Overview of revised Conceptual Framework

31 July 2019

Highlights

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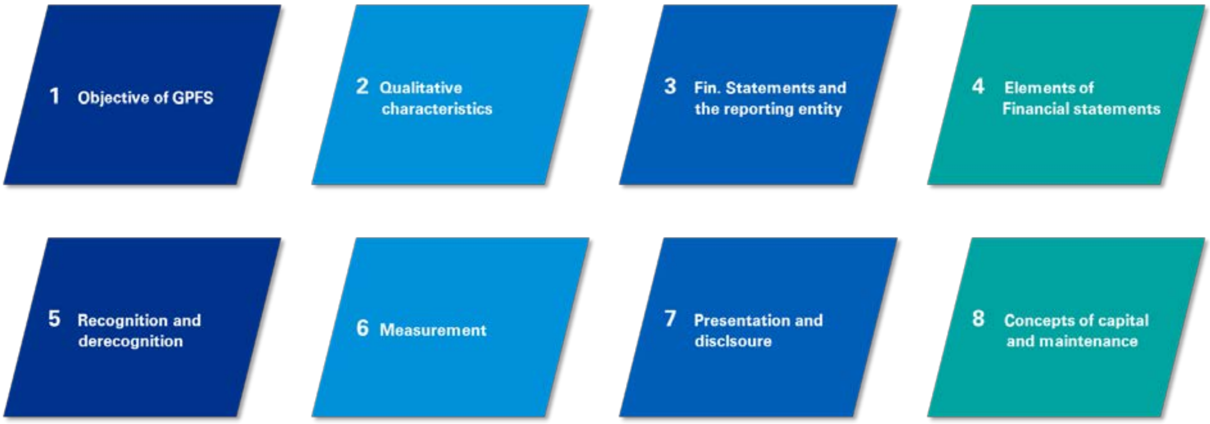
Background

The IASB issued a revised *Conceptual Framework for Financial Reporting* (RCF) in March 2018. The AASB proposed a two-phased approach to adopt the RCF in Australia. As part of the AASB's financial reporting framework project it is considering an entity's ability to prepare financial statements in accordance with Australian Accounting Standards.

Having the RCF in place is important so that entities that currently claim compliance with IFRS Standards can continue to do so.

The RCF applies to annual reporting periods beginning on or after 1 January 2020.

The new RCF has an introduction, eight chapters and a glossary.



Five of the chapters are new, or have been revised substantially:

- The reporting entity
- The elements of financial statements
- Recognition and derecognition
- Measurement; and
- Presentation and disclosure.

The RCF is about three times the length of the version it replaces.

Purpose

A practical tool that assists

Board	Preparers	All
to develop Standards	to develop consistent accounting policies	to understand and interpret Standards

Addresses fundamental issues

What is the objective of financial reporting?	What makes financial information useful?	What are assets, liabilities, equity, income and expenses, when should they be recognised and how should they be measured, presented and disclosed?

The RCF sets out the fundamental concepts of financial reporting that guide the IASB in developing IFRS Standards. It helps to ensure that the Standards are conceptually consistent and that similar transactions are treated the same way, providing useful information for investors and others.

The RCF sets out:

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

Why change?

The previous IASB *Conceptual Framework* was issued in 1989 and partly revised in 2010. It was incomplete and needed improvement – in particular:

- it was identified as a priority by stakeholders as part of the 2011 Agenda Consultation
- there were gaps that needed to be filled – for example, guidance on measurement, presentation and disclosure, including guidance on the use of profit/loss and other comprehensive income
- there was a need to update some guidance – for example, the definitions of assets and liabilities
- there was a need to clarify some guidance – for example, the role of measurement uncertainty and the roles of stewardship and prudence in financial reporting.

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

What's changed?

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

Updated	
Definitions	Definitions of an asset and a liability
Recognition	Criteria for including assets and liabilities in financial statements

Clarified			
Prudence	Stewardship	Measurement uncertainty	Substance over form

The RCF is more comprehensive than the old one. However, most of the concepts are not new – it codifies the IASB's thinking adopted in recent standards (for example, IFRS 16 *Leases*).

The granularity of guidance differs. Some chapters only highlight a list of choices for the IASB to apply when setting Accounting Standards – for example, measurement, and presentation and disclosures. Conversely other chapters provide more direction on how the IASB should make those choices – for example, assets and liabilities. The distinction between liabilities and equity has been removed from the RCF. It will be dealt with as a separate project.

The main changes to the RCF's principles have implications for how and when assets and liabilities are recognised and derecognised in the financial statements.

Some concepts are entirely new – for example, the practical ability approach to liabilities. It is unclear what challenges the IASB (and preparers) will encounter as new standards are developed.

Change	Impact and challenges
New 'bundles of rights' approach to assets	A physical object can be 'sliced and diced' from an accounting perspective. For example, in some circumstances a company would book as an asset a *right to use* an aircraft, rather than an aircraft itself. The challenge will be determining to what extent an asset can be split into different rights and the impact on recognition and derecognition.
New 'practical ability' approach for recognising liabilities	The old recognition thresholds are gone – a liability will be recognised if a company has no practical ability to avoid it. This may bring some liabilities on the balance sheet earlier than at present. However, if there is uncertainty over existence and measurement or a low probability of outflows, then this may result in no or delayed recognition in some cases. The challenge will be determining which future actions/costs a company has no 'practical ability' to avoid.
New control-based approach to derecognition	A company will take an asset off balance sheet when it loses control over all or part of it – i.e. the focus is no longer on the transfer of risks and rewards. The challenge will be determining what to do if the company retains some rights after the transfer.

Further details of changes to the RCF may be found in the [IASB Project Summary.]