March 2018

IFRS® Conceptual Framework
Project Summary

Conceptual Framework for Financial Reporting

Conceptual Framework at a glance

Introduction

The International Accounting Standards Board (Board) issued the revised *Conceptual Framework for Financial Reporting* (*Conceptual Framework*), a comprehensive set of concepts for financial reporting, in March 2018.

It sets out:

- the objective of financial reporting
- the qualitative characteristics of useful financial information
- a description of the reporting entity and its boundary
- definitions of an asset, a liability, equity, income and expenses
- criteria for including assets and liabilities in financial statements (recognition) and guidance on when to remove them (derecognition)
- measurement bases and guidance on when to use them
- concepts and guidance on presentation and disclosure

This Project Summary summarises:

- why the Board revised the *Conceptual Framework*
- the main changes from the previous *Conceptual Framework*
- the main concepts and guidance in each chapter of the *Conceptual Framework*

Purpose

- to assist the Board to develop IFRS Standards (Standards) based on consistent concepts, resulting in financial information that is useful to investors, lenders and other creditors
- to assist preparers of financial reports to develop consistent accounting policies for transactions or other events when no Standard applies or a Standard allows a choice of accounting policies
- to assist all parties to understand and interpret Standards

Status

- provides concepts and guidance that underpin the decisions the Board makes when developing Standards
- not a Standard
- does not override any Standard or any requirement in a Standard

Effective date

- immediately for the Board and the IFRS Interpretations Committee
- annual periods beginning on or after 1 January 2020 for preparers who develop an accounting policy based on the *Conceptual Framework*

Why have we revised the *Conceptual Framework*?

Previous *Conceptual Framework*

- issued in 1989 and partly revised in 2010
- useful, but incomplete and needed improvement

Priority
identified as a priority by stakeholders in the 2011 Agenda Consultation

Filling gaps
for example, guidance on measurement, presentation and disclosure

Updating
for example, the definitions of an asset and a liability

Clarifying
for example, the role of measurement uncertainty

Revised *Conceptual Framework*

- a comprehensive set of concepts for financial reporting

Approach

In revising the *Conceptual Framework*, the Board sought a balance between providing high-level concepts and providing enough detail for the *Conceptual Framework* to be useful to the Board and others.

The Board views the *Conceptual Framework* as a practical tool to help it develop Standards. Hence, the *Conceptual Framework* includes concepts that help the Board develop Standards and also discusses the factors the Board needs to consider in making judgements when application of the concepts does not lead to a single answer.

Main changes

The revised *Conceptual Framework* introduces the following main improvements:

New

Measurement	concepts on measurement, including factors to be considered when selecting a measurement basis
Presentation and disclosure	concepts on presentation and disclosure, including when to classify income and expenses in other comprehensive income
Derecognition	guidance on when assets and liabilities are removed from financial statements

Updated

Definitions	definitions of an asset and a liability
Recognition	criteria for including assets and liabilities in financial statements

Clarified

Prudence	**Stewardship**	**Measurement uncertainty**	**Substance over form**

Chapter 1—The objective of financial reporting

This chapter sets out the objective of general purpose financial reporting (financial reporting), what information is needed to achieve that objective and who the primary users (users) of financial reports are.

Objective of financial reporting

To provide financial information that is useful to users in making decisions relating to providing resources to the entity

Users' decisions involve decisions about

- buying, selling or holding equity or debt instruments
- providing or settling loans and other forms of credit
- voting, or otherwise influencing management's actions

To make these decisions, users assess

- prospects for future net cash inflows to the entity
- management's stewardship of the entity's economic resources

To make both these assessments, users need information about both

- the entity's economic resources, claims against the entity and changes in those resources and claims
- how efficiently and effectively management has discharged its responsibilities to use the entity's economic resources

Summary of changes

This chapter was issued in 2010 and went through extensive due process at that time. Therefore, in revising the *Conceptual Framework*, the Board did not fundamentally reconsider this chapter. However, it clarified why information used in assessing stewardship is needed to achieve the objective of financial reporting.

Stewardship

Users of financial reports need information to help them assess management's stewardship. The *Conceptual Framework* explicitly discusses this need as well as the need for information that helps users assess the prospects for future net cash inflows to the entity.

Users of financial reports

Users of financial reports are an entity's existing and potential investors, lenders and other creditors. Those users must rely on financial reports for much of the financial information they need.

Chapter 2—Qualitative characteristics of useful financial information

This chapter discusses what makes financial information useful.

For information to be useful it must both be **relevant** and provide a **faithful representation** of what it purports to represent. **Relevance** and **faithful representation** are the fundamental qualitative characteristics of useful financial information, and the guiding concepts that apply throughout the revised *Conceptual Framework*.

Fundamental qualitative characteristics

Relevance

- information is **relevant** if it is capable of making a difference to the decisions made by users
- financial information is capable of making a difference in decisions if it has predictive value or confirmatory value

Faithful representation

- information must **faithfully represent** the substance of what it purports to represent
- a faithful representation is, to the maximum extent possible, complete, neutral and free from error
- a faithful representation is affected by level of measurement uncertainty

Enhancing qualitative characteristics

Comparability | Verifiability | Timeliness | Understandability

- these four qualitative characteristics enhance the usefulness of information
- but they cannot make non-useful information useful

Cost constraint

- the benefit of providing the information needs to justify the cost of providing and using the information

Summary of changes

This chapter was issued in 2010 and went through extensive due process at that time. Therefore, in revising the *Conceptual Framework* the Board did not fundamentally reconsider this chapter. However, the Board clarified the roles of prudence, measurement uncertainty and substance over form in assessing whether information is useful.

Prudence

Neutrality is supported by the exercise of prudence. Prudence is the exercise of caution when making judgements under conditions of uncertainty. Prudence does not allow for overstatement or understatement of assets, liabilities, income or expenses.

Measurement uncertainty

Measurement uncertainty does not prevent information from being useful. However, in some cases the most relevant information may have such a high level of measurement uncertainty that the most useful information is information that is slightly less relevant but is subject to lower measurement uncertainty.

Chapter 3—Financial statements and the reporting entity

This chapter describes the objective and scope of financial statements and provides a description of the reporting entity.

Reporting entity

- an entity that is required, or chooses, to prepare financial statements
- not necessarily a legal entity—could be a portion of an entity or comprise more than one entity

Financial statements

a particular form of financial reports that provide information about the reporting entity's assets, liabilities, equity, income and expenses

Consolidated financial statements	Unconsolidated financial statements	Combined financial statements
provide information about assets, liabilities, equity, income and expenses of both the parent and its subsidiaries as a single reporting entity	provide information about assets, liabilities, equity, income and expenses of the parent only	provide information about assets, liabilities, equity, income and expenses of two or more entities that are not all linked by a parent-subsidiary relationship

Summary of changes

This chapter is new.

Boundary of a reporting entity

Determining the appropriate boundary of a reporting entity can be difficult if, for example, the entity is not a legal entity. In such cases, the boundary is determined by considering the information needs of the users of the entity's financial statements. Those users need information that is **relevant** and that **faithfully represents** what it purports to represent. A reporting entity does not comprise an arbitrary or incomplete collection of assets, liabilities, equity, income and expenses.

Chapter 4—The elements of financial statements

This chapter defines the five elements of financial statements—an asset, a liability, equity, income and expenses.

Previous definition of an asset	Revised definition of an asset
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	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

Main changes in the definition of an asset

- separate definition of an economic resource—to clarify that an asset is the economic resource, not the ultimate inflow of economic benefits
- deletion of 'expected flow'—it does not need to be certain, or even likely, that economic benefits will arise
- a low probability of economic benefits might affect recognition decisions and the measurement of the asset

Previous definition of a liability	Revised definition of a liability
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	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

Main changes in the definition of a liability

- separate definition of an economic resource—to clarify that a liability is the obligation to transfer the economic resource, not the ultimate outflow of economic benefits
- deletion of 'expected flow'—with the same implications as set out above for an asset
- introduction of the 'no practical ability to avoid' criterion to the definition of obligation

Summary of changes

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 definition of equity as the residual interest in the assets of the entity after deducting all its liabilities is unchanged. The Board's research project on Financial Instruments with Characteristics of Equity is exploring the distinction between liabilities and equity.

No practical ability to avoid

The revised *Conceptual Framework* discusses how the 'no practical ability to avoid' criterion is applied in the following circumstances:

(a) if a duty or responsibility arises from the entity's customary practices, published policies or specific statements—the entity has an obligation if it has no practical ability to act in a manner inconsistent with those practices, policies or statements.

(b) if a duty or responsibility is conditional on a particular future action that the entity itself may take—the entity has an obligation if it has no practical ability to avoid taking that action.

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Unit of account

the right(s) or obligation(s), or group of rights and obligations, to which recognition criteria and measurement concepts are applied

Selecting the unit of account

Relevance

- a unit of account is selected to provide **relevant** information about the asset or liability and any related income and expenses

Faithful representation

- a unit of account is selected to provide a **faithful represention** of the substance of the transaction or other event from which the asset, liability and any related income or expenses have arisen

Executory contract

An executory contract is a contract that is equally unperformed. It establishes a single asset or liability for the inseparable combined right and obligation to exchange economic resources.

Substance of contracts

To represent contractual rights and obligations faithfully, financial statements must report their substance. In some cases, the substance of such rights and obligations is clear from a contract's legal form. But, in other cases, the terms of the contract, or of a group or series of contracts, may require analysis to identify the substance of the rights and obligations.

Revised definition of income

Increases in assets, or decreases in liabilities, that result in increases in equity, other than those relating to contributions from holders of equity claims

Revised definition of expenses

Decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims

Although income and expenses are defined in terms of changes in assets and liabilities, information about income and expenses is just as important as information about assets and liabilities.

Chapter 5—Recognition and derecognition

This chapter discusses 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

Recognition criteria

Relevance

- whether recognition of an item results in **relevant** information may be affected by, for example:
  - low probability of a flow of economic benefits
  - existence uncertainty

Faithful representation

- whether recognition of an item results in a **faithful representation** may be affected by, for example:
  - measurement uncertainty
  - recognition inconsistency (accounting mismatch)
  - presentation and disclosure

Cost constraint

Cost constrains recognition decisions, just as it constrains other financial reporting decisions

Summary of changes

The previous recognition criteria were that an entity should recognise an item that met the definition of an element if it was probable that economic benefits would flow to the entity and if the item had a cost or value that could be determined reliably.

The revised recognition criteria refer explicitly to the qualitative characteristics of useful information.

The Board's aim was to develop a more coherent set of concepts, not to increase or decrease the range of assets and liabilities recognised.

Why recognition is important

Recognising assets, liabilities, equity, income and expenses depicts an entity's financial position and financial performance in structured summaries (the statements of financial position and financial performance). The amounts recognised in a statement are included in the totals and, if applicable, subtotals, in the statement. The statements are linked because income and expenses are linked to changes in assets and liabilities.

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Derecognition	The removal of all or part of a recognised asset or liability from an entity's statement of financial position

Derecognition normally occurs	
For an asset	For a liability
when the entity loses control of all or part of the recognised asset	when the entity no longer has a present obligation for all or part of the recognised liability

Derecognition aims to faithfully represent both

- any assets and liabilities retained after the transaction that led to the derecognition
- the change in the entity's assets and liabilities as a result of that transaction

Summary of changes

The guidance on derecognition is new.

Derecognition resulting from a transfer

Normally, a faithful representation of a transfer of an asset or liability is achieved by derecognition of the asset or liability with appropriate presentation and disclosure.

However, in limited cases, it may be necessary to continue to recognise a transferred component of an asset or liability together with a liability or asset for the proceeds received or paid, with appropriate presentation and disclosure.

Chapter 6—Measurement

This chapter describes various measurement bases and discusses factors to be considered when selecting a measurement basis.

Historical cost measurement bases

- historical cost provides information derived, at least in part, from the price of the transaction or other event that gave rise to the item being measured
- historical cost of assets is reduced if they become impaired and historical cost of liabilities is increased if they become onerous
- one way to apply a historical cost measurement basis to financial assets and financial liabilities is to measure them at amortised cost

Summary of changes

The previous version of the *Conceptual Framework* included little guidance on measurement. The revised *Conceptual Framework* describes what information measurement bases provide and explains the factors to consider when selecting a measurement basis.

Current value measurement bases

- current value provides information updated to reflect conditions at the measurement date
- current value measurement bases include:

fair value	• 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 • reflects market participants' current expectations about the amount, timing and uncertainty of future cash flows
value in use (for assets) fulfilment value (for liabilities)	• reflects entity-specific current expectations about the amount, timing and uncertainty of future cash flows
current cost	• reflects the current amount that would be: ▪ paid to acquire an equivalent asset ▪ received to take on an equivalent liability

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The factors to be considered when selecting a measurement basis are **relevance** and **faithful representation**, because the aim is to provide information that is useful to investors, lenders and other creditors

Factors to consider in selecting a measurement basis

Relevance

Relevance of information provided by a measurement basis is affected by:

characteristics of the asset or liability	contribution to future cash flows
• the variability of cash flows • sensitivity of the value to market factors or other risks • for example, amortised cost cannot provide relevant information about a deriviative	• whether cash flows are produced directly or indirectly in combination with other economic resources • the nature of the entity's business activities • for example, if assets are used in combination to produce goods or services, historical cost can provide relevant information about margins achieved in a period

Faithful representation

Whether a measurement basis can provide a **faithful representation** is affected by:

measurement inconsistency	measurement uncertainty
• if financial statements contain measurement inconsistencies (accounting mismatch), those financial statements may not faithfully represent some aspects of the entity's financial position and financial performance	• does not necessarily prevent the use of a measurement basis that provides relevant information • but if too high might make it necessary to consider selecting a different measurement basis

Cost constraint

Cost constrains the selection of a measurement basis, just as it constrains other financial reporting decisions

Selecting a measurement basis

In selecting a measurement basis, it is necessary to consider the nature of the information in both the statement of financial position and the statement(s) of financial performance.

The relative importance of each factor to be considered (see boxes) depends upon the facts and circumstances of individual cases.

Consideration of the factors and the cost constraint is likely to result in the selection of different measurement bases for different assets, liabilities, income and expenses.

Chapter 7—Presentation and disclosure

This chapter includes concepts on presentation and disclosure and guidance on including income and expenses in the statement of profit or loss and other comprehensive income.

The statement of profit or loss

- The statement of profit or loss is the primary source of information about an 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
- The statement(s) of financial performance include(s) a total (subtotal) for profit or loss
- In principle, all income and expenses are classified and included in the statement of profit or loss

Other comprehensive income

- 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 an asset or liability 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**

Recycling

- In principle, income and expenses included in other comprehensive income in one period are recycled to the statement of profit or loss in a future period when doing so results in the statement of profit or loss providing more **relevant** information or a more **faithful representation**
- When recycling does not result in the statement of profit or loss providing more **relevant** information or a more **faithful representation**, the Board may decide income and expenses included in other comprehensive income are not to be subsequently recycled

Summary of changes

This chapter is new.

Better Communication

Information about assets, liabilities, equity, income and expenses is communicated through presentation and disclosure in the financial statements.

Effective communication of information in financial statements makes that information more relevant and contributes to a faithful representation of an entity's assets, liabilities, equity, income and expenses.

The revised *Conceptual Framework* includes concepts that describe how information should be presented and disclosed in financial statements.

The Board is also working on several projects on the theme of Better Communication to make financial information more useful to investors, lenders and other creditors and to improve the communication of that information.

Amendments to References to the Conceptual Framework in IFRS Standards—a separate accompanying document

That document sets out amendments to Standards to update references to the *Conceptual Framework*.

Objective of the amendments	• Some Standards include explicit references to previous versions of the *Conceptual Framework* • These amendments update those references so they refer to the revised *Conceptual Framework*
Effects	• The Board expects the amendments to references to the *Conceptual Framework* in Standards will not have a significant effect on users and preparers of financial statements
Effective date and transition	• The amendments are effective for annual periods beginning on or after 1 January 2020, with earlier application permitted • The amendments should be applied retrospectively unless retrospective application would be impracticable or involve undue cost or effort

Exemptions

- IFRS 3 *Business Combinations*

To avoid unintended consequences, acquirers are required to apply the definitions of an asset and a liability and supporting concepts in the previous, rather than the revised, *Conceptual Framework*. The Board plans to assess how IFRS 3 can be updated without unintended consequences.

- Regulatory account balances

When developing accounting policies for regulatory account balances applying IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, entities are required to refer to the previous, rather than the revised, *Conceptual Framework*. This avoids entities revising those accounting policies twice within a short period: once for the revised *Conceptual Framework* and again when a revised Standard on rate-regulated activities is issued.

Important information

This Project Summary has been compiled by the staff of the IFRS Foundation for the convenience of interested parties. The views within this document are those of the staff who prepared this document and do not necessarily reflect the views or the opinions of the Board. The content of this Project Summary does not constitute any advice and is not to be considered as an authoritative document issued by the Board.

Official pronouncements of the Board are available in electronic format to eIFRS subscribers. Publications are available for ordering from the IFRS Foundation website at www.ifrs.org.

Other relevant documents

Conceptual Framework for Financial Reporting—describes the objective of, and the concepts for, general purpose financial reporting.

Basis for Conclusions on the Conceptual Framework for Financial Reporting—summarises the Board's considerations in developing the *Conceptual Framework*.

Amendments to References to the Conceptual Framework in IFRS Standards—sets out amendments to Standards, their accompanying documents and IFRS practice statements.

Feedback Statement—summarises the feedback on the proposals that led to the revised *Conceptual Framework.*

Notes

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