STAFF PAPER

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[EEG meeting]

Project	**Discount rates – present value measurements**	
Paper topic	Cover paper	

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Objectives for the session

1. The concept of the time value of money is a core principle of finance. This principle holds that money at the present time is worth more than the same amount of money at a future date. A common valuation technique, the present value measurement method uses expected future cash flows in a combination with a discount rate in order to arrive at a current period measurement. This method requires two main inputs: estimate of future cash flows, including their amount, timing and variability, and estimate of a discount rate consistent with the cash flows. Each of these inputs can take into account various factors, such as risk and uncertainty.

2. Most accounting measurements use either contractual or observable marketplace-determined amounts as a basis for measurement. However, accounting requirements sometimes require or allow estimated future cash flows as a basis for measuring an asset or a liability. These measurements may be based on the present value method.

3. IFRS written over the years have required different factors to be reflected in present value measurement in different Standards, which in turn means different discount rates are required or allowed to be used. Views received during the IASB's 2011 Agenda Consultation suggest that the reasons for using different discount rates are not well understood, with some respondents suggesting that such differences cause IFRS requirements to be inconsistent.

4. Responding to these views, the IASB has conducted a research project to examine discount rate requirements in IFRS to identify why those differences exist and assess whether there are any unjustified inconsistencies that the IASB should consider addressing.

5. The purpose of this EEG meeting is to present the findings of this research project to date and obtain input from the emerging economies perspective. We will also seek general advice from the EEG members, including views on possible future direction of the project. The IASB staff will then prepare revised papers and take them to the IASB with the aim of publishing a research paper in Q4 of 2015.

Questions for the EEG members

6. The papers for the meeting include the following questions for the EEG members (we do not number the questions here as some may appear in a different order in the papers):

   <u>Present value measurement in IFRS</u>

7. In which areas of IFRS is present value measurement most significant for your jurisdiction (for example are there many defined benefit obligations, provisions, insurance contracts or leases)?

8. Do you think the use of present value measurement in IFRS should be extended? If so, in which areas and why?

9. Before reading the papers for the meeting, were you aware that the IFRS requirements for present value measurement are different for different Standards? Do any of the differences create an issue in your jurisdiction? Which ones and why?

   <u>Practical application of present value measurement requirements</u>

10. Skills and resources. In your jurisdiction:

    (a) Is the concept of present value measurement generally understood, and consistently applied?

    (b) Is there sufficient guidance available to enable the elements of the present value calculation (eg future cash flows) to be determined?

11. Is the data required for present value measurement readily available in your jurisdiction, and if so is it consistently used? For example, are there any issues in determining whether there is a deep market in high-quality bonds in order to apply IAS 19 *Employee Benefits*, or finding a pre-tax rate for the value in use calculations in IAS 36 *Impairment of Assets*, or determining risk-free rate*?*

12. Are there economic factors in your jurisdiction not commonly found outside emerging economies that may have an effect on how present value measurement is applied (eg inflation, market liquidity)?

13. Do the benefits of present value measurement justify the costs of applying it in emerging economies?

The way forward

14. What should the IASB do about the identified differences and issues in the application of present value measurement?

15. What effects, if any, would there be for emerging economies if the IASB decided to address some of the issues; eg via

    (a) smaller projects on particular aspects? One example may be a project consider whether and how to include risk and liquidity adjustments in all present value measurements that require current values?

    (b) larger, cross-cutting project on present value measurement (similar to IFRS 13 *Fair Value Measurement*) setting a consistent methodology for present value measurement?

    (c) education or other material?