FAIR VALUE: UTILITY AND LIMITS

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This paper presents the utility and the limits of the fair value. We believe that any new product must be tried and tested before being imposed on the market and must be accepted by all potential users and those who will be affected, directly or indirectly and its advantages, disadvantages, risks, its cost must be predetermined and analyzed in a comprehensive and objective.We ask: Do financial statements at fair value meet users' expectations? The requirement to use fair value pricing model that was carrying was not accompanied by a parallel examination of its impact on the presentation of accounts.

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1. Introduction

We ask ourselves: Do financial statements at fair value meet users' expectations?

Now, if, in a first step, we must admit that meet the needs of investors and that between these requirements include, in particular, knowledge of the effects of market developments on the net assets of the company and its results, the value fair must be recognized as useful and necessary.

We also ask ourselves: Whether is it necessary to make a fair value accounting model, while information can be provided in the financial statements in a form and in a manner which does not affect the same accounts ? We consider that such information had less quality and reliability, if it was given direct deposit accounts markings.

But it should be noted that in many countries, the financial statements are defined as being intended primarily for the use and satisfaction of investors. We note this case in France .

The role of accounting information in the financial statements is to respond, on the one hand, micro-economic needs (for internal business leaders, especially in terms of knowledge of costs, the price of return, sources of information to verify the achievements and foundations reference to make estimates and forecasts for key management itself - external capital providers and third parties dealing with enterprises), on the other hand, especially for macro-state enterprises accounts are an indispensable tool to know the nation's economy and guide economic policy.

After thus extend the scope of the financial statements, it is clear that the incidence accounting models used are of major significance and their interpretation.

Internally, on the one hand, macroeconomic, on the other hand, any assessment that is not important than short term loses much of its interest and usefulness. Therefore, the fair value (ie market value of a particular day) assets and liabilities of the company from a management perspective and analysis on medium or long term is not significant.

2. Financial statements and fair value

Businesses and credit institutions are managed by their leaders based on short-term indicators, obsolete quickly. Their performance analysis can not be performed based on figures worthless (significant) on a specified date, but outdated and therefore useless the next day. Historical cost meanwhile retains validity throughout the life of the instrument.

Although there it is one of the most fundamental criticism to the extent that an accounting model whatever could affect the management of enterprises, on the contrary, will accurately reflect reality (based, of course, partly on conventions which have the advantage of to be consistent and permanent), we find it useful to develop in detail as it seems acceptable to many people concerned.

We also ask ourselves: Are financial statements based on fair value? We believe that consequences on the financial statements of the fair value were not sufficiently analyzed.

The requirement to use fair value pricing model that was carrying was not accompanied by a parallel examination of its impact on the presentation of accounts. It seems to be a quick response (if

not earlier) the anxiety born of exponentially growing use of financial instruments not recorded in the accounts (derivatives) and risks as a result of fundamental reflections on the advantages and disadvantages of this new model accounting.

Also, we want to prove the existence of the so-called "joint working group" created at the initiative of the American standardization bodies; Australian, British, Canadian and IASC and added that representatives from other countries (Germany, France, Japan) and responsible for examining a longer-term project on the generalized application of fair value.

This means, first, that those who take the initiative now to impose any fair value measurement basis of all or part of the financial instruments it implicitly acknowledge that they are not sure of the validity of their model, on the other hand, the decision Their was taken before the whole issue is put and resolved.

Thus, we believe in a fair value model, the design of the profit must be completely rethought. This has not been done today, and we must ask ourselves reading that can be made tax returns to their old format and therefore their understanding.

Concluding this section, we state that:

- whether the financial statements are intended mainly for investors, demonstration has been made that they wanted to have this information in the accounts; therefore, impose fair value accounting model is not justified;
- financial statements are not in any case and in many countries, only to meet the needs of investors and, in this framework, the fair value model is not only justified, but is likely to adversely affect business management remains founded usually on a long-term strategy.

3. Is this the end of the income statement?

Extensive application of "fair value" of all assets and liabilities in the balance sheet involves two major and interrelated consequences:

- abandoning performance criterion
- loss of income base for transactions

These two results refer to the income statement. Evaluation of the "fair value" is based on a vision that an asset is sold and a liability settled a debt steadily. This is a result virtual "continuous" because there is no actual transaction, the market provides information about what could be in terms of "going back". No need to register completion of an operation to validate its cost accounting "current" because the market offers monitoring of asset prices traded in the market (and in the absence of market techniques would lead to an amount equivalent to what would be on the market) .

The disappearance performance criterion involves abandoning the principle of historical cost and also the principle of prudence, to the extent that unrealized gains are caught in the account automatically (unrealized losses are in principle included mandatory historical cost).

Two companies (holding companies) have a portfolio of securities. First (A) made on 31 December in portfolios of securities and buy 1 January n + 1 ("round-trip"). The second (B) retains its state titles. The two companies will, in the sense of IASC, the same performance equals the change in fair value of securities portfolios: the first will be the gain realized on the market, the second will be a review of its portfolio. Less than a user of financial statements taken as a result latent is equivalent results achieved, performance measurement should be the same in the two cases?

For some the answer is yes; they believe instead that the historical cost model, the first company will be headed to trade only to allow it to delete the end result so that the fair value model prevents the passage through this trick. What if the two companies distribute as dividend?

In these circumstances, the profit is not appropriate traditional; it is sufficient for us convincing, consider a simple example in the banking sector.

Today, the interest margin is a key indicator for the number of credit units which has its place in net banking income and is subject to detailed analyzes and comments.

What is the interest margin when interest-bearing financial instruments are measured at their fair value. The net amount of interest (income proportionate instrument issued a loan for example, reduces the cost of refinancing) was so far found in the income of the institution that made the loan customer; Tomorrow credit and debt financing are evaluated between the opening date and closing date of the balance sheet at their fair value, the result for the period will correspond to the difference between the fair values of instruments, regardless of the amount of interest receivable and collection and paid and payable in the period. Clearly, therefore, the presentation of the profit must be changed radically; There is no logical reason not to keep interest here, even if, in addition, they are only meaningful and useful information for the bank (and client).

No need to extrapolate long to realize that profit, in these circumstances, it may be limited to a few words: to bring net changes (positive or negative) of the fair values of all instruments between the opening date and closing date fiscal year, one (or more) for overheads, one for amenities provisions.

We found just that no literature issued by regulatory bodies supporter of fair value accounting can not be found today on the subject.

4. Towards a new state performance

We note that to the extent that changes in fair values of certain instruments are not recognized in the income, but directly at the equity; it soon became apparent that these standards bodies only income alone is not enough to translate "performance" of the company for a period. Indeed, we must add variations fair values of all instruments that are recognized in profit or directly in equity.

Thus was born the reflection on a new state, called state performance: it is intended to translate into one document all elements which have the character of a profit, regardless of whether they are realized or unrealized, recorded in the income itself or own capital directly. In a model sheet at fair value on enterprise performance measurement period includes both the results obtained, whether latent values determined based on assessments of the market, on internal estimates. It becomes difficult to distinguish, at this level, between objective measurement of penalty and sanction management of the undertaking on the market value of assets and liabilities,
independent of any actual transaction.

In such a context, the hierarchy of the various financial statements should evolve; profit will lose all or part of its interest in favor of a performance state (but that performance), the balance will retain its significance as asset value, while cash flow statement should become the main working document, worthy of interest. Indeed, it is thanks to him and him alone than a third would show how the performance is effectively translated. Treasury announced the company and how the latter was generated and used. Table win free cash flow will finally point of nobility that he ought to have always and certainly will not be a recommended document, what in some countries, but mandatory.

But its use in the future before our conclusion is not a sign of renunciation, without actually accepting the fair value model.

The role of financial statements is to provide useful information for doing business and to take economic decisions and not to determine who should these decisions. Investors and creditors in general are the main users should be help in their decision making. Leaders have meanwhile more information and knowledge about their businesses than the first, and they may improve the quality of information that you provide them .

IASC said that fair value is introduced to provide useful financial statements for investors. The main qualities attributed fair value:

a) predictability

"Fair value" provides better enable future cash flows in the extent to which it integrates design, these future cash flows. "Fair value" is used when investor objectives favor the disclosure of accounting information.

b) counting the total value

Applying historical cost, everything that is not accounted for no cost. This principle implies not account for certain financial instruments, including products derived by definition does not require financial flows generally at home. Account users can not take them into account in assessing future cash flows. This lack of financial statements disappear with the advent of "fair value".

c) consistency with active management of financial risks

Most companies manage their interest rate risk and price and this, even for non-marketable instruments, such as swaps and it is not in relation with historical cost.

d) reduced complexity

Implementation is simple for short-term financial instruments (many reference market) and long-term instruments listed and it use "fair value" as part of active management of price risk.

e) performing accounts

The fair value is not based on the existence of a transaction. In other words, only transactions are recorded in historical cost. "Fair value" adds value to the company's decision and allow storage, for example, one or more financial instruments.

f) neutrality

"Fair value" is determined by reference to the external yes or directly on market values or in the absence of an active market by reference to a model based on the parameters of external data, it appears as a value "neutral" can say it is not influenced by the company.

g) comparability

"Fair value" allows to provide equivalent financial instruments comparable values, regardless of their date of entry in the accounts. Active management of price risk using derivatives to avoid asset value to fall and that the liabilities to rise. "Fair value" allows to consider this reality in the financial statements.

The limits and complaints of fair value are:

a) volatility: Volatility introduced by fair value does not always reflect real changes based events company and will not accurately reflect the reality of the transactions and financial position.

b) lack of database transactions: To the extent that it is not always based on the actual transactions of the enterprise.

c) cost of determining fair value

For fast and accurate, they lack information on the effects on business developments in the market, they may increase uncertainty and cause a distortion of prices; may be the source of an increase in the cost of capital for a firm.

If there is abundant literature on fair value deals including gaps existing accounting systems and practices:

- Old principles based primarily on the needs of industrial enterprises (financial instruments were not a concern);
- Lack of accountability (in stock) products;
- Irrelevance of the historical cost to translate faithfully management financial risks actively practiced increasingly frequently by all enterprises.

It does not exhibit a clear manner and therefore convincing as a clear indication in the annexes to fair value measurements of assets and liabilities of the undertaking is not a sufficient source of information.

We ask ourselves, why do we limit ourselves to certain assets and liabilities and not generalize application of the model?

5. Conclusion

The fair value accounting substituting historical cost model is implicitly supported by major standards bodies, FASB in the United States, IASC.

A criticism of this trend corresponds to one of archaic concepts of accounting, a rearguard battles and a non-innovative doctrinal positions taken and which do not reflect economic and financial developments in the world around us.

In fact, advocates of innovation and constant questioning of principles, tenets and conventions of any kind, so not only to better adapt to reality, especially to predict its evolution, we believe that:

- any new product must be tried and tested before being imposed on the market;
- its advantages, disadvantages, its risks, its cost must be predetermined and analyzed in a comprehensive and objective;
- acceptance by all potential users and those who will be affected, directly or indirectly, its use must also advance a consensus.

All these conditions do not appear united in terms of fair value. Reliability, objectivity, neutrality are certain qualities that can be assigned and shall be recognized indispensable in accounting.

Its impact on business management are such that many business leaders and other users of financial statements do not accept it as a management tool and financial reporting.

Its implications on the importance of financial statements in their present form and traditional were not analyzed, or at least exploited. Therefore, if they are used without substantial revision will lose all meaning and interest will not be exploitable which can lead to a result opposite to that sought.

These remarks do not mean that we take a systematic position against fair value. We believe instead that fair value is the most relevant measure evaluation:

- Transactions on their achievement, because it reflects the reality of the moment;
- Derivatives at their negotiation date (which is only a result of the above statement);
- All the tools to be quickly negotiated enterprise to get a fast buck (or commercial trading tools).

It has not proved to be a model for initial evaluations and future assets and liabilities (financial and / or non-financial) of the enterprise.

Volatility is introduced to measure company performance on a year or a shorter period and in equity we actually conducive to accurately reflect economic reality.

The debate can not therefore be terminated without sufficient prior consultation of all stakeholders; choice must be determined to be the result not only of technical work carried out successfully, but also of a democratic consensus (after the Anglo-Saxon term of art).

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