STAFF PAPER

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Project	**Conceptual Framework**		
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Purpose of paper

1. This paper summarises the feedback that the Board and staff received from investors and analysts (collectively referred to as 'users' in this paper) on the Exposure Draft *Conceptual Framework for Financial Reporting* ('the Exposure Draft') published by the Board in May 2015.
2. This summary includes feedback from users received through comment letters, face-to-face meetings and teleconferences.
3. This paper provides a high-level summary of the comments received. Where appropriate, we will provide a more detailed breakdown of the comments for future meetings.

Structure of paper

4. This paper is structured as follows:
    - (a) Demographic analysis (paragraphs 5-8)
    - (b) Scope of consultation (paragraphs 9-10)
    - (c) Summary of feedback on each topic:
        - (i) Stewardship (Chapter 1, paragraphs 11-16);

(ii) Prudence (Chapter 1, paragraphs 17-27);

(iii) Measurement (Chapter 6, paragraphs 28-45)

(iv) Profit or loss and OCI (Chapter 7, paragraphs 46-70);

(v) Business activities and long-term investment (paragraphs 71-82);

(vi) The objective of general purpose financial statements (other than comments on stewardship) and the qualitative characteristics of useful financial information (other than comments on prudence) (Chapters 1 and 2, paragraphs 83-98);

(vii) Financial statements and the reporting entity (Chapter 3, paragraphs 99-106);

(viii) The elements of financial statements (Chapter 4, paragraphs 107-119);

(ix) Recognition and derecognition (Chapter 5, paragraphs 120-128);

(x) Presentation and disclosure (other than profit or loss and OCI) (Chapter 7, paragraphs 129-144); and

(xi) Other issues (paragraphs 145-150).

Demographic analysis

5. The Board received 19 comment letters from users. Ten of those comment letters came from user groups and 9 came from individual companies. Two users stated that they were international organisations; other users indicated that they were located in Europe (with specific input from France, the Netherlands and the UK), Australia, Japan, Singapore and the US.

6. From June 2015 to November 2015, the Board and staff attended more than 20 meetings with users. Two-thirds of these meetings were in person. One-third of the meetings were telephone calls or videoconferences. Meetings with the Board's Capital Markets Advisory Committee and meetings organised jointly with the EFRAG were held in public. Other meetings were held in private. At least one staff member attended most meetings and at least one Board member attended half of the

meetings. For this summary, we have only included meetings specifically for users. This analysis does not cover meetings that included other participants in addition to users.

7. Most of the users who participated in the outreach stated that they were sharing their own views and not necessarily the views of their employers. However, some stated that they were representing the views of their associations or professional bodies. The majority of those who participated were equity analysts, or representatives of equity analysts, but we also consulted credit analysts, including analysts from credit rating agencies. Those who participated included both sell-side and buy-side analysts and a few were accounting analysts.

8. The users we spoke to were located in Europe (with specific input from Italy, Switzerland and the UK), Canada, Japan, Singapore and the US.

Scope of consultation

9. Because of the limited time of most users, we were unable to discuss all the topics covered by the Exposure Draft during the meetings. To best use the time available, we focussed on the topics of most relevance to users.

10. The following topics were most frequently discussed at meetings with, and in comment letters from, users:

    (a) Stewardship (Chapter 1, paragraphs 11-16);

    (b) Prudence (Chapter 1, paragraphs 17-27);

    (c) Measurement (Chapter 6, paragraphs 28-45);

    (d) Profit or loss and OCI (Chapter 7, paragraphs 46-70); and

    (e) Business activities and long-term investment (paragraphs 71-82).

Stewardship (Chapter 1)

Exposure Draft proposals

11. The Exposure Draft proposed giving more prominence, within the discussion of the objective of financial reporting, to the importance of providing information needed to assess management's stewardship of the entity's resources.

Summary of feedback

12. Half of the users or user groups who submitted a comment letter commented on this issue. Most of these users or user groups agreed with making stewardship more prominent in the *Conceptual Framework*.

13. One user from the US and a user group from the UK stated that financial statements are essentially confirmatory. The user group from the UK stated that, because of this confirmatory nature, the value of financial statements to investors is in part in assessing management's stewardship of the entity's resources.

14. However, a few users and user groups from the UK expressed concern that the *Conceptual Framework* continues to consider decision-usefulness as the primary objective of financial reporting and that information about management's stewardship is treated as part of the information needed to meet that primary objective. These users suggested that providing information about management's stewardship should be treated as an objective of financial reporting with equal prominence to the decision-usefulness objective. One user stated that stewardship should be the primary objective of financial reporting if there can only be one objective.

15. Other comments made by users included the following:

    (a) one user group from Japan stated that the meaning of 'stewardship' was unclear;

    (b) one user from the US stated that 'stewardship' should be defined with an emphasis on long-term consideration and the completeness, transparency and reliability of financial information;

(c) one user group from the UK stated that there is specific information that can only be found in the financial statements that is useful in assessing stewardship; and

(d) one user from the US stated that stewardship information should include environmental and social performance data.

16. One user from the UK stated that information about cash flows is important, because it is cash flows that enable liabilities to be repaid and returns to be made to shareholders. Hence, stewardship should not be made more prominent if it results in less of an emphasis on cash flows.

Prudence (Chapter 1)

Exposure Draft proposals

17. The Exposure Draft observed that 'prudence' is a term used with two different meanings:

(a) the need to be cautious when making judgements under conditions of uncertainty (cautious prudence); and

(b) a need for asymmetry: losses are recognised at an earlier stage than gains are (asymmetric prudence).

18. The Exposure Draft proposed reintroducing an explicit reference to the notion of prudence (with the meaning of cautious prudence) stating that prudence is important for achieving neutrality.

19. The Exposure Draft did not include asymmetric prudence as a necessary characteristic of useful information. However, the Exposure Draft included the Board's view that not all asymmetry is inconsistent with neutrality.

Summary of feedback

Reintroduction of prudence

20. Nearly two-thirds of the users or user groups that submitted a comment letter commented on this issue.

21. A majority of these users or user groups supported the reintroduction of ‘prudence’ as proposed in the Exposure Draft. Users who supported the reintroduction of ‘prudence’ as proposed in the Exposure Draft made the following comments:

    (a) one user group from Japan stated that because ‘relevance’ is a subjective criterion, the concept of ‘prudence’ should assist in narrowing that subjectivity; and

    (b) one user from the UK stated that the removal of ‘prudence’ in 2010 sent a signal that companies could be more optimistic, ie companies can use the more optimistic end of ranges when measuring an item.

22. One user group from the UK stated that it had some reservations about the reintroduction of the term ‘prudence’ but supported the proposal provided that the concept referred to ‘cautious prudence’.

23. A few users from Europe stated that the notion of prudence could be understood as a broader concept that could help users assess stewardship and understand whether management is taking more risks than shareholders would be comfortable with.

24. A few users and a user group from Europe disagreed with the reintroduction of ‘prudence’ because of concerns that a requirement to be prudent could conflict with neutrality. One user from the UK stated that some interpret prudence as a bias.

25. However, a few other users stated that ‘asymmetric prudence’ should be made more prominent in the *Conceptual Framework*:

    (a) a few users and user groups stated that the *Conceptual Framework* should acknowledge that ‘asymmetric prudence’ may at times be necessary:

        (i) one user from the UK stated that ‘asymmetric prudence’ may be necessary to deal with management’s optimistic bias;

        (ii) one international user group agreed with the use of asymmetric prudence but suggested that the Board should restrict the use of it because asymmetric accounting may result in financial reports that provide entities with more scope for judgement, which could lead to reduced comparability; and

        (iii) one user from the US suggested that ‘asymmetric prudence’, correctly understood, is consistent with neutrality.

(b) One user from the UK stated that 'asymmetric prudence' must be a core principle. In this user's view, 'cautious prudence' may be neutral but is not prudent, and a move away from prudence has led to pro-cyclicality in the economic system. This user also noted that prudence is already a legal requirement in many jurisdictions (for example, in the EU, prudence is a core requirement in companies complying with their legal duty to ensure that accounts present a 'true and fair view').

26. A few user groups from Europe stated that the implications of reintroducing 'prudence' were unclear. One user group from France questioned whether the reintroduction had a clear practical consequence.

27. Other comments from users included the following:

(a) one user group from the UK stated that 'cautious prudence' is more of a matter for preparers and not standard-setters and that this point should be clarified in the *Conceptual Framework*;

(b) one user from the UK stated that 'prudence' needs to be applied in the recognition of asset and liabilities but not in measurement;

(c) one user from the UK stated that reintroducing prudence may influence management communication with shareholders because of litigation concerns; and

(d) one user group from the UK stated that uncertainty is always present and that, consequently, caution is always required in making judgements. Accordingly, this user suggested deleting 'under conditions of uncertainty' from the definition of 'prudence'.

Measurement (Chapter 6)

Exposure Draft proposals

28. The Exposure Draft discussed:

(a) measurement bases and the information that they provide;

(b) factors to consider when selecting a measurement basis;

(c) situations in which more than one measurement basis provides relevant information; and

(d) measurement of equity.

Summary of feedback

Historical cost and current value

29. Nearly one-third of the users or user groups that submitted a comment letter commented on this issue.

30. One user and a few user groups explicitly agreed with the measurement bases identified in the Exposure Draft, namely historical cost and current value. One user group from the UK stated that it liked the way the Board included fair value as a subset of current value.

31. One user group from the UK stated that measurement bases come down to two—historical cost and fair value—and questioned whether it was necessary to consider more than two measurement bases.

32. One user group from Europe disagreed with the argument in the Exposure Draft that the use of historical cost can reduce comparability. In this user's view, if two entities have acquired similar assets at a different price, the entities should report those assets at different values.

Factors to consider when selecting a measurement basis

33. Nearly one third of the users or user groups that submitted a comment letter commented on this issue.

34. One user group from Japan generally agreed with the discussion in the Exposure Draft of factors to consider when selecting a measurement basis.

35. One user group from the UK stated that there needs to be clear guidance and principles as to when a particular measurement basis should be selected in a Standard.

36. One user from the US agreed that one factor to be considered when selecting a measurement basis for an asset or a liability is how the asset or liability contributes to future cash flows, which depends, in part, on the nature of the business activities

being conducted. This user noted that this factor would also be considered in determining whether income and expenses should be included in profit or loss or OCI.

37. One user group from the UK stated that considering entity-specific factors (such as the business model) in selecting a measurement basis has pros and cons. Considering entity-specific factors may have the potential of reporting information with greater relevance, but that must be weighed against both the loss of comparability between companies and the greater risk of management bias influencing the numbers.

38. One user group from the Netherlands stated that it agreed with the notion in paragraph BC6.56 of the Basis for Conclusions that measurement uncertainty is one of the factors that should be considered in assessing a measurement basis.

39. One international user group suggested that guidance similar to that suggested in the Discussion Paper should be reinstated:

(a) if assets contribute indirectly to future cash flows through use, cost-based measurements normally provide information that is more relevant and understandable; and

(b) if assets contribute directly to future cash flows by being sold, a current exit price is more likely to be relevant.

This user further suggested that the principle above also applies to debt, ie if the repurchase of the liability is a realistic option, fair value should be used, but if repurchase is not realistic, historical cost would be more relevant.

More than one measurement basis

40. Nearly one-third of the users or user groups that submitted a comment letter commented on this issue.

41. One user from Singapore and a few user groups agreed that in some cases a different measurement basis should be used for the statement of financial position and statement of profit loss and, in such cases, the remaining balance should be included in OCI. The user from Singapore stated that using different measurement bases can be justified depending on the entity's business model.

42. A few user groups from the UK stated that they were concerned that the use of more than one measurement basis within one set of financial statements makes those

financial statements less easy to understand. These users suggested that, if two perspectives are useful, one should be used for the primary financial statements and information based on the other should be provided in the notes.

43. One user from the UK suggested that the proposal to allow more than one measurement basis for the statement of financial position and statement of profit or loss was too complicated and may not be understood by users.

Other comments

44. One international user group stated that it would oppose any measurement concept that allows for the recognition of an asset or a liability using a probability-weighted amount. In this user's view, this valuation method would allow optimistic management to recognise assets when there may be a high probability the future value could be lower than the amount recorded on the balance sheet.

45. One user group from the UK disagreed with the argument in the Exposure Draft that an unobservable price can be faithfully represented so long as the estimates made are fully explained. This user questioned how this contributes to 'reliability'.

Profit or loss and OCI (Chapter 7)

Exposure Draft proposals

46. The Exposure Draft did not define profit or loss, but stated that the income and expenses included in the statement of profit or loss are the primary source of information about an entity's financial performance for the period.

47. Based on the Board's view on profit or loss, the Exposure Draft proposed a rebuttable presumption that all income and all expenses will be included in the statement of profit or loss. That presumption can only be rebutted if:

    (a) the income or expenses relate to assets or liabilities measured at current values; and

    (b) excluding those income or expenses from the statement of profit or loss would enhance the relevance of the information in that statement for the period.

48. Furthermore, the Exposure Draft proposed a presumption that items of income or expenses included in OCI in one period will be reclassified into the statement of profit or loss in some future period (recycled), if doing so will enhance the relevance of information included in the statement of profit or loss for that future period.

Summary of feedback

Profit or loss and performance

49. Nearly two-thirds of users or user groups that submitted a comment letter commented on this issue. Nearly half of those who commented on this issue stated that the Exposure Draft did not provide sufficient guidance on performance, the definitions of profit or loss and OCI or the basis for recycling.

50. One user group from the UK stated that there need to be clearly articulated principles as to what performance is and a closer alignment between performance and the entity's business model. One user from Europe stated that any future guidance on the use of OCI should be based on clear principles and, more importantly, should be easy to apply and verify.

51. A few user groups stated that the Board's project on performance reporting should address the reporting of income and expenses in profit or loss and OCI. One international user group stated that the *Conceptual Framework* project should not be delayed to address performance reporting issues.

'Primary source of information about an entity's financial performance'

52. Some users and user groups supported the proposed description of profit or loss as the primary source of information about an entity's performance.

53. One user group from the UK stated that, if profit or loss is the primary indicator of financial performance, sub-totals that make up comprehensive income should be defined, as should the terms 'profit', 'return' and 'performance'. In this user's view, the proliferation of non-GAAP earning measures is partly due to the lack of a definition of operating performance.

54. A few users disagreed with the proposals in the Exposure Draft:

    (a) One user from Australia stated profit or loss for the year is a snapshot of past performance and is only one aspect of performance, and not necessarily the most important aspect.

    (b) One international user group stated that both profit or loss and OCI carry relevant information and they act to complement each other when they are used in decision-making by investors.

55. One user group from the UK stated that the Exposure Draft does not provide guidance on what the statement ‘profit or loss is the primary source of information about an entity’s financial performance’ means in practice and suggested that this should be addressed.

Profit or loss

56. A few user groups supported the Board’s proposal to classify items of income and expenses into either profit or loss or OCI. In contrast, a few users from Europe suggested that this classification should not be made but that all items of income and expenses should be integrated.

57. A few users and user groups from Europe stated that profit or loss forms the starting-point of a user’s analysis. One user group from France stated it was their ‘favourite’ starting-point to assess performance and that they have never seen any users using comprehensive income as a starting-point to assess performance.

58. Some users from Europe indicated that measures such as operating profit, EBITDA and EBIT are important for their analysis (and in some cases more important than the profit or loss sub-total). These users encouraged the Board to define these measures or provide guidance that would promote consistency in the reporting of these measures.

59. A few users described the characteristics of profit or loss as follows:

    (a) a few members of an international user group proposed defining profit or loss as the profits attributed to the current accounting period to the shareholders of the reporting entity which is a going concern, using accrual accounting;

(b) one user group from Japan stated that profit or loss is required because it is the figure that has been realised in the period and belongs to shareholders;

(c) one user from Australia stated that it did not support any proposal that would report changes in the fair value of long-term investments in profit or loss;

(d) one user group from the UK stated that profit or loss should report items that measure the entity’s performance so that management can be held accountable for what it has done and OCI should include other items; and

(e) one user from the US stated that profit or loss should focus on the returns generated by the entity’s business model. The use of OCI should be restricted to cases in which current value measurements are not necessarily representative of performance, for example:

    (i) the revaluation gains and losses on assets that are not part of the entity’s business model;

    (ii) where the entity’s business model is one of long-term investments.

Use of OCI

60. Regarding the discussion on the use of OCI:

(a) a few user groups from the UK agreed with the statement in the Basis for Conclusions that ‘the use of OCI and recycling are not well understood by the user community and OCI is not looked at by many users’; and

(b) one user group from the Netherlands stated that it was pleased to see that the Board recognised that there is no single concept to justify the existence of all OCI items.

61. Regarding whether, and if so when, OCI should be used:

(a) one user from Australia stated that OCI should reflect the changes in investments measured at fair value that are not held for trading, or are readily tradable;

(b) one user group from the UK stated that use of OCI should be strictly limited. This user group stated that, because OCI is generally ignored by most investors, it would be better to abandon OCI entirely and simply allow companies to present an income statement with current value adjustments clearly broken out from operating figures so that investors can make their own assessment of underlying earnings;

(c) one user from the UK stated that the use of OCI should differ according to business models;

(d) two user groups, one from Japan and one from the UK, stated that whether the use of OCI would enhance the relevance of information in profit or loss is subject to interpretation and may lead to diversity in accounting treatments; and

(e) one user group from the Netherlands stated that the *Conceptual Framework* should clarify that any criteria for the use of OCI should only be applied to the standard-setting process of the Board and not be used by individual reporting entities. This user group stated that it did not consider that the Exposure Draft provides sufficiently useful guidance to the Board for future decisions about the use of OCI and concurred with the alternative view of Board members on this topic.

62. One user group from Europe highlighted that OCI should be presented clearly and understandably. This user group stated that companies should present similar OCI item in different ways which reduces comparability.

Recycling

63. A few user groups from the UK stated that, in the absence of a clear definition of profit or loss and OCI, the question of recycling cannot be usefully addressed.

64. A few users and user groups expressed support for recycling some but not all OCI items:

(a) one user from the US agreed with the rebuttable presumption on recycling;

(b) one user group from the UK suggested that all OCI items that are eventually realised through an external transaction should be recycled through profit or loss;

(c) one international user group stated that recycling some OCI items and not others can be justified because there are different sorts of OCI items; and

(d) one user group from Europe stated that items of income or expense should be permanently excluded from profit or loss when there is a compelling reason to do so (eg recycling would mislead users in terms of reporting the performance of the entity).

65. A few users and user groups expressed support for recycling all OCI items (full recycling):

(a) one user group from Japan disagreed with the rebuttable presumption that income or expense reported in OCI should be recycled, because it is unclear and may lead to diversity in practice. This user suggested deleting the rebuttable presumption and requiring full recycling of income or expenses reported in OCI;

(b) one user from the UK stated that all gains and losses should be included in profit or loss when they are realised. However, in order to avoid booking profits by selling liquid investments, a pragmatic exception should be made for such liquid investments;

(c) one international user group stated that some of its members believe that all OCI items should be recycled for the following reasons:

(i) full recycling would ensure that the cumulative amounts of profit or loss, cash flows and comprehensive income will be equal through the lifetime of the reporting entity; and

(ii) full recycling would make the distinction between retained earnings and accumulated OCI in the statement of financial position clearer. Proponents of this view see retained earnings as belonging to shareholders and as a source available for dividends. They see accumulated OCI as a temporary and unrealised gain resulting from changes in valuation and subject to fluctuations in the future; and

(d) one user from Singapore stated that OCI should be simply a bridging item between the statement of financial position and the statement of profit or loss to record any difference in measurement bases between the two. When the measurement differences reverse, they should be reported in profit or loss.

66. One user from Australia did not support the recycling of fair value changes in long-term investments from OCI to profit or loss, because the realisation of a long-term investment does not change its nature.

67. One user from the US stated that the accounting for equity securities carried at fair value through OCI in IFRS 9 is inconsistent with the rebuttable presumption that OCI items should subsequently be recycled and urged the Board to reconsider this issue.

68. One user group from Europe stated that it is important to separately disclose:

    (a) income or expenses generated and included directly in profit or loss this year; and

    (b) income or expenses generated during preceding years that have been reported in profit or loss as a result of recycling.

Other

69. One user group from the UK asked the Board to consider requiring entities to show both a historical cost profit and a current value profit.

70. One user group from Europe stated that no reference to any kind of 'return' should be made in the *Conceptual Framework*, because financial analysts use different calculation methods to calculate 'returns' based on the type of valuation. Accordingly, this user stated that the *Conceptual Framework* should not state that the purpose of the statement of profit or loss is to depict the return that an entity has made on its economic resources during the period.

Business activities and long-term investment

Exposure Draft proposals and summary of feedback

Business activities

71. The Exposure Draft did not include a general discussion on the role of a business model in financial reporting, but discussed how the way in which an entity conducts its business activities may affect:

    (a) the unit of account;

    (b) measurement; and

    (c) presentation and disclosure, including how to classify assets, liabilities, equity and items of income and expenses (including whether to include them in OCI instead of the statement of profit or loss).

72. Nearly one-third of users or user groups that submitted a comment letter commented on this issue.

73. One user from the US and a few user groups explicitly supported the Board's proposal to include guidance on how an entity's business activities may affect its financial statements, because financial statements can be made more relevant if the Board considers, when developing or revising particular Standards, how an entity conducts its business activities.

74. One user group from the UK explicitly agreed that there is no need for further consideration of business activities in the Exposure Draft.

75. One user from the US and a few user groups, stated that the *Conceptual Framework* should clarify how business activities affect the selection of the measurement bases. By doing so, the consistency of how income and expense is divided into profit or loss and OCI would be improved, thereby enhancing the relevance of profit or loss and OCI.

76. One user group from the UK stated that while entity specific information is of great interest to users, they would be wary of the Board routinely adopting a business model approach in setting Standards, because it risks compromising the comparability of information across companies.

77. One user group from Europe stated that the definition of an element should be a more dominant principle than the business model or the long-term or short-term nature of the business and cannot be overridden.

78. One user group from Europe stated that as statisticians they disagreed with the presentation of primary financial statements based on business activities.

Long-term investment

79. The Exposure Draft discussed the implications of long-term investment and long-term financing for the *Conceptual Framework*. The Board concluded that:

    (a) the proposals in the Exposure Draft provide sufficient tools for the Board to make appropriate Standard-setting decisions if future projects consider:

        (i) how to measure the long-term investments (or liabilities) of entities whose business activities include long-term investment; or

        (ii) whether such entities should report changes in the carrying amount of those investments (or liabilities) in the statement of profit or loss or OCI.

    (b) the *Conceptual Framework* contains sufficient and appropriate discussion of primary users and their information needs, and the objective of general purpose financial reporting, to address appropriately the needs of long-term investors.

80. Only a few user groups commented on this issue. Most of those user groups supported the Board's approach not to make references to the business activity of long-term investments. A few stated that 'long-term' is not defined and will be difficult to define.

81. One user group from the UK disagreed with the Board's observation that the Board did not focus too much on the needs of short-term investors.

82. One user from the US agreed that there is no reason to believe that long-term investors would need information that is not also needed by short-term investors.

The objective of general purpose financial reporting (Chapter 1) and the qualitative characteristics of useful financial information (Chapter 2)

Exposure Draft proposals

83. The Exposure Draft proposed continuing to identify relevance and faithful representation as the two fundamental qualitative characteristics of financial information.

84. The Exposure Draft proposed stating explicitly that a faithful representation represents the substance of an economic phenomenon instead of merely representing its legal form.

85. The Exposure Draft proposed clarifying that measurement uncertainty is one factor that can make financial information less relevant and, accordingly, there is a trade-off between the level of measurement uncertainty and other factors that make information relevant.

Summary of feedback

Substance over form

86. Nearly half of the users or user groups that submitted a comment letter commented on this issue. All of those that commented on this issue agreed with the proposed discussion on substance over form. However, one user group from the UK stated that it should not be forgotten that the concept introduces an element of subjectivity in deciding what the true form of the transaction is.

87. One user from the UK suggested including ‘confidence’ as a new qualitative characteristic. This user stated that ‘substance over form’ would be part of this new qualitative characteristic.

Trade-off between measurement uncertainty and relevance

88. Nearly one third of the users or user groups that submitted a comment letter commented on this issue. These users or user groups had mixed views on the discussion of the trade-off between measurement uncertainty and relevance:

    (a) one user group from the Netherlands agreed with the proposed discussion;

(b) one user group from Europe stated that an item with a high level of measurement uncertainty can still be relevant;

(c) one user from the UK and an international user group stated that measurement uncertainty has more impact on faithful representation than relevance; that is, if there is a high degree of uncertainty, there cannot be a faithful representation;

(d) one user group from the UK stated that, while a high level of measurement uncertainty can make financial information less relevant, the trade-off should not lead to the exclusion of information that helps users of financial reports to assess future cash flows; and

(e) one user group from the UK questioned the usefulness of the discussion.

'Relevance' and 'faithful representation' as the two fundamental qualitative characteristics

89. Nearly half of the users or user groups that submitted a comment letter commented on this issue.

90. One international user and a few user groups from Europe agreed that 'relevance' and 'faithful representation' should remain the two fundamental qualitative characteristics.

91. One user group from Japan stated that 'relevance' is subjective and hence may lack stability as a judgment criterion.

92. Some users supported reinstating 'reliability' as a qualitative characteristic of useful financial information:

(a) one user from the UK suggested that 'reliability' should be a separate qualitative characteristic that is given more weight than 'relevance';

(b) a few user groups stated that 'reliability' should be a separate qualitative characteristic that is given as much weight as 'relevance';

(c) one international user stated that 'reliability' should be reinstated as a component of 'faithful representation'; and

(d) one user group from the UK stated that 'reliability' should be reinstated as a fundamental qualitative characteristic and that measurement uncertainty and verifiability should be included within this characteristic.

93. One user from the UK suggested that the table in the Basis for Conclusions illustrating that 'faithful representation' virtually has the same meaning as 'reliability' should be included in the main text of the *Conceptual Framework*.

94. One user group from the UK stated that the idea that financial statements should be credible (that is, that they should provide reliable information that users can depend on) is a key concept that should be acknowledged in the *Conceptual Framework*.

Cost constraint

95. Chapter 2 of the Exposure Draft identified cost as a pervasive constraint on the information that can be provided in financial reports. The Exposure Draft also discussed the cost constraint in a number of other areas (for example, recognition and measurement). A few users and user groups were concerned that the cost constraint may lead to material or significant information being omitted from the financial statements.

Other comments

96. One user and a user group from the UK suggested that the *Conceptual Framework* should discuss 'true and fair view'.

97. The existing *Conceptual Framework* identifies 'existing and potential investors, lenders and other creditors' as the 'primary users' of financial reports. The Board did not propose any changes to the definition of 'primary users' in the Exposure Draft.

98. Nevertheless some users commented on the discussion of 'primary users':

(a) some users from the UK stated that the *Conceptual Framework* should focus on the needs of current equity investors (or perhaps those investors with a perpetual interest in the entity). They expressed the view that if current equity investors' needs are satisfied, the needs of other external users should also be satisfied;

(b) some members of a user group from the UK stated that the primary users should be current and potential equity investors. One member of this user group stated that distinguishing between equity investors and others is important for answering questions about financial performance; and

(c) a few user groups from Europe agreed with the existing definition of primary users. However, one of these user groups stated that primary users should not exclude other users such as employees, customers and regulators that also benefit from financial reporting.

Financial statements and the reporting entity (Chapter 3)

Exposure Draft proposals

99. The Exposure Draft discussed:

(a) the role of financial statements; and

(b) the description and boundary of a reporting entity.

Summary of feedback

Role of Financial Statements

100. Only a few users that submitted a comment letter commented on this section of the Exposure Draft:

(a) One international user group stated that the *Conceptual Framework* should discuss the purpose of, and interaction between, the statement of financial position, the statement(s) of financial performance and the statement of cash flows.

(b) One user group from France stated that the Exposure Draft should refer to the statement of cash flows as part of the financial statements.

(c) One user from the US explicitly agreed with the going concern assumption.

Description of the reporting entity

101. Nearly one-third of the users or user groups that submitted a comment letter commented on this issue. All of those who commented agreed with the proposed description of a reporting entity. One user from Singapore suggested that the Board should provide guidance on what constitutes a reporting entity that is not a legal entity.

Boundary of the reporting entity

102. One user group from Europe stated that the definition of 'control' in the Exposure Draft was different from that in existing Standards and, therefore, may cause confusion.

Perspective

103. The Exposure Draft included a statement that financial statements are prepared from the perspective of the entity as a whole, instead of from the perspective of any particular group of investors, lenders or other creditors. A few user groups commented on this statement:

    (a) one user group from the UK stated that shareholders support the parent company approach, but the needs of other users, such as lenders, may be different;

    (b) one international user group stated that, while the needs of users may be different among investors and creditors, the needs of the shareholder should be paramount because shareholders bear the highest risk; and

    (c) one user group from France stated that most users prefer the parent company approach.

Consolidated and unconsolidated financial statements

104. One European user group disagreed with the statement in the Exposure Draft that, in general, consolidated financial statements are more likely to provide useful information to users than unconsolidated financial statements.

105. One user from the US and a user group from Europe stated that an entity that controls one or more other entities should prepare both consolidated and unconsolidated financial statements.

Non-controlling interests

106. One user group from Europe disagreed with the statement in the Exposure Draft that consolidated financial statements of the parent are not intended to provide information to users of a subsidiary's financial statements. This user stated that both the unconsolidated financial statements of the subsidiary and the consolidated financial statements of the group to which the subsidiary belongs are crucial for analysis.

The elements of financial statements (Chapter 4)

Exposure Draft proposals

107. The Exposure Draft proposed revised definitions of the elements of financial statements (assets, liabilities, equity, income and expenses). The Exposure Draft did not propose to change the definitions of liabilities and equity to address the problems that arise in classifying instruments with the characteristics of both liabilities and equity. Instead, the Board stated that it is exploring those problems in its Financial Instruments with Characteristics of Equity research project.

108. The proposed definition of a liability referred to a 'present obligation'. The Exposure Draft proposed that an entity has a present obligation to transfer an economic resource if both:

(a) the entity has no practical ability to avoid the transfer; and

(b) the obligation has arisen from past events.

Summary of feedback

Assets and liabilities

109. Nearly one-third of the users or user groups that submitted a comment letter commented on the changes to the proposed definitions of the elements of financial statements.

110. One user group from the UK questioned why an asset is restricted to a 'present' economic resource. In this user group's view, an asset normally exists regardless of

whether it is currently controlled by the entity. Similarly, this user group questioned why the term ‘present’ was needed in the definition of a liability.

111. Another user group from the UK stated that it disagreed with the proposal that if one party has an obligation to transfer an economic resource, it follows that another party has a right to receive that economic resource. This user group was concerned that a liability may not be recognised if no one recognised an asset.

Equity

One user from the US and a user group from the UK supported the Board’s proposal to address the distinction between liabilities and equity in a separate project. However, another user group from the UK stated that the distinction between liabilities and equity needed to be discussed in the *Conceptual Framework*.

Income and expense

112. One user group from the UK stated that the *Conceptual Framework* should carry over the clarification in the existing *Conceptual Framework* that ‘income’ includes revenues and gains and ‘expenses’ include losses.

113. A few user groups from the UK stated that defining income and expense based on movements in balance sheet elements reinforces the perception that the Board is focussed on the balance sheet. One of these user groups stated that the Board should focus on the income statement because different ‘types’ of income are of different levels of usefulness for users. Another user group stated that the balance sheet and the income statement should be given equal prominence.

114. One user group from France stated that it does not oppose defining assets first, but in reality all users begin their analysis by looking at income and expenses (except when they deal with investment companies).

115. One user group from the UK stated that the definition of income (expenses) covers both inflows (outflows) and enhancements (depletions) of assets (liabilities). This user suggested that this point should be made clear in the *Conceptual Framework*.

Other potential elements

116. A few users made comments about other potential elements:

(a) one user group from Japan stated that 'profit or loss' should be defined as an element of financial statements;

(b) one user group from the UK suggested that the *Conceptual Framework* should define 'revenue' and discuss operating or ordinary activities; and

(c) one user group from the UK stated that the *Conceptual Framework* should define elements for:

   (i) the statement of changes in equity; and

   (ii) the statement of cash flows.

Present obligation

117. One user and a few user groups from the UK explicitly agreed with the proposals regarding when an entity has a present obligation.

118. Other comments from users included:

(a) one user group from the UK suggested referring to the concept of matching, because that concept would indicate when an entity has a present obligation;

(b) one user group from the UK stated that, in some jurisdictions, provisions, by law are required to be made for losses that are 'likely' to occur and that the Exposure Draft should acknowledge that such 'likely' losses meet the definition of a liability;

(c) one user group from Europe stated that a liability should be recognised if a transfer is 'probable';

(d) one user group from the UK stated that an obligation exists where any action available to an entity to avoid it is more adverse than settling that obligation, rather than when the action is 'significantly more adverse'; and

(e) one user from the US stated that more consideration should be given to the notion of economic compulsion.

Executory contracts

119. Only a few user groups that submitted a comment letter commented on the proposal related to executory contracts:

(a) one user group from the UK supported not revisiting trade date accounting; and

(b) one user group from Europe questioned how the recognition criteria for executory contracts would be applied in practice.

Recognition and derecognition (Chapter 5)

Exposure Draft proposals

120. On recognition, the Exposure Draft proposed that assets and liabilities (and any related income, expenses or changes in equity) should be recognised if such recognition provides users of financial statements with:

(a) relevant information about the asset or the liability and about any income, expenses or changes in equity;

(b) a faithful representation of the asset or the liability and of any income, expenses or changes in equity; and

(c) information that results in the benefits exceeding the cost of providing that information.

121. On derecognition, the Exposure Draft proposed that accounting requirements for derecognition should aim to represent faithfully both:

(a) the assets and liabilities (if any) retained after the transaction or other event that led to the derecognition; and

(b) the change in the entity's assets and liabilities as a result of that transaction or other event.

Summary of feedback

Recognition

122. Nearly one-quarter of users or user groups that submitted a comment letter commented on recognition.

123. One user group from the UK explicitly agreed with the discussion on recognition.

124. One user group from the UK stated that an item should only be recognised when it can be measured ‘reliably’. This user group further stated that an entity should not be required to be ‘marked to model’ because the item cannot be measured reliably.

125. Another user group from the UK stated that the Exposure Draft should emphasise that the alternative to recognising an asset or a liability is to disclose the item rather than to omit the item altogether.

126. Members of a few user groups supported including a probability criterion in the recognition criteria. These users suggested using ‘probable’ or ‘more likely than not’, and in cases when these suggested thresholds do not work, the probability criterion should be determined at the Standards level. Members of a user group from Japan preferred to have a probability criterion with an exception for derivatives.

127. One user from the UK stated that sell-side analysts and buy-side analysts may view the probability criterion differently:

(a) sell-side analysts in valuation may simply apply the probability of the event to the cost of the event and insert the expected value into a company’s valuation or balance sheet; and

(b) buy-side analysts would leave the expected value out of the valuation/balance sheet, but flag it as a risk factor in weighing up any decision to buy/sell the investment.

Derecognition

128. Only a few user groups from the UK commented on derecognition. Comments included the following:

(a) one explicitly agreed with the proposed discussion on derecognition;

(b) another stated that it was difficult to understand how to faithfully represent a transaction other than to reflect the changes in the assets and liabilities. This user group suggested that the concept of ‘substance over form’ should be considered in questions about derecognition; and

(c) yet another stated that both ‘control’ and ‘risks and rewards’ need to be considered in any approach to derecognition and that considering risks and rewards can help identify the substance of the transaction.

Presentation and disclosure, other than profit or loss and OCI (Chapter 7)

Exposure Draft proposals

129. The Exposure Draft discussed:

    (a) the objective and scope of financial statements; and

    (b) presentation and disclosure as communication tools.

Summary of feedback

The objective and scope of financial statements

130. Nearly one-third of users or user groups that submitted a comment letter commented on this issue.

131. One user from the UK suggested that the Board should fundamentally reconsider the structure of primary financial statements and urged the Board to expedite its project on primary financial statements.

132. One user group from Europe suggested that the *Conceptual Framework* should identify the primary financial statements.

133. One user group from the UK stated that reporting the cash flows of an entity should be the objective of financial statements.

134. One user group from the Netherlands suggested that the Board should make the linkage between primary financial statements more evident.

135. One user group stated that the first primary statement that users look at is the statement of profit or loss, because it provides information about the performance of the entity in the period. Nevertheless, this user group stated that the balance sheet is not a subordinate statement but the two primary financial statements are important.

136. A few users from Europe stated that the sector in which the entity operated could influence the user's analysis. For example, for entities that are highly leveraged (such as in the financial sector), the balance sheet is important and for entities that are not so highly leveraged (such as in the industry sector), profit or loss is more important unless the entity was in distress or having difficulties meeting its covenants.

137. One user group from Europe stated that the information provided in the statement of profit or loss must be correct and that it must be directly derived from the matching principle, rather than being indirectly derived from the changes in the measurement of assets and liabilities.

138. One user group from the UK stated that it was unclear when and why it may be appropriate to split the total income or expenses arising from changes in the carrying amount of an asset or a liability into components and to classify them separately.

139. A few user groups from Europe suggested that the terms ‘presentation’ and ‘disclosure’ should be defined and used consistently in the Standards.

140. One user from the US explicitly supported the proposal to exclude from financial statements forward-looking information that does not provide information about existing conditions.

Presentation and disclosure as communication tools

141. Only a few users or user groups that submitted a comment letter commented on this issue.

142. One user group from Europe agreed with the need for comparable information about preceding periods. However, this user group stated that it was important to determine the minimum level of detail in the primary financial statements, which would require comparable figures.

143. One user from the US stated that the *Conceptual Framework* should make an explicit reference to the disclosure of immaterial information as a key contributor to clutter in financial reports.

144. A few users from Europe stated that sensitivity analyses were extremely important because they helped users understand the outcome of potential changes to the assumptions made by management.

Other issues

Concepts of capital and capital maintenance

145. The Exposure Draft included a discussion of capital maintenance that was largely unchanged from the existing *Conceptual Framework*.

146. Only a few user groups from the UK commented on this Chapter. One of these user groups stated that the proposed Chapter was unhelpful because the Exposure Draft seems to be saying that profit can be calculated based on either nominal monetary units or units of constant purchasing power. Another user group stated that the discussion of capital maintenance should not be limited to situations of high inflation and suggested that the Chapter, as proposed, should be deleted.

Other

147. One user group from the UK suggested that the *Conceptual Framework* should consistently focus on financial statements, rather than on financial reporting.

148. A few user groups from the UK stated that the Exposure Draft, including the Basis for Conclusions, was too long and that a shorter document would be easier for users to digest and generate a greater degree of engagement from the user community.

149. Regarding Standards that depart from the *Conceptual Framework*:

    (a) one user from Singapore stated that any existing Standards that are identified as being inconsistent with the *Conceptual Framework* should be reviewed and, if necessary, revised;

    (b) a few user groups stated that the Exposure Draft should explain that departures from the *Conceptual Framework* are expected to be infrequent. One international user group stated that any departure should be carefully considered before it is included in future accounting Standards. One user group from the UK stated that it is important that any departure is subject to due process and is explained clearly; and

    (c) one user group from Europe agreed with not changing existing Standards immediately as a result of changing the *Conceptual Framework* and agreed that any decision to amend an existing Standard should follow the Board's normal due process for adding a project to its agenda.

150. One user from the UK emphasised the valuable and necessary role of judgement. In this user's view, rules designed to eliminate manipulation have created accounts that are too often precisely wrong rather than roughly right and that accounting manipulation can be handled by a robust audit.