

STAFF PAPER

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Accounting Standards Advisory Forum

Project	Conceptual Framework		
Paper topic	Measurement: redrafting the factors to consider in selecting a measurement basis		
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Introduction

1. The objective of this agenda item is:

To obtain input from ASAF members on how the Measurement Chapter of the Conceptual Framework should discuss the factors to consider when selecting a relevant measurement basis.
2. Most respondents to the Exposure Draft *Conceptual Framework for Financial Reporting* (the Exposure Draft) that commented on Chapter 6—Measurement agreed that:
 - (a) the Conceptual Framework should not require the use of a single measurement basis;
 - (b) the measurement bases discussed were appropriate; and
 - (c) the selection of a measurement basis should be based on the objective of financial reporting and the qualitative characteristics of useful financial information.
3. However, some respondents said that the Chapter failed to provide adequate guidance for the development of future accounting standards. A specific concern mentioned was that the link between the sections ‘measurement bases and the

information that they provide’ (paragraphs 6.4–6.47) and ‘Factors to consider when selecting a measurement basis’ (paragraphs 6.48–6.63) was not sufficiently clear.

4. In order to meet these concerns, the staff have been considering how to improve the discussion of the ‘factors to consider...’ section.
5. A revised draft of the relevant sections forms paper 4C ‘*Measurement: suggested redraft of parts of Chapter 6*’ for this meeting. So that ASAF members can appreciate the context, this draft includes the preceding material. We, however, would like the ASAF discussion to focus on the ‘factors to consider...’ section (from paragraph 6.48).
6. A summary of the main changes made to the preceding sections is set out in the Appendix to this paper. Although we do not plan to discuss these changes at the meeting, we would appreciate comments on them from ASAF members outside the meeting.
7. This draft will also be discussed by the Board in an educational session in September. An oral summary of that discussion will be given at the ASAF meeting.

Structure of this paper

8. This paper is structured as follows:
 - (a) The next section provides a summary of the section of the Exposure Draft headed ‘Factors to consider when selecting a measurement basis’ (paragraph 10)
 - (b) The approach taken in redrafting the ‘factors to consider...’ section is summarised in the next section (paragraphs 11–17)
9. Questions for ASAF members are set out after paragraph 17.

Summary of the Exposure Draft

10. The section of the Exposure Draft headed ‘Factors to consider when selecting a measurement basis’:

- (a) Made some general introductory comments, emphasising the importance of the qualitative characteristics in the selection of a measurement basis (paragraphs 6.48–6.52).
- (b) Discussed factors relating to relevance. It stated that in selecting a measurement basis, it is important to consider what information that measurement basis will produce in both the statement of financial position and the statement(s) of financial performance. It then identified two factors to consider when selecting a measurement basis which were described as follows:

- (a) how that asset or liability contributes to future cash flows. This will depend in part on the nature of the business activities conducted by the entity. For example, if a property is realised by sale, it will produce cash flows from that sale, but if a property is used in combination with other assets to produce goods and services, it will help produce cash flows from the sale of those goods and services.

- (b) the characteristics of the asset or the liability (for example, the nature or extent of the variability in the item’s cash flows, or the sensitivity of the value of the item to changes in market factors or to other risks inherent in the item).”

However, the Exposure Draft did not explicitly describe how the consideration of these factors might affect the conclusion reached.

- (c) Discussed measurement uncertainty as a factor affecting the relevance of information provided by a measurement basis, and distinguished measurement uncertainty and outcome uncertainty.
- (d) Discussed the implications for the selection of a measurement basis of faithful representation and the enhancing qualitative characteristics.

Approach to redrafting

11. Comments from respondents to the Exposure Draft suggest that the most significant change required is to clarify both the underlying principles and the implications of the following factors:
 - (a) the contribution of the asset to future cash flows (see paragraphs 6.54A–6.54G of Agenda Paper 4C); and
 - (b) the characteristics of the asset (see paragraphs 6.54H–6.54K of Agenda Paper 4C).
12. The redraft draws on discussions in earlier parts of the *Conceptual Framework* and reflects insights gained from the development of IFRS 9 *Financial Instruments*.
13. One way of making the guidance in the Measurement chapter more robust would be to prescribe the order in which the various factors would be considered and hence their priority (for example using a hierarchy or decision tree), but a detailed prescription does not seem to be achievable, as the relative importance of the factors depends on the specific circumstances being considered. Reflecting this view, the redraft does not prescribe the order in which the various factors would be considered. Indeed, more emphasis has been given to the thought that no one factor considered in isolation will be conclusive as to the measurement basis that should be selected (paragraph 6.49B of Agenda Paper 4C).¹
14. The point that, when selecting a measurement basis, it is important to consider what information that measurement basis will produce in both the statement of financial position and the statement(s) of financial performance has been relocated. It was made in the Exposure Draft in the context of relevance, but it seems to apply more generally. It is now in paragraph 6.49C of paper 4C.

¹ The Exposure Draft noted that ‘The relative importance of each of the factors [discussed in this section] will depend upon facts and circumstances’.

15. However, the redraft emphasises (in paragraph 6.49A) the importance of relevance, referring to paragraph 2.21 of the Exposure Draft. That paragraph reads:

The most efficient and effective process for applying the fundamental qualitative characteristics would usually be as follows (subject to the effects of enhancing characteristics and the cost constraint, which are not considered in this example). First, identify an economic phenomenon that is capable of being useful to users of the reporting entity's financial information. Second, identify the type of information about that phenomenon that would be most relevant if it is available and can be faithfully represented. Third, determine whether that information is available and can be faithfully represented. If so, the process of satisfying the fundamental qualitative characteristics ends at that point. If not, the process is repeated with the next most relevant type of information.

16. It is important that the *Conceptual Framework* should discuss faithful representation and the enhancing qualitative characteristics: the staff view is that the discussion of these in the Exposure Draft is appropriate. However, because they are considered only after the most relevant measurement basis has been identified, it seems unhelpful to expand that discussion to address their potential implications. This would either simply state the obvious or incur the risk of suggesting that specific requirements would be adopted in Standards, without an adequate consideration of relevance. For this reason, the redraft does not attempt to identify specific implications of faithful representation and the enhancing qualitative characteristics.
17. At its May meeting, the IASB tentatively decided to describe measurement uncertainty as a factor affecting faithful representation, rather than relevance. Accordingly, the discussion of measurement uncertainty has been relocated to the discussion of faithful representation with minor consequential changes.

Questions for ASAF members

What are your views on:

- (a) The general approach adopted in the redrafting, as reflected in the draft at Paper 4C, at paragraphs 6.54–6.54K?
- (b) The discussion of the contribution of the asset to future cash flows (Paper 4C, paragraphs 6.54A–6.54G)?
- (c) The discussion of the characteristics of the asset or liability (Paper 4C, paragraphs 6.54H–6.54K)?
- (d) Are there any other specific points on which you would wish to comment?

Appendix A

Summary of other changes made in the draft.

The following provides a summary of the main changes made in redrafting the exposure draft that are reflected in Paper 4C, other than those in paragraphs 6.54–6.54K.

Section	Paragraphs	Description of change
Introduction	6.1–6.3B	Redrafted for clarity.
Historical cost	6.6–6.17A	Discussion expanded to enhance the flow, and to expand the discussion of the information provided by historical cost.
Current cost	6.20A–6.20C	Relocated from the discussion of historical cost, and discussion of advantages and disadvantages expanded.
Summary of information provided	6.47, Table 6.1	Table rewritten to enhance clarity and add a description of the information provided by current cost.
Faithful representation: Measurement uncertainty	6.58A–6.58B	Discussion relocated from ‘relevance’ with minor consequential changes.