THE EFFECTS OF FAIR VALUE MEASUREMENT ON LONG TERM ASSETS

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Abstract

The objective of this study is to address fixed assets at fair value and after the adoption of the accounting system starting from January 2018 by reviewing the basic concepts of accounting measurement and its models of historical cost and fair value and what requirements are required in the Palestinian accounting environment, moreover, the various difficulties encountered in the application of fair value when measuring stability.

In order to achieve the objectives of the study, we took the SLC company as an applied case, as we relied on obtain information from the accountants of the company, in addition to the Palestinian market, and we reached a number of results, the most important of which is that use of fair value depends on many factors and the creation of a number of conditions, and as a result of the recent development that the world witnesses, and the changes in the economic circumstances, it is important to reach an optimal method adapts with this development, so, it became clear that the fair value method is the best in measuring financial events.

Introduction

In order to keep pace with global economic developments and changes in international accounting standards; Most countries strive to achieve global accounting standardization by adopting their financial and accounting reforms. However, some of these reforms do not recognize the application of the texts of international accounting standards in absolute terms, especially those standards related to accounting measurement and disclosure, but rather are adapted to the economic reality of each country. Among the reasons for the lack of absolute adoption of international accounting standards is the difference in the level of scientific and practical qualification between countries, especially in the economic, financial and accounting fields, in addition to the difference in the level of development companies have reached from one country to another.

Recently, and as a result of the development in economic events, the International Accounting Standards Board called for adopting a new measurement method, as the historical cost method became an old method and does not express the real financial position of the institutions, however, the International Accounting Standards Board issued ifrs13 as an attempt to prove the importance of adopting the fair value method, and called all companies around the world

to follow this standard, as it came to address the accusations against this method, and solving the criticisms directed to it.

The Purpose Of The Study

The study aims to :

1. Defining of fair value accounting in general, and the International Financial reporting standards (IFRS 13) and its role in facilitating the measurement of fair value.
2. Knowing the effect of applying the accounting measurement on the basis of fair value.
3. Providing a theoretical framework for the procedures that can be implemented when applying the fair value measurement.
4. Learning about opinions on revaluation of fixed assets at fair value and learn about valuation methods**.**

Research Methodology

This research has been applied to the long term assets for a Palestinian company, the research will present 2018 long term assets that has been prepared on the basis of the historical cost, then the values of long term assets components will be adjusted by using the fair value measurement after taking into consideration the method of calculating the fair value of each component, then the comparison and differences will be made between the fair value and historical cost to prove which is better between the two methods to show the real information related to the balance sheet components.

Research Design And Limitation Of The Study

The researcher will use the deductive approach through theoretical analysis of previous studies and researches. At the academic level, it will address the measurement of fair value in addition to the international financial report standard (IFRS 13), and at the professional level which required the corporation to use the fair value method as a model for measurement and disclosure in order to reach logical conclusions about the importance of information on levels of fair value measurement.

Data Sources

1. Main Sources

Data and information of the company's balance sheet with the information included in the Annual Financial Reports published by the company for the year 2018.

2. Secondary Sources

Books, scientific references, researches and related articles.

3. Data collection method: gathering and analyzing data and the information of the company.

Applied Study- Applying Fair Value Measurement On Long Term Assets Of Slc Company

In this study, the focus is on reevaluating the most important elements of the budget (financial position statement) by using fair value method instead of the method used by SLC Company which is historical cost method, as well as trying to achieve the objectives of the study, which aspires to know the role of fair value in producing reliable and appropriate information for making the right decisions.

Based on the above, this study will cover the following points:

- Showing the long term assets before the amendment.
- Applying Fair Value Method.
- Comparison between historical cost and the new method which is fair value method.

Long Term Assets

Table 1: Long term assets

Account	Amount in 1/1/2018	Addition	Value in 31/12/2018	Depreciation Rate	Current depreciation	Accumulated depreciation	Net value 31/12/2018
Land	151460	0	151460	0	0	0	151460
Buildings	768628	0	768628	4%	30745	492538	276090
Machines	575839	0	575839	7%	0	575838	1
New Machines	321965	94140	416105	7%	29128	129050	287055
Trucks	78170	6280	84450	10%	8445	84449	1
Work Tools	18260	0	18260	20%	3652	15220	3040
Electric Motor	13890	300	14190	10%	300	14189	1
Computers	30050	630	30680	20%	630	30679	1
furniture	15970	680	16650	10%	680	16649	1
PBX & FAX	5635	0	5635	25%	0	5634	1
Elevator	20050	0	20050	5%	1002	13845	6259
Electricity Network	53285	0	53285	10%	0	53284	1
Extinguishers	5025	0	5025	10%	0	5024	1
Scales	6180	0	6180	20%	0	6179	1
Laboratory	10975	0	10975	10%	0	10974	1
Total	2075382	102030	2177412		74582	1453552	723914

We notice from the table that the value of lands is still fixed as a result of using the historical cost method, and the value of many items and equipment are entirely finished, but the company is still using them. The company puts 1$ as a net value of expired items instead of 0$ to continue using them in the future, and the net value of non-monetary items was 723914$ at the end of 2018, this value does not represent the true and real value of these items.

- **Applying Fair Value Measurement to evaluate the elements of the balance sheet**

This method aims to reassess the elements of long term assets of SLC Company for the year 2018 which prepared on the basis of the historical cost method, this is through re-evaluation of the elements that had a market value, and therefore we can re-evaluate them. As for the rest of the elements that have not been re-evaluated, they are not re-evaluated because it reflects a current value.

1. Lands

The Arab Paints Company owns land of 1000 m^2, the market approach has been adopted to calculate the price of the land.

- Administrative position (valid for building and construction or not).

Depending on the specialists in the assessment field, real values of lands were taken to calculate the market price per square meter, the value of 230$ has been taken from the Real Estate Appraisal Authority by relying on the previous factors.

The market value of land = land area * Price per m^2

And the next table explains the accounting process:

Table 2: **Re-evaluation of land**

Account	Area (m^2)	The Price per m^2	Market Value
Lands	1200 m^2	230$	276000$

2. Buildings

The building of SLC Company has 25 years (useful life), 9 years represents the residual life (16 years used), where the Age-life Method was used to calculate the depreciation. The building area is 1000 m^2, and to calculate the market price of the company building, $1200 was taken from a table prepared by the Real Estate Appraisal Authority in Palestine based on several factors.

The net value of the building = replacement cost - depreciation + land value
= (building area * price/ m^2) - depreciation + (land area * price / m^2)

Table 3: Re-evaluation of buildings

Account	Price per m^2	Building Area	Building Value	Depreciation Rate 16/25	Depreciation Value	Land Value 1000 m^2 * 230 $	Net Value
Building	1200$	1000 m^2	1200000$	64%	(768000) $	230000$	662000$

After the re-evaluation of land and building, we divided the remaining items into items that re-evaluated in accordance with the cost approach and items that are re-evaluated in accordance with the market approach.

1. Items are re-evaluated based on market approach

Table 4: Re-evaluation of non-current assets according to market approach

Items	Current Market Value
Cars	20000$
Motors	3900$
Laptops	4100$
PBX	1800$
Scales	2300$

We notice from the table that the most of the items value increased, as a result of using fair value method, as this method takes into account the change in prices.

2. Items are re-evaluated based on cost approach

Table5: Re-evaluation of non-current assets according to cost approach

Items	The price of similar new items	Accumulated Depreciation	Net Value
Work Machines	660000$	575838$	84162$
New Work Machines	419000$	129050$	289950$
Tools	21300$	15220$	6080$
Furniture	18300$	16649$	1651$
Lift machine	22350$	13845$	8505$
Fire Tools	5300$	5024$	276$
Lab	13900$	10974$	2926$

We notice from the previous table that there are elements that did not have value, because they were consumed entirely, but the company is still using them in the production process, and this is the main defect in the historical cost method, also there is equipment that has value in the schedule before the revaluation process, but its value increased as a result of the change in prices in recent years, as this is one of the advantages of fair value.

- **Comparison between historical cost and fair value methods**

Table 6: Comparison between historical cost and the fair value methods

Account	Evaluation According to the Historical Cost Method			Re-evaluation according to Fair Value Measurement
	Value in 31/12/2018	Accumulated depreciation	Net value 31/12/2018	Net Fair Value
Land	151460	0	151460	276000$
Buildings	768628	492538	276090	662000$
Work Machines	575839	575838	1	84162$
New Work Machines	416105	129050	287055	289950$
Cars	84450	84449	1	20000$
Tools	18260	15220	3040	6080$
Motors	14190	14189	1	3900$
Laptops	30680	30679	1	4100$
Furniture	16650	16649	1	1651$
PBX	5635	5634	1	1800$
Lift Machine	20050	13845	6259	8505$
Fire Tools	5025	5024	1	276$
Scales	6180	6179	1	2300$
Lab	10975	10974	1	2926$
Total	2177412	1,453,552	723914	1363650$

Through the table, we can see that there are additional amounts added to the items of long term assets because of using the fair value, and this because that the fair value addresses the problem of change in power of cash, and this method uses one of three approaches to determine the actual value of element in the market. These approaches are: market, replacement cost and income approaches, as we used both market and replacement cost approaches.

The total value of long term assets was 723914 $ at the end of year 2018, while using of fair value method increased this value to 1363650 $, and the difference between the two amount is 639736 $. This amount increases the value of the company, and the entry of this transaction is:

Debit: Depreciation Expense 639736 $

Credit: Retained Earnings 639736 $

Conclusion

It has been found through the research that the historical cost method has become unworthy of use, especially as a result of the development in recent years, as it was found that its use misleads and reduces the delivery of necessary and necessary information to users of financial reports, where we found that the use of historical cost executes the value of some assets, while the company is still using these assets in production, while the use of the fair value shows in detail the true value of the assets, and reflects the value of the current assets without misleading the users of the financial statements, as it takes into consideration the change in power of cash from time to time, while the historical cost method does not consider that.