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Introduction

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Introduction

This issue of *International Accounting Policy Forum (IAPF)* is especially relevant to current policy debates in financial reporting.

The question of measurement has become increasingly controversial in recent years and standard setters have taken steps to open up debate on it. First, in 2005, the International Accounting Standards Board (IASB) published, though it did not endorse, *Measurement Bases for Financial Accounting – Measurement on Initial Recognition*, which advocated that all assets and liabilities should be measured initially at fair value, where this can be measured reliably. Then, in 2006, the IASB and the US Financial Accounting Standards Board (FASB) published the first in a series of discussion papers as part of their project to establish a common conceptual framework.

Although this first discussion paper was on 'the objective of financial reporting' and 'qualitative characteristics of decision-useful financial reporting information', it almost certainly has implications for measurement. Also in 2006, the FASB issued SFAS 157, *Fair Value Measurements*, which clarified how the FASB believes fair value should be defined and measured. An IASB discussion paper with the same title promptly followed this.

Most recently, in January and February 2007, the IASB and FASB hosted round tables in Hong Kong, London and Norwalk to discuss bases of measurement. These meetings were held as a first step in developing the boards' thinking on measurement ahead of its work on a discussion paper on measurement to be published as part of the conceptual framework project.

The Institute of Chartered Accountants in England & Wales (ICAEW) has taken a leadership position on this subject. In October 2006, as part of our Information for Better Markets campaign, we published *Measurement in financial reporting*. Our approach in this report is essentially a practical one. The critical test for financial reporting should be: what works? What information helps businesses, investors and other users of financial reporting to achieve their goals more effectively?

The report does not recommend any single 'best' basis of measurement. On the contrary, it argues that financial reporting measurement is a matter of evolving conventions, not something to which there are immutably right and wrong answers. It also argues that the purposes of financial reporting depend on its institutional context and that this context affects the costs and benefits of different measurement bases.

The report suggests that, in making decisions on measurement requirements, it may be appropriate:

- to adopt a mixed approach to measurement for different items in accounts; and
- to distinguish between different types of entity in accordance with their industry, ownership and governance structure, and size.

The report also proposes that decisions on the regulation of financial reporting measurement should be regarded as matters of public policy, subject to the overriding tests of cost-effectiveness and fitness for purpose and the same principles of good regulatory practice as other forms of regulation.

A practical, utilitarian approach must be based on evidence of what works rather than on a priori theory, and in our report we stress the need for evidence and recommend that standard setters' approach to measurement questions should be significantly more evidence-based than has typically been the case hitherto. In support of this objective we commissioned the five papers published here, presented at the ICAEW's Information for Better Markets Conference in December 2006. Mary Barth's paper gives us a standard setter's perspective on measurement issues. Wayne Landsman's looks at how fair value information affects markets, and Anne Beatty's at how changing measurement affects management behaviour. Stephen Penman's paper sets out how alternative approaches to measurement are rooted in the needs of users and how they actually use financial reporting information for valuation purposes. Stephen Zeff provides an historical context from the US in tracing the SEC's disapproval of most upward valuations from its founding in 1934 until 1972.

It gives some indication of the value of these five papers as contributions to the debate that the IASB and FASB put links to them, as well as to *Measurement in financial reporting*, on their websites as background material for their round tables on measurement. Indeed, the round tables provided strong evidence – at least as far as those affected by accounting standards are concerned – that in

important respects the debate has already moved on. Speakers at the round tables showed little appetite for the universal imposition of a single basis of measurement, and near-unanimous acceptance of mixed bases of measurement, with different items in the accounts measured in different ways. The practical question that needs answering concerns which bases produce the most useful information for different items. The answer may well vary with the needs of different businesses and different users of financial reports, and may also change over time. I believe that our report and the papers published here have contributed to this significant change in the focus of the measurement debate.

The papers in this issue of *IAPF* will certainly be useful to the ICAEW in the continuing development of our thought leadership work on measurement, and I trust that readers generally will find them helpful in developing their own thinking. I also hope that they will stimulate further research on the issues they address.

I am grateful to all the distinguished academic and practitioner contributors to this volume and, once again, to Pauline Weetman for her support and hard work as editor. Finally, I thank the ICAEW's charitable trusts, which generously provided funding to support the conference last December, preparation of the academic papers published here, and the costs of the publication itself.

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