

## STAFF PAPER

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## IASB Meeting

Project	Conceptual Framework		
Paper topic	Recognition		
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**Purpose of paper**

1. Chapter 5 of the Exposure Draft *Conceptual Framework for Financial Reporting* (‘the Exposure Draft’) includes concepts addressing the recognition process and recognition criteria.
2. In the March 2016 meeting, we provided a high-level summary of the comments received<sup>1</sup> on those concepts.
3. This paper considers whether the Board should make any changes to these proposals in response to the feedback received on the Exposure Draft. This paper does not discuss the concepts for *derecognition*, which will be discussed at a future meeting.

**Summary of staff recommendations**

4. The staff recommend that:
  - (a) the revised *Conceptual Framework* should confirm the approach to recognition as proposed in the Exposure Draft. This approach requires

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<sup>1</sup> AP10G. March 2016, IASB Meeting. <http://www.ifrs.org/Meetings/MeetingDocs/IASB/2016/March/AP10G-Conceptual-Framework.pdf>

recognition decisions to be made by reference to the qualitative characteristics of useful financial information;

- (b) consistently with this approach, the revised *Conceptual Framework* should not prescribe a ‘probability criterion’, ie it should not prohibit the recognition of assets or liabilities with a low probability of an inflow or outflow of economic benefits;
- (c) the concepts proposed in the Exposure Draft should be enhanced to provide more direction on the recognition of assets and liabilities with a low probability of inflows or outflows of economic benefits; and
- (d) the revised *Conceptual Framework* should identify only two criteria for recognition (relevance and faithful recognition). The need for benefits that exceed the costs should not be identified as a third distinct recognition criterion. Instead, the *Conceptual Framework* should explain that, as with all other areas of financial reporting, cost constrains recognition decisions and the benefits of the information provided to users of financial statements by recognition of an asset or a liability (and any related income, expenses or changes in equity) must be sufficient to justify the costs of providing that information.

## Structure of paper

- 5. The paper is structured as follows:
  - (a) background information
    - (i) Exposure Draft proposals (paragraphs 6-13); and
    - (ii) subsequent Board decisions (paragraphs 14-15).
  - (b) a summary and analysis of the main issues raised by respondents and staff recommendations for dealing with those issues. The main issues concerned:

- (i) Issue 1: the overall approach and removal of the probability criterion (paragraphs 18-39); and
  - (ii) Issue 2: the application of the cost constraint to recognition decisions (paragraphs 40-45).
- (c) three appendices, which:
- (i) illustrate how the staff think that the proposed concepts could be enhanced to provide more direction on the recognition of assets and liabilities with a low probability of inflows or outflows of economic benefits (Appendix A);
  - (ii) list the more minor comments and suggestions received from respondents (Appendix B); and
  - (iii) set out the staff views on the possible implications for IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* of the proposed recognition concepts (Appendix C).

## Background information

### ***Exposure Draft proposals (paragraphs 5.2–5.24 and BC5.1–BC5.48)***

#### *Recognition process*

6. Paragraph 5.2 of the Exposure Draft proposed to define recognition:

Recognition is 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 element.

[...]

7. Paragraphs 5.3-5.8 explained what the recognition process involves and the link that the recognition process establishes between the elements, the statement of financial position and the statement(s) of financial performance.

#### *Recognition criteria*

8. The existing *Conceptual Framework* specifies three recognition criteria that apply for the recognition of all assets and liabilities:

#### Existing criteria

- The item meets the definition of an asset or a liability.
- It is **probable** that any future economic benefit associated with the asset or liability will flow to or from the entity.
- The asset or liability has a cost or value that can be measured **reliably**.

9. However, some existing IFRS Standards do not apply a criterion based on the probability of future inflows or outflows ('the probability criterion'). In addition, those that do apply such a criterion use different thresholds. The thresholds include 'probable', 'more likely than not', 'virtually certain' and 'reasonably possible'.
10. There are also problems with the 'reliable measurement' criterion. In this context 'reliable' is usually interpreted as meaning that the item can be measured with a tolerable degree of measurement uncertainty (and perhaps also verifiable and free from error). Hence, the 'reliable measurement' criterion could be interpreted as prohibiting recognition of any value that has a high degree of measurement uncertainty, even though some values with high measurement uncertainty can provide useful information. In addition, using reliable measurement as a criterion could be confusing because the term 'reliability' is no longer defined in the *Conceptual Framework*.
11. Accordingly, the Exposure Draft proposed a new approach to recognition. Paragraph 5.9 explained that failure to recognise items that meet the definition of an element makes the statement of financial position and the statement(s) of financial performance less complete and can exclude useful information from financial statements. But it went on to acknowledge that in some circumstances, the recognition of some items that meet the definition of an element can provide information that is not useful. 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.
12. The supporting concepts noted that a consequence of this approach would be that recognition requirements may need to vary between IFRS Standards. And they identified circumstances in which recognition may not provide relevant information. These circumstances included some cases in which:
- (a) it is uncertain whether an asset exists, or is separable from goodwill, or whether a liability exists;
  - (b) there is only a low probability that an inflow or outflow of economic benefits will result; or
  - (c) a measurement of an asset or a liability is available (or can be obtained), but the level of measurement uncertainty is so high that the resulting information has little relevance and no other relevant measure is available (or can be obtained).
13. The Exposure Draft also proposed that it will often be a combination of the factors described in paragraph 12 above, instead of any single factor that causes information to lack relevance.

### ***Subsequent Board decisions***

- 14. At its May 2016 meeting, the Board tentatively decided to describe measurement uncertainty as a factor affecting faithful representation, not relevance.
- 15. This tentative decision has implications for the proposed recognition concepts. In particular, high measurement uncertainty would no longer be characterised as a factor that could affect decisions on whether recognition provides relevant information about an entity's assets, liabilities, income and expenses. Instead, it would be characterised

as a factor that could affect decisions on whether recognition would provide a faithful representation of the entity's assets, liabilities, income and expenses.

### ***Issues raised by respondents***

16. The respondents commented in particular on two aspects of the proposals:
  - (a) the overall approach and removal of probability criterion (paragraphs 18-39); and
  - (b) the application of the cost constraint (paragraphs 40-45) in recognition decisions
17. Other comments and suggestions from respondents are discussed in paragraphs 46-47.

## **Issue 1—overall approach and removal of probability criterion**

### ***Summary of feedback***

18. Many of the respondents who commented on the recognition proposals broadly agreed with the overall approach proposed in the Exposure Draft. Those broadly agreeing included many regulators, standard-setters, accountancy bodies and accounting firms. Of those who gave reasons for their support:
  - (a) some generally agreed with removing the probability criterion and instead including in the *Conceptual Framework* recognition criteria based on the qualitative characteristics;
  - (b) some agreed explicitly that the probability criterion is not appropriate for some types of assets and liabilities such as derivatives;
  - (c) some noted that as a consequence of the proposed approach to recognition concepts detailed recognition criteria would be considered at Standards level; and

- (d) a few supported what they described as the ‘even-handed’ approach proposed in the Exposure Draft, ie an approach that neither required recognition of all assets and liabilities nor set specified criteria.
19. Some respondents disagreed with the proposed recognition approach. Of these respondents, a few took the view that there should be a presumption (or overarching principle) that every item meeting the definition of an asset or a liability should be recognised. They stated that the Board could include an exception to this principle in individual IFRS Standards if it decided that recognition of a particular item would not meet the objective of financial reporting.
20. However, most of the respondents who disagreed with the proposed approach were concerned that it could lead to the recognition of too many assets and liabilities. Their main concerns—which were shared by some respondents who broadly agreed with the proposed approach—were that:
- (a) The proposals were too abstract and subjective. They did not provide enough direction, and, as a result, how the Board or preparers apply them could depend too much on individual perspectives. More concrete and robust proposals would be required to ensure that the Board develops Standards with consistent requirements that result in useful information.
- (b) The removal of the probability criterion, in combination with the removal of the reference to ‘expected’ from the definitions of an asset and a liability, could lead to requirements for entities to recognise more assets and liabilities with a low probability of inflows or outflows of economic benefits. Preparers of financial statements would have to perform unlimited searches for rights and obligations. And they might be required to recognise assets and liabilities for which recognition would not, in the view of those respondents, provide useful information. Some respondents noted that recognition of some assets or liabilities also results in recognition of income or an expense—and if future inflows or outflows are not probable, recognition of such assets and liabilities would usually result in the

recognition of income or an expense in one period that reverses in subsequent periods.

- (c) If assets and liabilities with a low probability of future inflows or outflows were recognised, they might have to be measured at expected value. Those expressing this view argued that measuring assets and liabilities at expected value is difficult and puts additional burdens on preparers of financial statements.
  - (d) The probability criterion has proved to be effective in practice. It is a more practical way of applying the qualitative characteristics than that proposed in the Exposure Draft:
    - (i) the proposed guidance addressing items with a low probability of a flow of economic benefits is not clear enough and will lead to many areas for doubt and inconsistency; and
    - (ii) ‘low probability’ is subjective because it is a relative term, and will be open to interpretation.
21. Some (predominantly European) respondents—including regulators and preparers of financial statements—suggested that the Board should assess the implications of the proposed changes to the recognition criteria (especially the removal of the probability criterion). They suggested that the Board should assess possible implications for both:
- (a) the Board in revising existing IFRS Standards or developing new IFRS Standards; and
  - (b) preparers applying the *Conceptual Framework* to develop an accounting policy in the absence of a specific IFRS Standard, or when the applicable Standard permits a choice of policies.

*Alternative suggestions*

22. Respondents with concerns about the proposed approach suggested various alternatives to that approach:

- (a) Some respondents disagreed with the proposal that recognition requirements might need to vary between IFRS Standards. They suggested that the *Conceptual Framework* should set out recognition criteria that could be applied consistently in all IFRS Standards. Some respondents specifically suggested retaining the probability criterion.
- (b) The Accounting Standards Board of Japan (ASBJ) suggested that:
- (i) for recognition of an asset or a liability that is a right or an obligation that arises from transactions, the probability criterion is unnecessary; whereas
  - (ii) for recognition of an asset or a liability or a group of assets and/or liabilities created from a right or an obligation (or rights and/or obligations) that arises from ‘other events’, the probability criterion is necessary. (For further details of the ASBJ’s suggestions, see [ASBJ Short Paper No. 2 Recognition Criteria in the Conceptual Framework](#),<sup>2</sup> which was Agenda Paper 3 for the December 2015 Accounting Standards Advisory Forum (ASAF) meeting.)
- (c) Some respondents asked for further guidance for assets or liabilities with a low probability of inflows or outflows. Suggestions included:
- (i) stating that the potential magnitude of the outcome should be considered.
  - (ii) specifying the level of probability at which assets and liabilities should be recognised.
  - (iii) clarifying whether the same level of probability should be applied for both assets and liabilities.
  - (iv) identifying the types of situations in which recognising an asset or liability with a low probability of inflows or outflows of economic benefits would not result in relevant information. Some respondents suggested adding examples.

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<sup>2</sup> <http://www.ifrs.org/Meetings/MeetingDocs/ASAF/2015/December/1512-ASAF-03-ASBJ-Short-Paper-No-2-Recognition-Criteria-in-the-CF.pdf>

- (v) including further guidance on the circumstances in which recognition may not result in faithful representation, or may not have benefits that exceed the cost of recognition.
- (d) Some respondents noted that some parts of the discussion refer to ‘low probability’, while other parts refer to ‘very low probability’. They suggested that the Board should either clarify any intentional difference between these terms, or use one term consistently.
- (e) Some respondents suggested highlighting more prominently that items that fail the recognition criteria still might need to be disclosed if information about these items provides relevant information to users of financial statements.

### **Staff analysis**

23. Although many respondents have expressed support for the proposed recognition concepts, some are concerned that removing the probability criterion from the *Conceptual Framework* itself could result in requirements to identify and recognise assets and liabilities that they think should not be recognised. They fear that the concepts will not be robust enough to ensure that the Board includes probability recognition criteria in IFRS Standards when this would be appropriate. Therefore, as noted in paragraph 21, some respondents have asked the Board to test the implications of the recognition proposals, and in particular the implications of removing the probability criterion.
24. The staff think that the Exposure Draft’s proposed changes to the recognition concepts would not have major implications for current or future projects:
- (a) the proposed concepts would align the *Conceptual Framework* with the recognition approach that the Board has already applied in some IFRS Standards and is likely to continue to apply whether or not it updates the *Conceptual Framework* (ie varying recognition requirements between Standards); and

(b) respondents to the Discussion Paper<sup>3</sup> had suggested that the proposed new concepts could lead to a change in the recognition requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. However, the staff have analysed the possible implications for IAS 37 and concluded that the proposed concepts could support retaining the existing recognition criteria in IAS 37. The staff conclusions were presented to the Board in July 2015. An extract from the paper explaining the conclusions on recognition is reproduced in Appendix C to this paper.

25. However, given the concerns expressed by some respondents, the Board might wish to consider ways of amending the proposed recognition concepts to provide more direction on the use of probability criteria in Standards. The staff have identified two alternative ways in which more direction could be provided:

(a) the *Conceptual Framework* could prescribe a probability criterion, which would prohibit the recognition of assets or liabilities with a low probability of an inflow or outflow of economic benefits (paragraphs 26-28). A probability criterion could be prescribed:

- (i) for all assets and liabilities (like the probability criterion in the existing *Conceptual Framework*), or
- (ii) for assets and liabilities that arise from events other than transactions (as suggested by the ASBJ—see paragraph 22(b));  
or

(b) the Board could confirm the approach proposed in the Exposure Draft, but enhance the supporting concepts to provide more direction on recognition of assets and liabilities with a low probability of future inflows or outflows (paragraphs 29-33).

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<sup>3</sup> Discussion Paper, A Review of the *Conceptual Framework* for Financial Reporting, 2013

*Alternative (a)—Prescribe a probability criterion*

26. The Board could consider this alternative (ie to prescribe a probability criterion) in response to the comments received on the Exposure Draft described in paragraph 20. Some respondents think that the probability criterion provided a practical filter for assets and liabilities whose recognition would be unlikely to provide relevant information. They also expressed the view that the probability criterion is less subjective and easier to apply than the approach proposed in the Exposure Draft.
27. The existing *Conceptual Framework* prescribes a probability criterion for all assets and liabilities. However, prescribing a criterion causes problems. As explained in paragraphs BC 5.8-5.9 of the Basis for Conclusions accompanying the Exposure Draft:
- BC5.8 Some existing Standards do not apply a probability recognition criterion, for example, IFRS 9 *Financial Instruments*. Those that do apply such a criterion use different probability thresholds. These include ‘probable’, ‘more likely than not’, ‘virtually certain’ and ‘reasonably possible’. The use of the different terms indicates a lack of consistency in the meaning attached at the Standards-level to the term probable used in the *Conceptual Framework*.
- BC5.9 Some have argued that a probability recognition criterion could prevent the recognition of some financial instruments, for example, derivatives. Moreover, it could sometimes result in a gain being recognised for a transaction when no economic gain has occurred. For example, suppose that, in exchange for receiving cash, an entity incurs a liability to pay a fixed amount if some unlikely event occurs in the future. If an outflow of economic benefits is not considered probable, the entity will recognise an immediate gain when it receives the cash.
28. As noted in paragraph 18, the new approach to recognition proposed in the Exposure Draft received broad support from many respondents, and respondents who supported

the proposal to remove the probability criterion have commented that the proposed approach provides a more conceptual approach to recognition. Furthermore, we think that it is difficult to set a probability threshold that could be applied across all IFRS Standards and in all recognition events. Moreover, assessing whether an inflow or outflow is probable is often highly subjective.

*Alternative (b)—Enhance the proposed concepts*

29. An alternative would be to confirm the approach proposed in the Exposure Draft, but enhance the supporting concepts to provide more direction on whether and when to recognise assets and liabilities with a low probability of inflows or outflows of economic benefits.
30. Those enhancements would not fundamentally change the approach proposed in the Exposure Draft:
  - (a) they would not change the statements in paragraph 5.9 of the Exposure Draft that:
    - (i) failure to recognise items that meet the definition of an element makes the statement of financial position and the statement(s) of financial performance less complete and can exclude useful information from financial statements; but
    - (ii) in some circumstances, the recognition of some items that meet the definition of an element can provide information that is not useful;
  - (b) they would not change the proposal in paragraph 5.9 that an entity should recognise an asset or a liability if recognition provides users of financial statements with useful information and recognition results in benefits exceeding the cost of providing that information (paragraphs 40-45);
  - (c) they would not change the proposal in paragraph 5.13(b) of the Exposure Draft that recognition of an existing asset or a liability may not provide relevant information if there is only a low probability that an inflow or outflow of economic benefits will result from the asset or liability; and

- (d) they would not change the clarification in paragraph 5.14 that deciding whether recognition will provide relevant information requires exercise of judgement and that it will often be a combination of factors, instead of any single factor, that causes information to lack relevance.
31. However, the enhancements would affect paragraphs 5.17–5.19 of the Exposure Draft, which discuss assets and liabilities with a low probability of inflows or outflows of economic benefits. The objectives of the enhancements would be to ensure that:
- (a) in deciding whether particular assets or liabilities should be recognised, the Board takes into account any applicable reasons why recognition of assets and liabilities with a low probability of inflow or outflow might not provide useful information; and
- (b) the concepts for recognition of such assets or liabilities are balanced: the drafting does not suggest that either recognition or non-recognition is the ‘preferred’ outcome.
32. We think that the first objective could be met by identifying in the *Conceptual Framework* some of the reasons why recognition of assets and liabilities with a low probability of future inflows and outflows might not provide useful information. We have identified three possible reasons:
- (a) The most relevant information about assets and liabilities with a low probability of future inflows or outflows will often be information about the amount, timing and likelihood of the possible outflows. This information is typically communicated by explanatory disclosures. Recognition decisions need to consider whether recognising an asset or a liability would provide additional relevant information beyond that provided by disclosure.
- (b) Whether recognition provides additional relevant information may depend, at least in part, on the way in which the asset or liability has arisen, ie whether it has arisen from a transaction or some other event.

- (c) A low probability of future inflows or outflows could contribute to measurement uncertainty and hence might need to be taken into consideration in assessing whether recognition would provide useful information. This might occur because, for example:
    - (i) historical data may not provide a long enough observation period in which to estimate the frequency of a low probability outcome. For example, a 50 year observation period would not provide much evidence about the frequency of an event that occurs only once every 200 years; and
    - (ii) if the probability of future inflows or outflows is low, but their possible magnitude is high, the measure of an asset or a liability may be highly sensitive to small changes in estimates of the probability.
33. We have also identified refinements that might help avoid any suggestion that recognition is the ‘preferred’ outcome for assets or liabilities with a low probability of inflows or outflows. These refinements could include:
- (a) redrafting paragraphs 5.18 and 5.19 so that there is as much discussion of situations in which recognition may provide information that *is not* relevant as of situations in which recognition may provide information that *is* relevant. This could be achieved by including examples for each situation. In the Exposure Draft, there was an example of the first situation (paragraph 5.18), but no example of the second situation (paragraph 5.19).
  - (b) making the drafting more consistent by referring to ‘low’ probability throughout the chapter instead of ‘very low’ probability in some places.

### ***Drafting illustration***

34. Appendix A to this paper illustrates how we think the enhancements discussed in paragraphs 33 could be drafted if the Board were to approve those enhancements without making more fundamental changes to the proposed concepts for recognition.

35. The illustration includes all of the enhancements that would be reflected in the paragraphs discussing relevance. The illustration does not include one enhancement that would instead be reflected in the paragraphs discussing faithful representation, ie the suggestion in paragraph 32(c) that a low probability of future inflows or outflows could also contribute to measurement uncertainty. The wording of this refinement would have to be considered alongside other changes required to implement the Board's decision to characterise measurement uncertainty as a factor affecting faithful representation (instead of relevance).

### ***Staff conclusions and recommendations***

36. Given the broad support for the approach to recognition proposed in the Exposure Draft, the staff recommend that this approach should form the basis of the recognition concepts in the revised *Conceptual Framework*. In other words, as proposed in the Exposure Draft, recognition decisions should be made by reference to the qualitative characteristics of useful financial information.
37. Consistently with that recommendation, and for the reasons in paragraphs 27-28, the staff recommend that the *Conceptual Framework* should not prescribe a probability criterion, ie it should not prohibit the recognition of assets or liabilities with a low probability of an inflow or outflow of economic benefits (irrespective of whether those assets or liabilities arise from transactions or other events).
38. The staff think that it could be helpful to provide more direction on the recognition of assets and liabilities with a low probability of inflows or outflows of economic benefits. Hence we recommend enhancing the concepts discussing such assets and liabilities, and suggest that the enhancements could encompass the matters described in paragraphs 32–33.
39. The ASAF discussed the suggestions for enhancements at its meeting on 7 July 2016. The discussions were held too late to be reported in detail in this paper. However, several ASAF members expressed support for the suggested enhancements. And

although some members had questions or comments on some of the details, only the ASBJ<sup>4</sup> expressed broad disagreement. The ASBJ said that it still thinks that the *Conceptual Framework* should retain the existing probability criterion. The staff will provide a more detailed oral report at the Board meeting.

**Question 1—Assets and liabilities with a low probability of future inflows or outflows**

- (a) Do you agree that the revised *Conceptual Framework* should confirm the approach to recognition as proposed in the Exposure Draft? This approach requires recognition decisions to be made by reference to the qualitative characteristics of useful financial information?
- (b) Do you agree that, consistently with this approach, the revised *Conceptual Framework* should not prescribe a ‘probability criterion’, ie it should not prohibit the recognition of assets or liabilities with a low probability of an inflow or outflow of economic benefits?
- (b) Do you agree that the concepts proposed in the Exposure Draft should be enhanced to provide more direction on the recognition of assets and liabilities with a low probability of inflows or outflows of economic benefits?

**Issue 2—Application of the cost constraint**

***Summary of feedback***

40. A few preparers of financial statements explicitly agreed with the proposal to identify cost-benefit considerations (the ‘cost constraint’) as one of the three criteria to be considered in recognition decisions. However, some respondents across all categories expressed concerns about this proposal. They argued that:

- (a) the cost constraint should not be given a level of importance or prominence similar to that of ‘relevance’ and ‘faithful representation’. It should be identified as a constraint on the two main criteria, not as a separate criterion in its own right;

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<sup>4</sup> Refer ASBJ’s paper in paragraph 22(b)

- (b) the cost constraint is a general constraint or an overarching concept in financial reporting. Identifying it as a specific recognition criterion could give the impression that the constraint does not apply in other areas if it is not specifically mentioned;
- (c) the proposed concepts for recognition could be applied by preparers of financial statements for some transactions. But, in the view of some respondents, only the Board—and not individual preparers of financial statements—should be allowed to reach decisions on cost-benefit considerations. The respondents argued that preparers of financial statements are not in a position to assess the benefits of recognition for users of financial statements; and
- (d) materiality provides a more conceptually sound basis for the decision of whether or not to recognise an asset or liability.

### **Staff analysis**

41. Although the cost constraint is a general constraint in financial reporting, the staff do not agree with the suggestion that the *Conceptual Framework* should not refer to the cost constraint when discussing concepts for recognition. As explained in BC2.33 of the Basis for Conclusions on the Exposure Draft, the cost constraint plays a particularly important role in decisions about recognition. Therefore, we think it is important that the recognition concepts refer to the cost constraint.
42. However, the staff accept the arguments of respondents who suggested that the cost-benefit criterion should be expressed as a constraint on the two main criteria (relevance and faithful representation), not as a separate criterion in its own right. As those respondents noted, the cost-benefit criterion is articulated in Chapter 2 of the *Conceptual Framework* as a constraint on the qualitative characteristics of useful financial information. And Chapter 6 of the Exposure Draft also proposed to articulate the cost-benefit criterion as a constraint on application of the qualitative

characteristics<sup>5</sup>. To be consistent with Chapter 2 and Chapter 6, the recognition chapter could identify two recognition criteria (relevance and faithful representation), and then separately state that, as with all other areas of financial reporting, cost constrains recognition decisions and that the benefits of the information provided to users of financial statements by recognising an element must be sufficient to justify the cost of providing that information.

43. As noted in paragraph 40(c), some respondents noted that the proposed concepts for recognition could be applied by preparers of financial statements for some transactions. However, this is true of other aspects of the *Conceptual Framework* and is not specific to the proposed recognition concepts alone.
44. As noted in paragraph 40(d), some respondents are of the view that the application of materiality would provide a more appropriate basis for recognition decisions than the cost-benefit criterion. The staff is of the view that the concepts of materiality and cost constraint are not alternatives and have different purposes. Information could be material, but the costs of recognition could exceed the benefits. Furthermore, the refinements suggested in paragraphs 41-42 would be helpful in clarifying the role of the cost constraint in making recognition decisions.

**Staff recommendation**

45. The staff recommend that the revised *Conceptual Framework* should identify only two criteria for recognition (relevance and faithful recognition); the need for benefits that exceed the costs should not be identified as a third distinct recognition criterion. Instead, the *Conceptual Framework* should explain that, as with all other areas of financial reporting, cost constrains recognition decisions. The benefits of the information provided to users of financial statements by recognition of an asset or a liability (and any related income, expenses or changes in equity) must be sufficient to justify the costs of providing that information.

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<sup>5</sup> Paragraph 6.50 of the Exposure Draft

**Question 2—Cost constraint**

Do you agree with staff recommendation in paragraph 45?

**Other comments and suggestions**

46. A few respondents argued that the recognition concepts should describe measurement uncertainty as a factor that affects faithful representation, not relevance. These comments reflected respondents' views on the description of measurement uncertainty more generally in the *Conceptual Framework*. As noted in paragraphs 14-15 above, the Board has already discussed these views and has tentatively decided to describe measurement uncertainty as a factor affecting faithful representation, not relevance. The recognition concepts will be redrafted accordingly.
47. Respondents made various other, more minor or detailed, comments on recognition. These comments and suggestions are explained in Appendix B, with staff recommendations. We think that, in each case, the comment could be addressed in drafting, or that no action is required. Accordingly, we will not raise any of these comments for discussion in the Board meeting, unless requested to do so by a Board member.

## Appendix A—Drafting illustration—possible refinements to recognition concepts

The original text is from the Exposure Draft. Suggested insertions are underlined, and suggested deletions are struck through.

### Relevance

5.13 Information about assets, liabilities, equity, income and expenses is relevant to users of financial statements. However, if one or more of the following factors applies, recognition may not provide relevant information:

- (a) ...;
- (b) if an asset or a liability exists, but there is only a low probability that an inflow or outflow of economic benefits will result (see paragraphs 5.17–5.19); or
- (c) ....

5.14 Deciding whether recognition will provide relevant information requires the exercise of judgement. It will often be a combination of the factors described in paragraphs 5.13, instead of any single factor, that causes information to lack relevance. Moreover, other factors may also cause information to lack relevance.

### Existence uncertainty and separability

5.15 ....

5.16 .....

### Low probability of a flow of economic benefits

5.17 An asset or a liability can exist even if there is a low probability that there will be an inflow or outflow of economic benefits (see paragraphs 4.13 and 4.27).

~~5.18 Even if the probability of an inflow or outflow of economic benefits is low, recognition of the asset or the liability may provide relevant information, especially if the measurement of the asset or the liability reflects the low probability and is accompanied by explanatory disclosures. For example, if an asset is acquired, or a liability is incurred, in an exchange transaction for an observable price, its cost reflects the low probability that economic benefits will flow and that cost may be relevant information.~~

~~5.19 However, users of financial statements may, in some cases, not find it useful for an entity to recognise assets and liabilities with very low probabilities of inflows and outflows of economic benefits.~~

- 5.18 If the probability of an inflow or outflow of economic benefits is low, the most relevant information may be that provided by disclosure of information about the asset or the liability in the notes to the financial statements. That information may include information about the possible amounts of any inflows or outflows of economic benefits, their possible timing and the factors affecting their likelihood.
- 5.19 Whether recognition of the asset or liability provides additional relevant information beyond that provided by disclosure could depend on factors such as how the asset or liability arose. For example:
- (a) if an asset is acquired, or a liability is incurred, in an exchange transaction for an observable price, its cost reflects the low probability that economic benefits will flow and that cost may be relevant information. Furthermore, not recognising the asset or liability would result in the recognition of income or an expense at the time of the exchange, which might not be a faithful representation of the transaction (see paragraph 5.23(a)).
  - (b) if an asset or a liability arose from an event other than an exchange transaction, that asset or the liability might not have a cost. In such circumstances, recognition of the asset or the liability typically results in recognition of income or an expense. Users of financial statements might not regard the recognition of the asset and income, or the liability and expense, as relevant information if there is only a low probability that the asset or liability will result in an inflow or outflow of economic benefits.

## APPENDIX B—Other comments and suggestions for guidance on recognition concepts

Respondent comment or suggestion	Staff recommendation	Reason for staff recommendation
<p><b>B1</b> Consider whether enhancing qualitative characteristics have any specific implications for recognition.</p>	<p>No further action.</p>	<p>The enhancing qualitative characteristics could help in choosing between two measurements that both provide relevant information and a faithful representation. But they would not be relevant in recognition decisions. If recognition provides relevant information, a faithful representation and has benefits that exceed the costs, an asset or liability should be recognised even if enhancing qualitative characteristics are not present. Conversely, if recognition does meet all these three criteria, the asset or liability would not be recognised even if the qualitative enhancing characteristics were present.</p>
<p><b>B2</b> The recognition proposals should include specific reference to 'reliability' and provide guidance about how information that is reliable contributes to faithful representation.</p>	<p>No further action.</p>	<p>The Board discussed reliability as a qualitative characteristic and decided to continue using the term 'faithful representation'. We think that many use the term 'reliability' to mean measurement uncertainty which is now described under faithful representation.</p>
<p><b>B3</b> There should be more substantive guidance on how uncertainty affects recognition.</p>	<p>No further action.</p>	<p>Paragraphs 5.15–5.16 and 5.20–5.21 of the Exposure Draft proposed extensive discussion on how uncertainty affects recognition. If the Board agrees with the staff recommendation to add discussion of how a low probability of inflows our outflows could contribute to measurement uncertainty, the final <i>Conceptual Framework</i> will contain even more discussion than the Exposure Draft.</p>

Respondent comment or suggestion	Staff recommendation	Reason for staff recommendation
<b>B4</b> Paragraph 5.11 of the Exposure Draft appears to suggest that when an element is not recognised, disclosure would be sufficient to compensate. However, due to the different roles of the face of financial statements and related disclosure, disclosure cannot compensate for the non-recognition of an element. Furthermore, the term 'compensate' is inappropriate.	Consider in drafting.	The paragraph in the Exposure Draft was simply trying to make the point that if recognition of an element <i>would not</i> provide useful information, information disclosed about that element is very important and should be prominent. We should consider how to make that point without implying that, where recognition <i>would</i> provide useful information, disclosure compensates for non-recognition.
<b>B5</b> Paragraph 5.12 of the Exposure Draft should also refer to liabilities, and not only assets.	Correct in drafting.	Liability was omitted while drafting the Exposure Draft.
<b>B6</b> Paragraph 5.13 provides indicators of when information may not be relevant. Clarify that these indicators should not be considered in isolation, but may need to be traded-off against one another.	No further action.	Paragraph 5.14 explains that it will often be a combination of the factors described in paragraph 5.13, instead of any single factor, that causes information to lack relevance.
<b>B7</b> The general discussion in paragraphs 5.4-5.8 would be better placed in chapter 7 because it explains how the accounting model links the various summary statements.	Consider in drafting.	We will review the location after all decisions have been taken about the content of the final <i>Conceptual Framework</i> .

Respondent comment or suggestion	Staff recommendation	Reason for staff recommendation
<p><b>B8</b> Suggest that paragraph 5.9 be redrafted and made more consistent with the discussion that follows that paragraph:</p> <p>(a) suggest that the first two sentences of paragraph 5.9 are removed to follow the general principle of recognition and combined in such a way that it is generally presumed that failing to recognise all assets and liabilities would make the financial statements less useful, etc., but that there are circumstances in which not recognising an element is appropriate. The material in paragraphs 5.11 and 5.12 would then explain this principle.</p> <p>(b) The sentence ‘Failure to recognise from financial statements’ in paragraph 5.9 is too definitive (using the verb makes), and seems contrary to paragraph 5.11. It is also inconsistent with the second sentence in that paragraph, which uses ‘can’, in which case paragraph 5.11 makes better sense.</p>	<p>Consider in drafting.</p>	<p>Such a refinement might be useful to ensure that the statement in paragraph 5.9 does not appear to be inconsistent with other statements in that paragraph and/or other concepts in the recognition chapter.</p>
<p><b>B9</b> Delete the discussion on matching in paragraph 5.8 of the Exposure Draft. Otherwise, it could cause confusion, for example, as to whether the recognition of income/expenses should be guided by (a) the matching of income and expenses, or (b) the derecognition of related assets/liabilities.</p>	<p>No further action.</p>	<p>The discussion on matching is largely carried forward from the existing <i>Conceptual Framework</i> and is regarded as important by some stakeholders. We do not think it will be read to suggest that decisions about recognition should be guided by a matching objective.</p>
<p><b>B10</b> The proposals should state that the potential magnitude of the outcome should be considered when considering the recognition of an asset or liability with a low probability of a future inflow or outflow of economic benefits.</p>	<p>No further action.</p>	<p>We do not think that the potential magnitude of the outcome would necessarily be a factor to consider (other than as part of an assessment of materiality). Even if the potential magnitude is very high, recognition might not provide relevant information if the probability of that outcome is low.</p>
<p><b>B11</b> The concepts should specify the level of probability that should be regarded as ‘low probability’, and whether the same level applies to both assets and liabilities.</p>	<p>No further action</p>	<p>We think that this would be a decision that should be taken at a Standards level. Prescribing a particular probability threshold in the <i>Conceptual Framework</i> would be inconsistent with the overall approach proposed.</p>

Respondent comment or suggestion	Staff recommendation	Reason for staff recommendation
<b>B12</b> Clarify that relevance should be assessed from the perspective of a user of financial statements, and not from the perspective of the management preparing the financial statements. Such a clarification would help counter the inherent risk of management understating liabilities.	Consider in drafting.	Such clarification might be useful, especially for recognition decisions being taken by preparers of financial statements.
<b>B13</b> The discussion of existence uncertainty and separability would be better placed in the chapter discussing the definitions of an asset and a liability.	No further action.	Existence uncertainty does not arise from uncertainty about the definitions. It arises from uncertainty about events, or the consequences of those events. And the need to consider existence uncertainty arises mainly in decisions about recognition and measurement.
<b>B14</b> Clarify that decisions regarding existence uncertainty and separability need to be taken at an IFRS Standards level.	No further action.	It is implicit in the approach that all decisions about recognition need to be taken at Standards level.
<b>B15</b> The Exposure Draft placed too much emphasis on the impact of high measurement uncertainty in recognition decisions. High measurement uncertainty alone should not be sufficient reason to preclude recognition since a high level of measurement uncertainty does not necessarily imply that the information resulting from recognition lacks relevance. Too much focus on measurement uncertainty might lead to non-recognition of assets and liabilities whose recognition would provide useful information.	Consider in drafting.	A high level of measurement uncertainty does not necessarily mean that recognition would not provide useful information. We think that that message is conveyed by paragraph 5.20. But several respondents (including the International Actuarial Association) appear to think that the balance is not quite right. We think that any changes would be minor.
<b>B16</b> Additional disclosure requirements referred in the Exposure Draft should be decided at an IFRS Standards level rather than in the <i>Conceptual Framework</i> .	Review during drafting.	The references to disclosure in the recognition chapter are not intended to establish concepts for disclosure.
<b>B17</b> It is not clear whether the cost constraint should be assessed only when an item first arises, or whether it should be assessed on an ongoing basis.	No further action.	We do not think such a clarification is necessary in the <i>Conceptual Framework</i> . This aspect could be addressed at Standards level for a particular type of asset or liability.

## APPENDIX C—POSSIBLE IMPLICATIONS FOR IAS 37 OF CONCEPTUAL FRAMEWORK PROPOSALS ON RECOGNITION

As explained in paragraph 24(b) of the paper, in July 2015, the staff presented Agenda Paper 14C *Possible Implications for IAS 37 of the Conceptual Framework proposals* to the Board. This paper contained the staff's analysis of possible implications of various concepts proposed in the *Conceptual Framework Exposure Draft*, including the proposed recognition concepts. The staff concluded that the proposed recognition concepts could support retaining the existing recognition criteria in IAS 37, including the existing 'probability' criterion.

The relevant section of that paper is reproduced below.

### 2 Recognition criteria

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#### ***Recognition is an important aspect of IAS 37***

- 2.1 'Recognition' of an asset or a liability is the inclusion of the asset or liability at a monetary amount in relevant totals in the statement of financial position. Recognition requires a single monetary amount to be assigned to the liability.
- 2.2 IAS 37 was developed to address liabilities that are subject to uncertainty. Some of those liabilities (such as contractual warranty obligations) are subject only to 'outcome uncertainty'—it is certain that the entity has a liability but uncertain what outflows, if any, will be required to settle the liability. Others (such as a possible liability to pay damages for an alleged act of wrong-doing) are also subject to significant 'existence uncertainty'—ie, the existence or non-existence of the liability is disputed and will be confirmed only on the occurrence of a future event, such as a court ruling.
- 2.3 In the face of significant existence or outcome uncertainty, the question of whether a particular liability should be assigned a single monetary amount and recognised in the financial statements is an important one.

#### ***IAS 37 specifies three recognition criteria***

- 2.4 IAS 37 specifies that liabilities within its scope should be recognised if three recognition criteria are all met:
- (a) if, on the basis of all available evidence, it is more likely than not that a present obligation exists; and

- (b) if it is probable (= more likely than not) that an outflow of resources will be required to settle the obligation; and
  - (c) if a reliable estimate can be made of the amount of the obligation.<sup>6</sup>
- 2.5 The recognition criteria are consistent with existing concepts. The ‘probable outflows’ and ‘reliable estimate’ criteria mirror the two recognition criteria specified in the existing *Conceptual Framework*.<sup>7</sup> There is no specific reference to existence uncertainty in the existing *Conceptual Framework*.
- 2.6 IAS 37 notes that, except in extremely rare cases, an entity will be able to determine a range of possible outcomes and can therefore make an estimate of the obligation that is sufficiently reliable for recognition.

***The IASB previously proposed to remove the ‘probable outflows’ criterion***

- 2.7 The recognition criteria in IAS 37 have been the subject of much debate in the past. The debate has focused on the ‘probable outflows’ recognition criterion.
- 2.8 Although the criterion is specified in the existing *Conceptual Framework*, it is not in other Standards. In particular, when the IASB revised IFRS 3 *Business Combinations*, it decided to omit the probable outflows criterion from that Standard. The IASB’s reasons were that:
- (a) an asset or a liability should be recognised if it satisfies the definitions in the *Framework*. Otherwise the financial statements are incomplete.
  - (b) if there is a low probability of a future outflow, that factor can be reflected by measuring the liability at an amount that reflects the low probability.<sup>8</sup>
- 2.9 In its previous project to amend IAS 37, the IASB also proposed to remove the probable outflows criterion from IAS 37. The IASB’s main reasons were that:
- (a) the amendment would ensure that all liabilities within the scope of IAS 37 were treated consistently, regardless of whether they had been assumed in a business combination or incurred separately.<sup>9</sup>

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<sup>6</sup> IAS 37, paragraphs 14, 15 and 23.

<sup>7</sup> *The Conceptual Framework for Financial Reporting*, paragraphs 4.38 and 4.46.

<sup>8</sup> IFRS 3, paragraph BC272.

<sup>9</sup> Exposure Draft of Proposed Amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, June 2005, paragraph BC22.

- (b) recognition of a liability can provide useful information, even if outflows are not probable. For example, an increase in the amount recognised from one period to the next can give an early indication of a change in management’s assessment of the probability, or possible amount, of future cash flows.
- (c) probability would still play a role in recognition if it is uncertain whether a liability exists.
- (d) the probable outflows criterion was inconsistent with the IASB’s proposal to require entities to measure liabilities within the scope of IAS 37 at ‘expected value’, ie to take into account all possible outcomes and their probabilities.<sup>10</sup>

***Many stakeholders argued that the probable outflows criterion serves a useful purpose***

2.10 Most respondents to the 2005 Exposure Draft opposed the IASB’s proposal to remove the probable outflows criterion from IAS 37. And many went on to reiterate their opposition when responding to the IASB’s limited scope re-exposure of revised proposals for measurement, published in 2010.

Respondents to the two Exposure Drafts expressed views that:

- (a) recognition of liabilities for which there is only a low probability of a cash outflow does not provide relevant financial information. Disclosure provides more useful information.
- (b) the cost to financial statement preparers of recognising and measuring low probability liabilities may outweigh the benefits to users. The cost of identifying all the possible outcomes and estimating the probability of each is disproportionate to the amounts likely to be recognised.
- (c) the probable outflows criterion is a useful filter that avoids the need for consideration of whether a liability exists. In its absence, IAS 37 would be more complex to apply, leading to greater diversity.
- (d) without the probable outflows criterion, entities might need to identify and recognise liabilities for undetected acts of wrongdoing. Recognition would increase the risk of future detection and prejudice the outcome of any action taken against the company.
- (e) consistency with other standards, such as IFRS 3, is not important. Differences in the nature of the transactions—especially for assets and liabilities acquired in a business combination—justify different requirements. The different criteria have not caused major problems for users or preparers.

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<sup>10</sup>IASB Update June 2006

- (f) The IASB should change conceptual criteria only after wider debate within the conceptual framework project. Accordingly, any revisions to IAS 37 should be postponed until the IASB completed its review of the *Conceptual Framework*.<sup>11</sup>

***The Conceptual Framework Exposure Draft proposes a new approach***

- 2.11 The *Conceptual Framework* Exposure Draft proposes a new approach to recognition.
- 2.12 Whereas the existing *Conceptual Framework* specifies two specific recognition criteria (probable outflows and reliable measurement) that should be applied in all Standards, the Exposure Draft proposes that recognition requirements may need to vary between Standards.<sup>12</sup> It explains that:

5.9 Failure to recognise items that meet the definition of an element makes the statement of financial position and the statement(s) of financial performance less complete and can exclude useful information from financial statements. On the other hand, in some circumstances, the recognition of some items that meet the definition of an element can provide information that is not useful. An entity recognises an asset or a liability (and any related income, expenses or changes in equity) 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 benefits exceeding the cost of providing that information. [Cross references omitted.]

- 2.13 The *Conceptual Framework* Exposure Draft goes on to provide further guidance. Of particular note for liabilities within the scope of IAS 37 is its proposals that:

- (a) recognition may not provide relevant information:
  - (i) if it is uncertain whether an asset or a liability exists;
  - (ii) if an asset or a liability exists, but there is only a low probability that an inflow or outflow of economic benefits will result; or

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<sup>11</sup> This list combines comments received on:

- (a) the 2005 Exposure Draft (see IASB meeting February 2006, Appendix to Agenda Paper 8, *Comment Letter Summary*, paragraphs 36-43); and
- (b) the 2010 Exposure Draft (see IASB meeting, September 2010, Appendix A to Agenda Paper 7 *Liabilities—amendments to IAS 37, Comment letter summary*).

<sup>12</sup> *Conceptual Framework* Exposure Draft, paragraph 5.10.

- (iii) if all of the measurements of a liability that could be obtained have such a level of measurement uncertainty that the resulting information has little relevance.<sup>13</sup>
- (b) it will often be a combination of these factors, instead of any single factor, that causes information to lack relevance.<sup>14</sup>

*Existence uncertainty*

2.14 In its discussion of existence uncertainty, the *Conceptual Framework* Exposure Draft specifically refers to a type of liability that is within the scope of IAS 37 and for which recognition may not provide relevant information:

5.16 For some liabilities, it may be unclear whether a past event causing an obligation has occurred. For example, if another party claims that the entity has committed an act of wrongdoing and should compensate the other party for that act, it may be uncertain whether the act occurred or whether the entity committed it. In some such cases, the uncertainty about the existence of an obligation, possibly combined with a low probability of outflows of economic benefits and a high level of measurement uncertainty, may mean that the recognition of a single amount would not provide relevant information. Whether or not the liability is recognised, disclosures about the uncertainties associated with the liability may be needed.

*Low probability of an inflow or outflow of economic benefits*

2.15 In its discussion of assets and liabilities with a low probability of inflows or outflows, the *Conceptual Framework* Exposure Draft proposes that:

5.18 Even if the probability of an inflow or outflow of economic benefits is low, recognition of the asset or the liability may provide relevant information, especially if the measurement of the asset or the liability reflects the low probability and is accompanied by explanatory disclosures. For example, if an asset is acquired, or a liability is incurred, in an exchange transaction for an observable price, its cost reflects the low probability that economic benefits will flow and that cost may be relevant information.

5.19 However, users of financial statements may, in some cases, not find it useful for an entity to recognise assets and liabilities with very low probabilities of inflows and outflows of economic benefits.

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<sup>13</sup>*Conceptual Framework* Exposure Draft, paragraph 5.13.

<sup>14</sup>*Conceptual Framework* Exposure Draft, paragraph 5.14.

*Measurement uncertainty*

2.16 In its discussion of measurement uncertainty, the *Conceptual Framework* Exposure Draft proposes concepts that closely reflect the guidance in IAS 37. It notes that the use of reasonable estimates is an essential part of the preparation of financial statements and does not necessarily undermine their usefulness.<sup>15</sup> However, it goes on to give examples of situations in which a high level of measurement uncertainty may contribute to information having little relevance, including a situation in which:

5.21(a) the range of possible outcomes is extremely wide and the likelihood of each outcome is exceptionally difficult to estimate. In such cases, the most relevant information for users of financial statements might relate to the range of outcomes and the factors affecting their likelihoods. When that information is relevant (and can be provided at a cost that does not exceed the benefits), disclosure of that information in the notes to the financial statements may be appropriate, regardless of whether the entity also recognises the asset or liability. However, in some cases, trying to capture that information in a single number may not provide any further relevant information. ...

***The proposed concepts could support the existing criteria in IAS 37***

2.17 If the IASB were to revisit the IAS 37 recognition criteria and consider the proposed concepts, it could reach different conclusions from those it reached in its previous project to amend IAS 37. The proposed concepts acknowledge that recognition requirements may need to vary between Standards. Hence, applying the proposed concepts, consistency with other Standards would not in itself be a reason for removing the probable outflows criterion from IAS 37.

2.18 Liabilities within the scope of IAS 37 have characteristics that are different from those of other liabilities and that might justify different recognition criteria. Existence uncertainty can be a more important factor for some liabilities within the scope of IAS 37 than for many other liabilities. But even once existence uncertainty has been addressed, there are other differences to consider.

2.19 Most liabilities within the scope of IAS 37 have one particular characteristic that tends to distinguish them from many other liabilities: they cannot be measured by reference to an observable transaction price. They tend not to be traded, so do not have an observable *current* transaction price. Perhaps more unusually, there is typically no exchange transaction that provides an observable *historical* transaction price for the liability (proceeds that the entity received in exchange for incurring the liability). For example:

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<sup>15</sup>*Conceptual Framework* Exposure Draft, paragraph 5.20.

- (a) liabilities for acts of wrongdoing, environmental rehabilitation obligations and other obligations imposed by governments arise from an entity’s activities, not from a direct exchange transaction; and
  - (b) although warranty obligations arise from a direct exchange transaction, those within the scope of IAS 37 do not have an observable transaction price: warranty obligations are within the scope of IAS 37 only if the customer does not have the option to purchase the warranty separately.<sup>16</sup>
- 2.20 Where they exist, observable transaction prices (whether historical or current) can often be obtained at a relatively low cost, take into account the probability of future inflows or outflows and are usually subject to relatively little measurement uncertainty. Consequently, even if the only observable transaction price for a liability is a historical one, there is likely to be at least one measure of the liability for which the benefits of recognition exceed the costs—further recognition criteria may not be necessary. It could be argued that the need for recognition criteria in IAS 37 stems in part from the absence of *any* observable transaction price.
- 2.21 I have not identified any obvious conflicts between the existing IAS 37 criteria and the proposed concepts. Indeed there is considerable alignment. The *Conceptual Framework* Exposure Draft specifically identifies existence uncertainty, a low probability of outflows and exceptionally high measurement uncertainty as factors that, individually or in combination, may cause the information provided by recognition to lack relevance. And the *Conceptual Framework* Exposure Draft envisages information being disclosed about liabilities with high measurement uncertainty (see the extract below paragraph 2.16 ) that is very similar to the information required by IAS 37.
- 2.22 Some people might interpret the proposed concepts as suggesting recognition thresholds somewhat lower than those applied at present in IAS 37. For example:
- (a) the *Conceptual Framework* Exposure Draft envisages that recognition of a particular liability may not provide useful information if there is only a ‘low’ probability of outflows. Low is not defined. But some people might argue that the 50% threshold in IAS 37 filters out more liabilities than just those with ‘low’ probabilities—a probability of 45%, say, is not particularly low.
  - (b) the *Conceptual Framework* Exposure Draft states that it will often be a combination of factors (existence uncertainty, a low probability of outflows and exceptionally high measurement uncertainty) that lead to a conclusion that recognition would not provide sufficiently useful information to justify the cost. IAS 37 requires only one of these factors to be present for non-

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<sup>16</sup>IFRS 15 *Revenue from Contracts with Customers*, paragraph B30.

recognition of a liability (if the liability fails any one of the three recognition criteria, it is not recognised).

2.23 Accordingly, if the IASB were to apply the proposed concepts to the recognition criteria in IAS 37, it might consider whether the existing thresholds are too high. However, when the IASB develops new financial reporting requirements, the IASB's objective should be to address problems with the existing requirements.<sup>17</sup> Combining this objective with the recognition concepts proposed in the *Conceptual Framework* Exposure Draft suggests that the IASB would consider lowering the existing thresholds only if it has evidence that:

- (a) there are examples in practice of liabilities that do not satisfy existing IAS 37 recognition criteria but whose recognition would provide useful information to investors, lenders or other creditors; and
- (b) the costs of recognising these liabilities would not exceed the benefits.

2.24 The IASB could consult users and preparers of financial statements to identify any such liabilities.

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<sup>17</sup>*IASB and IFRS Interpretations Committee Due Process Handbook*, paragraph 4.6.