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STAFF PAPER

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Project	**Conceptual Framework**		
Paper topic	Proposed amendments—IAS 1 and IAS 8		
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Purpose of this paper

1. The purpose of this paper is to discuss whether any amendments would be needed to IAS 1 *Presentation of Financial Statements* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* following the revision of the *Conceptual Framework for Financial Reporting* (the '*Conceptual Framework*').

2. The staff recommend the following amendments to IAS 1 and IAS 8:

   (a) replacing the term 'reliability' with 'faithful representation' in the paragraphs that refer to reliability as a qualitative characteristic of useful financial information;

   (b) replacing references to the *Framework* with references to the *Conceptual Framework*;

   (c) updating the quotes from the *Conceptual Framework* included in these Standards;

   (d) updating the description of fair presentation in paragraph 15 of IAS 1 and the guidance for entities on developing accounting policies in paragraphs 10-11 of IAS 8 to reflect the updated qualitative characteristics in Chapter 3 and the wider range of concepts to be included in the revised *Conceptual Framework*;

   (e) updating paragraph 28 of IAS 1 to reflect the changes in the guidance on recognition in the *Conceptual Framework* Exposure Draft; and

(f) removing from paragraph 118 of IAS 1 the examples of measurement bases.

Analysis

3. As discussed in Agenda Paper 10C, the staff have carried out a review of existing Standards to identify potential inconsistencies with the concepts that the IASB has tentatively decided to include in the *Conceptual Framework* Exposure Draft.

4. Two of the existing Standards—IAS 1 and IAS 8—rely directly on the guidance in the *Conceptual Framework* and act as a direct link between the Standards and the *Conceptual Framework*. IAS 1 prescribes the basis for preparation of general purpose financial statements and requires the application of the *Conceptual Framework* in order to achieve fair presentation in financial statements. IAS 8 provides guidance to help entities develop and apply accounting policies when there are no specifically applicable IFRSs.

5. The guidance in these Standards is based on the qualitative characteristics in the *Conceptual Framework*, and the concepts in the *Conceptual Framework* are essential to the application of these Standards. Consequently, the staff propose that the IASB should make some amendments to these Standards, as described below:

   (a) paragraph 6 describes proposed amendments to IAS 1; and

   (b) paragraph 7 describes proposed amendments to IAS 8.

Proposed amendments to IAS 1

6. Proposed amendments to IAS 1 are identified in Appendix A. The staff propose the following amendments:

   (a) replacing the term ‘reliability’ with ‘faithful representation’ in the paragraphs that refer to reliability as a qualitative characteristic of useful financial information. The staff proposals on clarifying the term ‘reliability’ in the Standards are discussed in more detail in Agenda Paper 10F;

(b) replacing references to the *Framework* with references to the *Conceptual Framework* (as discussed in Agenda Paper 10E) and updating the quote from the *Conceptual Framework* included in the definition of materiality in paragraph 7 of the Standard;

(c) updating the description of fair presentation in paragraph 15 of IAS 1 to reflect the updated qualitative characteristics in Chapter 3 and the wider range of concepts to be included in the revised *Conceptual Framework*. Currently, paragraph 15 refers only to the definitions and recognition criteria for assets, liabilities, income and expenses in the *Framework*, whereas the revised *Conceptual Framework* will have a wider scope (for example, it will include concepts relating to derecognition). The proposed general reference to the concepts in the *Conceptual Framework* will also continue to work if the *Conceptual Framework* is revised again in the future;

(d) removing from paragraph 118 the examples of measurement bases. This would not affect the meaning of the sentence in which they are included, but it would help to avoid inconsistency if the titles of measurement bases or their classification change in the future; and

(e) amending paragraph 28, which refers to recognition criteria for elements in the *Framework*. In May 2014 the IASB tentatively decided to replace the recognition criteria with factors to consider in deciding whether to recognise an asset or a liability. The staff propose updating paragraph 28 to reflect the changes in the guidance on recognition in the Exposure Draft.

Question 1
Do you agree with the amendments to IAS 1 proposed in Appendix A and summarised in paragraph 6?

Proposed amendments to IAS 8

7. Proposed amendments to IAS 8 are identified in Appendix B. The staff propose the following amendments:

   (a) consistently with our proposed changes to IAS 1:

      (i) replacing the term ‘reliability’ with ‘faithful representation’ where it refers to a qualitative characteristic of useful financial information;

      (ii) replacing references to the *Framework* with references to the *Conceptual Framework;* and

      (iii) updating the quote from the *Conceptual Framework* that is included in the definition of materiality in paragraph 6 of the Standard;

   (b) amending paragraph 10, which provides guidance to entities on developing accounting policies when no Standard specifically applies to a transaction, other event or condition to reflect:

      (i) the revision of qualitative characteristics in 2010; and

      (ii) the IASB’s tentative decision in May 2014 to reinstate explicit references to prudence and substance over form. The staff believe it would be beneficial to retain references to prudence and substance over form in the Standard, as well as in the *Conceptual Framework*, because the *Conceptual Framework* is not a Standard and does not directly impose requirements on preparers.

   (c) amending the hierarchy of pronouncements in paragraph 11 to reflect the wider range of concepts to be provided in the revised *Conceptual Framework*. Currently, paragraph 11 refers only to the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Framework*, while the revised *Conceptual Framework* will have a wider scope. The proposed general reference to the concepts in the *Conceptual Framework* will also continue to work if the *Conceptual Framework* is revised again in the future.

Question 2

Do you agree with the amendments to IAS 8 proposed in Appendix B and summarised in paragraph 7?

Effective date

8. In July 2014 the IASB discussed transition and effective date for the revised *Conceptual Framework* and tentatively decided that a transition period of at least approximately 18 months should be allowed for entities that use the *Conceptual Framework* to develop and apply accounting policies for a transaction, other event or condition for which no IFRS specifically applies. It also tentatively decided that early application should be permitted.

9. Agenda Paper 10I for the July 2014 IASB meeting noted that the IASB would need to consider where to place the effective date for the revised *Conceptual Framework*. Possible options are:

   (a) setting the effective date in the revised *Conceptual Framework* itself; or

   (b) stating in the revised *Conceptual Framework* that it supersedes the previous version, ie it will come into force immediately after publication, and setting within IAS 8 the effective date for entities that, in accordance with IAS 8, use the *Conceptual Framework* in developing an accounting policy.

10. The staff recommend that the amendments proposed to IAS 1 and IAS 8 should have a transition period of at least approximately 18 months, in line with that confirmed by the IASB in July 2014. Transition to the revised *Conceptual Framework* for preparers will be achieved by replacing references to the *Framework* with references to the *Conceptual Framework* in these Standards. These Standards will specify the effective date for that replacement, ie setting the effective date in the *Conceptual Framework* itself will not be necessary.

Question 3

Do you agree with the suggested transition to the *Conceptual Framework* through the proposed amendments to IAS 1 and IAS 8?

Appendix A—Proposed amendments to IAS 1

This Appendix describes the amendments to IAS 1 that the staff propose the IASB should make when it finalises the revised Conceptual Framework. *An entity shall apply the amendments for annual periods beginning on or after [date to be inserted]. Amended paragraphs are shown with new text underlined and deleted text struck through.*

Par.	Proposed text
IN11	The previous version of IAS 1 used the titles 'balance sheet' and 'cash flow statement' to describe two of the statements within a complete set of financial statements. IAS 1 uses 'statement of financial position' and 'statement of cash flows' for those statements. The new titles reflect more closely the function of those statements, as described in the *Conceptual Framework for Financial Reporting*~~[1]~~ (see paragraphs BC14–BC21 of the Basis for Conclusions). ~~[1] The reference to the *Framework* is to IASC's *Framework for the Preparation and Presentation of Financial Statements*, adopted by the IASB in 2001. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*.~~
7	***Material* Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.** Assessing whether an omission or misstatement could influence economic decisions of users, and so be material, requires consideration of the characteristics of those users. The *Conceptual Framework for Financial Reporting* ~~*Framework for the Preparation and Presentation of Financial Statements*~~ states in paragraph QC32 ~~25[2]~~ that 'financial reports are prepared for users who ~~are assumed to~~ have a reasonable knowledge of business and economic activities and who review and analyse ~~accounting and a willingness to study~~ the information diligently ~~with reasonable diligence~~.' Therefore, the assessment needs to take into account how users with such attributes could reasonably be expected to be influenced in making economic decisions. ~~[2] IASC's *Framework for the Preparation and Presentation of Financial Statements* was adopted by the IASB in 2001. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*. Paragraph 25 was superseded by Chapter 3 of the *Conceptual Framework*.~~
15	**Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the concepts ~~definitions and recognition criteria for assets, liabilities, income and expenses~~ set out in the *Conceptual Framework*.~~[3]~~ The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.** ~~[3] Paragraphs 15–24 contain references to the objective of financial statements set out in the *Framework [for the Preparation and Presentation of Financial Statements]*. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*, which replaced the objective of financial statements with the objective of general purpose financial reporting: see Chapter 1 of the *Conceptual Framework*.~~
17	In virtually all circumstances, an entity achieves a fair presentation by compliance with applicable IFRSs. A fair presentation also requires an entity: (a) to select and apply accounting policies in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. IAS 8 sets out a hierarchy of authoritative guidance that management considers in the absence of an IFRS that specifically applies to an item. (b) to present information, including accounting policies, in a manner that provides useful financial

Par.	Proposed text
	~~relevant, reliable, comparable and understandable~~ information. Financial information is useful if it is relevant and faithfully represents what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable. (c) to provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.
19	**In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*, the entity shall depart from that requirement in the manner set out in paragraph 20 if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure.**
20	**When an entity departs from a requirement of an IFRS in accordance with paragraph 19, it shall disclose:** **(a) that management has concluded that the financial statements present fairly the entity's financial position, financial performance and cash flows;** **(b) that it has complied with applicable IFRSs, except that it has departed from a particular requirement to achieve a fair presentation;** **(c) the title of the IFRS from which the entity has departed, the nature of the departure, including the treatment that the IFRS would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the objective of financial statements set out in the *Conceptual Framework*, and the treatment adopted; and** **(d) for each period presented, the financial effect of the departure on each item in the financial statements that would have been reported in complying with the requirement.**
23	**In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*, but the relevant regulatory framework prohibits departure from the requirement, the entity shall, to the maximum extent possible, reduce the perceived misleading aspects of compliance by disclosing:** **(a) the title of the IFRS in question, the nature of the requirement, and the reason why management has concluded that complying with that requirement is so misleading in the circumstances that it conflicts with the objective of financial statements set out in the *Conceptual Framework*; and** **(b) for each period presented, the adjustments to each item in the financial statements that management has concluded would be necessary to achieve a fair presentation.**
24	For the purpose of paragraphs 19–23, an item of information would conflict with the objective of financial statements when it does not represent faithfully the transactions, other events and conditions that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to influence economic decisions made by users of financial statements. When assessing whether complying with a specific requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*, management considers: (a) why the objective of financial statements is not achieved in the particular circumstances; and

Par.	Proposed text
	(b) how the entity's circumstances differ from those of other entities that comply with the requirement. If other entities in similar circumstances comply with the requirement, there is a rebuttable presumption that the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*.
28	When the accrual basis of accounting is used, an entity recognises items as assets, liabilities, equity, income and expenses (the elements of financial statements) when they satisfy the definitions for those elements and qualify for recognition in accordance with ~~and recognition criteria for those elements in~~ the *Conceptual Framework*.[4] ~~[4] replaced by the *Conceptual Framework* in September 2010~~
46	For example, a significant acquisition or disposal, or a review of the presentation of the financial statements, might suggest that the financial statements need to be presented differently. An entity changes the presentation of its financial statements only if the changed presentation provides a faithful and more relevant representation ~~information that is reliable and more relevant~~ to users of the financial statements and the revised structure is likely to continue, so that comparability is not impaired. When making such changes in presentation, an entity reclassifies its comparative information in accordance with paragraphs 41 and 42.
60	**An entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position in accordance with paragraphs 66–76 except when a presentation based on liquidity provides a faithful and more relevant representation ~~information that is reliable and more relevant~~. When that exception applies, an entity shall present all assets and liabilities in order of liquidity.**
63	For some entities, such as financial institutions, a presentation of assets and liabilities in increasing or decreasing order of liquidity provides a faithful and more relevant representation ~~information that is reliable and more relevant~~ than a current/non-current presentation because the entity does not supply goods or services within a clearly identifiable operating cycle.
64	In applying paragraph 60, an entity is permitted to present some of its assets and liabilities using a current/non-current classification and others in order of liquidity when this provides a faithful and more relevant representation ~~information that is reliable and more relevant~~. The need for a mixed basis of presentation might arise when an entity has diverse operations.
89	Some IFRSs specify circumstances when an entity recognises particular items outside profit or loss in the current period. IAS 8 specifies two such circumstances: the correction of errors and the effect of changes in accounting policies. Other IFRSs require or permit components of other comprehensive income that meet the *Conceptual Framework*'s[5] definition of income or expense to be excluded from profit or loss (see paragraph 7). ~~[5] In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*.~~
99	**An entity shall present an analysis of expenses recognised in profit or loss using a classification based on either their nature or their function within the entity, whichever provides a faithful and more relevant representation ~~information that is reliable and more relevant~~.**
105	The choice between the function of expense method and the nature of expense method depends on historical and industry factors and the nature of the entity. Both methods provide an indication of those costs that might vary, directly or indirectly, with the level of sales or production of the entity. Because each method of presentation has merit for different types of entities, this Standard requires management to select the presentation that provides a faithful and more relevant representation ~~is reliable and more relevant~~. However, because information on the nature of expenses is useful in

Par.	Proposed text
	predicting future cash flows, additional disclosure is required when the function of expense classification is used. In paragraph 104, ‘employee benefits’ has the same meaning as in IAS 19.
118	It is important for an entity to inform users of the measurement basis or bases used in the financial statements ~~(for example, historical cost, current cost, net realisable value, fair value or recoverable amount)~~ because the basis on which an entity prepares the financial statements significantly affects users’ analysis. When an entity uses more than one measurement basis in the financial statements, for example when particular classes of assets are revalued, it is sufficient to provide an indication of the categories of assets and liabilities to which each measurement basis is applied.

Appendix B—Proposed amendments to IAS 8

This Appendix describes the amendments to IAS 8 that the staff propose that the IASB should make when it finalises the revised Conceptual Framework. *An entity shall apply the amendments for annual periods beginning on or after [date to be inserted]. Amended paragraphs are shown with new text underlined and deleted text struck through.*

Paragraph	Proposed text
1	The objective of this Standard is to prescribe the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The Standard is intended to enhance the relevance of an entity's financial statements and the faithfulness of the representation they provide ~~reliability of an entity's financial statements~~, and the comparability of those financial statements over time and with the financial statements of other entities.
6	***Material*** **Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.** Assessing whether an omission or misstatement could influence economic decisions of users, and so be material, requires consideration of the characteristics of those users. The *Conceptual Framework for Financial Reporting* ~~*Framework for the Preparation and Presentation of Financial Statements*~~ states in paragraph QC32 ~~25~~~~[2]~~ that 'financial reports are prepared for users who ~~are assumed to~~ have a reasonable knowledge of business and economic activities and who review and analyse ~~accounting and a willingness to study~~ the information diligently ~~with~~ ~~reasonable diligence~~.' Therefore, the assessment needs to take into account how users with such attributes could reasonably be expected to be influenced in making economic decisions. ~~[2] IASC's *Framework for the Preparation and Presentation of Financial Statements* was adopted by the IASB in 2001. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*. Paragraph 25 was superseded by Chapter 3 of the *Conceptual Framework*.~~
8	IFRSs set out accounting policies that the IASB has concluded result in financial statements containing useful ~~relevant and reliable~~ information about the transactions, other events and conditions to which they apply. Those policies need not be applied when the effect of applying them is immaterial. However, it is inappropriate to make, or leave uncorrected, immaterial departures from IFRSs to achieve a particular presentation of an entity's financial position, financial performance or cash flows.
10	**In the absence of an IFRS that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in financial information that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. To be useful, information must:** **(a) be relevant ~~to the economic decision-making needs of users~~; and** **(b) faithfully represent what it purports to represent. A faithful representation ~~reliable, in that the financial statements~~:** **(i) is complete in all material respects ~~represent faithfully the financial position, financial performance and cash flows of the entity~~;** **(ii) is neutral, supported by the exercise of prudence. Prudence is the exercise of caution when making judgements under conditions of uncertainty to ensure that assets, liabilities, income and expenses are neither overstated nor understated ~~reflect the economic substance of transactions, other events and conditions, and not merely the legal form~~;**

Paragraph	Proposed text
	(iii) free from error; and ~~are neutral, ie free from bias;~~ (iv) reflects the economic substance of transactions, other events and conditions, and not merely their legal form. ~~are prudent; and~~ ~~(v) are complete in all material respects.~~
11	**In making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order:** **(a) the requirements in IFRSs dealing with similar and related issues; and** **(b) the concepts ~~the definitions, recognition criteria, and measurement concepts for assets, liabilities, income and expenses~~ in the *Conceptual Framework*.~~[3]~~** ~~[3] In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*.~~
14	**An entity shall change an accounting policy only if the change:** **(a) is required by an IFRS; or** **(b) results in the financial statements providing a faithful ~~reliable~~ and more relevant representation ~~information about~~ of the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows.**
29	**When a voluntary change in accounting policy has an effect on the current period or any prior period, would have an effect on that period except that it is impracticable to determine the amount of the adjustment, or might have an effect on future periods, an entity shall disclose:** **(a) the nature of the change in accounting policy;** **(b) the reasons why applying the new accounting policy provides a faithful ~~reliable~~ and more relevant representation ~~information~~;** **(c) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment:** **(i) for each financial statement line item affected; and** **(ii) if IAS 33 applies to the entity, for basic and diluted earnings per share;** **(d) the amount of the adjustment relating to periods before those presented, to the extent practicable; and** **(e) if retrospective application is impracticable for a particular prior period, or for periods before those presented, the circumstances that led to the existence of that condition and a description of how and from when the change in accounting policy has been applied.** **Financial statements of subsequent periods need not repeat these disclosures.**