

STAFF PAPER

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Project	Conceptual Framework		
Paper topic	Measurement: Relationship with Qualitative Characteristics		
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Objective and structure of this paper

1. The existing *Conceptual Framework* provides little guidance on measurement and when particular measurements should be used. The IASB plans to include in the revised *Conceptual Framework* guidance that assists the IASB in developing measurement requirements in new or revised Standards.
2. In developing such guidance, the IASB has considered the objective of financial reporting and the fundamental qualitative characteristics of useful financial information.
3. The Discussion Paper (DP/2013/1) *A Review of the Conceptual Framework for Financial Reporting* (hereinafter referred to as the ‘Discussion Paper’) included a number of proposals about how the qualitative characteristics of useful financial information might affect measurement. During 2014, the IASB has redeliberated these proposals, in the light of comments received on the Discussion Paper, and made a number of additional tentative decisions regarding how the qualitative characteristics might affect measurement. The objective of this paper is to discuss some of these proposals and tentative decisions.
4. This paper is structured as follows:
 - (a) relevance;
 - (b) measurement uncertainty;

- (c) faithful representation;
 - (d) understandability; and
 - (e) timeliness, verifiability and comparability.
5. Agenda Paper 1B provides the background of the discussions in this paper. That Agenda Paper was prepared for information purposes only and will not be discussed at this meeting.

Relevance

6. The Discussion Paper suggested, and most respondents who commented agreed, that when the IASB selects a measurement basis, it should consider the nature and relevance of resulting information produced in both the statement of financial position and the statement(s) of profit or loss and other comprehensive income (OCI). At its Board meeting in July 2014 the IASB confirmed this position.

Measurement uncertainty

7. Some respondents to the Discussion Paper suggested that one of the factors that should be considered in selecting a measurement basis is the reliability of different measurement bases (ie the degree of measurement uncertainty associated with a particular measurement).
8. At its Board meeting in July 2014 the IASB discussed this issue and noted that paragraph QC16 of the existing *Conceptual Framework*¹ suggests that if the level of uncertainty associated with an estimate is very high then that estimate might not provide relevant information.
9. At that meeting the IASB tentatively decided that the *Conceptual Framework* should state that:
- (a) the level of uncertainty associated with the measurement of an item is one of the factors that should be considered when selecting a measurement basis; and

¹ See Appendix A for the text of paragraph QC16.

- (b) if a measurement is subject to a high degree of measurement uncertainty, the fact does not, by itself, mean that the measurement does not provide relevant information.

Faithful representation

10. The Discussion Paper stated that:

- (a) the fundamental characteristic of faithful representation has fewer implications for measurement than relevance;
- (b) a perfectly faithful representation is free from error, but this does not mean that measurements must be perfectly accurate in all respects. An estimate of an unobservable price can be faithfully represented if it is described clearly and accurately as being an estimate, the nature and limitations of the estimating process are explained and no errors have been made in selecting and applying an appropriate process for developing the estimate; and
- (c) when deciding whether a particular measurement faithfully represents an entity's financial position and performance, the IASB may need to consider how best to portray any link between items. When assets and liabilities are related in some way, using different measurements for those assets and liabilities can create a measurement inconsistency (sometimes called an 'accounting mismatch'). Measurement inconsistencies can result in financial statements that do not faithfully represent the reporting entity's financial position and performance. Consequently, the IASB may conclude in some circumstances that requiring (or permitting) the same measurement approach for related assets or liabilities may provide more useful information for users of financial statements than using different measurement approaches. This may be particularly likely when the cash flows from one item are contractually linked to the cash flows from another item.

11. The Discussion Paper did not include a specific question on how the qualitative characteristic of faithful representation could affect measurement. Consequently, few respondents commented on this issue:
- (a) A few respondents disagreed with the idea that an estimate of an unobservable price could be a faithful representation if adequate disclosures were made. These respondents agreed that an estimate of an unobservable price could be a faithful representation of that estimate. However, if uncertainties associated with that estimate are too large, the estimate could not be a faithful representation of the item being depicted.
 - (b) One respondent stated that it is not possible to consider whether an item has been faithfully represented without first identifying the measurement objective for that item. For example, historical cost faithfully depicts the purchase price of an asset, fair value faithfully depicts the price for which the entity could sell the asset.
 - (c) One respondent stated that the suggestions in the Discussion Paper gave too much prominence to relevance and understated the importance of faithful representation.
 - (d) A few respondents stated that including the effects of changes in own credit in the measurement of liabilities may not result in a faithful representation if those effects are not expected to be realised.
 - (e) One respondent stated that hedge accounting may be required to ensure that the links between related items are faithfully represented.
12. At its Board meeting in July 2014 the IASB tentatively decided:
- (a) to retain the discussion of faithful representation included in the Discussion Paper; and
 - (b) to note in the measurement section that a faithful representation by itself does not necessarily result in useful information. The information provided by the representation must also be relevant.

Understandability

13. The Discussion Paper suggested that the more measurements that are used, and the more changes there are in the types of measurement used for particular items, the harder it is to understand how those measurements interact to depict the entity's financial position and financial performance. The IASB's preliminary view was that it should limit the number of different measures used to the smallest number necessary to provide relevant information.
14. Many of those who commented agreed with the IASB's preliminary view that the number of measurement bases used should be the smallest number necessary to provide relevant information. The main reasons cited were that limiting the number of measurement bases would increase the comparability and understandability of financial statements.
15. However, some respondents disagreed with this preliminary view stating that there should not be an artificial limit on the number of measurement bases used. A different measurement basis should be used if the IASB believes it will provide relevant information to the users of financial information.
16. Some respondents suggested that if the IASB adopted a single measurement basis for all assets and liabilities, the need to minimise the number of measurement bases used would not arise.
17. The IASB discussed this issue at its Board meeting in July 2014. The IASB noted that it was not the IASB's intention to impose an artificial limit on the number of measurement bases used when developing Standards and agreed that a different basis should be used if it would provide relevant information to users of financial statements.
18. However, because requiring a new or different measurement basis increases costs and complexity, the IASB tentatively decided to explain the need to weigh the benefits of introducing a new or different measurement basis against any increased costs or complexity.

Timeliness, Verifiability and Comparability

19. The Discussion Paper stated that:

- (a) timeliness means providing information while it still has the potential to be useful. Timeliness has no specific implication for measurement that is not already embodied in the fundamental characteristic of relevance. If changes in prices or value are relevant, the measurement used should result in recognising them when they occur (rather than at some point in the future);
- (b) verifiability implies using measurements that can be independently corroborated either directly (such as observing prices in transactions in which the entity participated or can observe) or indirectly (such as checking inputs to a model). If a particular measurement cannot be verified, the IASB believes that it should consider using a different measurement, or requiring disclosures that enable users of financial statements to understand the assumptions used; and
- (c) comparability implies using measurements that are the same between periods and between entities. Using the smallest number of measurements, as discussed in the context of understandability, would contribute to comparability.

20. The Discussion Paper did not include a specific question on how considering the enhancing qualitative characteristics of timeliness, verifiability and comparability could affect decisions on measurement. Consequently, few respondents commented on this section of the Discussion Paper. Those commenting suggested that:

- (a) verifiability has a significant role to play in the selection of measurement bases; and
- (b) comparability could be enhanced by removing the ability for preparers to choose between different measurement bases.

21. At its Board meeting in July 2014, the IASB tentatively decided to retain the discussion of timeliness, verifiability and comparability in the Discussion Paper.

Questions for participants

22. There are three questions for participants.

Question 1: Measurement uncertainty

Do you agree with the tentative decision in paragraph 9, that is:

(a) the level of uncertainty associated with the measurement of an items is one of the factors that should be considered when selecting a measurement basis; and

(b) if a measurement is subject to a high degree of measurement uncertainty, the fact does not, by itself, mean that the measurement does not provide relevant information?

Why or why not?

Question 2: Understandability

Do you agree with the IASB's change in emphasis from having the smallest number of measurement bases to explaining the need to weigh the benefits of introducing a new or different measurement basis against any increased costs or complexity (paragraph 18)? Why or why not?

Question 3: Other implications

Do you have any other comments on the relationship between the qualitative characteristics, the cost constraint and measurement? In particular, do you think the qualitative characteristics have other implications for measurement?