

Comments on Conceptual Framework (CF) Papers

Gaps in the IFRS CF
Articulation Profit or Loss,
and OCI in the CF
Tom Scott, November 2017

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board (the Board) or IFRS Foundation.

General contributions—both papers

- Informative reviews of significant literature on conceptual alternatives for financial reporting
- The “clean surplus” relationship is important
 - Essentially that over an entity’s life cash flows (other than from providers of capital) and comprehensive income (accruals) should be equal
- That guidance on the choice of measurement method, especially historical cost versus current value (not just fair value) can be improved
- That measurement rests, in part, on business plans, and hence a business model
 - ‘business activities’ are used in CF rather than ‘business model’

Contributions—gaps paper Barker and Texeira

- That asset and liability changes leading to income and expenses are sometimes not one directional, as explained in the CF
 - assets and liabilities recognition is sometimes related to recognition of income and expenses
 - “reconciled back to it”
- Some important concepts remain, or are significantly developed, at the standards level
- Guidance on measurement method choice is incomplete
- Guidance on unit of account is incomplete
- Advocate for more emphasis on transactions

- Useful history of alternate ways to decompose profit
- Clean surplus relationship does not hold for profit or loss
- Distinguishing allocation of performance elements between profit or loss and other comprehensive income (OCI) is incomplete
- Paper provides some useful analysis of these issues
- Advocate for the use of deprival values

Board's view (versus myth one)— statement of financial position emphasis

- Assets and liabilities are the basic conceptual building blocks of the Conceptual Framework:
 - income and expenses are derived from changes in assets and liabilities
 - Because this approach is the best way to capture income and expenses and financial performance
 - Assets and liabilities as basic elements do not imply a statement of financial position emphasis

Board's view (versus myth two)—current values are optimal for balance sheet

- Assets and liabilities are the basic conceptual elements of the conceptual framework
 - CF allows for a mixed measurement approach
 - Based on relevance and faithful representation
 - assets and liabilities as basic elements do not imply that the assets and liabilities are best captured by measuring using current values (not just fair values) .

- The sum of profit or loss and OCI (also known as comprehensive income) satisfies clean surplus
- Forecasting future cash flows, abnormal earnings, or ROE should always involve more than simply extrapolating from current profit or loss, comprehensive income, abnormal earnings, or cash flows.
 - Financial performance should be assessed broadly and selecting inputs to valuation models can use all information provided in all statements

Conceptual Framework—the big (ger) changes for future standard-setting

Recognition & derecognition

Uncertain liabilities

Role of prudence and stewardship

Measurement

Use of OCI

Guidance on selecting a measurement basis

Information in both the statement of financial position and the statement(s) of financial performance

Relevance

Faithful representation

Characteristics of the asset or liability

Measurement inconsistency ('accounting mismatch')

Contribution to future cash flows

Measurement uncertainty

Enhancing qualitative characteristics and cost constraint

Guidance on selecting a measurement basis

Elaborate on Relevance	Historical cost	Current value
Asset characteristics: <ul style="list-style-type: none">• sensitivity of value to market factors?• CF highly variable?	Stable CF and stable value	<ul style="list-style-type: none">• Highly variable CF• High sensitivity to value changes
How asset is used: <ul style="list-style-type: none">• Produce CF in combination or directly?	Produce CF in combination/ measure cost of asset consumption	Produce CF directly
Then consider <i>faithful representation</i> <ul style="list-style-type: none">• accounting mismatch?• measurement uncertainty?		
Cost-benefit concerns? Enhancing characteristics acceptable?		

Profit or loss and OCI in CF

Profit or loss

Primary source of information about performance

Default location for income and expenses—Historical cost-based measurements here

Other comprehensive income

Exceptional circumstances

Only some changes in current values of assets and liabilities

Classification into profit or loss and OCI and recycling

Relevance

Faithful representation

Only the Board can make decisions on OCI and recycling

Contact us

Keep up to date



@IFRSFoundation



IFRS Foundation



www.ifrs.org



IFRS Foundation

Comment on our work



go.ifrs.org/comment