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**The Present Value Model Under Uncertainty**

The present value model under uncertainty assumes that each set of possible states is publicly known and complete, that the state realization is publicly observable, and that the state probabilities are objective and publically known (Scott 29). Absent these assumptions, the model ceases to function accurately and with its intended purpose. Accountants do not work in ideal environments and cannot use such a model to produce financial statements with predictive and feedback value. Furthermore the process would likely be beyond the constraints of cost benefit. Accounting must therefore incorporate systems that can materially provide predictive value, feedback, timely information on a basis that is neutral, verifiable, and valid. Due to the fact that assumptions under the present value model would be constantly changing and subject to interpretation, the accounting model cannot be incorporated into daily reporting for either small or large entities due the aforementioned shortcomings.

William R. Scott defines net income as to “not exist as a well-defined construct” (Scott 45). Conventional net income does not take into account state probabilities and therefore does not reflect uncertainty facing an entity. Present value of assets and liabilities, however, are highly subjective. Charging management with such values is likely present a moral, as well as logistical hazard. Something seemingly simple such as an interest rate used to gage present and future values could vary dramatically depending on the underlying index chosen for the task. Ultimately historical cost has been adopted to limit the subjective decision making that management must undertake. Organizations such as The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) have incorporated generations of accounting pronouncements to set standards. Ultimately the representational faithfulness of the accounting work must be upheld in order for metrics such as net income to be comparable. Because net income is not a perfect measurement, it must be able to be compared to the statements of other entities so that it is useful to end users. End users such as investors must take and analyze this information based on a uniform standard to make investment decisions. Therefore, the “quality” of net income and underlying company assets is typically reflected in the long term stock prices of the entity.

Accounting produced under ideal conditions takes into account a given fixed interest rate, states of nature, state of probabilities, and state realization publicly observable (Scott 30). The information thus reports the resulting present values of expected cash flows and reports them on the income statement. Such accounting can formally incorporate uncertainty. The ultimate limitation of such accounting is that conditions in the real world are constantly subject to change. Furthermore, managers and accountants charged with deciding on what assumptions should be made could modify the results by assuming favorable circumstances. Thus, the current accounting systems implemented under GAAP strive to provide a conceptual framework in which accounting information is bother useful and relevant to its end users.