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IASB Issues Updated Conceptual Framework for Financial Reporting

Underpinning for pronouncements designed to help preparers as well as standard setters

The underlying concepts for the standards that guide financial reporting were originally developed in 1989, and partially revised in 2010. While that Framework has proven to be useful, the International Accounting Standards Board (IASB) determined that a revision was needed to fill in missing gaps, while also updating and clarifying certain areas. Though the original Framework was primarily intended for use by standard setters, the new revision was designed to form "a balance between providing high-level concepts and providing enough detail for the *Conceptual Framework* to be useful to the Board and others.

The purpose of the newly revised *Conceptual Framework for Financial Reporting*, issued on March 29, 2018, is stated as follows:

(a) To assist the Board to develop Standards that are based on consistent concepts;
(b) To assist preparers to develop consistent accounting policies when no Standard specifically applies to a transaction or other event or when a Standard allows a choice of accounting policy; and
(c) To assist all parties to understand and interpret Standards.

This broader application will prove especially helpful to practitioners in the jurisdictions that have, or will, move from the rules based approach, such as found in Financial Accounting Standards Board (FASB) standards, to the principles based approach of International Financial Reporting Standards. Those practitioners, while no longer having as many specific rules to direct how transactions are recorded, can now turn to the revised Framework as an additional source where direct guidance is lacking.

The Framework makes clear that, though helpful guidance is provided, the Framework itself is not a standard, nor does it override any standard. The Framework is effective immediately for the IASB and generally in 2020 for preparers.

The Framework presents some new areas of focus, updates others, and clarifies still others. The new areas center on measurement, presentation and disclosure, and derecognition. Updated are the definitions for assets and liabilities, and their recognition criteria in financial statements. The existing concepts of prudence, stewardship, measurement uncertainty, and substance over form are clarified.

The new chapter on measurement describes the three approaches to be used. The factors of relevance and faithful representation are applied to determine which approach to use in each instance. The Framework explains the approaches as follows:

1. Fair value
   a. the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date;
   b. reflects market participants' current expectations about the amount, timing and uncertainty of future cash flows;
2. Value in use (for assets), fulfilment value (for liabilities)

    a. reflects entity-specific current expectations about the amount, timing and uncertainty of future cash flows.
3. Current cost
    a. reflects the current amount that would be:
        i. paid to acquire an equivalent asset,
        ii. received to take on an equivalent liability.

The new chapter on presentation and disclosure emphasizes the importance of effective communication in the financial statements by providing concepts to assist in attaining that goal. Specific detail distinguishes when income or expenses should be included in other comprehensive income versus the statement of profit or loss.

An explanation of the criteria for derecognition (removal) of an asset or liability from the statement of financial position is added to the chapter that covers recognition (inclusion). Derecognition normally occurs "when the entity loses control of all or part of the recognised asset," or "when the entity no longer has a present obligation for all or part of the recognised liability."

The other significant change concerns the definition of an asset and a liability.

For an asset:

- Previous definition - A resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.
- Revised definition – A present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits.

For a liability:

- Previous definition - A present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.
- Revised definition - A present obligation of the entity to transfer an economic resource as a result of past events. An obligation is a duty or responsibility that the entity has no practical ability to avoid.

Further details can be found at [IASB completes revisions to its Conceptual Framework](http://www.ifrs.org/news-and-events/2018/03/iasb-completes-revisions-to-its-conceptual-framework/)

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