International Financial Reporting Standards

Expected value
and other measures of uncertain future cash flows

The views expressed in this presentation are those of the presenter,
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Official positions of the IASB on accounting matters are determined only after
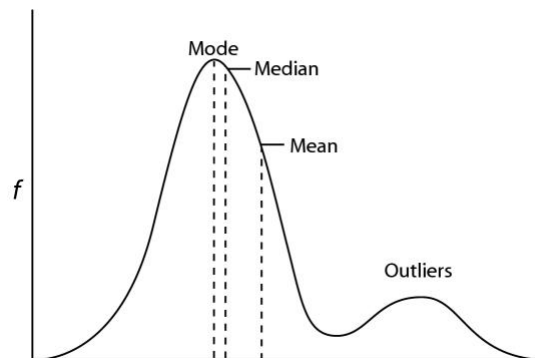extensive due process and deliberation.

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Central estimates

Accounting description	Alternative statistical term
Expected value	$=$ mean
Maximum amount more likely than not to occur	$\cong$ median
Most likely outcome	$=$ mode

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Skewed distributions

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Which central estimate?

- predictive qualities
- robustness
- consistency with measurement objectives
- costs versus benefits

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Expected value

Properties

- implicit in estimates of value
  - fair value
  - value in use
- long run outcome ⇨ no net gain or loss on settlement
- includes outliers and sensitive to changes in outliers
- no cliff edges
- sum of parts = whole

Useful estimate if...

- most relevant measure is current value
- transactions recur frequently
- outliers are important to investors
- two likely outcomes with similar probabilities
- specifying unit of account would be difficult

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Maximum amount more likely than not to occur

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Properties

- minimises average gains and losses on settlement
- excludes outliers and insensitive to changes in outliers
- no need to estimate outliers
- implicit 50% recognition threshold
- cliff edges
- sum of parts ≠ whole

Useful estimate if...

- transactions do not recur frequently
- outliers are not important to investors
- outliers subject to greater estimation uncertainty than central outcomes
- benefits of expected value do not outweigh greater costs

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Most likely outcome

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Properties

- not necessarily a central estimate
- lower probability, but higher amounts, of gains and losses on settlement
- sensitive to interval width
- cliff edges
- sum of parts ≠ whole
- easiest to estimate

Useful estimate if...

- distribution approximately symmetrical about most likely outcome
- benefits of other measures do not outweigh greater costs

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Summary

- **expected value**

    to measure current value or if transactions recur frequently or

    if outliers are important or to avoid cliff edges or if difficult to specify unit of account

- **maximum amount more likely than not to occur**

    if transactions do not recur frequently or if outliers are not important or

    if outliers are subject to greater estimation uncertainty than central outcomes or

    if benefits of expected value do not outweigh greater costs

- **most likely outcome**

    if distribution is approximately symmetrical about most likely outcome or

    if benefits of other measures do not outweigh greater costs

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