurement of the liability. An entity

presents the required quantitative disclosures in tabular format unless another format is more appropriate.

Fair Value Concept

The concept of fair value as stated in PSAK 68 is considered to better reflect the current economic reality. The fair value in PSAK 68 is more about the exit price, rather than the transaction price. In this concept, fair value measurement assumes that transactions to sell assets or transfer liabilities occur in the principal market for the asset or liability, or if there is no principal market, then in the most profitable market.

The concept of fair value, which is currently considered to have advantages compared to book value (historical cost) and has replaced book value which has been the basis used in measuring fixed assets or other financial items, is a concept that is widely applied throughout the world. . A business organization that wants to grow and develop into a global, public or multinational company must be ready to apply the fair value concept in its accounting. There are 5 things that companies need to do in an effort to adapt to the fair value concept, namely:

1. Try to understand and deepen the concept of fair value accounting.
2. The business company prepares a gap analysis to understand what must be done to close the gap between current practices and what must be done in applying fair value.
3. Companies must develop information systems that accommodate new standards that apply fair value.
4. The Company improved its information technology system to accommodate requests for applying fair value.
5. The company carries out trials with parallel runs until it is confident that the new system is ready to go live.

These five things must receive full support from top management by considering the use of consultant services to help everyone. Determining fair value using a market price approach can predict a company's profit/loss. In general, the application of fair value will benefit the Indonesian economy. Because, if a fair value assessment is not carried out, national economic assets, both those owned by the private sector and the government, have so far been valued too low, far lower than their fair value. For example, plantation company assets currently still use book value.

Compared to book value/cost, fair value has three advantages, namely that financial reports are more relevant for basic decision making, increase the comparability of financial reports, and the information is closer to what users of financial reports want. The fair value concept makes financial reports more transparent, fair value seeks to increase the provision of more transparent information for all parties. In addition, fair

value increases comparability. By applying the concept of fair value to all companies in the world, all financial reports have very high comparability and will result in more fundamental business decisions. The disadvantage of fair value is that fair value attempts to provide transparent information by valuing assets at the price level that would result if they were immediately liquidated, so it is very sensitive to the market.

Table and Figure
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