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Accounting Recognition and Measurement Theory: A Conceptual and Empirical Comparison of Historical Cost and Fair Value

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ABSTRACT
This study aims to examine the conceptual and empirical debate between historical cost and fair value within the context of accounting recognition and measurement theory. This issue is significant because the measurement basis applied in financial reporting directly influences the quality of accounting information, particularly in terms of relevance and faithful representation. This study adopts a qualitative approach using a structured literature review design. The data consist of secondary sources obtained from reputable journal articles, accounting standards, academic books, and official documents related to financial reporting. The data were analyzed using qualitative content analysis by identifying, classifying, and synthesizing the literature based on the themes of recognition, measurement, historical cost, fair value, relevance, faithful representation, volatility, stewardship, and decision usefulness. The findings indicate that historical cost offers advantages in terms of objectivity, verifiability, stability, and stewardship because it is based on actual transactions that can be objectively verified. However, it has limitations in reflecting current economic values. In contrast, fair value provides greater relevance and decision usefulness because it reflects current market conditions. Nevertheless, it may introduce subjectivity, measurement uncertainty, and volatility in financial statements, particularly when fair values are estimated using unobservable inputs. This study concludes that neither historical cost nor fair value is universally superior. Instead, a mixed measurement model represents a more appropriate approach, as it enables the proportional application of historical cost and fair value according to the characteristics of assets and liabilities, as well as the objectives of financial reporting.

Keywords: Fair Value, Faithful Representation, Historical Cost, Measurement, Recognition.

I. Introduction

Financial reporting plays a fundamental role in providing economic information that is useful to investors, creditors, regulators, and other stakeholders in assessing an entity's financial position, performance, and future prospects. The quality of information presented in financial statements is determined not only by the completeness of disclosures but also by the accuracy of the recognition and measurement of financial statement elements. In financial accounting, recognition refers to the process of determining whether an

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asset, liability, income, or expense should be included in the financial statements, whereas measurement refers to the monetary basis used to assign values to those elements. Consequently, the selection of an appropriate measurement basis is a critical issue because it directly influences the relevance, faithful representation, comparability, and overall usefulness of accounting information for financial statement users. According to the Conceptual Framework for Financial Reporting, useful financial information must possess two fundamental qualitative characteristics: relevance and faithful representation (IFRS Foundation, 2018). Relevance refers to the capacity of information to influence users' economic decisions, whereas faithful representation requires information to be complete, neutral, and free from material error. Within this framework, the choice of a measurement basis represents one of the central conceptual issues because no single measurement approach is capable of achieving both characteristics equally in all circumstances. Barth (2014) argues that measurement is a fundamental aspect of financial reporting because accounting standards require a sound conceptual foundation for selecting the measurement basis that best reflects the characteristics of assets, liabilities, and the objectives of financial reporting. The debate over measurement bases generally focuses on two principal approaches: historical cost and fair value. Historical cost measures assets and liabilities based on the transaction price or acquisition cost at the time an economic event occurs. This approach offers advantages in terms of objectivity and verifiability because it is supported by actual transaction evidence. Consequently, the information produced is relatively stable, readily auditable, and generally considered reliable for evaluating management stewardship. However, the primary limitation of historical cost is its inability to reflect changes in current economic values, particularly when assets or liabilities are highly sensitive to fluctuations in market prices, interest rates, credit risk, or other economic conditions.

In contrast, fair value measures assets and liabilities based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This approach is generally regarded as more relevant because it reflects current economic conditions and provides information that is more responsive to market developments. Hitz (2007) explains that the principal argument in favor of fair value lies in its decision usefulness, as fair value is considered to provide a closer representation of current economic value than historical cost. Similarly, Landsman (2007) demonstrates that capital market research has consistently found fair value information to be value relevant for investors, particularly when it is derived from observable market inputs. Nevertheless, the application of fair value is not without criticism. A major concern arises when fair value cannot be determined from an active market, requiring entities to rely on valuation techniques, internal assumptions, and professional judgment. Under IFRS 13, fair value measurements are classified into a three-level hierarchy based on the observability of the inputs used. Level 1 measurements rely on quoted prices in active markets and are considered the most reliable, whereas Level 3 measurements rely on unobservable inputs and therefore involve greater subjectivity and measurement uncertainty. Song et al. (2010) found that Level 1 and Level 2 fair value measurements generally exhibit greater value relevance than Level 3 measurements. They also found that the usefulness of fair value information is influenced by the effectiveness of corporate governance mechanisms. The debate between historical cost and fair value extends beyond conceptual arguments to empirical evidence. Gassen and Schwedler (2010) show that financial statement users clearly distinguish between mark-to-market and mark-to-model fair value measurements. Fair values derived from active market prices are generally perceived as more useful for decision-making, whereas those obtained through valuation models are considered less reliable because they depend heavily on assumptions and estimates. Furthermore, Laux and Leuz (2010) argue that the debate surrounding fair value intensified following the global financial crisis, as fair value accounting was believed to contribute to greater volatility in financial statements. However, their empirical evidence does not support the claim that fair value accounting was the primary cause of the crisis. Instead, they conclude that the issue is considerably more complex and is influenced by market conditions, asset liquidity, regulatory oversight, and the quality of accounting standard implementation.

Recent studies further suggest that the debate between historical cost and fair value cannot be resolved by declaring either approach universally superior. McDonough et al. (2020) emphasize that fair value accounting continues to evolve and requires further research, particularly regarding estimation quality,

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disclosure practices, auditability, and their implications for users' decision-making. Likewise, Goh et al. (2021) find that confidence in fair value accounting depends largely on users' perceptions of its benefits and costs, as well as their trust in the conceptual framework underlying accounting standard setting. These findings indicate that the central issue in accounting measurement is not simply choosing between historical cost and fair value but determining how to produce accounting information that is relevant, faithfully represented, verifiable, transparent, and consistent with the economic characteristics of the financial statement elements being measured. In contemporary accounting practice, financial reporting standards increasingly adopt a mixed measurement model, whereby different measurement bases are applied according to the characteristics of assets, liabilities, and the objectives of financial reporting. This approach recognizes that historical cost and fair value serve complementary rather than competing roles. Historical cost is more appropriate for assets and liabilities that require stability, objectivity, and strong transactional evidence, whereas fair value is better suited for items whose values are significantly influenced by market conditions and are therefore more relevant for assessing current economic circumstances. Consequently, the conceptual and empirical debate between these two measurement approaches remains highly relevant, particularly in efforts to improve the quality of financial reporting and to strengthen the harmonization of IFRS- and PSAK-based accounting standards. Based on the foregoing discussion, this article aims to examine the conceptual and empirical debate between historical cost and fair value within the framework of accounting recognition and measurement theory. Specifically, it analyzes the characteristics, strengths, limitations, and implications of these two measurement bases for the quality of financial reporting, with particular emphasis on relevance, faithful representation, earnings volatility, and decision usefulness for investors. This article is expected to contribute to the development of accounting theory by providing a comprehensive conceptual perspective while also offering practical insights into the importance of selecting a measurement basis that is balanced, transparent, and aligned with the objectives of financial reporting.

II. Literature Review and Hypothesis Development

2.1. Accounting Theory of Recognition and Measurement

Recognition and measurement are two fundamental concepts in accounting theory that determine how transactions and economic events are presented in financial statements. Recognition refers to the process of including an element in the financial statements when it satisfies the definition of an asset, liability, equity, income, or expense and provides information that is both relevant and faithfully representative of the underlying economic substance. Measurement, on the other hand, refers to the process of determining the monetary amount assigned to a financial statement element after it has been recognized. Therefore, recognition determines what is recorded, whereas measurement determines the amount at which it is reported in the financial statements. According to the Conceptual Framework for Financial Reporting, useful financial information must possess the two fundamental qualitative characteristics of relevance and faithful representation (IFRS Foundation, 2018). Relevance refers to the ability of accounting information to influence users' economic decisions by providing predictive and confirmatory value. Relevant information enables investors, creditors, and other stakeholders to evaluate an entity's future cash flow prospects, financial performance, and associated risks. Faithful representation, in contrast, requires information to be complete, neutral, and free from material error. Together, these qualitative characteristics provide the conceptual basis for evaluating the appropriateness of alternative accounting measurement bases. Modern accounting standards recognize multiple measurement bases rather than relying on a single approach. These include historical cost, current value, fair value, value in use, and fulfilment value. Barth (2014) argues that measurement requires a robust conceptual foundation because the selection of a measurement basis directly influences the quality of financial reporting. An inappropriate measurement basis may reduce the relevance, faithful representation, or ability of accounting information to reflect the underlying economic substance of a transaction.

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Among the various measurement bases, historical cost and fair value have generated the greatest conceptual and empirical debate. Historical cost measures assets and liabilities based on the transaction price at the date of acquisition or when an obligation is incurred. This approach is widely recognized for its objectivity, verifiability, and consistency because it is supported by actual transaction evidence. Consequently, historical cost information is generally regarded as reliable and well suited to evaluating management stewardship. However, its principal limitation is its inability to reflect current economic values, particularly when market prices or economic conditions change substantially. In contrast, fair value measures assets and liabilities based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This approach is considered more relevant because it reflects current market conditions and provides more timely information. Hitz (2007) explains that proponents of fair value accounting support this measurement basis primarily because of its decision usefulness, arguing that fair value provides more useful information for economic decision-making than historical cost. Likewise, Landsman (2007) demonstrates that fair value information is often value relevant for investors, particularly when applied to financial instruments and assets with observable market prices. Despite these advantages, the application of fair value introduces concerns regarding measurement uncertainty. IFRS 13 classifies fair value measurements into a three-level hierarchy based on the observability of the valuation inputs. Level 1 measurements rely on quoted prices in active markets for identical assets or liabilities and therefore provide the highest degree of objectivity. Level 2 measurements use observable inputs other than quoted market prices, whereas Level 3 measurements rely on unobservable inputs and involve greater management assumptions and professional judgment (IFRS Foundation, 2021). Song et al. (2010) found that Level 1 and Level 2 fair value measurements generally exhibit greater value relevance than Level 3 measurements because users place greater confidence in information derived from observable market inputs.

Fundamentally, the debate between historical cost and fair value reflects the trade-off between relevance and faithful representation. Historical cost provides information that is more objective and verifiable but is less responsive to changes in economic value. Conversely, fair value provides more relevant and timely information but may introduce subjectivity when active market prices are unavailable. Laux and Leuz (2010) found that criticism of fair value accounting intensified following the global financial crisis because fair value was believed to increase financial statement volatility. Nevertheless, they concluded that the available empirical evidence is insufficient to support the claim that fair value accounting was the primary cause of the crisis. Instead, the effectiveness of fair value depends on factors such as the context of its application, the quality of valuation inputs, market conditions, regulatory oversight, and the quality of financial reporting disclosures. Accordingly, accounting recognition and measurement theory considers the selection of an appropriate measurement basis to be a critical determinant of financial reporting quality. Recognition and measurement practices that comply with accounting standards enhance the comparability, transparency, relevance, and faithful representation of financial information. Conversely, inappropriate recognition or the use of an unsuitable measurement basis may reduce information quality and adversely affect the decisions of investors, creditors, regulators, and other stakeholders.

2.2. Conceptual Framework

The conceptual framework of this study is based on the relationship between accounting measurement bases and the quality of financial reporting. The measurement basis applied in financial statements is regarded as a key factor influencing the qualitative characteristics of accounting information, particularly relevance and faithful representation. Relevance reflects the ability of accounting information to influence users' economic decisions, whereas faithful representation reflects the extent to which financial information faithfully depicts the underlying economic substance by being complete, neutral, and free from material error. Within the context of this study, historical cost is positioned as a measurement basis that emphasizes objectivity, reliability, and verifiability. Because historical cost is derived from actual transactions, the resulting information can be readily verified by auditors and other independent parties. Consequently, this approach is considered particularly effective in supporting management stewardship and accountability. However, historical cost information may become less relevant when the carrying amount differs substantially from the current economic value of the underlying assets or liabilities. Conversely, fair value is positioned as a measurement basis that emphasizes relevance and decision usefulness. Fair value information is more responsive to changes in market conditions, enabling investors and creditors to assess the economic value of assets, financial risks, and future business prospects more effectively. Nevertheless, these advantages depend heavily on the quality of the valuation inputs. Fair values derived from active market prices are generally considered more reliable and relevant than those estimated using internal valuation models. Gassen and Schwedler (2010) demonstrate that financial statement users distinguish between mark-to-market and mark-to-model fair value measurements, indicating that the source of valuation inputs significantly influences users' perceptions of the usefulness and credibility of accounting information.

Furthermore, disclosure quality plays a critical role in the application of fair value accounting. When fair value measurements rely on unobservable inputs, entities are expected to provide comprehensive disclosures regarding valuation techniques, key assumptions, sensitivity analyses, and the applicable level within the fair value hierarchy. McDonough et al. (2020) emphasize that fair value accounting continues to require improvements in estimation quality, disclosure practices, auditability, and its implications for users' decision-making. Similarly, Goh et al. (2021) find that confidence in fair value accounting is influenced by users' perceptions of its benefits and costs, as well as their trust in the underlying measurement process. Based on the preceding discussion, the conceptual framework of this study proposes that compliance with accounting recognition and measurement principles contributes to improving the quality of financial reporting. Furthermore, historical cost is conceptually expected to provide stronger support for faithful representation because of its objectivity and verifiability, whereas fair value is expected to enhance the relevance of accounting information by reflecting current economic conditions. Nevertheless, the effectiveness of fair value depends not only on the measurement basis itself but also on the observability of valuation inputs and the quality of the accompanying disclosures.

2.3. Hypothesis Development

Recognition and measurement are fundamental components of financial reporting because they determine whether a transaction or economic event is recognized and how its value is presented in the financial statements. According to the Conceptual Framework for Financial Reporting, useful accounting information must possess the qualitative characteristics of relevance and faithful representation (IFRS Foundation, 2018). Barth (2014) argues that the selection of an appropriate measurement basis should be grounded in a sound conceptual framework because measurement decisions directly influence the quality of financial information provided to users of financial statements. Consequently, compliance with accounting standards in the recognition and measurement of financial statement elements is expected to enhance the quality of financial reporting by producing information that is more relevant, comparable, and capable of faithfully representing the underlying economic substance.

H1 : Compliance with accounting standards in recognition and measurement has a positive effect on the quality of financial reporting.

Historical cost is a measurement basis that records assets and liabilities at the amount of consideration exchanged when an asset is acquired or a liability is incurred. This approach is recognized for its objectivity and verifiability because the reported amounts are supported by actual transaction evidence that can be independently verified. Within the conceptual framework of faithful representation, high-quality financial information should be complete, neutral, and free from material error (IFRS Foundation, 2018). Barth (2014) further explains that the selection of a measurement basis should consider the qualitative characteristics of accounting information. Accordingly, historical cost is expected to enhance faithful

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representation because it is more readily verifiable and involves less subjectivity than measurement approaches based primarily on estimates.

H2 : The use of historical cost has a positive effect on the faithful representation of financial reporting information.

Fair value is a measurement basis that reflects the current market value of an asset or liability at the measurement date. This approach is generally regarded as more relevant because it reflects prevailing economic conditions and provides information that is more useful for investors' decision-making. Hitz (2007) argues that the principal justification for fair value accounting lies in its decision usefulness, as fair value information better supports the economic decisions of financial statement users. Similarly, Landsman (2007) demonstrates that evidence from capital markets supports the value relevance of fair value information, particularly when it relates to assets and liabilities measured using observable market data. Therefore, the use of fair value is expected to improve the relevance of financial reporting information.

H3 : The use of fair value has a positive effect on the relevance of financial reporting information.

Although fair value is considered highly relevant, its usefulness depends on the quality of the inputs used in the valuation process. IFRS 13 classifies fair value measurements into three levels based on the observability of valuation inputs. Level 1 measurements rely on quoted prices in active markets, Level 2 measurements use observable market inputs other than quoted prices, whereas Level 3 measurements rely on unobservable inputs and involve greater management judgment and estimation (IFRS Foundation, 2021). Song et al. (2010) found that Level 1 and Level 2 fair value measurements exhibit greater value relevance than Level 3 measurements because observable inputs are perceived as more credible by investors. Therefore, greater observability of fair value inputs is expected to enhance the relevance of fair value information.

H4 : The observability of fair value inputs has a positive effect on the relevance of fair value information.

Despite its advantages, fair value measurement may introduce greater measurement uncertainty, particularly when active market prices are unavailable. In such situations, entities must rely on valuation models and internal assumptions, increasing the degree of subjectivity in the measurement process. Laux and Leuz (2010) argue that criticism of fair value accounting primarily concerns the volatility and valuation uncertainty that may arise, especially during periods of financial crisis or market illiquidity. Likewise, McDonough et al. (2020) emphasize that the quality of fair value estimates depends on estimation techniques, auditability, and disclosure practices, all of which influence the reliability of fair value information. Accordingly, greater measurement uncertainty is expected to weaken the positive relationship between fair value measurement and faithful representation.

H5 : Measurement uncertainty weakens the positive effect of fair value on the faithful representation of financial reporting information.

Disclosure quality plays a critical role in enhancing the usefulness of fair value information. When fair value measurements are based on complex valuation techniques and unobservable inputs, financial statement users require transparent disclosures regarding valuation methods, key assumptions, measurement inputs, and sensitivity analyses. Gassen and Schwedler (2010) demonstrate that the decision usefulness of accounting measurements depends significantly on users' perceptions of the information provided. Similarly, Goh et al. (2021) found that users' confidence in fair value accounting is influenced by their perceptions of its benefits, associated costs, and the credibility of the measurement process. Therefore, high-

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quality fair value disclosures are expected to strengthen the positive effect of fair value information on investors' decision usefulness.

H6 : The quality of fair value disclosures strengthens the positive effect of fair value information on investors' decision usefulness.

III. Result and Discussion

This study adopts a qualitative approach using a structured literature review design. This approach was selected because the study aims to examine the conceptual and empirical debate between historical cost and fair value within the context of accounting recognition and measurement theory. A literature review is considered appropriate because accounting measurement issues extend beyond recording practices and involve conceptual foundations, qualitative characteristics of financial information, the development of accounting standards, and empirical evidence regarding the usefulness of accounting information for financial statement users. According to Snyder (2019), a literature review as a research method enables researchers to systematically identify, evaluate, integrate, and synthesize existing knowledge within a particular field. In accounting research, a structured literature review can also facilitate conceptual mapping, identification of theoretical debates, and the development of future research directions (Massaro et al., 2016). This study employs a descriptive-analytical approach. The descriptive component is used to explain the concepts of recognition, measurement, historical cost, fair value, relevance, faithful representation, stewardship, and decision usefulness. Meanwhile, the analytical component is applied to compare the strengths and limitations of historical cost and fair value based on accounting theory, the Conceptual Framework for Financial Reporting, accounting standards, and previous empirical studies. Therefore, this study does not merely summarize existing literature but also provides a critical synthesis of the relationship between accounting measurement bases and the quality of financial reporting information. The data used in this study consist of secondary data obtained from reputable international journal articles, relevant national journal articles, academic books, accounting standards, and official documents issued by accounting standard-setting bodies. The primary sources include literature discussing financial reporting measurement, fair value accounting, historical cost, value relevance, measurement uncertainty, faithful representation, and the qualitative characteristics of financial information. Furthermore, this study incorporates authoritative accounting documents, including the Conceptual Framework for Financial Reporting and IFRS 13 Fair Value Measurement, as normative references for analyzing measurement bases and the qualitative characteristics of financial statements.

The data collection process was conducted through literature review and documentation. The literature search was performed using academic databases, including ScienceDirect, Wiley Online Library, Emerald Insight, Taylor & Francis Online, SAGE Journals, the American Accounting Association Digital Library, and Google Scholar. The keywords used in the search process included “historical cost,” “fair value accounting,” “measurement in financial reporting,” “financial reporting quality,” “value relevance of fair value,” “fair value hierarchy,” “measurement uncertainty,” “faithful representation,” “decision usefulness,” and “stewardship accounting.” These keywords were combined using Boolean operators, such as AND and OR, to refine the search results and ensure alignment with the research objectives. The inclusion criteria applied in this study consist of the following: (1) articles discussing recognition, measurement, historical cost, fair value, or financial reporting quality; (2) articles published in reputable international or relevant national academic journals; (3) articles providing conceptual or empirical contributions to the debate on accounting measurement bases; (4) articles available in full-text format; and (5) articles with clear publication information, including journal title, volume, issue, page numbers, and DOI when available. The exclusion criteria include articles that are not directly related to accounting measurement, non-academic publications, opinion-based articles without methodological foundations, publications with unclear source information, and literature discussing historical cost or fair value only from a normative perspective without examining its implications

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for financial reporting quality. The literature selection process was conducted through several stages. The first stage involved identifying relevant literature based on predetermined keywords. The second stage consisted of an initial screening process based on article titles and abstracts to assess their relevance to the research focus. The third stage involved an eligibility assessment through a comprehensive review of the full-text articles. The final stage involved selecting the literature used as the basis for analysis. This procedure follows the principles of systematic literature review, which emphasize transparency, traceability, and replicability in the literature selection process (Tranfield et al., 2003). Although this study does not apply quantitative meta-analysis, transparent reporting principles are maintained to ensure that the literature selection process can be academically justified.

The data analysis technique employed in this study is qualitative content analysis. This technique is used to identify major themes within the literature, classify conceptual arguments, and compare empirical findings that support or criticize the application of historical cost and fair value. Qualitative content analysis is appropriate for document-based research because it enables researchers to systematically categorize, interpret, and synthesize textual information (Elo & Kyngäs, 2008). In accounting and organizational research, content analysis is also widely applied to examine themes, patterns, and conceptual relationships within academic literature (Duriau et al., 2007). The analysis process was conducted through three main stages. First, data reduction was performed by selecting and filtering information relevant to the research objectives. Literature that was unrelated to recognition, measurement, historical cost, fair value, relevance, faithful representation, stewardship, and decision usefulness was excluded from the main analysis. Second, categorization was conducted by grouping the selected literature into several thematic areas, including the conceptual foundations of accounting measurement, the advantages and limitations of historical cost, the advantages and limitations of fair value, value relevance of fair value, measurement uncertainty, financial statement volatility, and implications for accounting standards. Third, synthesis was conducted by integrating conceptual perspectives and empirical findings to develop a comprehensive understanding of the debate between historical cost and fair value. To strengthen the analytical process, this study applies a thematic synthesis approach. Thematic synthesis was conducted by comparing arguments across studies, identifying similarities and differences in findings, and evaluating the contribution of each source to the research topic. Literature supporting historical cost was analyzed primarily from the perspectives of objectivity, verifiability, stability, and stewardship. Meanwhile, literature supporting fair value was analyzed based on relevance, predictive value, decision usefulness, and the ability to reflect current market conditions. Critical perspectives were also examined to understand concerns related to volatility, subjectivity, measurement uncertainty, and potential estimation bias arising from fair value measurements.

The validity of the findings was maintained through source triangulation and the establishment of a literature audit trail. Source triangulation was conducted by comparing information obtained from academic articles, accounting standards, and scholarly books to ensure that the analysis was not dependent on a single type of source. The literature audit trail involved documenting the sources reviewed, research themes discussed, theoretical arguments presented, and contributions of each article to the analysis. This procedure enhances the transparency and credibility of literature-based research. Furthermore, this study prioritizes publications from reputable journals and sources with identifiable DOIs to ensure that the selected references are verifiable and traceable. This study has several methodological limitations. First, it relies on secondary data and therefore does not involve statistical testing based on specific companies or datasets. Second, the study focuses specifically on the conceptual and empirical debate between historical cost and fair value and does not examine all existing accounting measurement bases in detail. Third, the literature synthesis is limited to studies and accounting standards identified through the selected search strategy, meaning that some relevant literature may not have been included. Nevertheless, the structured literature review approach provides a rigorous foundation for understanding theoretical developments, empirical evidence, and the implications of accounting standards related to recognition and measurement. Through this methodology, this study seeks to provide a systematic, critical, and comprehensive analysis of the debate between historical cost and fair value. This approach enables the study not only to explain the conceptual differences between

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the two measurement bases but also to evaluate their respective contributions to financial reporting quality, particularly regarding relevance, faithful representation, volatility, stewardship, and decision usefulness.

IV. Results and Discussion

4.1. Research Findings

The literature review indicates that the debate between historical cost and fair value cannot be understood simply as a dichotomy between an traditional measurement approach and a modern alternative. Both measurement bases have distinct orientations, advantages, and limitations in providing financial reporting information. Historical cost demonstrates greater strengths in terms of objectivity, verifiability, stability, and its role in supporting management stewardship. In contrast, fair value provides stronger advantages in terms of relevance, timeliness, predictive value, and the usefulness of information for economic decision-making. The first finding indicates that historical cost tends to generate information that is more stable and easier to verify. This is because assets and liabilities are recorded based on acquisition costs or actual transaction values at the time economic events occur. These characteristics make historical cost more closely aligned with the concept of faithful representation, particularly regarding neutrality and verifiability. Supported by transaction evidence, such as invoices, contracts, and other relevant documentation, accounting information based on historical cost can be more readily examined by auditors and independent parties. However, the second finding reveals that the reliability advantage of historical cost also represents its primary limitation. Because reported values are not continuously adjusted to reflect current market conditions, historical cost information may become less relevant when significant changes occur in economic values. Under conditions of inflation, fluctuations in asset prices, changes in interest rates, or shifts in market risks, historical carrying amounts may differ substantially from current economic values. Consequently, financial statements may provide stable information but may not fully capture prevailing economic conditions. The third finding demonstrates that fair value provides a significant advantage by generating more relevant information for financial statement users. Fair value measurement reflects market prices or estimated current values at the measurement date. Therefore, the resulting information is more responsive to economic changes and more useful for investors in evaluating firm value, risk exposure, and future cash flow prospects. Fair value is particularly beneficial for assets and liabilities whose values are highly influenced by market fluctuations, including financial instruments, investment properties, and other assets with active markets.

The fourth finding highlights that the application of fair value also creates important challenges related to subjectivity and measurement uncertainty. When active market prices are available, fair value measurement provides a relatively high level of objectivity. However, when fair value is determined using valuation techniques and internal assumptions, the resulting information becomes more dependent on professional judgment and estimation processes. In this context, the fair value hierarchy plays an important role. Level 1 fair value measurements provide the highest degree of reliability because they are based on quoted prices in active markets, whereas Level 3 measurements involve the greatest risk of subjectivity because they rely on unobservable inputs. The fifth finding indicates that the use of fair value may contribute to increased volatility in financial statements. Changes in the market values of assets and liabilities may directly affect profit or loss, equity, or other comprehensive income, depending on the applicable accounting treatment. This volatility can be interpreted from two perspectives. On the one hand, volatility may be considered a limitation because it reduces earnings stability and increases uncertainty in evaluating financial performance. On the other hand, volatility may also represent relevant information because it reflects actual changes in economic conditions and market values. The sixth finding shows that contemporary accounting standards generally avoid adopting a single measurement basis universally. Instead, IFRS and PSAK commonly apply a mixed measurement model, which involves the use of different measurement bases according to the characteristics of assets, liabilities, and financial reporting objectives. This approach recognizes that historical

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cost and fair value serve complementary functions rather than competing purposes. Historical cost is more appropriate for elements requiring stability and verifiability, whereas fair value is more suitable for elements requiring current information and greater responsiveness to market conditions. Overall, the findings of this study can be summarized as presented in Table 1.

Table 1. Comparative Synthesis of Historical Cost and Fair Value Measurement Bases

Aspect Examined	Historical Cost	Fair Value	Implications for Financial Reporting Quality
Measurement basis	Acquisition cost or historical transaction value	Market value or estimated current value	Determines the orientation and characteristics of reported information
Main strength	Objective, stable, and highly verifiable	Relevant, current, and responsive to market conditions	Reflects the trade-off between faithful representation and relevance
Main weakness	Limited ability to reflect current economic values	Potential subjectivity and financial statement volatility	Requires an appropriate balance in selecting measurement approaches
Alignment with qualitative characteristics	Supports faithful representation and stewardship	Supports relevance and decision usefulness	Reflects different purposes and users of accounting information
Main risk	Carrying amounts may become outdated over time	Measurement uncertainty and reliance on management estimates	Requires sufficient disclosure and transparency
Standard-setting implication	Appropriate for assets measured based on stable transaction values	Appropriate for financial instruments, investment properties, and market-sensitive assets	Supports the application of a mixed measurement model

4.2. Discussion

The findings of this study reinforce the argument that historical cost remains an important measurement basis in financial reporting, despite the increasing adoption of fair value by modern accounting standards. The primary advantage of historical cost lies in its objectivity and verifiability. Historical cost information is derived from actual transactions and can therefore be supported by reliable documentary evidence. Within the Conceptual Framework for Financial Reporting, this characteristic is consistent with faithful representation, which requires financial information to be complete, neutral, and free from material error (IFRS Foundation, 2018). Barth (2014) further emphasizes that the selection of a measurement basis should be based on the qualitative characteristics of financial information rather than merely on established accounting practices. The relevance of historical cost is also closely associated with the stewardship function of financial reporting. From a stewardship perspective, financial statements serve as a mechanism for evaluating how effectively management manages resources entrusted by shareholders. Stable, objective, and verifiable information is essential because it enables users to assess managerial accountability and performance. Ball (2006) argues that the quality of accounting information is influenced not only by the adoption of accounting standards but also by reporting incentives, monitoring mechanisms, and the effectiveness of standard implementation. Therefore, historical cost remains valuable in supporting control mechanisms, auditing processes, and assessments of managerial responsibility. Nevertheless, the findings also highlight the limitations of historical cost, particularly when measuring assets and liabilities that are significantly influenced by market fluctuations. Historical values may become less informative when economic

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conditions change substantially. For instance, assets acquired several years earlier may have current market values that differ considerably from their historical carrying amounts. Under such circumstances, historical cost information may remain reliable but may not provide sufficient relevance for investment decision-making. This limitation is consistent with Barth's (2014) argument that the selection of a measurement basis should consider whether the resulting information effectively fulfills the objectives of financial reporting.

In contrast, fair value provides a significant contribution to the relevance of financial reporting information. Fair value measurement reflects current market conditions and provides information that is closer to the economic value of assets and liabilities at the reporting date. Hitz (2007) explains that the primary justification for fair value accounting is decision usefulness, referring to the ability of accounting information to support users in making rational economic decisions. Landsman (2007) also demonstrates that capital market research provides substantial evidence regarding the value relevance of fair value information, particularly for financial assets and liabilities. These findings support the argument that fair value provides more informative signals for investors when market values are observable and reliable. However, the application of fair value cannot be separated from concerns regarding the hierarchy and quality of measurement inputs. Fair value determined from active market prices differs significantly from fair value estimated through internal valuation models. Song et al. (2010) found that Level 1 and Level 2 fair value measurements generally demonstrate greater value relevance than Level 3 measurements. This finding indicates that investors place greater confidence in fair value information supported by observable market inputs. Therefore, the usefulness of fair value information depends not only on the measurement basis itself but also on the degree of input observability used in the valuation process. Another important issue associated with fair value measurement is financial statement volatility. The findings indicate that fair value may increase fluctuations in earnings, equity, or other comprehensive income because changes in market values are recognized in financial reporting. Laux and Leuz (2010) explain that criticism of fair value accounting intensified following the global financial crisis because fair value was perceived as potentially increasing financial statement volatility. However, they also emphasize that empirical evidence does not sufficiently support the conclusion that fair value accounting was the primary cause of the crisis. Therefore, volatility resulting from fair value measurements should not automatically be viewed as a weakness; rather, it may provide relevant information regarding changes in underlying economic conditions.

In this regard, volatility must be interpreted within the appropriate context. When volatility reflects genuine changes in economic conditions, it may enhance the relevance of financial reporting information. Conversely, when volatility arises from unreliable estimates, biased management assumptions, or illiquid markets, the quality of accounting information may deteriorate. McDonough et al. (2020) emphasize that research on fair value accounting should not only focus on value relevance but also consider estimation quality, auditability, disclosure practices, and the implications of measurement decisions for users. Therefore, the effectiveness of fair value accounting depends significantly on the quality of its implementation. The findings further demonstrate that disclosure quality plays an important role in mitigating the limitations associated with fair value measurement. When fair value is determined using valuation techniques, financial statement users require additional disclosures regarding valuation methods, assumptions, inputs, and sensitivity to changes in estimates. Gassen and Schwedler (2010) show that the usefulness of accounting measurements depends on users' perceptions of the quality and reliability of the information disclosed. Similarly, Goh et al. (2021) find that confidence in fair value accounting is influenced by stakeholders' perceptions of its benefits, costs, and the credibility of the measurement process. Therefore, fair value should not be presented merely as a numerical amount but should be accompanied by transparent disclosures that enable users to evaluate the reliability of the underlying estimates. The findings also indicate that the debate between historical cost and fair value should not be framed as a question of determining which measurement basis is universally superior. In contemporary financial reporting practice, different measurement bases serve different purposes. Historical cost is more appropriate when reporting objectives emphasize verifiability, stability, and accountability. Conversely, fair value is more suitable when reporting objectives emphasize

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relevance, timeliness, and the assessment of current economic values. Accordingly, the mixed measurement model represents a more practical approach than the exclusive application of a single measurement basis.

The implications of these findings suggest that standard setters and financial statement preparers should consider the economic characteristics of assets and liabilities when determining appropriate measurement bases. For property, plant, and equipment used in long-term operations and not intended for immediate sale, historical cost may provide stable and verifiable information. In contrast, for financial instruments and other assets with active market prices, fair value may provide more relevant information for investors. Therefore, financial reporting quality is determined not only by the choice between historical cost and fair value but also by the extent to which the selected measurement basis reflects the economic characteristics of the reported financial statement elements. Within the Indonesian accounting context, this discussion is particularly relevant because Indonesian Financial Accounting Standards (PSAK), which have converged with IFRS, also adopt a mixed measurement approach. Property, plant, and equipment may generally be measured using either the cost model or the revaluation model, while investment properties and certain financial instruments may be measured using fair value in accordance with applicable standards. This approach demonstrates that Indonesian accounting standards recognize the need to balance relevance and faithful representation. Nevertheless, the implementation of fair value in Indonesia continues to require supporting conditions, including active markets, competent independent valuation professionals, effective corporate governance, and adequate disclosure practices. Overall, the findings of this study demonstrate that historical cost and fair value should not be viewed as mutually exclusive approaches but rather as complementary measurement bases with different functions in financial reporting. Historical cost provides advantages in terms of reliability, objectivity, and accountability, whereas fair value provides advantages in terms of relevance, timeliness, and decision usefulness. Therefore, the central issue in accounting measurement is not determining which approach is inherently superior, but rather ensuring that both measurement bases are applied appropriately and proportionally to produce financial statements that are relevant, faithfully represented, transparent, and useful for decision-making.

V. Conclusion

Based on the discussion, it can be concluded that the concepts of recognition and measurement in accounting play a fundamental role in determining the quality of financial reporting information. Recognition determines whether an economic transaction or event should be recognized and presented in the financial statements, whereas measurement determines the monetary amount assigned to the recognized financial statement elements. Within this context, historical cost and fair value represent two primary measurement bases with distinct characteristics, advantages, and limitations. Historical cost emphasizes objectivity, verifiability, and information stability because it is based on actual transactions supported by reliable evidence. Consequently, this measurement basis tends to provide more reliable information and supports the stewardship function of management. However, its primary limitation lies in its inability to adequately reflect current economic values, particularly when significant changes occur in market conditions. In contrast, fair value provides more relevant information because it reflects current market values and economic conditions at the measurement date. The application of fair value enables investors and other financial statement users to assess an entity's economic position more accurately, particularly for assets and liabilities with active markets. Nevertheless, fair value also has limitations, especially when its determination relies on valuation techniques, management assumptions, and estimation processes. Under such circumstances, the resulting information may involve greater subjectivity and measurement uncertainty. Furthermore, fair value may increase volatility in reported earnings and asset values because changes in market values are recognized in financial statements. Therefore, historical cost and fair value reflect a fundamental trade-off between the qualitative characteristics of faithful representation and relevance. The findings of this study further demonstrate that neither measurement basis is universally superior to the other. Historical cost is more appropriate when financial reporting objectives emphasize stability, verifiability, and accountability, whereas

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fair value is more suitable when reporting objectives emphasize relevance, timeliness, and decision usefulness. Accordingly, contemporary accounting standards increasingly adopt a mixed measurement model that allows historical cost and fair value to be applied proportionally according to the characteristics of assets, liabilities, and financial reporting objectives. Therefore, financial reporting quality is determined not merely by the selection of a measurement basis but also by the extent to which the selected basis reflects the economic substance of transactions and meets the information needs of financial statement users.

The implications of this study suggest that financial statement preparers should carefully determine appropriate measurement bases by considering the characteristics of assets and liabilities, prevailing market conditions, and reporting objectives. The application of historical cost or fair value should not be performed mechanically but should instead consider the balance between relevance and faithful representation. For accounting standard setters, the findings highlight the importance of developing accounting standards that remain responsive to changes in the business environment, particularly by enhancing transparency in fair value measurements through adequate disclosures regarding valuation techniques, key assumptions, and levels of measurement uncertainty. For investors and other users of financial statements, a comprehensive understanding of the characteristics, strengths, and limitations of historical cost and fair value is essential to ensure that accounting information is interpreted appropriately and supports sound economic decision-making. This study has several limitations, primarily because it adopts a literature review approach and does not conduct empirical testing involving specific companies or industry sectors. Therefore, future research is encouraged to empirically investigate the effects of historical cost and fair value applications in specific sectors in Indonesia, such as banking, property, manufacturing, and consumer goods. Future studies may also examine the relationship between fair value measurements and earnings volatility, the value relevance of accounting information, disclosure quality, and investor decision-making behavior. Through further empirical investigation, future research is expected to provide broader evidence regarding the effectiveness of historical cost and fair value in enhancing the quality of financial reporting.

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