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Part A

Issued Standards and the *Conceptual Framework for Financial Reporting*

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globally comparable information, those Standards are also of vital importance to regulators around the world.

(c) contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation. For businesses, the use of a single, trusted accounting language derived from Standards based on the *Conceptual Framework* lowers the cost of capital and reduces international reporting costs.

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Introduction

1.1 The objective of general purpose financial reporting forms the foundation of the *Conceptual Framework*. Other aspects of the *Conceptual Framework*—the qualitative characteristics of, and the cost constraint on, useful financial information, [Refer: Chapter 2] a reporting entity concept, [Refer: Chapter 3] elements of financial statements, [Refer: Chapter 4] recognition and derecognition, [Refer: Chapter 5] measurement, [Refer: Chapter 6] presentation and disclosure [Refer: Chapter 7] —flow logically from the objective.

Objective, usefulness and limitations of general purpose financial reporting

1.2 The objective of general purpose financial reporting[1] [Refer: Basis for Conclusions paragraphs BC1.4–BC1.7] is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions [Refer: Basis for Conclusions paragraphs BC1.27–BC1.31] relating to providing resources to the entity.[2] Those decisions involve decisions about:

(a) buying, selling or holding equity and debt instruments;

(b) providing or settling loans and other forms of credit; or

(c) exercising rights to vote on, or otherwise influence, management's actions that affect the use of the entity's economic resources.

1.3 The decisions described in paragraph 1.2 depend on the returns that existing and potential investors, lenders and other creditors expect, for example, dividends, principal and interest payments or market price increases. Investors', lenders' and other creditors' expectations about returns depend on their assessment of the amount, timing and uncertainty of (the prospects for) future net cash inflows to the entity and on their assessment of management's stewardship of the entity's economic resources. Existing and potential investors, lenders and other creditors need information to help them make those assessments.

1.4 To make the assessments described in paragraph 1.3, existing and potential investors, lenders and other creditors need information about:

(a) the economic resources of the entity, claims against the entity and changes in those resources and claims (see paragraphs 1.12–1.21); and

1 Throughout the *Conceptual Framework*, the terms 'financial reports' and 'financial reporting' refer to general purpose financial reports and general purpose financial reporting unless specifically indicated otherwise.

2 Throughout the *Conceptual Framework*, the term 'entity' refers to the reporting entity unless specifically indicated otherwise.

(b) how efficiently and effectively the entity's management and governing board[3] have discharged their responsibilities to use the entity's economic resources (see paragraphs 1.22–1.23). [Refer: Basis for Conclusions paragraphs BC1.32–BC1.41]

1.5 Many existing and potential investors, lenders and other creditors cannot require reporting entities to provide information directly to them and must rely on general purpose financial reports for much of the financial information they need. Consequently, they are the primary users to whom general purpose financial reports are directed.[4]

[Refer: Basis for Conclusions paragraphs BC1.9–BC1.26]

1.6 However, general purpose financial reports do not and cannot provide all of the information that existing and potential investors, lenders and other creditors need. Those users need to consider pertinent information from other sources, for example, general economic conditions and expectations, political events and political climate, and industry and company outlooks.

1.7 General purpose financial reports are not designed to show the value of a reporting entity; but they provide information to help existing and potential investors, lenders and other creditors to estimate the value of the reporting entity.

1.8 Individual primary users have different, and possibly conflicting, information needs and desires. The Board, in developing Standards, will seek to provide the information set that will meet the needs of the maximum number of primary users. However, focusing on common information needs does not prevent the reporting entity from including additional information that is most useful to a particular subset of primary users.

1.9 The management of a reporting entity is also interested in financial information about the entity. However, management need not rely on general purpose financial reports because it is able to obtain the financial information it needs internally.

[Refer: Basis for Conclusions paragraph BC1.22]

1.10 Other parties, such as regulators [Refer: Basis for Conclusions paragraphs BC1.23–BC1.26] and members of the public other than investors, lenders and other creditors, may also find general purpose financial reports useful. However, those reports are not primarily directed to these other groups.

1.11 To a large extent, financial reports are based on estimates, judgements and models rather than exact depictions. The *Conceptual Framework* establishes the concepts that underlie those estimates, judgements and models. The concepts are the goal towards which the Board and preparers of financial reports strive. As with most goals, the *Conceptual Framework*'s vision of ideal financial reporting is unlikely to be achieved in full, at least not in the short term.

3 Throughout the *Conceptual Framework*, the term 'management' refers to management and the governing board of an entity unless specifically indicated otherwise.

4 Throughout the *Conceptual Framework*, the terms 'primary users' and 'users' refer to those existing and potential investors, lenders and other creditors who must rely on general purpose financial reports for much of the financial information they need.

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because it takes time to understand, accept and implement new ways of analysing transactions and other events. Nevertheless, establishing a goal towards which to strive is essential if financial reporting is to evolve so as to improve its usefulness.

Information about a reporting entity's economic resources, claims against the entity and changes in resources and claims

[Refer: Basis for Conclusions paragraphs BC1.44–BC1.48]

1.12 General purpose financial reports provide information about the financial position of a reporting entity, which is information about the entity's economic resources and the claims against the reporting entity. Financial reports also provide information about the effects of transactions and other events that change a reporting entity's economic resources and claims. Both types of information provide useful input for decisions relating to providing resources to an entity.

Economic resources and claims

1.13 Information about the nature and amounts of a reporting entity's economic resources and claims can help users to identify the reporting entity's financial strengths and weaknesses. That information can help users to assess the reporting entity's liquidity and solvency, its needs for additional financing and how successful it is likely to be in obtaining that financing. That information can also help users to assess management's stewardship of the entity's economic resources. Information about priorities and payment requirements of existing claims helps users to predict how future cash flows will be distributed among those with a claim against the reporting entity.

1.14 Different types of economic resources affect a user's assessment of the reporting entity's prospects for future cash flows differently. Some future cash flows result directly from existing economic resources, such as accounts receivable. Other cash flows result from using several resources in combination to produce and market goods or services to customers. Although those cash flows cannot be identified with individual economic resources (or claims), users of financial reports need to know the nature and amount of the resources available for use in a reporting entity's operations.

Changes in economic resources and claims

1.15 Changes in a reporting entity's economic resources and claims result from that entity's financial performance (see paragraphs 1.17–1.20) and from other events or transactions such as issuing debt or equity instruments (see paragraph 1.21). To properly assess both the prospects for future net cash inflows to the reporting entity and management's stewardship of the entity's economic resources, users need to be able to identify those two types of changes.

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1.16 Information about a reporting entity's financial performance helps users to understand the return that the entity has produced on its economic resources. Information about the return the entity has produced can help users to assess management's stewardship of the entity's economic resources. Information about the variability and components of that return is also important, especially in assessing the uncertainty of future cash flows. Information about a reporting entity's past financial performance and how its management discharged its stewardship responsibilities is usually helpful in predicting the entity's future returns on its economic resources.

Financial performance reflected by accrual accounting

1.17 Accrual accounting depicts the effects of transactions and other events and circumstances on a reporting entity's economic resources and claims in the periods in which those effects occur, even if the resulting cash receipts and payments occur in a different period. This is important because information about a reporting entity's economic resources and claims and changes in its economic resources and claims during a period provides a better basis for assessing the entity's past and future performance than information solely about cash receipts and payments during that period.

1.18 Information about a reporting entity's financial performance during a period, reflected by changes in its economic resources and claims other than by obtaining additional resources directly from investors and creditors (see paragraph 1.21), is useful in assessing the entity's past and future ability to generate net cash inflows. That information indicates the extent to which the reporting entity has increased its available economic resources, and thus its capacity for generating net cash inflows through its operations rather than by obtaining additional resources directly from investors and creditors. Information about a reporting entity's financial performance during a period can also help users to assess management's stewardship of the entity's economic resources.

1.19 Information about a reporting entity's financial performance during a period may also indicate the extent to which events such as changes in market prices or interest rates have increased or decreased the entity's economic resources and claims, thereby affecting the entity's ability to generate net cash inflows.

Financial performance reflected by past cash flows

1.20 Information about a reporting entity's cash flows during a period also helps users to assess the entity's ability to generate future net cash inflows and to assess management's stewardship of the entity's economic resources. That information indicates how the reporting entity obtains and spends cash, including information about its borrowing and repayment of debt, cash dividends or other cash distributions to investors, and other factors that may affect the entity's liquidity or solvency. Information about cash flows helps users understand a reporting entity's operations, evaluate its financing and investing activities, assess its liquidity or solvency and interpret other information about financial performance.

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Introduction

2.1 The qualitative characteristics of useful financial information discussed in this chapter identify the types of information that are likely to be most useful to the existing and potential investors, lenders and other creditors for making decisions about the reporting entity on the basis of information in its financial report (financial information).

2.2 Financial reports provide information about the reporting entity's economic resources, claims against the reporting entity and the effects of transactions and other events and conditions that change those resources and claims. (This information is referred to in the *Conceptual Framework* as information about the economic phenomena.) Some financial reports also include explanatory material about management's expectations and strategies for the reporting entity, and other types of forward-looking information.

2.3 The qualitative characteristics of useful financial information[5] apply to financial information provided in financial statements, as well as to financial information provided in other ways. Cost, which is a pervasive constraint on the reporting entity's ability to provide useful financial information, applies similarly. However, the considerations in applying the qualitative characteristics and the cost constraint may be different for different types of information. For example, applying them to forward-looking information may be different from applying them to information about existing economic resources and claims and to changes in those resources and claims.

Qualitative characteristics of useful financial information

[Refer: Basis for Conclusions paragraphs BC2.9–BC2.69]

2.4 If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable.

Fundamental qualitative characteristics

[Refer: Basis for Conclusions paragraphs BC2.9–BC2.57]

2.5 The fundamental qualitative characteristics are relevance and faithful representation.

Relevance

[Refer: Basis for Conclusions paragraphs BC2.12–BC2.20]

2.6 Relevant financial information is capable of making a difference in the decisions made by users. Information may be capable of making a difference in a decision even if some users choose not to take advantage of it or are already aware of it from other sources. **[Refer: Basis for Conclusions paragraphs BC2.12–BC2.14]**

5 Throughout the *Conceptual Framework*, the terms 'qualitative characteristics' and 'cost constraint' refer to the qualitative characteristics of, and the cost constraint on, useful financial information.

2.7 Financial information is capable of making a difference in decisions if it has predictive value, confirmatory value or both. **[Refer: Basis for Conclusions paragraphs BC2.15 and BC2.16]**

2.8 Financial information has predictive value if it can be used as an input to processes employed by users to predict future outcomes. Financial information need not be a prediction or forecast to have predictive value. Financial information with predictive value is employed by users in making their own predictions.
[Refer: Basis for Conclusions paragraph BC2.17]

2.9 Financial information has confirmatory value if it provides feedback about (confirms or changes) previous evaluations.

2.10 The predictive value and confirmatory value of financial information are interrelated. Information that has predictive value often also has confirmatory value. For example, revenue information for the current year, which can be used as the basis for predicting revenues in future years, can also be compared with revenue predictions for the current year that were made in past years. The results of those comparisons can help a user to correct and improve the processes that were used to make those previous predictions.

Materiality
[Refer: Basis for Conclusions paragraphs BC2.18–BC2.20A]

2.11 Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports (see paragraph 1.5) make on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report. Consequently, the Board cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation.

Faithful representation

[Refer: Basis for Conclusions paragraphs BC2.21–BC2.51]

2.12 Financial reports represent economic phenomena in words and numbers. To be useful, financial information must not only represent relevant phenomena, but it must also faithfully represent the substance of the phenomena that it purports to represent. In many circumstances, the substance of an economic phenomenon and its legal form are the same. If they are not the same, providing information only about the legal form would not faithfully represent the economic phenomenon (see paragraphs 4.59–4.62). **[Refer: Basis for Conclusions paragraphs BC2.32 and BC2.33]**

2.13 To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral and free from error. Of course, perfection is seldom, if ever, achievable. The Board's objective is to maximise those qualities to the extent possible.

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2.14 A complete depiction includes all information necessary for a user to understand the phenomenon being depicted, including all necessary descriptions and explanations. For example, a complete depiction of a group of assets would include, at a minimum, a description of the nature of the assets in the group, a numerical depiction of all of the assets in the group, and a description of what the numerical depiction represents (for example, historical cost or fair value). For some items, a complete depiction may also entail explanations of significant facts about the quality and nature of the items, factors and circumstances that might affect their quality and nature, and the process used to determine the numerical depiction.

2.15 A neutral depiction is without bias in the selection or presentation of financial information. A neutral depiction is not slanted, weighted, emphasised, de-emphasised or otherwise manipulated to increase the probability that financial information will be received favourably or unfavourably by users. Neutral information does not mean information with no purpose or no influence on behaviour. On the contrary, relevant financial information is, by definition, capable of making a difference in users' decisions.

[Refer: Basis for Conclusions paragraphs BC2.34–BC2.36]

2.16 Neutrality is supported by the exercise of prudence. Prudence is the exercise of caution when making judgements under conditions of uncertainty. The exercise of prudence means that assets and income are not overstated and liabilities and expenses are not understated.[6] Equally, the exercise of prudence does not allow for the understatement of assets or income or the overstatement of liabilities or expenses. Such misstatements can lead to the overstatement or understatement of income or expenses in future periods.

[Refer: Basis for Conclusions paragraphs BC2.37–BC2.45]

2.17 The exercise of prudence does not imply a need for asymmetry, for example, a systematic need for more persuasive evidence to support the recognition of assets or income than the recognition of liabilities or expenses. Such asymmetry is not a qualitative characteristic of useful financial information. Nevertheless, particular Standards may contain asymmetric requirements if this is a consequence of decisions intended to select the most relevant information that faithfully represents what it purports to represent.

[Refer: Basis for Conclusions paragraphs BC2.41–BC2.45]

2.18 Faithful representation does not mean accurate in all respects. Free from error means there are no errors or omissions in the description of the phenomenon, and the process used to produce the reported information has been selected and applied with no errors in the process. In this context, free from error does not mean perfectly accurate in all respects. For example, an estimate of an unobservable price or value cannot be determined to be accurate or inaccurate. However, a representation of that estimate can be faithful if the amount is described clearly and accurately as being an estimate, the nature and limitations of the estimating process are explained, and no errors have

6 Assets, liabilities, income and expenses are defined in Table 4.1. They are the elements of financial statements.

been made in selecting and applying an appropriate process for developing the estimate.

2.19 When monetary amounts in financial reports cannot be observed directly and must instead be estimated, measurement uncertainty arises. The use of reasonable estimates is an essential part of the preparation of financial information and does not undermine the usefulness of the information if the estimates are clearly and accurately described and explained. Even a high level of measurement uncertainty does not necessarily prevent such an estimate from providing useful information (see paragraph 2.22).

[Refer: Basis for Conclusions paragraphs BC2.46–BC2.49]

Applying the fundamental qualitative characteristics

[Refer: Basis for Conclusions paragraphs BC2.52–BC2.57]

2.20 Information must both be relevant and provide a faithful representation of what it purports to represent if it is to be useful. Neither a faithful representation of an irrelevant phenomenon nor an unfaithful representation of a relevant phenomenon helps users make good decisions.

2.21 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, information about which 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. Third, determine whether that information is available and whether it can provide a faithful representation of the economic phenomenon. 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.

2.22 In some cases, a trade-off between the fundamental qualitative characteristics may need to be made in order to meet the objective of financial reporting, which is to provide useful information about economic phenomena. For example, the most relevant information about a phenomenon may be a highly uncertain estimate. In some cases, the level of measurement uncertainty involved in making that estimate may be so high that it may be questionable whether the estimate would provide a sufficiently faithful representation of that phenomenon. In some such cases, the most useful information may be the highly uncertain estimate, accompanied by a description of the estimate and an explanation of the uncertainties that affect it. In other such cases, if that information would not provide a sufficiently faithful representation of that phenomenon, the most useful information may include an estimate of another type that is slightly less relevant but is subject to lower measurement uncertainty. In limited circumstances, there may be no estimate that provides useful information. In those limited circumstances, it may be necessary to provide information that does not rely on an estimate.

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Enhancing qualitative characteristics

[Refer: Basis for Conclusions paragraphs BC2.58–BC2.69]

2.23 Comparability, verifiability, timeliness and understandability are qualitative characteristics that enhance the usefulness of information that both is relevant and provides a faithful representation of what it purports to represent. The enhancing qualitative characteristics may also help determine which of two ways should be used to depict a phenomenon if both are considered to provide equally relevant information and an equally faithful representation of that phenomenon.

Comparability

[Refer: Basis for Conclusions paragraphs BC2.58 and BC2.59]

2.24 Users' decisions involve choosing between alternatives, for example, selling or holding an investment, or investing in one reporting entity or another. Consequently, information about a reporting entity is more useful if it can be compared with similar information about other entities and with similar information about the same entity for another period or another date.

2.25 Comparability is the qualitative characteristic that enables users to identify and understand similarities in, and differences among, items. Unlike the other qualitative characteristics, comparability does not relate to a single item. A comparison requires at least two items.

2.26 Consistency, although related to comparability, is not the same. Consistency refers to the use of the same methods for the same items, either from period to period within a reporting entity or in a single period across entities. Comparability is the goal; consistency helps to achieve that goal.

2.27 Comparability is not uniformity. For information to be comparable, like things must look alike and different things must look different. Comparability of financial information is not enhanced by making unlike things look alike any more than it is enhanced by making like things look different.

2.28 Some degree of comparability is likely to be attained by satisfying the fundamental qualitative characteristics. A faithful representation of a relevant economic phenomenon should naturally possess some degree of comparability with a faithful representation of a similar relevant economic phenomenon by another reporting entity.

2.29 Although a single economic phenomenon can be faithfully represented in multiple ways, permitting alternative accounting methods for the same economic phenomenon diminishes comparability.

Verifiability

[Refer: Basis for Conclusions paragraphs BC2.60–BC2.62]

2.30 Verifiability helps assure users that information faithfully represents the economic phenomena it purports to represent. Verifiability means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation. Quantified information need not be a single point

estimate to be verifiable. A range of possible amounts and the related probabilities can also be verified.

2.31 Verification can be direct or indirect. Direct verification means verifying an amount or other representation through direct observation, for example, by counting cash. Indirect verification means checking the inputs to a model, formula or other technique and recalculating the outputs using the same methodology. An example is verifying the carrying amount of inventory by checking the inputs (quantities and costs) and recalculating the ending inventory using the same cost flow assumption (for example, using the first-in, first-out method).

2.32 It may not be possible to verify some explanations and forward-looking financial information until a future period, if at all. To help users decide whether they want to use that information, it would normally be necessary to disclose the underlying assumptions, the methods of compiling the information and other factors and circumstances that support the information.

Timeliness

[Refer: Basis for Conclusions paragraphs BC2.63–BC2.65]

2.33 Timeliness means having information available to decision-makers in time to be capable of influencing their decisions. Generally, the older the information is the less useful it is. However, some information may continue to be timely long after the end of a reporting period because, for example, some users may need to identify and assess trends.

Understandability

[Refer: Basis for Conclusions paragraphs BC2.66–BC2.69]

2.34 Classifying, characterising and presenting information clearly and concisely makes it understandable.

2.35 Some phenomena are inherently complex and cannot be made easy to understand. Excluding information about those phenomena from financial reports might make the information in those financial reports easier to understand. However, those reports would be incomplete and therefore possibly misleading.

2.36 Financial reports are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently. At times, even well-informed and diligent users may need to seek the aid of an adviser to understand information about complex economic phenomena.

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Applying the enhancing qualitative characteristics

2.37 Enhancing qualitative characteristics should be maximised to the extent possible. However, the enhancing qualitative characteristics, either individually or as a group, cannot make information useful if that information is irrelevant or does not provide a faithful representation of what it purports to represent.

[Refer: Basis for Conclusions paragraphs BC2.9 and BC2.11]

2.38 Applying the enhancing qualitative characteristics is an iterative process that does not follow a prescribed order. Sometimes, one enhancing qualitative characteristic may have to be diminished to maximise another qualitative characteristic. For example, a temporary reduction in comparability as a result of prospectively applying a new Standard may be worthwhile to improve relevance or faithful representation in the longer term. Appropriate disclosures may partially compensate for non-comparability.

The cost constraint on useful financial reporting

[Refer: Basis for Conclusions paragraphs BC2.73 and BC2.74]

2.39 Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting that information. There are several types of costs and benefits to consider.

2.40 Providers of financial information expend most of the effort involved in collecting, processing, verifying and disseminating financial information, but users ultimately bear those costs in the form of reduced returns. Users of financial information also incur costs of analysing and interpreting the information provided. If needed information is not provided, users incur additional costs to obtain that information elsewhere or to estimate it.

2.41 Reporting financial information that is relevant and faithfully represents what it purports to represent helps users to make decisions with more confidence. This results in more efficient functioning of capital markets and a lower cost of capital for the economy as a whole. An individual investor, lender or other creditor also receives benefits by making more informed decisions. However, it is not possible for general purpose financial reports to provide all the information that every user finds relevant.

2.42 In applying the cost constraint, the Board assesses whether the benefits of reporting particular information are likely to justify the costs incurred to provide and use that information. When applying the cost constraint in developing a proposed Standard, the Board seeks information from providers of financial information, users, auditors, academics and others about the expected nature and quantity of the benefits and costs of that Standard. In most situations, assessments are based on a combination of quantitative and qualitative information.

2.43 Because of the inherent subjectivity, different individuals' assessments of the costs and benefits of reporting particular items of financial information will vary. Therefore, the Board seeks to consider costs and benefits in relation to financial reporting generally, and not just in relation to individual reporting entities. That does not mean that assessments of costs and benefits always justify the same reporting requirements for all entities. Differences may be appropriate because of different sizes of entities, different ways of raising capital (publicly or privately), different users' needs or other factors.

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IFRS 1

First-time Adoption of International Financial Reporting Standards

The text of the unaccompanied standard, IFRS 1, is contained in Part A of this edition. Its effective date when issued was 1 July 2009. The text of the Basis for Conclusions on IFRS 1 is contained in Part C of this edition. This part presents the following documents:

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Guidance on implementing IFRS 1 *First-time Adoption of International Financial Reporting Standards*

This guidance accompanies, but is not part of, IFRS 1.

Introduction

IG1 This implementation guidance:

(a) explains how the requirements of the IFRS interact with the requirements of some other IFRSs (paragraphs IG2–IG62, IG64 and IG65). This explanation addresses those IFRSs that are most likely to involve questions that are specific to first-time adopters.

(b) includes an illustrative example to show how a first-time adopter might disclose how the transition to IFRSs affected its reported financial position, financial performance and cash flows, as required by paragraphs 24(a) and (b), 25 and 26 of the IFRS (paragraph IG63).

IAS 10 *Events after the Reporting Period*

IG2 Except as described in paragraph IG3, an entity applies IAS 10 in determining whether:

(a) its opening IFRS statement of financial position reflects an event that occurred after the date of transition to IFRSs; and

(b) comparative amounts in its first IFRS financial statements reflect an event that occurred after the end of that comparative period.

IG3 Paragraphs 14–17 of the IFRS require some modifications to the principles in IAS 10 when a first-time adopter determines whether changes in estimates are adjusting or non-adjusting events at the date of transition to IFRSs (or, when applicable, the end of the comparative period). Cases 1 and 2 below illustrate those modifications. In case 3 below, paragraphs 14–17 of the IFRS do not require modifications to the principles in IAS 10.

(a) Case 1 – Previous GAAP required estimates of similar items for the date of transition to IFRSs, using an accounting policy that is consistent with IFRSs. In this case, the estimates in accordance with IFRSs need to be consistent with estimates made for that date in accordance with previous GAAP, unless there is objective evidence that those estimates were in error (see IAS 8 *Basis of Preparation of Financial Statements*). The entity reports later revisions to those estimates as events of the period in which it makes the revisions, rather than as adjusting events resulting from the receipt of further evidence about conditions that existed at the date of transition to IFRSs.

[Refer: paragraphs 14 and 15]

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(b) Case 2 – Previous GAAP required estimates of similar items for the date of transition to IFRSs, but the entity made those estimates using accounting policies that are not consistent with its accounting policies in accordance with IFRSs. In this case, the estimates in accordance with IFRSs need to be consistent with the estimates required in accordance with previous GAAP for that date (unless there is objective evidence that those estimates were in error), after adjusting for the difference in accounting policies. The opening IFRS statement of financial position reflects those adjustments for the difference in accounting policies. As in case 1, the entity reports later revisions to those estimates as events of the period in which it makes the revisions.

For example, previous GAAP may have required an entity to recognise and measure provisions on a basis consistent with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, except that the previous GAAP measurement was on an undiscounted basis. In this example, the entity uses the estimates in accordance with previous GAAP as inputs in making the discounted measurement required by IAS 37.

[Refer: paragraphs 14 and 15]

(c) Case 3 – Previous GAAP did not require estimates of similar items for the date of transition to IFRSs. Estimates in accordance with IFRSs for that date reflect conditions existing at that date. In particular, estimates of market prices, interest rates or foreign exchange rates at the date of transition to IFRSs reflect market conditions at that date. This is consistent with the distinction in IAS 10 between adjusting events after the reporting period and non-adjusting events after the reporting period.

[Refer: paragraphs 14 and 15]

IG Example 1 Estimates
Background
Entity A's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information **[Refer: paragraphs 21 and 22]** for one year. In its previous GAAP financial statements for 31 December 20X3 and 20X4, entity A:
(a) made estimates of accrued expenses and provisions at those dates;
(b) accounted on a cash basis for a defined benefit pension plan; and
(c) did not recognise a provision for a court case arising from events that occurred in September 20X4. When the court case was concluded on 30 June 20X5, entity A was required to pay CU1,000[a] and paid this on 10 July 20X5.

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IG Example 1 Estimates

In preparing its first IFRS financial statements, entity A concludes that its estimates in accordance with previous GAAP of accrued expenses and provisions at 31 December 20X3 and 20X4 were made on a basis consistent with its accounting policies in accordance with IFRSs. Although some of the accruals and provisions turned out to be overestimates and others to be underestimates, entity A concludes that its estimates were reasonable and that, therefore, no error had occurred. As a result, accounting for those overestimates and underestimates involves the routine adjustment of estimates in accordance with IAS 8.

Application of requirements

In preparing its opening IFRS statement of financial position at 1 January 20X4 and in its comparative statement of financial position at 31 December 20X4, entity A:

(a) does not adjust the previous estimates for accrued expenses and provisions; and **[Refer: paragraphs 14 and 15]**

(b) makes estimates (in the form of actuarial assumptions) necessary to account for the pension plan in accordance with IAS 19 *Employee Benefits*. Entity A's actuarial assumptions at 1 January 20X4 and 31 December 20X4 do not reflect conditions that arose after those dates. For example, entity A's:

(i) discount rates at 1 January 20X4 and 31 December 20X4 for the pension plan and for provisions reflect market conditions at those dates; and

(ii) actuarial assumptions at 1 January 20X4 and 31 December 20X4 about future employee turnover rates do not reflect conditions that arose after those dates – such as a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan in 20X5. **[Refer: paragraphs 14 and 16]**

The treatment of the court case at 31 December 20X4 depends on the reason why entity A did not recognise a provision in accordance with previous GAAP at that date.

Assumption 1 – Previous GAAP was consistent with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Entity A concluded that the recognition criteria were not met. **[Refer: IAS 37 paragraph 14]** In this case, entity A's assumptions in accordance with IFRSs are consistent with its assumptions in accordance with previous GAAP. Therefore, entity A does not recognise a provision at 31 December 20X4. **[Refer: paragraphs 14 and 15]**

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IG Example 1 Estimates

Assumption 2 – Previous GAAP was not consistent with IAS 37. Therefore, entity A develops estimates in accordance with IAS 37. Under IAS 37, an entity determines whether an obligation exists at the end of the reporting period by taking account of all available evidence, including any additional evidence provided by events after the reporting period. **[Refer: IAS 37 paragraphs 14–16]** Similarly, in accordance with IAS 10 *Events after the Reporting Period*, the resolution of a court case after the reporting period is an adjusting event after the reporting period if it confirms that the entity had a present obligation at that date. **[Refer: IAS 10 paragraphs 8 and 9]** In this instance, the resolution of the court case confirms that entity A had a liability in September 20X4 (when the events occurred that gave rise to the court case). Therefore, entity A recognises a provision at 31 December 20X4. Entity A measures that provision by discounting the CU1,000 paid on 10 July 20X5 to its present value, using a discount rate that complies with IAS 37 and reflects market conditions at 31 December 20X4. **[Refer: IAS 37 paragraphs 36–47]**

[Refer: paragraphs 31 and 33]

(a) In this guidance monetary amounts are denominated in 'currency units (CU)'.

IG4 Paragraphs 14–17 of the IFRS do not override requirements in other IFRSs that base classifications or measurements on circumstances existing at a particular date. Examples include:

(a) the distinction between finance leases and operating leases for a lessor (see IFRS 16 *Leases* **[Refer: IFRS 16 paragraphs 61–66 and B53–B57]** and paragraph IG14);

(b) the restrictions in IAS 38 *Intangible Assets* that prohibit capitalisation of expenditure on an internally generated intangible asset if the asset did not qualify for recognition when the expenditure was incurred; **[Refer: IAS 38 paragraphs 48–67]** and

(c) the distinction between financial liabilities and equity instruments (see IAS 32 *Financial Instruments: Presentation*). **[Refer: IAS 32 paragraphs 11 (definitions of a financial liability and an equity instrument), 15–32 and AG3–AG35]**

IAS 12 *Income Taxes*

IG5 An entity applies IAS 12 to temporary differences between the carrying amount of the assets and liabilities in its opening IFRS statement of financial position and their tax bases.

[Refer: paragraphs 7–9]

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IG6 In accordance with IAS 12, the measurement of current and deferred tax reflects tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. **[Refer: IAS 12 paragraphs 46–49]** An entity accounts for the effect of changes in tax rates and tax laws when those changes are enacted or substantively enacted. **[Refer: IAS 12 paragraphs 47 and 60]**

[Refer: paragraphs 7–9]

IAS 16 *Property, Plant and Equipment*

IG7 If an entity's depreciation methods and rates in accordance with previous GAAP are acceptable in accordance with IFRSs, **[Refer: IAS 16 paragraphs 43–62]** it accounts for any change in estimated useful life or depreciation pattern prospectively from when it makes that change in estimate (paragraphs 14 and 15 of the IFRS and paragraph 61 of IAS 16). However, in some cases, an entity's depreciation methods and rates in accordance with previous GAAP may differ from those that would be acceptable in accordance with IFRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life). If those differences have a material effect on the financial statements, the entity adjusts accumulated depreciation in its opening IFRS statement of financial position retrospectively so that it complies with IFRSs. **[Refer: paragraphs 14 and 16]**

IG8 An entity may elect to use one of the following amounts as the deemed cost of an item of property, plant and equipment:

(a) fair value at the date of transition to IFRSs (paragraph D5 of the IFRS), in which case the entity gives the disclosures required by paragraph 30 of the IFRS;

(b) a revaluation in accordance with previous GAAP that meets the criteria in paragraph D6 of the IFRS;

(c) fair value at the date of an event such as a privatisation or initial public offering (paragraph D8 of the IFRS);

(d) an allocation of an amount determined under previous GAAP that meets the criteria in paragraph D8A of the IFRS; or

(e) the carrying amount under previous GAAP of an item of property, plant and equipment that is used, or was previously used, in operations subject to rate regulation (paragraph D8B of the IFRS).

IG9 Subsequent depreciation is based on that deemed cost and starts from the date for which the entity established the deemed cost.

IG10 If an entity chooses as its accounting policy the revaluation model in IAS 16 for some or all classes of property, plant and equipment, it presents the cumulative revaluation surplus as a separate component of equity. **[Refer: IAS 16 paragraphs 31–42]** The revaluation surplus at the date of transition to IFRSs is based on a comparison of the carrying amount of the asset at that date with its cost or deemed cost. If the deemed cost is the fair value at the date of transition to IFRSs, the entity gives the disclosures required by paragraph 30 of the IFRS.

IG11 If revaluations in accordance with previous GAAP did not satisfy the criteria in paragraph D6 or D8 of the IFRS, an entity measures the revalued assets in its opening statement of financial position on one of the following bases:

(a) cost (or deemed cost) less any accumulated depreciation and any accumulated impairment losses under the cost model in IAS 16; **[Refer: IAS 16 paragraph 30]**

(b) deemed cost, being the fair value at the date of transition to IFRSs (paragraph D5 of the IFRS); or

(c) revalued amount, if the entity adopts the revaluation model in IAS 16 **[Refer: IAS 16 paragraphs 31–42]** as its accounting policy in accordance with IFRSs for all items of property, plant and equipment in the same class.

IG12 IAS 16 requires each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item to be depreciated separately. However, IAS 16 does not prescribe the unit of measure for recognition of an asset, ie what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to an entity's specific circumstances (see IAS 16 paragraphs 9 and 43).

IG13 In some cases, the construction or commissioning of an asset results in an obligation for an entity to dismantle or remove the asset and restore the site on which the asset stands. An entity applies IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* in recognising and measuring any resulting provision. **[Refer: IAS 37 paragraphs 14–26 and 36–52, and example 3 in Implementation Guidance part C to IAS 37]** The entity applies IAS 16 in determining the resulting amount included in the cost of the asset, before depreciation and impairment losses. **[Refer: IAS 16 paragraph 16(c)]** Items such as depreciation and, when applicable, impairment losses cause differences between the carrying amount of the liability and the amount included in the carrying amount of the asset. An entity accounts for changes in such liabilities in accordance with IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. However, paragraph D21 of IFRS 1 provides an exemption for changes that occurred before the date of transition to IFRSs, and prescribes an alternative treatment where the exemption is used. An example of the first-time adoption of IFRIC 1, which illustrates the use of this exemption, is given at paragraphs IG201–IG203.

IFRS 16 *Leases*

IG14 At the date of transition to IFRSs, a lessor classifies leases as operating leases or finance leases on the basis of circumstances existing at the inception of the lease (IFRS 16 paragraph 66). Lease classification is reassessed only if there is a lease modification. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the underlying asset) or changes

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in circumstances (for example, default by the lessee) do not give rise to a new classification of a lease.

[Refer:
paragraphs 7 and 10
IFRS 16 paragraph 66]

IG15 [Deleted]

IG16 [Deleted]

IFRS 15 *Revenue from Contracts with Customers*

IG17 If an entity has received amounts that do not yet qualify for recognition as revenue in accordance with IFRS 15 (for example, the proceeds of a sale that does not qualify for revenue recognition), the entity recognises a liability in its opening IFRS statement of financial position and measures that liability at the amount received, adjusted (if appropriate) for a significant financing component in accordance with IFRS 15.

[Refer: paragraphs 7–9]

IAS 19 *Employee Benefits*

IG18 [Deleted]

IG19 An entity's actuarial assumptions **[Refer: IAS 19 paragraphs 75–98]** at the date of transition to IFRSs are consistent with actuarial assumptions made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those assumptions were in error (paragraph 14 of the IFRS). The impact of any later revisions to those assumptions is an actuarial gain or loss of the period in which the entity makes the revisions.

[Refer: paragraph 15]

IG20 An entity may need to make actuarial assumptions **[Refer: IAS 19 paragraphs 75–98]** at the date of transition to IFRSs that were not necessary in accordance with its previous GAAP. Such actuarial assumptions do not reflect conditions that arose after the date of transition to IFRSs. In particular, discount rates and the fair value of plan assets at the date of transition to IFRSs reflect market conditions at that date. Similarly, the entity's actuarial assumptions at the date of transition to IFRSs about future employee turnover rates do not reflect a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan that occurred after the date of transition to IFRSs (paragraph 16 of the IFRS).

IG21 In many cases, an entity's first IFRS financial statements will reflect measurements of employee benefit obligations at three dates: the end of the first IFRS reporting period, the date of the comparative statement of financial position and the date of transition to IFRSs. IAS 19 encourages an entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. To minimise costs, an entity may request a qualified actuary to carry out a detailed actuarial valuation at one or two of these dates and roll the valuation(s) forward or back to the other date(s). Any such roll forward or roll back reflects any material transactions and other material events (including changes in market prices and interest rates) between those dates (IAS 19 paragraph 57).

IAS 21 *The Effects of Changes in Foreign Exchange Rates*

IG21A An entity may, in accordance with previous GAAP, have treated goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation as assets and liabilities of the entity rather than as assets and liabilities of the foreign operation. If so, the entity is permitted to apply prospectively the requirements of paragraph 47 of IAS 21 to all acquisitions occurring after the date of transition to IFRSs.

[Refer: paragraphs D12 and D13]

IFRS 3 *Business Combinations*

IG22 The following examples illustrate the effect of Appendix C of the IFRS, assuming that a first-time adopter uses the exemption.

[Refer: paragraph C1]

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IG Example 2 Business combination
Background
Entity B's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information **[Refer: paragraphs 21 and 22]** for 20X4 only. On 1 July 20X1, entity B acquired 100 per cent of subsidiary C. In accordance with its previous GAAP, entity B:
(a) classified the business combination as an acquisition by entity B.
(b) measured the assets acquired and liabilities assumed at the following amounts in accordance with previous GAAP at 31 December 20X3 (date of transition to IFRSs):
(i) identifiable assets less liabilities for which IFRSs require cost-based measurement at a date after the business combination: CU200 (with a tax base of CU150 and an applicable tax rate of 30 per cent).
(ii) pension liability (for which the present value of the defined benefit obligation measured in accordance with IAS 19 *Employee Benefits* is CU130 and the fair value of plan assets is CU100): nil (because entity B used a pay as you go cash method of accounting for pensions in accordance with its previous GAAP). The tax base of the pension liability is also nil.
(iii) goodwill: CU180.
(c) did not, at the acquisition date, recognise deferred tax arising from temporary differences associated with the identifiable assets acquired and liabilities assumed.

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IG Example 2 Business combination
Application of requirements **[Refer: paragraph C1]**
In its opening (consolidated) IFRS statement of financial position, entity B:
(a) classifies the business combination as an acquisition by entity B even if the business combination would have qualified in accordance with IFRS 3 as a reverse acquisition by subsidiary C (paragraph C4(a) of the IFRS).
(b) does not adjust the accumulated amortisation of goodwill. Entity B tests the goodwill for impairment in accordance with IAS 36 *Impairment of Assets* **[Refer: IAS 36 paragraphs 80–99]** and recognises any resulting impairment loss, based on conditions that existed at the date of transition to IFRSs. If no impairment exists, the carrying amount of the goodwill remains at CU180 (paragraph C4(g) of the IFRS).
(c) for those net identifiable assets acquired for which IFRSs require cost-based measurement at a date after the business combination, treats their carrying amount in accordance with previous GAAP immediately after the business combination as their deemed cost at that date (paragraph C4(e) of the IFRS).
(d) does not restate the accumulated depreciation and amortisation of the net identifiable assets in (c), unless the depreciation methods and rates in accordance with previous GAAP result in amounts that differ materially from those required in accordance with IFRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life in accordance with IFRSs). If no such restatement is made, the carrying amount of those assets in the opening IFRS statement of financial position equals their carrying amount in accordance with previous GAAP at the date of transition to IFRSs (CU200) (paragraph IG7). **[Refer: paragraphs 14 and 15]**
(e) if there is any indication that identifiable assets are impaired, tests those assets for impairment, based on conditions that existed at the date of transition to IFRSs (see IAS 36). **[Refer: Implementation Guidance paragraphs IG39–IG43]**

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IG Example 2 Business combination

(f) recognises the pension liability, and measures it, at the present value of the defined benefit obligation (CU130) less the fair value of the plan assets (CU100), giving a carrying amount of CU30, with a corresponding debit of CU30 to retained earnings (paragraph C4(d) of the IFRS). However, if subsidiary C had already adopted IFRSs in an earlier period, entity B would measure the pension liability at the same amount as in subsidiary C's financial statements (paragraph D17 of the IFRS and IG Example 9).

(g) recognises a net deferred tax liability of CU6 (CU20 at 30 per cent) arising from:

(i) the taxable temporary difference of CU50 (CU200 less CU150) associated with the identifiable assets acquired and non-pension liabilities assumed, less

(ii) the deductible temporary difference of CU30 (CU30 less nil) associated with the pension liability.

The entity recognises the resulting increase in the deferred tax liability as a deduction from retained earnings (paragraph C4(k) of the IFRS). If a taxable temporary difference arises from the initial recognition of the goodwill, entity B does not recognise the resulting deferred tax liability (paragraph 15(a) of IAS 12 *Income Taxes*).

IG Example 3 Business combination—restructuring provision

Background

Entity D's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information **[Refer: paragraphs 21 and 22]** for 20X4 only. On 1 July 20X3, entity D acquired 100 per cent of subsidiary E. In accordance with its previous GAAP, entity D recognised an (undiscounted) restructuring provision **[Refer: IAS 37 paragraphs 70–83]** of CU100 that would not have qualified as an identifiable liability in accordance with IFRS 3. **[Refer: IFRS 3 paragraphs 10–17]** The recognition of this restructuring provision increased goodwill by CU100. At 31 December 20X3 (date of transition to IFRSs), entity D:

(a) had paid restructuring costs of CU60; and

(b) estimated that it would pay further costs of CU40 in 20X4, and that the effects of discounting were immaterial. At 31 December 20X3, those further costs did not qualify for recognition as a provision in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. **[Refer: IAS 37 paragraphs 14–26]**

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IG Example 3 Business combination—restructuring provision

Application of requirements

[Refer: paragraph C1]

In its opening IFRS statement of financial position, entity D:

(a) does not recognise a restructuring provision (paragraph C4(c) of the IFRS).

(b) does not adjust the amount assigned to goodwill. However, entity D tests the goodwill for impairment in accordance with IAS 36 *Impairment of Assets*, **[Refer: IAS 36 paragraphs 80–99]** and recognises any resulting impairment loss (paragraph C4(g) of the IFRS).

(c) as a result of (a) and (b), reports retained earnings in its opening IFRS statement of financial position that are higher by CU40 (before income taxes, and before recognising any impairment loss) than in the statement of financial position at the same date in accordance with previous GAAP.

IG Example 4 Business combination—intangible assets

Background

Entity F's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information **[Refer: paragraphs 21 and 22]** for 20X4 only. On 1 July 20X1 entity F acquired 75 per cent of subsidiary G. In accordance with its previous GAAP, entity F assigned an initial carrying amount of CU200 to intangible assets that would not have qualified for recognition in accordance with IAS 38 *Intangible Assets*. **[Refer: IAS 38 paragraphs 9–17 and 33–41]** The tax base of the intangible assets was nil, giving rise to a deferred tax liability (at 30 per cent) of CU60.

On 31 December 20X3 (the date of transition to IFRSs) the carrying amount of the intangible assets in accordance with previous GAAP was CU160, and the carrying amount of the related deferred tax liability was CU48 (30 per cent of CU160).

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Bases for Conclusions

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Annotated

With extensive cross-references and other notes

International Accounting Standards Board

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Conceptual Framework for Financial Reporting

Conceptual Framework for Financial Reporting (*Conceptual Framework*) (issued March 2018) was issued by the International Accounting Standards Board (Board).

The text of the *Conceptual Framework* is contained in Part A of this edition. This part presents the following accompanying document:

BASIS FOR CONCLUSIONS

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History of the project

BC0.1 In 1989, the Board's predecessor body, the International Accounting Standards Committee, issued the *Framework for the Preparation and Presentation of Financial Statements* (1989 Framework).

BC0.2 In 2004, the Board and the US national standard-setter, the Financial Accounting Standards Board (FASB), started a joint project to revise their conceptual frameworks.

BC0.3 The first phase of the project was to develop chapters that describe the objective of general purpose financial reporting and the qualitative characteristics of useful financial information. In developing these chapters, the Board and the FASB published a Discussion Paper in 2006 (2006 Discussion Paper) and an Exposure Draft in 2008 (2008 Exposure Draft).[1] After considering feedback on those documents and information gained from outreach, in 2010 the Board and the FASB issued two chapters of a revised *Conceptual Framework for Financial Reporting* (2010 *Conceptual Framework*). The chapters on the objective of general purpose financial reporting and qualitative characteristics of useful financial information came into effect as soon as they were issued. The remaining text of the 1989 *Framework* was carried forward to the 2010 *Conceptual Framework* unchanged.

BC0.4 In addition to finalising the chapters on the objective of general purpose financial reporting and qualitative characteristics of useful financial information, the Board and the FASB:

(a) published a Discussion Paper and then an Exposure Draft (2010 Exposure Draft) on the concept of a reporting entity;[2]

(b) discussed the definitions of the elements of financial statements; and

(c) discussed and held public round-table meetings about measurement.

BC0.5 This work did not lead to further revisions at that time because in 2010 the Board and the FASB suspended work on the *Conceptual Framework* to concentrate on other projects.

BC0.6 In 2011, the Board carried out a public consultation on its agenda. Most respondents to that consultation identified the Conceptual Framework as a priority project for the Board. Consequently, in 2012 the Board restarted its Conceptual Framework project.

BC0.7 Before 2010, the Board and the FASB had planned to complete the project in eight separate phases, but completed only one phase—on objectives and qualitative characteristics. On restarting the project in 2012, the Board decided to develop a complete set of proposals for a revised *Conceptual Framework* instead of continuing with the phased approach. Developing the *Conceptual Framework* as a whole enabled the Board and stakeholders to see more clearly the links between different aspects of the *Conceptual Framework*.

1 See the Discussion Paper *Preliminary Views on an Improved Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting Information* published in 2006 and the Exposure Draft *An Improved Conceptual Framework for Financial Reporting: Chapters 1 and 2* published in 2008.

2 See the Discussion Paper *Preliminary Views on an Improved Conceptual Framework for Financial Reporting—The Reporting Entity* published in 2008 and the Exposure Draft *Conceptual Framework for Financial Reporting—The Reporting Entity* published in 2010.

BC0.8 In developing the revised *Conceptual Framework*, the Board published a Discussion Paper in 2013 (2013 Discussion Paper) and an Exposure Draft in 2015 (2015 Exposure Draft).[3] After considering feedback on these documents and information gained from outreach, in 2018 the Board completed its Conceptual Framework project when it issued the revised *Conceptual Framework for Financial Reporting (2018 Conceptual Framework)*.

BC0.9 The work since restarting the project in 2012 was not conducted jointly with the FASB. The 2018 *Conceptual Framework* includes limited changes to the chapters on the objective of general purpose financial reporting and qualitative characteristics of useful financial information. The FASB did not make corresponding changes to its Statements of Financial Accounting Concepts.

Revision in 2018—approach and scope

BC0.10 Although the 2010 *Conceptual Framework* had helped the Board when developing IFRS Standards (Standards):

(a) some important areas were not covered;

(b) the guidance in some areas was unclear; and

(c) some aspects were out of date.

BC0.11 In developing the 2018 *Conceptual Framework*, the Board built on the 2010 *Conceptual Framework*—filling in gaps, as well as clarifying and updating it, but not fundamentally reconsidering all aspects of the 2010 *Conceptual Framework*. In particular, although the Board reconsidered some aspects of chapters on the objective of financial reporting and qualitative characteristics of useful financial information, it did not reconsider those chapters fundamentally. In selecting that approach, the Board noted that these chapters went through extensive due process during the development of the 2010 *Conceptual Framework*.

BC0.12 The Board normally establishes a consultative group for major projects. For the Conceptual Framework project, the Board used the Accounting Standards Advisory Forum (ASAF) as its consultative group. The ASAF is an advisory group to the Board. It comprises national accounting standard-setters and regional bodies with an interest in financial reporting. The Board discussed a range of topics with the ASAF during the development of the 2018 *Conceptual Framework*.

BC0.13 In developing the 2018 *Conceptual Framework*, the Board sought a balance between providing high-level concepts and providing enough detail for the 2018 *Conceptual Framework* to be useful to the Board and others. Some stakeholders stated that in some areas the Board's proposals merely described

3 See the Discussion Paper *A Review of the Conceptual Framework for Financial Reporting* published in 2013 and the Exposure Draft *Conceptual Framework for Financial Reporting* published in 2015.

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the factors that the Board would consider in making judgements when developing Standards. They expressed the view that, as a result, the proposals did not examine fundamental concepts and were not sufficiently aspirational. The Board did not share that view. The Board viewed the *Conceptual Framework* as a practical tool to help it to develop Standards. The Board concluded that a *Conceptual Framework* would not fulfil this role if it described concepts without explaining the factors the Board needs to consider in making judgements when the application of concepts does not lead to a single answer, or leads to conflicting answers.

BC0.14 In developing the 2018 *Conceptual Framework*, the Board drew on some concepts developed in recent standard-setting projects. The Board's aim in doing so was to reflect the Board's most developed thinking on these matters, not to justify its standard-setting decisions or current practice.

BC0.15 The 2018 *Conceptual Framework* does not address classification of financial instruments with characteristics of both liabilities and equity because the Board did not want to delay other much-needed improvements to the *Conceptual Framework*. The Board is exploring how to distinguish liabilities from equity in its research project on Financial Instruments with Characteristics of Equity. If necessary, the *Conceptual Framework* will be updated as one possible outcome of that project (see paragraph BC4.45).

BC0.16 The discussion of capital and capital maintenance in the 2018 *Conceptual Framework* is unchanged from the 2010 *Conceptual Framework*. That discussion originally appeared in the 1989 *Framework* (see paragraphs BC8.1–BC8.4). The Board may consider revising that discussion in the future if it considers that necessary.

BC0.17 In developing the 2018 *Conceptual Framework*, the Board did not address the equity method of accounting, the translation of amounts denominated in foreign currency or the restatement of the measuring unit in hyperinflation. The Board concluded that these issues would best be dealt with if it were to carry out projects to consider revising Standards on these topics.

Purpose (paragraph SP1.1)

BC0.18 The 2010 *Conceptual Framework* included a long list of possible uses of the *Conceptual Framework*. In 2018, the Board streamlined the list, identifying three main uses of the *Conceptual Framework*: assisting the Board in developing Standards, assisting preparers in developing accounting policies when no Standard applies to a particular transaction or other event (or when a Standard allows a choice of accounting policy) and assisting all parties in understanding and interpreting Standards.

BC0.19 The Board considered whether to focus the stated purpose of the *Conceptual Framework* by stating that its primary purpose would be only to assist the Board in developing Standards. The Board rejected this approach because acknowledging the assistance the *Conceptual Framework* can give to other parties would not prevent the Board from developing focused and consistent concepts that will help it to develop Standards.

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BC0.20 Although preparers apply the *Conceptual Framework* in developing accounting policies when no Standard applies to a particular transaction or other event or when a Standard allows a choice of accounting policy, a few aspects of the *Conceptual Framework* can only be applied by the Board. In such cases, the 2018 *Conceptual Framework* indicates that the Board may make particular decisions in developing Standards (for example, see paragraph 7.17).

Status (paragraphs SP1.2–SP1.3)

BC0.21 The 1989 *Framework* and the 2010 *Conceptual Framework* stated that the *Conceptual Framework* is not a Standard and does not override any specific Standards. In the 2018 *Conceptual Framework*, the Board reconfirmed this status.

BC0.22 The Board found that the status of the *Conceptual Framework* has worked well in practice. Also, an explicit statement that the *Conceptual Framework* does not override any requirements in a Standard prevents entities from attempting to override inappropriately Standards those entities might view as contradicting the *Conceptual Framework*.

BC0.23 In some stakeholders' view, the Board should never develop Standards that depart from the *Conceptual Framework*. The Board disagreed with this view. In some circumstances, the Board might need to depart from aspects of the *Conceptual Framework*. It is helpful for the *Conceptual Framework* to acknowledge this, and to specify that such departures are appropriate only if needed to meet the objective of general purpose financial reporting. That need might arise because conceptual thinking or the economic environment may change, and new or revised Standards might need to reflect these changes.

BC0.24 Some respondents to the 2015 Exposure Draft expressed concerns about the implications of the proposals for future Standards. In particular, they expressed concerns about proposed changes to the definitions of an asset and a liability. In response, the Board tested the revised definitions of an asset and a liability and the guidance supporting those definitions (see paragraphs BC4.19–BC4.22). One of the aims of this test was to enable both the Board and stakeholders to assess implications of the revised concepts for future Standards. In addition, the Board tested for inconsistencies between the revised concepts and existing Standards.

BC0.25 The aim of these tests was not to identify whether the Board should develop proposals to amend any Standards following the revision of the *Conceptual Framework*. Amending a Standard is not an automatic consequence of that revision. Changes to Standards are made to address deficiencies in financial reporting. Any changes to the *Conceptual Framework* that highlight inconsistencies in the Standards must be considered by the Board in the light of other priorities when developing its work plan.[4]

4 See paragraph 4.23 of the IFRS Foundation *Due Process Handbook*.

BC0.26 The *IFRS for SMEs*® Standard includes a section on the concepts and basic principles underlying the financial statements of small and medium-sized entities. That section is based on the 1989 *Framework*. The Board will consider whether it should amend this section of the *IFRS for SMEs* Standard when it next reviews that Standard.

Transition to the 2018 *Conceptual Framework*

BC0.27 The Board and the IFRS Interpretations Committee will start using the 2018 *Conceptual Framework* immediately once it is issued. If, when developing a draft IFRIC® Interpretation, the IFRS Interpretation Committee is faced with an inconsistency between a Standard (including any Standard developed on the basis of the 1989 *Framework* or the 2010 *Conceptual Framework*) and the concepts in the 2018 *Conceptual Framework*, it will refer the issue to the Board, as required by the IFRS Foundation *Due Process Handbook*.[5]

BC0.28 The revised concepts will guide the Board when it develops or revises Standards. However, changes to the *Conceptual Framework* will not automatically lead to changes in existing Standards (see paragraph BC0.25). Accordingly, changes to the *Conceptual Framework* will have no immediate effect on the financial statements of most reporting entities. Preparers of financial statements could be directly affected by the changes only if they need to use the *Conceptual Framework* to develop an accounting policy when no Standard applies to a particular transaction or other event or when a Standard allows a choice of accounting policy.[6] To achieve transition to the 2018 *Conceptual Framework* for such entities, the Board issued *Amendments to References to the Conceptual Framework in IFRS Standards* in 2018. Where appropriate, that document replaces references in Standards to the 1989 *Framework* with references to the 2018 *Conceptual Framework* and updates related quotations.

Business activities

BC0.29 In developing the 2018 *Conceptual Framework*, the Board concluded that the nature of an entity's business activities can affect the relevance of some types of financial information and that the Board may need to consider that factor when developing or revising Standards.

BC0.30 The Board disagreed with the view expressed by some stakeholders that considering the nature of an entity's business activities necessarily leads to subjectivity and impairs comparability of financial statements. An entity's business activities are a matter of fact that can in most cases be determined

5 See paragraph 7.8 of the IFRS Foundation *Due Process Handbook*.

6 If no Standard specifically applies to a transaction, other event or condition, paragraph 11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires entities to consider the *Conceptual Framework* in developing and applying an accounting policy for that transaction. If a Standard permits a choice of accounting policy, entities select an accounting policy subject to an overall requirement in IAS 1 *Presentation of Financial Statements* that financial statements must provide a fair presentation of the entity's financial position, financial performance and cash flows. The link between fair presentation and the concepts in the *Conceptual Framework* is described in paragraph 15 of IAS 1.

objectively. Hence, if entities conduct the same type of business activities, the Board expects that those activities would be reflected in a similar manner in the entities' financial statements.

BC0.31 The Board considered whether the nature of business activities should be considered in all areas of standard-setting and should be embedded in the *Conceptual Framework* as an overarching concept. The Board concluded that the nature of an entity's business activities does not affect all areas of financial reporting in the same way and to the same extent and so it should not be included as an overarching concept. Accordingly, the 2018 *Conceptual Framework* does not include a general discussion of how an entity's business activities affect financial reporting decisions. Instead, the 2018 *Conceptual Framework* describes that factor in the context of:

(a) the selection of the unit of account (see paragraph 4.51(a)(iv)).

(b) the selection of a measurement basis for an asset or liability and for related income and expenses (see paragraphs 6.54–6.57). In some cases, this would lead to some items of income or expenses being included in other comprehensive income (see the discussion of more than one measurement basis in paragraphs 6.83–6.86).

(c) classification of assets, liabilities, equity, income or expenses (see paragraph 7.7).

BC0.32 The concept of business activities is discussed in the 2018 *Conceptual Framework* to assist the Board in developing Standards. In a particular Standard, the concept of business activities can be further explained and developed. The discussion of business model in IFRS 9 *Financial Instruments* is one example of how the Board has applied the concept of business activities.

BC0.33 The Board decided to use the term 'business activities' rather than the term 'business model' in the 2018 *Conceptual Framework*. The term 'business model' is used with a range of different meanings by various organisations, for example, the International Integrated Reporting Council, the Enhanced Disclosure Task Force of the Financial Stability Board and various regulators. Adopting the term 'business model' in the 2018 *Conceptual Framework* could have led to confusion with those definitions.

Implications of long-term investment

BC0.34 The subject of long-term investment has attracted a great deal of attention from governments and others. Governments have indicated that encouraging long-term investment is an important tool for promoting economic growth.

BC0.35 The Board considered the role of its Standards in promoting long-term investment and noted that:

(a) the Board makes an important contribution to the promotion of investment, including long-term investment, by producing Standards that require transparent financial reporting. This is a precondition for the healthy and efficient functioning of financial markets. Transparent financial reporting helps market participants to make more efficient

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and informed resource allocation and other economic decisions and thus makes investment more attractive to capital providers (investors and lenders). It also provides useful inputs for an assessment of stewardship.

(b) it is not, however, the role of the Standards to encourage or discourage any type of investments. Instead, standard-setting decisions are driven by the need for entities to provide useful information.

BC0.36 When developing the 2018 *Conceptual Framework*, the Board considered whether the *Conceptual Framework* will provide the Board with sufficient and appropriate tools to enable it, when developing Standards, to consider:

(a) the business activity of long-term investment (see paragraphs BC0.37–BC0.39); and

(b) the information needs of long-term investors (see paragraphs BC0.40–BC0.43).

Long-term investment as a business activity

BC0.37 The Board considered a suggestion made by some stakeholders that it should identify long-term investment as a particular type of business activity (or business model) and develop specific measurement and presentation and disclosure requirements for entities conducting that business activity. Some stakeholders expressing those views suggested that:

(a) entities should not use a current value measurement basis for their long-term investments and for their liabilities; or

(b) if a current value measurement basis is used for those investments and liabilities, income and expenses resulting from remeasurement should be included in other comprehensive income, not in the statement of profit or loss.

BC0.38 As discussed in paragraphs 6.54–6.57 of the 2018 *Conceptual Framework*, the nature of the business activities being conducted affects how an asset or liability contributes to future cash flows. Thus, the nature of an entity's business activities is considered in selecting a measurement basis for an asset or liability and for related income and expenses. Moreover, in some cases, considering the nature of an entity's activities may lead to some items of income and expenses being included in other comprehensive income (see paragraphs 6.85–6.86). The Board concluded that the discussion on this factor in the 2018 *Conceptual Framework* provides sufficient tools for the Board to make appropriate standard-setting decisions if future projects consider how to account for the long-term investments of entities whose business activities include long-term investment or for their liabilities.

BC0.39 For the following reasons, the Board decided that the 2018 *Conceptual Framework* should not refer explicitly to the business activity of long-term investment:

(a) referring explicitly to any particular business activity would inappropriately embed excessive detail in the *Conceptual Framework*; and

(b) the *Conceptual Framework* does not refer to any other business activity.

Information needs of long-term investors

BC0.40 Some stakeholders suggested that the *Conceptual Framework* should emphasise the information needs of long-term investors and that their information needs may differ from those of short-term investors. Views expressed by these stakeholders included the following:

(a) the Board focuses too much on the needs of short-term investors.

(b) the Board gives too much weight to the needs of potential investors and not enough weight to the needs of existing long-term investors. Existing long-term investors own the reporting entity and bear the residual risks of ownership. Hence, these stakeholders argue that long-term investors need information that helps them to assess management's stewardship of the entity's economic resources.

(c) the Board makes excessive use of current value measurement bases, particularly those reflecting market-participant assumptions, such as fair value, and those measurement bases provide information more relevant to short-term investors than to investors who are interested in long-term value creation.

(d) excessive use of current value measurement bases (especially for long-term investments) and recognition of unrealised gains in the statement of profit or loss may:

(i) lead to excessive and volatile dividend distributions that are not in the best interest of long-term investors;

(ii) lead to inflated management remuneration (including bonuses); and

(iii) encourage short-termism and financial engineering and discourage long-term investment.

BC0.41 For the following reasons, the Board disagreed with the views expressed in paragraph BC0.40:

(a) the Board does not place more emphasis on the needs of short-term investors than on the needs of long-term investors. The Board considers both long-term investors and short-term investors to be primary users of financial statements. Moreover, the Board believes that there is no reason why short-term investors would need information that is not also needed by long-term investors.

(b) the *Conceptual Framework* identifies both existing and potential investors as primary users of financial statements. The Board's discussions with users in its project on the *Conceptual Framework* and in many other projects have identified no reasons why existing investors

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would need information that differs from the information needed by potential investors. Furthermore, the changes made by the 2018 *Conceptual Framework* to the discussion of the objective of general purpose financial reporting highlight the importance of providing information to help investors to assess management's stewardship of the entity's economic resources. The 2018 *Conceptual Framework* states explicitly that decisions relating to providing resources to the entity include decisions about exercising rights to vote on, or otherwise influence, management's actions that affect the use of the entity's economic resources. Thus, the 2018 *Conceptual Framework* clarifies that the needs of existing investors (including long-term investors) are considered when making decisions about the usefulness of financial information (see paragraphs BC1.36–BC1.37).

(c) when the Board has decided to require or permit current value measurement bases, that has not been because of a belief that those measurement bases would be particularly useful to short-term investors. Instead, the Board's decisions have been driven by an assessment of what information is most likely to be useful to the primary users of financial statements, including both long-term and short-term investors. Under the concepts in Chapter 6—*Measurement* of the 2018 *Conceptual Framework*, this will continue to be the case.

(d) in the Board's view, accounting information (such as reported profit) is not, and should not be, the sole determinant of distributions of dividends and bonuses. Distribution policy is affected by many other factors, for example, the entity's financing needs, current and projected liquidity, the risks faced by the entity, legal constraints and (in the case of bonus decisions) remuneration policy and incentive arrangements. These factors differ by entity, by country and over time. It would be neither desirable nor feasible for the Board to consider them in standard-setting decisions.

BC0.42 For these reasons, the Board concluded that the 2018 *Conceptual Framework* contains sufficient and appropriate discussion of primary users and their information needs, and of the objective of general purpose financial reporting, to address appropriately the needs of long-term investors.

BC0.43 Conceivably, long-term investors may need entities to provide some information that is not also needed by short-term investors; for example, long-term investors may have more extensive needs for information to support decisions to vote on, or otherwise influence, management's actions. However, the Board concluded that to help it to identify what information particular Standards should require entities to provide, there is no need for the *Conceptual Framework* to contain a specific reference to the needs of long-term investors. When the Board develops Standards, it routinely seeks input and feedback from investors, including long-term investors, to help ensure that it understands what information they need.

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In 2018, the Board made limited changes to Chapter 1 of the Conceptual Framework. A description of the Board's considerations in developing those changes was added to the original Basis for Conclusions on this chapter. The Board added a date to the heading of each section of the Basis for Conclusions to indicate when that section was developed. Sections of the Basis for Conclusions that reflect the Board's considerations at the time of developing the chapter in 2010 were not updated in 2018 except to add and update cross-references and to make minor necessary editorial changes.

Introduction

BC1.1 The first version of Chapter 1 was developed jointly with the FASB and issued in 2010 (see paragraph BC0.3). Consequently, this Basis for Conclusions includes some references to the FASB's literature.

Revision in 2018

BC1.2 When the Board restarted its work on the Conceptual Framework project in 2012, it did not reconsider Chapter 1 fundamentally (see paragraph BC0.11). Although some respondents to the 2013 Discussion Paper agreed with this approach, many stated that the Board should reconsider one or more aspects of Chapter 1. In the light of these comments, the Board considered whether to make changes in the following areas:

(a) primary users (see paragraphs BC1.18–BC1.20); and

(b) stewardship (see paragraphs BC1.32–BC1.41).

BC1.3 The FASB has not made any changes to its Concepts Statement No. 8 *Conceptual Framework for Financial Reporting—Chapter 1, The Objective of General Purpose Financial Reporting* corresponding to the limited changes made by the Board in 2018. The Board concluded that the clarity achieved by its improvements to Chapter 1 outweighs the disadvantages of divergence in those respects from the FASB's version.

General purpose financial reporting (2010)

BC1.4 Consistently with the Board's responsibilities, the *Conceptual Framework* establishes an objective of financial reporting and not just of financial statements. Financial statements are a central part of financial reporting, and most of the issues that the Board addresses involve financial statements. Although the scope of FASB Concepts Statement No. 1 *Objectives of Financial Reporting by Business Enterprises* was financial reporting, the other FASB concepts statements focused on financial statements. The scope of the Board's *Framework for the Preparation and Presentation of Financial Statements*, which was published by the Board's predecessor body in 1989 (1989 *Framework*), dealt with financial statements only. Therefore, for both boards the scope of the 2010 *Conceptual Framework* is broader than the scopes of their previous frameworks.[7]

7 With the exception of Chapters 1 and 2, the 2018 *Conceptual Framework* focuses on (general purpose) financial statements rather than on (general purpose) financial reports (see paragraph 3.1).

BC1.5 Some stakeholders suggested that advances in technology may make general purpose financial reporting obsolete. New technologies, for example the use of eXtensible Business Reporting Language (XBRL), may make it practicable in the future for reporting entities either to prepare or to make available the information necessary for different users to assemble different financial reports to meet their individual information needs.

BC1.6 To provide different reports for different users, or to make available all of the information that users would need to assemble their own custom-designed reports, would be expensive. Requiring users of financial information to assemble their own reports might also be unreasonable, because many users would need to have a greater understanding of accounting than they have now. Therefore, the Board concluded that for now a general purpose financial report is still the most efficient and effective way to meet the information needs of a variety of users.

BC1.7 In the 2006 Discussion Paper, the Board used the term 'general purpose external financial reporting'. External was intended to convey that internal users such as management were not the intended beneficiaries for general purpose financial reporting as established by the Board. During redeliberations, the Board concluded that this term was redundant. Therefore, Chapter 1 uses 'general purpose financial reporting'.

Financial reporting of the reporting entity (2010)

BC1.8 Some respondents to the 2008 Exposure Draft said that the reporting entity is not separate from its equity investors or a subset of those equity investors. This view has its roots in the days when most businesses were sole proprietorships and partnerships that were managed by their owners who had unlimited liability for the debts incurred in the course of the business. Over time, the separation between businesses and their owners has grown. The vast majority of today's businesses have legal substance separate from their owners by virtue of their legal form of organisation, numerous investors with limited legal liability and professional managers separate from the owners. Consequently, the Board concluded that financial reports should reflect that separation by accounting for the entity (and its economic resources and claims) rather than its primary users and their interests in the reporting entity.[8]

Primary users (paragraphs 1.5, 1.8–1.10)

Primary users (2010)

BC1.9 The objective of financial reporting in paragraph 1.2 refers to existing and potential investors, lenders and other creditors. The description of the primary users in paragraph 1.5 refers to existing and potential investors, lenders and other creditors who cannot require reporting entities to provide information directly to them. Paragraph 1.10 states that 'regulators and members of the public other than investors, lenders and other creditors' may

8 See also paragraph 3.8 of the 2018 *Conceptual Framework* and paragraphs BC3.9–BC3.10.

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