

The IASB proposes new appendices. Because they are new, no mark-up has been used.

Appendix A Cash-flow-based measurement techniques

CROSS-CUTTING THEMES

This appendix is an integral part of the [draft] Conceptual Framework for Financial Reporting.

A1 Sometimes, a measure determined using a **measurement basis** described in Chapter 6 cannot be observed. In some such cases, it can be estimated using **cash-flow-based measurement techniques**. In particular:

- (a) the **value in use of an asset** and the **fulfilment value of a liability** can only be determined using such a technique; and
- (b) if fair value cannot be observed, it would need to be estimated using a cash-flow-based measurement technique or another technique.

A2 **Cash-flow-based measurement techniques** are not measurement bases; they are a means of estimating a measure. Hence, when using such a technique, it is necessary to identify the objective of using that technique (ie which measurement basis is **being used**) and, in the light of that objective, whether the technique includes using the following factors:

- (a) estimates of future cash flows.
- (b) possible variations in the estimated amount and timing of future cash flows for the asset or the liability being measured, caused by the uncertainty inherent in the cash flows (see paragraphs A6–A10).
- (c) the time value of money.
- (d) the price for bearing the uncertainty inherent in the cash flows (ie a **risk premium** or **risk discount**). That price is not captured by the techniques used to measure a single amount within the central part of the range of possible cash flows (see paragraphs A6–A10). That price depends on the extent of the uncertainty. It also reflects the fact that investors would generally pay less for an asset (or expect to receive more for taking on a liability) that has uncertain cash flows than for an asset (or liability) whose cash flows are certain.
- (e) other factors, such as liquidity, that market participants would take into account in the circumstances.

A3 For a liability, the factors mentioned in paragraph A2(b) and A2(d) include **the possibility that the entity may fail to fulfil the liability (own credit risk)**. [See worked example in IAS 37 calculations](#)

A4 Not all of the factors listed in paragraph A2 are considered in every cash-flow-based measurement. However, if such a technique is used to estimate fair value, it will need to capture all of the factors and adopt the perspective of market participants. Estimates of **fulfilment value** or **value in use** adopt the perspective of the entity.

A5 **Cash-flow-based measurement techniques** can be used to customise measurement bases (for example, departing from fair value by choosing to

A measurement basis is a measure of an asset or a liability (and income and expenses) that allows an evaluation of the item with respect to specified firm objectives such as

- Fair value (disposal or acquisition)
- VIU
- Cost
- NRV
- Current replacement cost

Techniques (e.g. DCF)
Perspectives (e.g. market participants; entity perspective)

e.g.

- determine fair values
- VIU

update only some of the factors listed in paragraph A2). Customising measurement bases may sometimes result in information that is more relevant to the users of financial statements. However, they may also be more difficult for users of financial statements to understand. Hence, the reasons for customisation in a Standard will need to be explained in the Basis for Conclusions on that Standard.

Possible variations in the estimated amount and timing of cash flows

A6 **Uncertainties about the amount of any cash flows are important characteristics of assets and liabilities.** When measuring an asset or a liability by reference to uncertain future cash flows, it is necessary to represent the range of possible cash flows by selecting a single amount. **The most relevant amount is usually one from within the central part of the range (a central estimate).**

A7 **Different central estimates provide different information.** For example:

- (a) the **expected value** (the **probability-weighted average**, also known as the statistical mean) **reflects the entire range of outcomes and gives more weight to the outcomes that are more likely.** It is not intended to predict the ultimate inflow or outflow of cash (or other economic benefits) arising from that asset or liability.
- (b) the **maximum amount** that is **more likely than not to occur** (similar to the statistical median) indicates that the probability of a **subsequent loss is no more than 50 per cent and that the probability of a subsequent gain is no more than 50 per cent.**
- (c) the **most likely outcome** (the **statistical mode**) predicts the ultimate inflow or outflow arising from an asset or a liability.

Existence uncertainty may exist even where measurement uncertainty has been eliminated

A8 Each of these central estimates is illustrated in the following example:

Example

Probability (%)	Cash flow (CU) ^(a)
40	100
30	200
30	500

(a) In this [draft] *Conceptual Framework*, monetary amounts are denominated in 'currency units' (CU).

In this example:

- (a) The **expected value** (the mean) is CU250 (40% × CU100 + 30% × CU200 + 30% × CU500).
- (b) The **maximum amount** that is **more likely than not to occur** (the median) is CU200. (The **probability** that the cash flow will be more than CU200 is less than 50 per cent and the **probability that** the cash flow will be less than CU200 is less than 50 per cent.)

(c) The most likely outcome (the mode) is CU100. It is the outcome with the highest probability.

A9 As noted in paragraph A2, a central estimate does not capture the price for bearing the uncertainty that the ultimate outcome may differ from that central estimate.

A10 No one central estimate gives complete information about the range of possible outcomes. To provide complete information, disclosure may be needed.