

Revised Conceptual Framework for Financial Reporting

Introduction

The International Accounting Standards Board (Board) issued the revised Conceptual Framework for Financial Reporting (*Conceptual framework*) which is comprehensive set of concepts for financial reporting.

This guidance paper sets out why the Board revised the old Conceptual Framework, the main changes from the previous Conceptual Framework and the main concepts and guidance in each chapter of the revised Conceptual Framework.

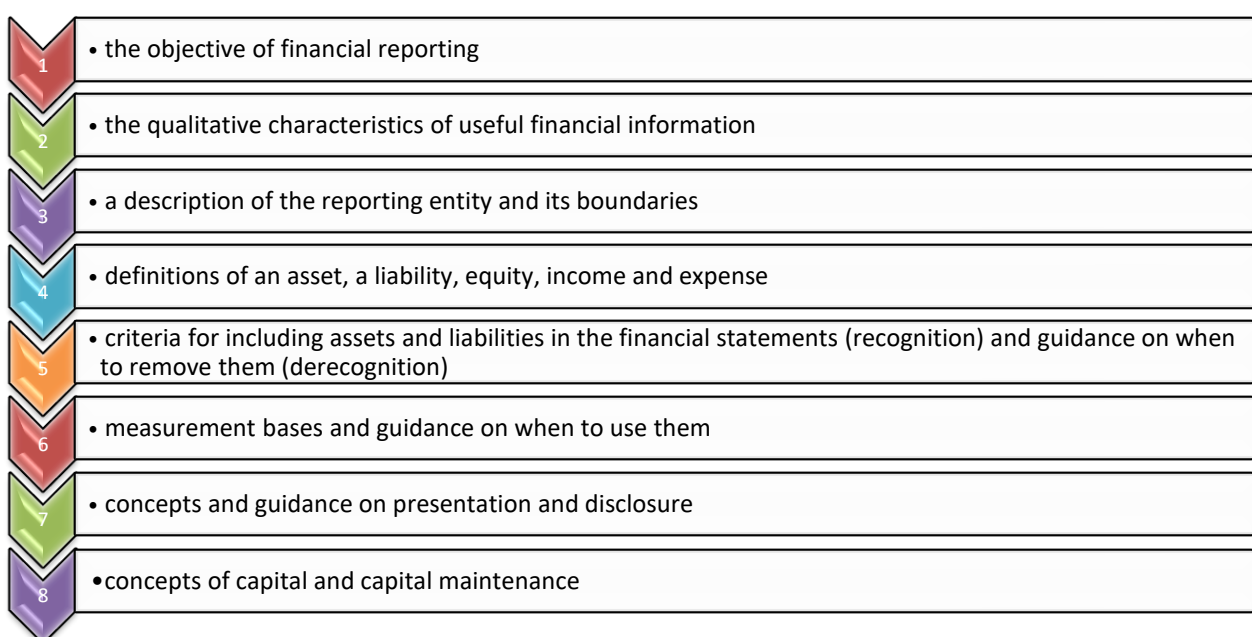
The revised Conceptual Framework is immediately effective, (published March (2018), for the Board and the IFRS Interpretations Committee and annual periods beginning on or after 1 January 2020 for preparers who develop an accounting policy based on the Conceptual Framework.

This guidance paper should be read with the following supporting materials:

- [Project Summary](#) providing a high-level introduction to the revised Conceptual Framework. ([external IFRS.org link](#))
- [Feedback Statement](#) summarising the Board's response to the comments it received to its consultation on the proposals that led to the revised Conceptual Framework. ([external IFRS.org link](#))
- [Fact Sheet](#) outlining six short facts. ([external IFRS.org link](#))
- [Video](#) featuring Hans Hoogervorst introducing the revised Conceptual Framework. ([external YouTube link](#))

Structure

The revised Conceptual Framework sought to achieve a balance between providing high-level concepts and providing sufficient details and sets this out, per chapter, as follows:



Reason for the revision

The old Conceptual Framework was issued in 1989 and was partly revised in 2010. It was useful, but the framework was incomplete and needed improvement. In the 2011 Agenda Consultation, revising of the Conceptual framework was identified as a priority by stakeholders. In priority, the revised standard needed to fill the gaps on measurement, presentation and disclosure, updating the definitions of an asset and a liability and providing some clarity of the role of measurement uncertainty.

Main changes

The revised Conceptual framework introduces the following main changes:

New

- Guidance on when assets and liabilities are removed from financial statements – *see chapter 5*
- Concepts on measurement, including factors to be considered when selecting a measurement basis – *see chapter 6*
- Concepts on presentation and disclosure, including when to classify income and expenses in other comprehensive income – *see chapter 7*

Refined

- Definitions of an asset and a liability – *see chapter 4*
- Criteria for including assets and liabilities in financial statement – *see chapter 4*

Clarified

- Stewardship – *see chapter 1*
- Prudence – *see chapter 2*
- Measurement uncertainty – *see chapter 2*
- Substance over form – *see chapter 4*

Summary of changes per chapter

Chapter 1 – The objective of general purpose financial reporting

This chapter sets out the objective of general purpose financial reporting. The chapter emphasises that the financial information provided in the financial statements are to be useful to the users in making decisions relating to providing resources, either in cash or another financial instrument, to the entity.

User decisions involve:

- The buying, selling or holding of equity or debt instruments;
- Providing or settling loans or other forms of credit;
- Voting, or otherwise influencing managements actions.

User of the financial reports are:

- the entity's existing and potential investors;
- the entity's existing and potential lenders;
- the entity's other creditors.

To make these decisions, users assess:

- The prospects of future net cash inflows to the entity. This could be through the realisation of assets or the future revenue generated in the ordinary activities of the entity. It also emphasises that users need information about any claims against the entity.
- Managements stewardship of the entity's economic resources. To make this assessment, users need information about how efficiently and effectively management has discharged its responsibilities to use the entity's economic resources and any changes that affect the entity's resources.

Chapter 2 – Qualitative characteristics of useful financial information

This chapter reinforces that for information to be useful, it must be both **relevant** and provide a **faithful representation** of what it purports to represent. Although the changes were limited the Board clarified the roles of **prudence**, **measurement uncertainty**, and **substance over form** (addressed in chapter 4) in assessing whether information is useful.

These qualitative characteristics can be defined as follows:

Relevance: <ul style="list-style-type: none"> Information is relevant if it is capable of making a difference to the decisions made by the users; Financial information can make a difference in decisions if it has predictive value or confirmatory value. 	Faithful Representation: <ul style="list-style-type: none"> Information must faithfully represent the substance of what it purports to represent; Faithful representation is, to the maximum extent possible, complete, neutral and free from error; Faithful representation is affected by measurement uncertainty.
Prudence: <ul style="list-style-type: none"> Neutrality is supported by the existence of prudence. Prudence is the exercise of caution when making judgements under conditions of uncertainty. It does not allow for overstatements or understatement of assets, liabilities, equity, income or expenses. 	Measurement uncertainty: <ul style="list-style-type: none"> It does not prevent information from being useful. However, the most relevant information that is subject to high measurement uncertainty reduces the usefulness of such information.

The fundamental qualitative characteristics (relevance and faithful representation) and the enhancing qualitative characteristics (comparability, verifiability, timeliness, and understandability) effect of useful financial information. Interestingly, the enhancing qualitative characteristics cannot make non-useful information useful.

Chapter 3 – Financial statements and the reporting entity

This chapter is new and describes the objective and scope of financial statements and provides a description of the reporting entity. It also introduces guidance to determining the appropriate boundary of a reporting entity.

Reporting entity	<ul style="list-style-type: none"> an entity that is required, or chooses, to prepare financial statements. The entity does not necessarily need to be a legal entity, it could be a portion of an entity or comprise of more than one entity.
Financial Statements	<ul style="list-style-type: none"> a particular form of financial reports that provide information about the reporting entity's assets, liabilities, equity, income and expenses.
Consolidated financial statements	<ul style="list-style-type: none"> information about assets, liabilities, equity, income and expenses of both the parent and its subsidiaries as a single reporting entity.
Unconsolidated financial statements	<ul style="list-style-type: none"> information about assets, liabilities, equity, income and expenses of the parent entity.
Combined financial statements	<ul style="list-style-type: none"> information about assets, liabilities, equity, income and expenses of two or more entities that are not all linked by a parent-subsidiary relationship.

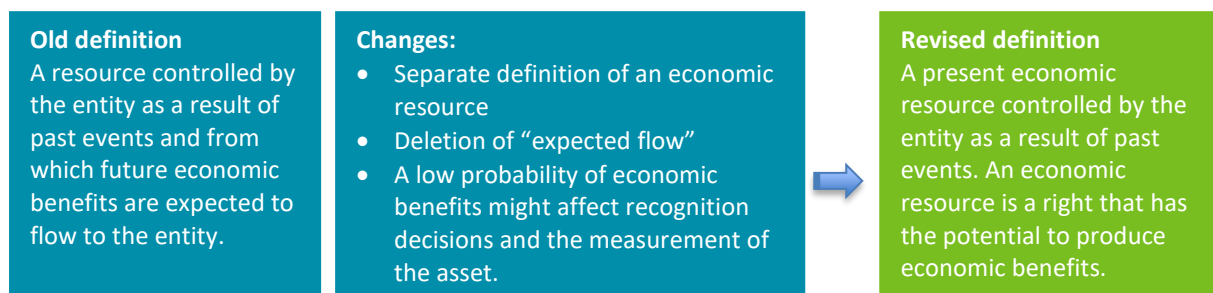
In determining the boundary of a reporting entity, the entity would consider the information needs of the users. Those users need information that is relevant and that faithfully represent what it purports to represent.

Chapter 4 – The elements of financial statements

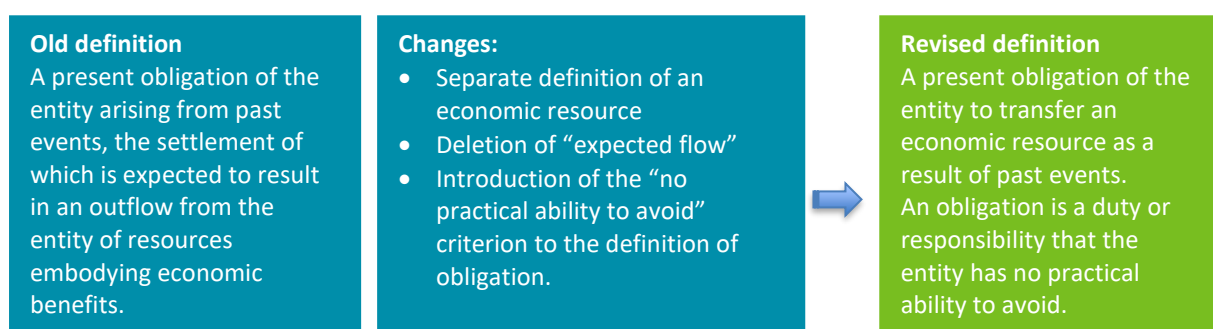
The definitions of an asset and a liability have been refined and the definitions of income and expenses have been updated only to reflect that refinement.

The main changes are as follows:

- Definition of an asset:



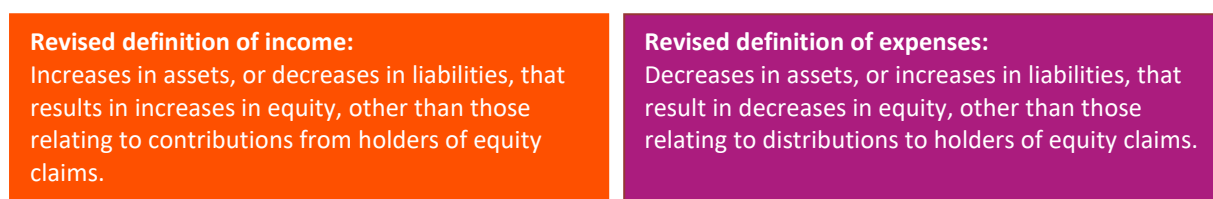
- Definition of a liability:



- Definition of equity:

The residual interest in the assets of the entity after deducting all its liabilities

- Definition of income and expenses



Chapter 5 – Recognition and derecognition

This chapter discusses the criteria for including assets and liabilities in financial statements (recognition) and guidance on when to remove them (derecognition).

- Recognition

“The process of capturing for inclusion in the statement of financial position or the statement(s) of financial performance an item that meets the definition of an asset, a liability, equity, income or expenses. Recognition is appropriate if it results in both relevant information about assets, liabilities, equity, income and expenses and a faithful representation of those items, because the aim is to provide information that is useful to investors, lenders and other creditors.”

- Derecognition

“The removal of all or part of a recognised asset or liability from an entity’s statement of financial position. Derecognition normally occurs when the entity loses control of all or part of the recognised asset or no longer has a present obligation for all or part of the recognised liability”

Chapter 6 – Measurement

The revised Conceptual Framework describes what information measurement bases provide and explains the factors to consider when selecting a measurement basis.

Historical cost measurement bases:

- Derived from the transaction price
- For assets – reduced if they become impaired
- For liabilities – increased if they become onerous
- One way to apply this measurement basis is to measure them at amortised costs.

Current value measurement bases:

- Current value provides information updated to reflect conditions at the measurement date.
- Bases include:
 - Fair value
 - For assets – value in use
 - For liabilities – fulfilment value
 - Current costs – reflects the current amount that would be:
 - Paid to acquire an equivalent asset or
 - Received to take on an equivalent liability

The factors to be considered when selecting a measurement basis are relevance and faithful representation. Relevance of information provided by a measurement basis is affected by the characteristic of the assets or liability and contribution to future cash flows. Faithful representation is affected by measurement uncertainty and/or measurement inconsistency.

Chapter 7 – Presentation and disclosure

This chapter is new and includes concepts on presentation and disclosure. The statement of profit or loss is the primary source of information about the entity’s financial performance for the reporting period. Profit or loss could be a section of a single statement of financial performance or a separate statement. In principle, all income and expenses are classified and included in the statement of profit or loss.

In exceptional circumstances, the Board may decide to exclude from the statement of profit or loss income or expenses arising from a change in current value of assets or liabilities and include those income and expenses in other comprehensive income. The Board may make such a decision when doing so would result in the statement of profit or loss providing more relevant information or a more faithful representation. Income and expenses included in other comprehensive income in one period may or may not be recycled to the statement of profit or loss in a future period if it results in the statement of profit or loss providing more relevant information and a more faithful representation.

Chapter 8 – Concepts of capital and capital maintenance

This chapter is largely a carry forward from the old Conceptual Framework. The content of the chapter discusses concepts of financial and physical capital, concepts of capital maintenance and the determination of profit including capital maintenance adjustments.

Cost constraint

The revised Conceptual Framework makes note of cost constrain as follows:

- The benefit of providing the information needs to justify the cost of providing and using the information – *chapter 2: Qualitative characteristics of useful financial information.*

- Cost constraints recognition decisions, just as it constrains other financial reporting decisions – *chapter 5: Recognition and derecognition and chapter 6: Measurement.*

References to the Conceptual Framework

Together with the revised Conceptual Framework, the IASB has also issued: Amendments to References to the Conceptual Framework in IFRS Standards. The document contains amendments to IFRS 2, IFRS 3, IFRS 6, IFRS 14, IAS 1, IAS 8, IAS 34, IAS 37, IAS 38, IFRIC 12, IFRIC 19, IFRIC 20, IFRIC 22, and SIC-32.

Conclusion

Information about assets, liabilities, equity, income and expenses is communicated in the financial statements. Better and more effective communication makes that information more relevant and contributes to a faithful representation of the entity's performance.