

# **Conceptual Framework – Measurement Roundtable Discussions**

## **Background Materials**

**Hong Kong, SAR PRC – 16, 17 January 2007**

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### **Introduction**

Measurement is a key aspect of financial reporting. In fact, it is at the heart of what accountants do. A non-accountant would be astonished to realise that measurement is one of the most under-developed areas of the current conceptual frameworks of standard setters world wide. Most frameworks cover this fundamental topic in one or two paragraphs. For example, the IASB Framework simply lists examples of measurement bases, such as historical cost and realisable value, and measurement techniques, such as present value, standard setters might consider. FASB Concepts Statement 5 similarly describes the bases (attributes) used in present practice. But neither framework provides an analysis of the advantages and disadvantages of each basis, or criteria for choosing among them when measurement requirements for a standard are determined.

Filling these gaps is the overall objective of the measurement phase of the IASB's and FASB's current joint project which will update, complete and converge their respective frameworks. The objective of the Roundtables is to provide constituents with their first opportunity to participate in this process of developing measurement concepts, and to do so before the IASB and the FASB begin their deliberations. You are invited to express your ideas, views, suggestions and concerns about measurement in general. The questions set out later in this note are intended only to provide some minimal structure to the discussion, not to pre-empt debate on any aspect of measurement participants think is worth considering. Similarly, the references to additional background material are to help those with the time and inclination to review others' thinking on the topic prior to the discussion. They are in no way intended as 'required reading'.

For their part, the Boards hope that early consultation with constituents will help both to enhance the quality of the eventual conclusions and to accelerate the development of this critical component of the conceptual framework.

## Where are we now?

Even without specific guidance from their frameworks, standard setters have had to decide on measurement requirements in standards projects. For example, SFASs 115 and 133 and IAS 39 use fair value or amortised cost to measure various categories of financial assets and liabilities. Standard setters made these decisions based on judgements about which basis of measurement in that particular instance best satisfied the qualitative characteristics of financial information described in another part of those frameworks — relevance, reliability, comparability, understandability. And of course, today's standard setters inherited some current measurement practices and haven't yet reconsidered them.

Not surprisingly, this combination of history and somewhat ad hoc decision-making by a few generations of standard setters has resulted in the 'mixed bag' of measurement bases we use today. The first of the three parts of the measurement phase of the conceptual framework project, or Milestone I, focuses on measurement bases. Its purpose is to develop a common language – to carefully identify, define and describe the measurement bases we currently use as well as those that have been proposed to date. Having this common language to describe the ways we might measure things is important. Today, not only do we use one term as shorthand to describe a variety of different bases, but we also use several terms to describe what is really just one basis. It is no wonder discussions about measurement are full of misunderstandings.

To date, staff has developed a preliminary list of candidate measurement bases. They can broadly be classified by whether they reflect prices or values and by whether they reflect past, present or future information. The descriptions of these bases, and the terms currently used to describe them, are included in the reference material. Suffice it to say that, based on this analysis, an entity using the *cost* model for property, plant and equipment could be using as many as six different bases. These include:

- Past gross entry price – the consideration given in exchange for an asset including transaction costs– for example, purchased land
- Accumulated past entry price – the consideration paid to construct or assemble an asset over a period of time including transaction costs– for example, a self-constructed building
- Allocated past gross entry price – the amount arrived at by allocating a past gross entry price to multiple assets– for example, a plant acquired in a business combination or basket purchase
- Amortised/depreciated past price – the amount of the originally recorded past entry price that remains after allocating some of it to subsequent accounting periods – for example, all PP&E depreciated over its useful life
- Current exit price – the price that would be received to sell an asset – for example, for an impaired asset *or*, under IAS 36, value-in-use – the discounted net cash flows an entity expects to receive from the use of an asset – if that were higher.

## **Where are we going?**

Milestone II will evaluate the candidate measurement bases in terms of the qualitative characteristics of decision-useful information and any other relevant criteria that can be identified. This part of the project essentially formalises the process standard setters have had to carry out on their own in each standards level project. Milestone III will draw conceptual conclusions from the evaluation results of Milestone II and address practical issues of using those measurement bases that rated most highly in the Milestone II evaluations.

Once the measurement phase of the conceptual framework project is complete, standard setters will finally have a measurement toolbox. Only high-quality tools will be in the box and they will be properly labelled so everyone knows what they are. And the toolbox will come with a set of instructions that will tell standard setters which tool is best for which job. After that, when developing any new standard, they will have clear conceptual guidance on which measurement basis would be appropriate. Like all other parts of the revised framework, new measurement concepts will be applied one standard at a time. Revising all existing standards to be consistent with the revised framework in a single project is clearly impossible.

## **What are the questions for discussion at the Roundtables?**

Because comparability is an important qualitative characteristic of financial information, an observer might find it odd that accountants have developed so many different ways to measure the same things. Financial instruments are most obvious example. And it is widely recognised that our so-called 'mixed measurement attribute' model can produce results that do not reflect the underlying economics in some situations. Logically, this would seem to beg the question: why isn't one measurement basis used for all financial statement purposes? Or you could ask: what model using more than one basis would reflect the economics of many types of businesses properly?

Accordingly, the measurement phase of the conceptual framework project has to answer the following critical questions:

1. If more than one measurement basis is used, what are those bases and when should they be used? For example:
  - a. One basis for initial recognition and another(s) for subsequent measurement?
  - b. One basis for all the assets and liabilities of certain sectors and another(s) for other sectors?
  - c. One basis for certain types of assets and liabilities and another(s) for other types?

- d. One basis for a certain type of assets and another(s) for the same type of liabilities?
2. If only one measurement basis should be used for all purposes, which one and why?
3. What are the practical problems of using the bases you identify? Should these problems preclude their use in some or all situations? Are there ways to address those problems without impairing the usefulness of that basis?

The Boards are interested in your views on these questions and any others you think should be answered, and most importantly, the reasons for those views.

### **Other reference material**

Additional background material can be accessed on the Boards' respective websites – [www.iasb.org](http://www.iasb.org) and [www.fasb.org](http://www.fasb.org). It includes:

1. a list of the issues identified for the measurement phase of the conceptual framework project, by Milestone.
2. a list of the candidate measurement bases staff has identified, including definitions and synonyms currently used.
3. a list of the candidate measurement bases classified by whether the basis is a value or a price and by whether it reflects past, present or future information.
4. sample IFRS and US GAAP statements of financial position listing the various measurement bases currently used to represent the assets and liabilities recognised.