Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West VIC 8007

via email: standard@aasb.gov.au

17 January 2014

Dear Kevin

Re: IASB Discussion Paper *A Review of the Conceptual Framework for Financial Reporting*

I am enclosing a copy of PricewaterhouseCooopers' response to the International Accounting Standards Board's Discussion Paper *A Review of the Conceptual Framework for Financial Reporting*.

The letter reflects the views of the PricewaterhouseCoopers (PwC) network of firms and as such includes our own comments on the matters raised. PwC refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

I would welcome the opportunity to discuss our firm's views at your convenience. Please contact me on (03) 8603 3868 if you would like to discuss our comments further.

Yours sincerely,

Jan McCahey
Partner, PricewaterhouseCoopers

pwc

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

14 January 2014

Discussion Paper – A Review of the Conceptual Framework for Financial Reporting

We are pleased to respond to the invitation by the IASB to comment on the Discussion Paper, 'A Review of the Conceptual Framework for Financial Reporting' (the 'Discussion Paper'), on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of those member firms that commented on the Discussion Paper.

'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We support the IASB's efforts to revise the Conceptual Framework (the 'Framework'). The Discussion Paper is a positive step forward and begins to analyse some challenging issues. It is not always clear, however, how this analysis will translate into a final Framework. The Discussion Paper includes a number of undefined terms, including 'objectives', 'indicators' and 'principles', and does not always explain how they interact. The IASB should consider the structure of the Framework during the exposure draft phase – for example, some of the detail in the Discussion Paper might be included as the 'basis for conclusions' in the final Framework, and some of the key terms might be defined.

Purpose and status of the Framework

We agree that the primary purpose of the Framework is to assist the IASB in identifying the concepts that will be used in standard setting. The Framework can also be used to help preparers both understand and interpret existing standards and in the rare cases where there is no guidance, but it should not be used to override specific standards. We believe that most circumstances are addressed by existing standards, either explicitly or through analogy, and suggest that this notion is reflected in the guidance for selecting accounting policies in IAS 8.

Some of the IASB's existing standards might be inconsistent with the revised Framework. The IASB should determine whether and how these inconsistencies should be considered as part of the Agenda Consultation process.

The Framework should focus on 'concepts' rather than mandating consistent principles that should be applied to every standard. 'Concepts' are general ideas or notions from which principles might be derived. Principles should be addressed at the standards level.

The different views in the Discussion Paper illustrate that competing objectives are inherent in financial reporting. These arise from the diverse needs of financial statements users. The existence of competing objectives and the implications for standard setting should be acknowledged in the Framework. The IASB should then explain at the standards level when and why one objective was prioritised over another and, as a result, which concepts were applied. Exceptions to the Framework should be clearly identified and explained.

The Discussion Paper does not acknowledge the existence of these competing objectives, and appears to try to fit existing practice or a range of potential outcomes into a single objective. For example, measuring inventory at cost is supported by describing it as 'an asset used in business operations' rather than 'an asset held for sale'. It would be better supported by acknowledging that there are two competing objectives – namely, to reflect the value of the asset at a point in time, and to reflect an entity's performance over a period of time – and that one of these objectives was determined by the IASB to be the more important in these circumstances.

Elements, recognition and derecognition

We support the direction of the Discussion Paper and agree with the proposal that 'probability' be excluded from the definition of assets and liabilities. This clarifies the distinction between the definition, recognition and measurement and should translate into more clarity at the standards level. The revised definition puts greater pressure on identifying the unit of account. The Framework should acknowledge this, and the IASB should be clear at the standards level about what unit of account has been selected and why it has been selected.

We acknowledge the IASB's efforts to provide additional guidance on the definition of assets and liabilities and to address complex practice issues. We are concerned that the Discussion Paper addresses each of these items in isolation and, as a result, does not consider the interaction between different aspects of the Framework. For example, the determination of what conditional obligations meet the definition of a liability will affect the composition of equity. The Discussion Paper does not explicitly address this interaction.

We support further discussion in the Framework of the elements included in all primary financial statements. This recognises that all primary financial statements are equally important to users and helps to 're-balance' the focus between the statement of financial position and other statements.

We support the objectives proposed in the Discussion Paper for recognition and derecognition. We understand why probability could influence a decision based on relevance, faithful representation and the relative costs and benefits of applying a recognition threshold at the standards level. We are concerned, however, that the indicators described in the Discussion Paper do not clearly explain how probability is relevant and how this is different from the measurement objective. We also believe that determining the unit of account and assessing whether the nature of the element has changed should drive the accounting treatment for derecognition.

Conditional liabilities

Limiting liabilities to obligations that are legal, contractual or unconditional excludes useful information about future cash flows. We believe that a liability also exists in connection with some obligations that are conditional on future events that depend on an entity's actions. The definition can be difficult to interpret and apply when obligations are conditional. Both View 2 and View 3 described in the Discussion Paper highlight some of the factors that might be considered to determine whether a liability exists. We do not believe, however, that either of these views enhances the definition of a liability or provides the concepts necessary to develop clear and unambiguous guidance at the standards level.

We acknowledge that it is extremely difficult to encapsulate which conditional liabilities should be recognised in a single definition. The Framework, however, should explain the factors that might be considered to determine whether an obligation meets the definition of a liability. The relative importance of these factors might vary depending on the nature of the obligation and so the final determination should be made at the standards level. This approach should be applied consistently to financial and non-financial liabilities.

Economic compulsion itself is not a 'past event' and does not create a liability. This is because economic compulsion is specific to the entity and does not create an obligation to a party separate from the entity. A conditional or constructive obligation might create economic compulsion, but economic compulsion does not necessarily create an obligation.

Liabilities or equity

We support defining 'equity' as the residual interest. This approach simplifies the distinction between liabilities and equity, and reflects the widely accepted idea that equity represents claims on the assets of an entity after all other claims are settled. However, we believe that difficult decisions will still be needed at the standards level for complex financial instruments.

The proposed 'strict obligation' approach to distinguish between liabilities and equity has merits, because it uses the proposed definition of a liability in the Framework and reflects obligations to transfer resources from the perspective of the entity. This potentially reduces complexity. However, it addresses only one objective, presenting the claims on resources from the perspective of the entity, and might therefore create challenges for complex financial instruments with characteristics of both equity and liabilities. We understand that the idea of reallocating the 'residual' between various 'classes' of equity aims to provide additional information that is not provided by the strict obligation approach. However, we believe that the IASB should first evaluate what information about a particular class of equity claim is important; only then can it properly consider how that information should be communicated in the financial statements.

The IASB should also assess the potential challenges of relying exclusively on the definition of a liability to distinguish between liabilities and equity. This is especially important for complex financial instruments that some believe have characteristics of both liabilities and equity, such as those that include alternative settlement methods or where the entity's equity instruments are used as settlement currency. For example, some believe that reflecting the perspective of the shareholder and classifying equity instruments that are used as currency as liabilities provides more useful information. We believe these challenges will need to be addressed at the standards level, with any departure from the Framework explained clearly. The IASB should however acknowledge the competing objectives in the Framework.

pwc

Measurement

We support a mixed measurement model and a measurement objective that is linked to the qualitative characteristics. We are concerned, however, that the Discussion Paper has too many detailed rules, and we suggest that measurement should be addressed at a higher level. The Framework should focus on broad measurement concepts by describing the nature of inputs to measurement and when those inputs should be updated.

The Framework should also describe how the IASB will address potentially competing measurement objectives at the standards level – for example, whether the measurement should reflect value at a point in time or an entity's performance over a period of time. The IASB might prioritise one competing objective over another at the standards level, require disclosure of a secondary measurement basis or require a different measurement basis for the statement of financial position and the income statement, with the difference recognised in other comprehensive income (OCI). The IASB should explain at the standards level the rationale for selecting one measurement basis over another, or for using two different measurement bases in the primary financial statements.

We agree that the way in which an asset or liability contributes to future cash flows should be a factor in selecting an appropriate measurement basis. However, other factors should also be considered, reflecting the objectives of all of the primary financial statements.

Presentation and disclosure

We support the approach to disclosures and materiality. The Framework should be limited to concepts and should not prescribe a 'model' or 'format'. Judgement should be required to determine the nature and extent of disclosures based on relevance, considering specifically the existing definition of materiality. We also support the ongoing work by the IASB on the Disclosure Initiative. A single standards-level project to address disclosures should help to clarify the objective of disclosures and the link to the qualitative characteristics, particularly relevance and understandability. The concepts articulated in the Framework should guide this project.

We support the IASB's proposal to retain a subtotal for profit or loss. Investors seek relevant performance measures to make economic decisions about providing resources to entities. We believe that the importance that some investors place on profit or loss, or components thereof, leads to the conclusion that all items of income and expenses should be recycled when the reason for initial exclusion no longer applies. Determining when to recycle is complex in some circumstances. The point of recycling should be addressed at the standards level and, where a pragmatic solution or an exception to the Framework is necessary, it should be identified clearly.

We support a restricted notion of what should be recorded in OCI, but we do not believe that the distinction between bridging items, mismatch items and transitory remeasurements described in the Discussion Paper is necessary. All items that are considered for inclusion initially in OCI arise from a decision to measure an element of financial statements differently in the statement of financial position and the income statement, and there is no need to categorise these items.

Other areas

There is no shared understanding among users, preparers and regulators of what prudence means and therefore, the term 'prudence' could be interpreted differently. We do not believe it is appropriate to re-introduce the word 'prudence' into the Framework. However, we do agree with the definition of 'prudence' included in the previous Framework and believe it is consistent with the notion of 'neutrality'. This definition reflects a degree of caution in the exercise of judgements, but does not reflect, for example, recognition of liabilities that do not exist. An explicit reference in the Framework to the need for caution in decision making, together with enhanced guidance in IAS 1, should address some constituents' concerns while preserving the concept of neutrality.

We recognise the importance that some users ascribe to stewardship. We believe that the concept is adequately explained in Chapter 1 of the Framework in the description of the objective of the financial statements, but we support a more explicit reference to the term 'stewardship' within that description.

Our answers to the specific questions in the Discussion Paper provide more detail on the views expressed above and are included in the Appendix.

If you have any questions on this letter, please contact John Hitchins, PwC Global Chief Accountant (+44 207 804 2497) or Tony de Bell (+44 207 213 5336).

Yours faithfully

PricewaterhouseCoopers

PricewaterhouseCoopers

APPENDIX

Section 1 – Introduction

***Question 1** – Paragraphs 1.25–1.33 set out the proposed purpose and status of the Conceptual Framework. The IASB's preliminary views are that:*

(a) the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs; and

(b) in rare cases, in order to meet the overall objective of financial reporting, the IASB may decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. If this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard.

Do you agree with these preliminary views? Why or why not?

We agree that the primary purpose of the Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs. The Framework can also be used to help preparers both understand and interpret existing standards and also in the rare cases where there is no guidance, but it should not be used to override specific standards. We believe that most circumstances are addressed by existing standards, either explicitly or through analogy. For example, IAS 37 and IAS 38 address the accounting for a number of assets and liabilities that are not specifically identified in other standards. The IASB should explain this in the basis for conclusions in the final Framework and consider whether this notion should be reflected in the guidance for selecting accounting policies in IAS 8. IAS 8 should be amended to clarify that paragraph 11(b) of IAS 8 should be applied only in rare circumstances.

Some aspects of the Framework should only be used by preparers to help understand standard-setting decisions and not used for interpretation or to override standards-level guidance. For example, cost benefit decisions and the determination of what should be recorded in OCI should only be made by the IASB. The Framework should be clear about what aspects of the guidance are strictly specific to standard setting.

Conflicts between new standards and the Framework should be identified clearly during the standard-setting process. The revised Framework will allow the IASB to explain standard-setting decisions (for example, distinguishing between an item that is not an asset and an item that is an asset that is not recognised). The Framework should clearly identify competing objectives. The IASB should explain, in the basis for conclusions to individual standards, when one objective is prioritised over another.

Section 2 – Elements of financial statements

***Question 2** – The definitions of an asset and a liability are discussed in paragraphs 2.6–2.16. The IASB proposes the following definitions:*

(a) an asset is a present economic resource controlled by the entity as a result of past events.

(b) a liability is a present obligation of the entity to transfer an economic resource as a result of past events.

(c) an economic resource is a right, or other source of value, that is capable of producing economic benefits.

Do you agree with these definitions? Why or why not? If you do not agree, what changes do you suggest, and why?

We support the direction of the Discussion Paper and the distinction between the definition, recognition and measurement. The proposals enable the IASB to better explain its decisions at the standards level. This should include, for each standard, a clear explanation about when an asset or liability exists, the nature of that asset or liability (including the unit of account), when it should be recognised and derecognised, and how it should be measured.

We agree that 'probability' should be removed from the definition of assets and liabilities. It is not necessary, because the definition addresses whether an asset or liability exists. The approach is complemented by the clarification that an asset (or liability) is the right (or obligation) rather than the related inflow (or outflow) of economic benefits. Existence uncertainty is therefore inherent in the judgement about whether a right or obligation exists. Uncertainty about existence is rare in practice and can be addressed at the standards level.

The definitions of assets and liabilities encompass the following ideas:

- the existence of the resource or obligation;
- the fact that it resulted from a past event; and
- a reference to 'present'.

The reference to 'present' is redundant in this context. It might also be misunderstood when applied at the standards level. For example, does an instrument (such as an option) that is conditional on a future event create a present obligation now, or only when it has been exercised? The Discussion Paper addresses this issue by proposing additional guidance on conditional liabilities. This guidance relies on the notion of identifying the past event and not the concept of 'present'. This reinforces that 'present' is not necessary. See further discussion in our response to Question 6.

We agree with the definition of 'economic resource' and 'control' for the purpose of the Framework. The definition of control encompasses two components – the ability to direct and economic benefits. Both these components are essential to determining whether an entity has control over a resource. The implications of this definition are further developed in the guidance on derecognition, specifically for distinction between principal and agent. These implications should also be addressed as part of the definition of an asset, which is where the concept of control is first considered.

***Question 3** – Whether uncertainty should play any role in the definitions of an asset and a liability, and in the recognition criteria for assets and liabilities, is discussed in paragraphs 2.17–2.36. The IASB's preliminary views are that:*

(a) the definitions of assets and liabilities should not retain the notion that an inflow or outflow is 'expected'. An asset must be capable of producing economic benefits. A liability must be capable of resulting in a transfer of economic resources.

(b) the Conceptual Framework should not set a probability threshold for the rare cases in which it is uncertain whether an asset or a liability exists. If there could be significant uncertainty about whether a particular type of asset or liability exists, the IASB would decide how to deal with that uncertainty when it develops or revises a Standard on that type of asset or liability.

(c) the recognition criteria should not retain the existing reference to probability.

Do you agree? Why or why not? If you do not agree, what do you suggest, and why?

pwc

We agree that uncertainty is not relevant to the definition of an asset or liability or the recognition criteria (see our response to Questions 2 and 8). The discussion about uncertainty has clarified the distinction between the definition, recognition and measurement. However, some of the indicators of when it is relevant to recognise an asset or a liability cannot be distinguished from the concept of outcome uncertainty, as further discussed in our response to Question 8.

Question 4 *– Elements for the statement(s) of profit or loss and OCI (income and expense), statement of cash flows (cash receipts and cash payments) and statement of changes in equity (contributions to equity, distributions of equity and transfers between classes of equity) are briefly discussed in paragraphs 2.37–2.52.*
Do you have any comments on these items? Would it be helpful for the Conceptual Framework to identify them as elements of financial statements?

We support further discussion in the Framework of the elements included in all primary financial statements. This recognises that all primary financial statements are equally important to users, and helps to 're-balance' the focus between the statement of financial position and other statements.

We agree with the list of elements for which definitions will be developed. The IASB should consider removing the distinction in the existing Framework between revenue and gains. The distinctions between revenue and gains, and between expenses and losses, do not require description in the Framework because such components are not accounting elements for the purposes of the Framework. These distinctions are primarily an issue of presentation and offsetting of income and expenses. Presentation and offsetting have already been addressed in the Framework, and specific guidance on how they apply to income and expenses would be better placed in IAS 1.

We support guidance on the distinction between profit or loss and OCI (see our response to Questions 19-21).

Section 3 – Additional guidance to support the asset and liability definitions

Question 5 *– Constructive obligations are discussed in paragraphs 3.39–3.62. The discussion considers the possibility of narrowing the definition of a liability to include only obligations that are enforceable by legal or equivalent means. However, the IASB tentatively favours retaining the existing definition, which encompasses both legal and constructive obligations—and adding more guidance to help distinguish constructive obligations from economic compulsion. The guidance would clarify the matters listed in paragraph 3.50.*
Do you agree with this preliminary view? Why or why not?

We believe that limiting liabilities to obligations that are contractual or unconditional will exclude useful information from the primary financial statements (see our response to Question 6).

Question 6 *– The meaning of 'present' in the definition of a liability is discussed in paragraphs 3.63–3.97. A present obligation arises from past events. An obligation can be viewed as having arisen from past events if the amount of the liability will be determined by reference to benefits* *received, or activities conducted, by the entity before the end of the reporting period. However, it is unclear whether such past events are sufficient to create a present obligation if any requirement to transfer an economic resource remains conditional on the entity's future actions. Three different views on which the IASB could develop guidance for the Conceptual Framework are put forward:*

(a) View 1: a present obligation must have arisen from past events and be strictly unconditional. An entity does not have a present obligation if it could, at least in theory, avoid the transfer through its future actions.

(b) View 2: a present obligation must have arisen from past events and be practically unconditional. An obligation is practically unconditional if the entity does not have the practical ability to avoid the transfer through its future actions.

(c) View 3: a present obligation must have arisen from past events, but may be conditional on the entity's future actions.

The IASB has tentatively rejected View 1. However, it has not reached a preliminary view in favour of View 2 or View 3.

Which of these views (or any other view on when a present obligation comes into existence) do you support? Please give reasons?

Limiting liabilities to obligations that are legal, contractual or unconditional will exclude useful information about future cash flows from the primary financial statements. Users often seek information on liabilities to help predict future cash outflows. Potential cash outflows related to conditional or constructive obligations arising from past events are important to understanding the financial performance and position of an entity.

We agree that a liability exists where a past event creates a contractual or legal obligation to transfer economic benefits that is unconditional or conditional on future events outside the control of the entity. A liability might also exist in connection with some obligations that are conditional on future events that depend on an entity's actions because recognition of such liabilities often provides useful information about the entity's performance or future cash flows. The Discussion Paper considers conditional obligations separately from constructive obligations. The idea of 'conditions' should not be explored in isolation. A constructive obligation is, by definition, conditional because the entity can choose not to fulfil the obligation.

The definition of a liability includes the notion both that an obligation exists and that a past event has occurred. The definition can be difficult to interpret and apply where obligations are conditional. Both View 2 and View 3 described in the Discussion Paper explain some of the factors that might be considered to determine whether a liability exists. We do not believe, however, that either of these views enhances the definition of a liability or provides the concepts necessary to develop clear and unambiguous guidance at the standards level.

View 3 widens the number of obligations that meet the definition of a liability by focusing only on the existence of a past event. It puts pressure on 'ring fencing' the past event and would require significant interpretation at the standard level. It does not provide additional insight into the definition of a liability, and so does not meet the objective of assisting the IASB in setting standards.

We understand that the intention of View 2 is to reflect economic substance by recognising obligations where the remaining condition is not substantive. There are different interpretations of the concept of 'practically unconditional': some interpret it as very close to strictly unconditional, while others focus on how the entity would 'rationally' behave. It would be difficult to consistently apply the concept in standard setting and in practice. We also note that 'practically unconditional' might be confused with economic compulsion, especially where the conditions are linked to the ongoing operations of the entity.

We believe that it is extremely difficult to encapsulate which conditional liabilities should be recognised in a single definition. Instead, the Framework should explain the factors that might be considered to determine whether a liability arises from an obligation conditional on future events that depend on an entity's actions. The following factors, for example, might indicate that an obligation meets the definition of a liability:

- the entity has received a benefit or a resource from another party which implies that resources will be transferred in exchange for that benefit;
- the entity's past practice creates a valid expectation in another party that the entity will transfer a resource; and
- the terms of the arrangement create a valid expectation in another party that the entity has no realistic alternative other than to transfer resources.

The relative importance of these factors might depend on the nature of the obligation and so the final determination should be made at the standards level. We believe, however, that the concepts should apply consistently to financial and non-financial liabilities, and that exceptions should be addressed and explained at the standards level.

Economic compulsion itself is not a 'past event' and does not create a liability. A conditional or constructive obligation might create economic compulsion, but economic compulsion does not necessarily create an obligation. For example, an entity might be economically compelled to pay a non-contractual employee benefit because it has a constructive obligation to the employee arising from past practice and because it has received the service. The entity does not have an obligation to pay the benefit because it is economically compelled to do so.

A liability can only arise from an obligation to transfer resources to a party separate from the entity and not from an obligation to the entity itself. For example, an entity might be economically compelled to maintain manufacturing equipment but it has not created a responsibility to another party. The responsibility to maintain the equipment is driven by a responsibility to the entity itself rather than to another party.

The IASB should also explore some practical challenges not currently addressed in the Discussion Paper:

- How does the unit of account affect whether there has been a past event? For example, a lease with an extension option could be seen as two separate units of account: an obligation for the initial term, and a right of renewal. The past event might only relate to the obligation for the initial term, with the right of renewal being accounted for separately.

- Does the past event consist of receipt of an economic resource or a past activity? The Framework acknowledges that an asset might be consumed immediately. A past activity might be interpreted more widely than where the entity receives an 'asset' (even if that asset is not recognised or measured at nil). For example, the past activity might be operating in a market or jurisdiction where the counterparty is a government or regulator (such as the payment of taxes or levies).

- How does the guidance on conditional liabilities interact with the distinction between liabilities and equity, and is the selected approach consistent with either of the approaches presented in the Discussion Paper? We believe that the definition of a liability should be applied consistently to the identification of liabilities in the context of distinguishing between liabilities and equity.

We have suggested a number of clarifications and further areas for consideration above. We emphasise, however, that the Framework should be limited to concepts, and the application of those concepts should be addressed at a standards level.

***Question 7** – Do you have comments on any of the other guidance proposed in this section to support the asset and liability definitions?*

We have no further comments.

Section 4 – Recognition and derecognition

***Question 8** – Paragraphs 4.1–4.27 discuss recognition criteria. In the IASB's preliminary view, an entity should recognise all its assets and liabilities, unless the IASB decides when developing or revising a particular Standard that an entity need not, or should not, recognise an asset or a liability because:*

(a) recognising the asset (or the liability) would provide users of financial statements with information that is not relevant, or is not sufficiently relevant to justify the cost; or

(b) no measure of the asset (or the liability) would result in a faithful representation of both the asset (or the liability) and the changes in the asset (or the liability), even if all necessary descriptions and explanations are disclosed.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

All assets and liabilities should be recognised unless recognition does not provide relevant information or no measurement would result in a faithful representation. We agree that cost benefit should be considered in this assessment, but not specifically in the recognition criteria. The overarching concept is already included in the Framework and does not need to be mentioned specifically in the recognition section.

The Discussion Paper provides a number of indicators of when it might not be relevant to recognise an asset or liability. 'Relevance' means different things for different elements. For example, the recognition of financial assets, financial liabilities and some other elements provides users with information to help predict future cash flows. Users might look to non-financial assets for information about how the entity is using its resources and its return on capital. These different objectives should be considered to evaluate relevance in the context of recognition, which might necessitate different recognition guidance for different elements. The evaluation of relevance should also consider all the primary financial statements, including the impact on the income statement.

We support the decision not to include a probability-based recognition threshold in the Framework. Outcome uncertainty is best addressed through measurement. A recognition threshold might be applied at a standards level if it is consistent with the recognition concept. The decision to include a threshold in a specific standard should be explained in the basis for conclusions. We understand why probability could influence a decision based on relevance, faithful representation and the relative costs and benefits of applying a recognition threshold at the standards level. This might be articulated in the Framework but the indicators in the Discussion Paper do not clearly explain how probability is relevant for this assessment and how this is different from the measurement objective, as further discussed below.

We support the IASB's efforts to explain how the qualitative characteristics might be applied in the context of recognition. However, we do not believe that indicators are necessary to achieve this, and we have a number of concerns about the proposed indicators:

- It is not clear how the indicators relate to relevance. For example, the indicators about measurement uncertainty seem to focus on faithful representation. Information might not be relevant because there is no measure that is faithfully representative, but uncertainty is not a measure of relevance in its own right.

- We understand why probability could influence a decision on relevance, faithful representation and cost benefit. The reference to low probability, however, might be mistaken for a threshold.

- The indicator about meeting the financial statement objectives is not useful. It can only be applied to internally generated goodwill and does not provide any additional insight into how the qualitative characteristics might be applied in the context of recognition. If the IASB believes that there should be an exception for internally generated goodwill, it should identify the exception specifically at the standards level.

Question 9 *– In the IASB's preliminary view, as set out in paragraphs 4.28–4.51, an entity should derecognise an asset or a liability when it no longer meets the recognition criteria. (This is the control approach described in paragraph 4.36(a)). However, if the entity retains a component of an asset or a liability, the IASB should determine when developing or revising particular Standards how the entity would best portray the changes that resulted from the transaction. Possible approaches include:*
(a) enhanced disclosure;
(b) presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations, to highlight the greater concentration of risk; or
(c) continuing to recognise the original asset or liability and treating the proceeds received or paid for the transfer as a loan received or granted.
Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We agree with the broad objective of the accounting requirements for derecognition. Derecognition should represent faithfully both the resources and obligations remaining after the transaction, and also the changes in the resources and obligations as a result of the transaction. History should not affect how existing circumstances are reflected in the statement of financial position. This is best reflected through the 'control' approach described in the Discussion Paper.

The Discussion Paper presents an alternative approach based on the transfer of risk and rewards. A control approach does not, however, necessarily conflict with the concept of risk and rewards. The concept of exposure to risk and rewards is embedded in the concept of control through the idea of economic benefits (see further discussion in our response to Question 2). This is currently demonstrated by the principles in existing standards. For example, power and benefits both appear in the definition of 'control' in IFRS 10, and the transfer of risk and rewards is an indicator of transfer of control in the proposed standard on revenue recognition. An entity might appear to transfer control of an asset but retain a number of risks and rewards. It is unlikely in these circumstances that the entity has lost control of all of the resources inherent in the asset. This would be inconsistent with the idea that control generally comes with risk and rewards.

The unit of account is important in the context of the control approach. The unit of account, and determining whether the nature of the element has changed, should drive the accounting. If the remaining asset is different, the original asset should be fully derecognised and a new asset recognised. If the asset remaining is the same, the unit of account might be defined at a lower level than the original asset, and the units that are no longer controlled should be derecognised. Derecognition of the portion of the units that are no longer controlled is commonly understood as partial derecognition. This determination should be made at the standards level.

We acknowledge that the evaluation of risk and rewards works well in current practice, especially for complex financial instruments. We believe that this is because in many cases the unit of account does not separately capture different components of risk. A practical solution might be to evaluate the entire asset or liability on the basis of whether or not a significant portion of the risk and rewards has transferred. This would demonstrate whether the entity is likely to retain 'control' over the majority of the resources that comprise the asset, and would not necessarily conflict with the notion of control.

The concept of principal and agent is fundamental to the evaluation of control. We agree with the proposals in the Discussion Paper for applying this concept to derecognition. We also agree that an entity is likely to be acting only as an agent if it has the appearance of control but it is not exposed to risk and rewards.

There is no clear distinction between derecognition, amortisation and impairment. For example, is amortisation of an intangible asset a remeasurement or derecognition of the used portion of an asset, and how is this different from impairment? This should be clarified in the Framework and clearly articulated at the standards level.

Section 5 – Definition of equity and distinction between liabilities and equity instruments

Question 10 *– The definition of equity, the measurement and presentation of different classes of equity, and how to distinguish liabilities from equity instruments are discussed in paragraphs 5.1–5.59. In the IASB's preliminary view:*

(a) the Conceptual Framework should retain the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities.

(b) the Conceptual Framework should state that the IASB should use the definition of a liability to distinguish liabilities from equity instruments. Two consequences of this are:

  (i) obligations to issue equity instruments are not liabilities; and

  (ii) obligations that will arise only on liquidation of the reporting entity are not liabilities (see paragraph 3.89(a)).

(c) an entity should:

(i) at the end of each reporting period update the measure of each class of equity claim. The IASB would determine when developing or revising particular Standards whether that measure would be a direct measure, or an allocation of total equity.
(ii) recognise updates to those measures in the statement of changes in equity as a transfer of wealth between classes of equity claim.
(d) if an entity has issued no equity instruments, it may be appropriate to treat the most subordinated class of instruments as if it were an equity claim, with suitable disclosure. Identifying whether to use such an approach, and if so, when, would still be a decision for the IASB to take in developing or revising particular Standards.
Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We support the direction of the proposal to distinguish between liabilities and equity in the Framework. There remain challenges in this area, and we believe that difficult decisions will still be needed at the standards level for complex financial instruments that have characteristics of both liabilities and equity. We have considered the proposals in light of those challenges. We do not believe, however, that the Discussion Paper adequately acknowledges and analyses those challenges.

We support the proposal to define equity as the residual interest and to use the definition of a liability to distinguish liabilities from equity instruments. Both liabilities and equity represent claims against an entity's assets, and presenting these claims as two separate elements provides useful information. Defining both equity and liabilities independently of each other is likely to result in some items being captured in both definitions and others being captured in neither definition. Equity as the residual interest of the entity simplifies the distinction between liabilities and equity at the conceptual level. This approach is also consistent with the widely accepted idea that equity represents claims on the assets after all other claims are settled.

The IASB's proposed 'strict obligation' approach to distinguish between liabilities and equity has merits because it is consistent with the definition of a liability and reflects obligations to transfer resources from the perspective of the entity. We support the notion of using the definition of a liability to draw the dividing line. We also agree that obligations to issue equity instruments and obligations arising only on liquidation of the reporting entity are not liabilities.

The IASB should however consider the implications of relying only on the definition of a liability. This approach will potentially reduce complexity, but might also create challenges with some complex financial instruments that some believe have characteristics of both equity and liabilities, such as those that include alternative settlement methods or where the entity's equity instruments are used as settlement currency. For example, some believe that reflecting the perspective of the shareholder and classifying equity instruments that are used as currency as liabilities provides more useful information. We believe these challenges will need to be addressed at the standards level, with any departure from the Framework explained clearly.

The IASB however should acknowledge these challenges and others by considering competing objectives in the Framework and how they might be addressed at the standards level. It should determine what information might be decision-useful and who needs that information. The competing objectives that might be addressed include:

- Should the distinction be based on claims against the entity itself or the shareholders of the entity?

- Should the distinction consider whether the holder of an instrument participates in the risks and rewards of the entity or how claims will be settled (liquidity)? This conflict was highlighted in recent discussions about the accounting for written puts.

- Should the distinction consider only the contractual terms of settlement or how the entity intends to settle the claim? This conflict is apparent in current practice.

The IASB should also explicitly acknowledge in the Framework that it is applying an 'entity' approach as opposed to the 'shareholder' approach, and it should explain how other competing objectives will be addressed.

We understand that the idea of reallocating within equity aims to provide additional information that might be lost where the strict obligation approach is applied. The current distinction between primary and secondary equity claim holders and the proposed reallocation between claims might provide this information. However, the distinction between primary and secondary claims and the objective or information need that 're-allocation' is designed to address is not clear. We believe that the IASB should first evaluate what information about a particular class of equity claim is important; only then can it properly consider how that information should be communicated in the financial statements.

We are also concerned that relevance and, in particular, understandability might be impaired where the 're-allocation' approach is applied to standard setting and then in practice. The IASB should further explore the practical limitations of applying this approach, and in particular:

- The examples in the Discussion Paper assist with understanding how re-allocations will be reflected in the statement of changes in equity. However, the examples are too simple to demonstrate the practical implications of the model, and we suggest that the IASB considers more complex situations with multiple and bifurcated instruments that are encountered in practice.

- The Discussion Paper suggests that equity instruments might be remeasured to explain the interaction between different claims. Chapter 6 of the Discussion Paper does not currently address how the measurement objective might be applied to equity and the impact on the statement of changes in equity. Defining the measurement objective would provide more clarity on whether the reallocations will provide relevant information.

The information provided in the financial statements will depend on the nature of the claim and might need to address several competing objectives (for example, by considering more than one measurement basis). We do not believe that measuring all secondary equity claims at fair value necessarily provides useful information about those claims. The IASB should explore more methods to communicate this information. Options might include reallocating all claims based on an allocation of net assets rather than fair value or using disclosure. These decisions should be made and described at a standards level, but the concepts and tools for making these decisions should be made available by the Framework.

We do not agree with the 'exception' in the Framework for when an entity has issued no equity instruments. A decision to treat the most subordinated class of instruments as equity appears to be an exception. The objective of this treatment is not explained and is not clearly linked to a concept. Exceptions should be considered at the standards level only.

Section 6 – Measurement

Question 11 *– How the objective of financial reporting and the qualitative characteristics of useful financial information affect measurement is discussed in paragraphs 6.6–6.35. The IASB's preliminary views are that:*

(a) the objective of measurement is to contribute to the faithful representation of relevant information about:
   (i) the resources of the entity, claims against the entity and changes in resources and claims; and
   (ii) how efficiently and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.

(b) a single measurement basis for all assets and liabilities may not provide the most relevant information for users of financial statements;

(c) when selecting the measurement to use for a particular item, the IASB should consider what information that measurement will produce in both the statement of financial position and the statement(s) of profit or loss and OCI;

(d) the relevance of a particular measurement will depend on how investors, creditors and other lenders are likely to assess how an asset or a liability of that type will contribute to future cash flows. Consequently, the selection of a measurement:
   (i) for a particular asset should depend on how that asset contributes to future cash flows; and
   (ii) for a particular liability should depend on how the entity will settle or fulfil that liability.

(e) the number of different measurements used should be the smallest number necessary to provide relevant information. Unnecessary measurement changes should be avoided and necessary measurement changes should be explained; and

(f) the benefits of a particular measurement to users of financial statements need to be sufficient to justify the cost.

Do you agree with these preliminary views? Why or why not? If you disagree, what alternative approach to deciding how to measure an asset or a liability would you support?

We agree with a measurement objective that is linked to the qualitative characteristics, and that 'relevance' is the most important characteristic. The Framework should specify that 'faithful representation' and the enhancing characteristics are important to selecting the measurement basis. For example, the enhancing characteristics of 'verifiability' and 'timeliness' are important to the 'relevance' of a particular measure. 'Comparability' is relevant to consistency from period to period, but largely depends on how each entity deploys assets or liabilities within its business. We suggest that the detailed analysis about how assets or liabilities affect future cash flows is replaced with a focus on concepts that link to these qualitative characteristics.

We support a mixed measurement model. A single measurement basis, although conceptually sound, does not always provide the most decision-useful information. We acknowledge that this creates complexity. For example, many investors evaluate performance based on a return on capital, which cannot be determined if the statement of financial position and the income statement reflect current values and changes in current values, respectively. This demonstrates that a single measurement basis using current value might not provide the most useful information.

The Framework should describe how the IASB will address potentially competing objectives at the standards level. For example, the selection of a measurement basis might consider:

- *Point in time or performance during the period*: Is the objective of the measure to reflect value at a point in time (value in use or exchange) or an entity's performance over a period of time (cash flows generated directly or indirectly over time)? For example, inventory at current value reflects the amount at which the asset could be converted to cash. This might provide useful information about future cash flows. Inventory at cost, with income recognised on sale, might provide useful information about the entity's performance and its return on capital.

- *Business model or consistency*: Is the objective to reflect how the entity uses the assets and liabilities in its business (which might be more relevant) or to measure similar assets and liabilities in the same way across all entities (which might increase comparability)? For example, measuring all property at fair value might increase comparability across entities, but it might not reflect that some entities only hold property for use in combination with other assets in a way that will not result in direct cash flows.

The consideration of risk might also reveal additional competing objectives. For example, a market-based exit price measure might be more relevant if the objective is to reflect liquidity risk, but not all market fluctuations are relevant to an entity's credit risk position. An entry price or a cost-based measure adjusted for credit impairment might be more relevant to meeting that objective.

The Framework should explain the possible approaches to competing objectives, such as prioritising one competing objective over another, the disclosure of a secondary measurement basis or using a different measurement basis for the statement of financial position and for the income statement with the difference recognised in OCI. The IASB should explain, at the standards level, the rationale for selecting one measurement basis over another or for using two different measurement bases in the primary financial statements.

The competing objectives should capture the impact on all primary financial statements. The Framework should not pre-judge the determination of the most appropriate measure at the standards level based purely on the reporting objective for particular assets and liabilities.

We are concerned that the Discussion Paper has too many detailed rules and that measurement needs to be addressed at a 'higher' level. The Framework should identify the factors to be considered in selecting the measurement basis (discussed further in our response to Question 12). It should not identify the measurements to be used for specific assets or liabilities; this should be a standards-level decision.

We agree that there is merit in limiting the number of measures, as this helps to reduce complexity. However, there is a balance between limiting the number of measures and providing relevant information. Aggregation into three categories of measurement is arbitrary and will not necessarily provide useful information. For example, 'other cash flow-based measurement' is a broad category used to capture all measures that do not fit within the other two categories. There also seems to be overlap between the three categories; in particular, entry price and fair value (that is, market-based measures) are often based on the present value of estimated future cash flows which is implicit in all market prices. It might be more helpful to view the measurement alternatives in terms of two broad categories of current value and historical cost measures (see our response to Question 12).

The objective of measurement specifically refers to cost benefit. Cost benefit should be considered in the selection of a measurement basis; however, this is an overarching concept that does not require specific attention in the measurement section. It should be used by the IASB to explain why a specific measurement basis has been selected at the standards level. We do not agree that costs to preparers increase, and benefits to users decrease, as the subjectivity of the measurement increases. For example, the final result in a binary outcome might be subjective but relatively low cost to estimate. This assertion should be removed from the Framework.

Question 12 *– The IASB's preliminary views set out in Question 11 have implications for the subsequent measurement of assets, as discussed in paragraphs 6.73–6.96. The IASB's preliminary views are that:*

(a) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, cost-based measurements normally provide information that is more relevant and understandable than current market prices.

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

(c) if financial assets have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information.

(d) if an entity charges for the use of assets, the relevance of a particular measure of those assets will depend on the significance of the individual asset to the entity.

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

The Framework should identify the factors to be considered in selecting the measurement basis. It should not provide detailed rules and it should not identify the measurements to be used for specific assets or liabilities; this should be a standards-level decision. We agree that how an asset or liability contributes to future cash flows should be a factor in selecting an appropriate measurement basis. However, other factors might also need to be considered and would largely depend on the objective of each of the primary financial statements, as noted in our response to Question 11.

In addition to considering how the asset or liability is deployed in the business (how it is expected to impact future cash flows), the IASB might consider:

- whether the objective of the measure is to assess performance relating to that asset or liability or the entity over time, rather than the value of a specific asset at a point in time;
- whether one measure better reflects the entity's risk of exposure to significant variability in cash flows when compared with other measures;
- whether changes in fair value (or another current measure) would or can be realised in the ordinary course of business;
- whether cost or proceeds can be determined for the asset or liability;
- the duration of the cash flows (to establish if discounting is appropriate);
- whether there is a disconnect between initial and subsequent cash flows; and
- whether market price changes in the asset or liability have a disproportionate impact on value.

The Framework should require a holistic assessment of the facts and circumstances and these indicators in light of the measurement objective. Each factor is not necessarily determinative on its own.

Both current value and historical cost measures (as suggested in our response to Question 11) could include measures that encompass the concepts above. For example, current value measures could be further refined to distinguish between those that are notional settlement value (undiscounted), expected value (which might reflect variability, and be updated for current circumstances, possibly discounted or undiscounted), and fair value (based on market participant assumptions and discounted).

We also note that many of the assumptions in the Discussion Paper could be challenged. For example:

- *A current exit price is always more relevant for assets that will be sold*: It is not clear why this should be the case. For example, the Discussion Paper suggests that inventory is held for sale, but is more akin to an asset that is used in combination with other assets to generate cash flows that should be measured using a cost-based measure. This is tenuous and could equally be extended to other assets held for sale.

- *A cost-based measurement is more relevant than current market price information for assets that do not generate cash flows directly or are used in combination with other assets*: We wonder whether this refers to the relevance of the business model, in which case it should be described in that way.

- *Cash-flow-based measures are likely the only viable measures for liabilities without stated terms*: We are unclear why this should be the case, since a market-based measure could also be a viable alternative.

Question 13 *– The implications of the IASB's preliminary views for the subsequent measurement of liabilities are discussed in paragraphs 6.97–6.109. The IASB's preliminary views are that:*
(a) cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms.
(b) a cost-based measurement will normally provide the most relevant information about:
(i) liabilities that will be settled according to their terms; and
(ii) contractual obligations for services (performance obligations).
(c) current market prices are likely to provide the most relevant information about liabilities that will be transferred.
Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

See our response to Question 12.

Question 14 *– Paragraph 6.19 states the IASB's preliminary view that for some financial assets and financial liabilities (for example, derivatives), basing measurement on the way in which the asset contributes to future cash flows, or the way in which the liability is settled or fulfilled, may not provide information that is useful when assessing prospects for future cash flows. For example, cost-*

based information about financial assets that are held for collection or financial liabilities that are settled according to their terms may not provide information that is useful when assessing prospects for future cash flows:

(a) if the ultimate cash flows are not closely linked to the original cost;

(b) if, because of significant variability in contractual cash flows, cost-based measurement techniques may not work because they would be unable to simply allocate interest payments over the life of such financial assets or financial liabilities; or

(c) if changes in market factors have a disproportionate effect on the value of the asset or the liability (ie the asset or the liability is highly leveraged).

Do you agree with this preliminary view? Why or why not?

We agree that cost-based information is not useful for derivatives and other similar instruments. However, as described in our response to Question 12, the Framework should not specify a measure for any particular class of asset or liability. The relevant factors used to select an appropriate measure, in light of the measurement objective, should assist in identifying those situations where a cost-based measure would not be appropriate.

Question 15 *– Do you have any further comments on the discussion of measurement in this section?*

Section 5 of the Discussion Paper proposes that some claims on the entity that are classified as equity might be remeasured to facilitate the re-allocation within equity between claim holders. If such claims are to be remeasured, the basis for remeasurement should be addressed by the measurement concepts. The focus on cash flows might be difficult to apply to many instruments that would be classified as equity. See our response to Questions 11 and 12.

Section 7 – Presentation and disclosure

Question 16 *– This section sets out the IASB's preliminary views about the scope and content of presentation and disclosure guidance that should be included in the Conceptual Framework. In developing its preliminary views, the IASB has been influenced by two main factors:*

(a) the primary purpose of the Conceptual Framework, which is to assist the IASB in developing and revising Standards (see Section 1); and

(b) other work that the IASB intends to undertake in the area of disclosure (see paragraphs 7.6–7.8), including:

(i) a research project involving IAS 1, IAS 7 and IAS 8, as well as a review of feedback received on the Financial Statement Presentation project;

(ii) amendments to IAS 1; and

(iii) additional guidance or education material on materiality.

Within this context, do you agree with the IASB's preliminary views about the scope and content of guidance that should be included in the Conceptual Framework on:

(a) presentation in the primary financial statements, including:

(i) what the primary financial statements are;

(ii) the objective of primary financial statements;

(iii) classification and aggregation;

(iv) offsetting; and

(v) the relationship between primary financial statements.

(b) disclosure in the notes to the financial statements, including:
(i) the objective of the notes to the financial statements; and
(ii) the scope of the notes to the financial statements, including the types of information and disclosures that are relevant to meet the objective of the notes to the financial statements, forward-looking information and comparative information.

Why or why not? If you think additional guidance is needed, please specify what additional guidance on presentation and disclosure should be included in the Conceptual Framework.

We agree with the approach to the scope and content of the 'presentation and disclosure' section of the Framework that is proposed in the Discussion Paper. The Framework should include concepts rather than a 'model' or 'format'. Judgement should be used to determine the nature and extent of disclosures based on relevance, considering specifically the existing definition of materiality (see response to Question 17).

We agree with the preliminary views on presentation and disclosure. Specifically, we agree that:

- The objective of the primary financial statements is to provide summarised information in a manner that is useful, and that all primary financial statements have equal importance.
- Appropriate aggregation and classification can enhance effective communication and understandability.
- Offsetting generally does not provide the most useful information.
- The objective of the notes to the financial statements is to support the primary financial statements and provide additional information about the entity, the elements and how efficiently and effectively management have discharged their responsibilities.

We support the ongoing work by the IASB on the Disclosure Initiative. A standards-level project on disclosures should explore how disclosures can be used to achieve the qualitative characteristics of the financial statements with a focus on relevance and understandability. Disclosure requirements should include the objective of the proposed disclosures and should be established on a standard-by-standard basis in accordance with an overall framework. Articulating clear objectives will help management make better judgements on the information to be disclosed and facilitate a better understanding by users.

We support the proposal to exclude forward-looking information that does not provide information about existing conditions. Such forward-looking information could be included in management commentary or other reporting mechanisms.

Question 17 *– Paragraph 7.45 describes the IASB's preliminary view that the concept of materiality is clearly described in the existing Conceptual Framework. Consequently, the IASB does not propose to amend, or add to, the guidance in the Conceptual Framework on materiality. However, the IASB is considering developing additional guidance or education material on materiality outside of the Conceptual Framework project.*
Do you agree with this approach? Why or why not?

We agree that the guidance provided in the existing Framework, along with that in the accounting standards is sufficient; however, additional consultation around the qualitative aspects of materiality and its application to the inherent subjectivity in financial reporting would be helpful.

The concept of materiality is well understood by preparers and auditors, but further dialogue might enhance consistent application and more appreciation of the different perspectives of all stakeholders across territories. There might be a benefit from additional consideration of the qualitative aspects of materiality and application in practice, especially for narrative disclosures.

Any further guidance should be placed in IAS 1 (that is, outside the Framework) and be based on principles, rather than compliance or rules. Practical issues in applying materiality in financial reporting arise from a more 'rule-based' approach, which is used by many preparers in practice. Separate educational material should encourage preparers to apply professional judgement and adopt a less prescriptive approach to materiality.

***Question 18** – The form of disclosure requirements, including the IASB's preliminary view that it should consider the communication principles in paragraph 7.50 when it develops or amends disclosure guidance in IFRSs, is discussed in paragraphs 7.48–7.52.*
Do you agree that communication principles should be part of the Conceptual Framework? Why or why not?
If you agree they should be included, do you agree with the communication principles proposed? Why or why not?

We agree with the communication principles described in the Discussion Paper. However, they appear to duplicate the qualitative characteristics, and it is not clear how these principles and the qualitative characteristics are connected. For example, there are explicit references to understandability and comparability, but there is no clear link to the complete set of qualitative characteristics. These concepts might be better expressed by linking disclosures to the qualitative characteristics, rather than using different principles as the basis for developing disclosures.

Section 8 – Presentation in the statement of comprehensive income—profit or loss and other comprehensive income

***Question 19** – The IASB's preliminary view that the Conceptual Framework should require a total or subtotal for profit or loss is discussed in paragraphs 8.19–8.22.*
Do you agree? Why or why not?
If you do not agree do you think that the IASB should still be able to require a total or subtotal profit or loss when developing or amending Standards?

We support the proposal to retain a subtotal for profit or loss. Investors seek relevant performance measures to make economic decisions about providing resources to entities. Many start with certain important totals or subtotals and adjust those reported amounts to suit their needs. These are the reported measures that often move market prices.

Some have suggested that entities should simply report all results in a disaggregated manner without subtotals, not even for net income. This would allow individual investors to select the components they see as most appropriately conveying their view of performance. We understand this perspective; but the reality is that investors rely upon key measures – such as operating income, income before tax, net income and earnings per share – as a starting point for their analyses of an entity's performance and for comparison purposes. It is not a coincidence that these key measures dominate financial communications with investors. It would not be practical, or desirable, to eliminate them.

We believe that the importance that some investors place on profit or loss, or components thereof, leads to the conclusion that all items of income and expenses should be recycled when the reason for initial exclusion from net income no longer applies. Some others believe that results should be recognised once only, whether in net income or outside it. Items recognised in OCI should not therefore be recycled and 'recognised again' in net income. We disagree with this conclusion, given the importance that some investors and the capital markets place on net income, or components thereof, as a starting point for their analyses.

Determining when to recycle is complex in some circumstances. However, this is not a reason not to recycle. Practical solutions can be achieved at the standards level for recycling specific items where it is relevant to the performance of the entity. This might include practical expedients or exceptions to the Framework for items such as pension remeasurements. If the IASB determines that some items should be permanently excluded from profit or loss for practical reasons, such as cost benefit, those circumstances should be identified and explained as exceptions to the Framework.

Question 20 *– The IASB's preliminary view that the Conceptual Framework should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss, ie recycled, is discussed in paragraphs 8.23–8.26.*
Do you agree? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss? Why or why not?
If you do not agree, how would you address cash flow hedge accounting?

See our response to Question 19.

Question 21 *– In this Discussion Paper, two approaches are explored that describe which items could be included in OCI: a narrow approach (Approach 2A described in paragraphs 8.40–8.78) and a broad approach (Approach 2B described in paragraphs 8.79–8.94).*
Which of these approaches do you support, and why?
If you support a different approach, please describe that approach and explain why you believe it is preferable to the approaches described in this Discussion Paper.

We agree that a profit or loss subtotal should be included, and support the notion that 'all items of income and expense should be recognised in profit or loss unless recognising in OCI enhances the relevance of profit or loss in the period' (as described in both approaches 2A and 2B described in the Discussion Paper). We believe that all items recorded in OCI should be recycled when the reason for initial exclusion from net income no longer applies (see our response to Question 19). This is broadly consistent with approach 2A, but the approach might be developed differently, as discussed below.

We acknowledge the IASB's efforts to develop a principle to determine the items that should be recorded initially in OCI, but we agree with the statement in the Discussion Paper that no single attribute can operationally or meaningfully distinguish between items to be recorded in profit or loss and OCI. However, some of the attributes described and dismissed in the Discussion Paper might be relevant to determining whether an amount should be recorded initially in OCI. Many of the arguments presented against using these attributes point towards difficult judgements. The Framework should be explicit that such judgements should be made by the IASB during the standard-setting process. This will reduce the risk of inconsistent application of the Framework by preparers. 'Non-recurring' and 'non-operating' are not appropriate considerations. IAS 1 provides guidance on the presentation of non-recurring and non-operating items, and the need for further guidance should be considered in the separate research project on IAS 1.

Investors would be better served by minimising the types of excluded items. Only some remeasurements caused by market movements that are not useful for investors to assess entity performance in the current period should be excluded. Standard setters should engage investors to understand their views about information that should be excluded from net income during the standard-setting process.

We support a more restricted notion of what should be recorded in OCI, but we do not believe that the distinction between bridging items, mismatch items and transitory remeasurements made in the Discussion Paper is necessary. All items that are considered for inclusion initially in OCI arise from a decision to measure an element of financial statements differently in the statement of financial position and the income statement, and there is no need to categorise these items.

The 'narrow' approach proposed in the Discussion Paper does not address all the remeasurements that might be considered for inclusion in profit or loss. For example, the analysis does not identify pension remeasurements as a mismatch or a bridging item. The IASB, however, has also concluded that employee benefit obligations should be measured differently on the statement of financial position and in the income statement. This decision was based on the qualitative characteristics, including relevance, which suggests that employee benefit remeasurements should continue to be recorded initially in OCI.

Decisions about measurements should be based on the principles discussed in Chapter 6 of the Discussion Paper. The current proposals in the Discussion Paper for assets and liabilities might not be adequate to address the concept of performance (see our response to Question 11). Where remeasurements do not portray current-year performance or help investors to predict future performance or cash flows, the effect should be eligible for exclusion from profit or loss.

Items initially recorded outside profit or loss should be recycled where the reason for initial exclusion no longer applies. Determining the timing of recycling is complex. Practical solutions can be achieved for recycling some items where it is relevant to the performance of the entity. In some cases, the point of recycling might be a long time from the initial recognition in OCI. The point of recycling should be addressed at the standards level, and exceptions to the Framework should be clearly identified.

Section 9 – Other issues

Question 22 – Chapters 1 and 3 of the existing Conceptual Framework

Paragraphs 9.2–9.22 address the chapters of the existing Conceptual Framework that were published in 2010 and how those chapters treat the concepts of stewardship, reliability and prudence. The IASB will make changes to those chapters if work on the rest of the Conceptual

Framework highlights areas that need clarifying or amending. However, the IASB does not intend to fundamentally reconsider the content of those chapters.
Do you agree with this approach? Please explain your reasons.
If you believe that the IASB should consider changes to those chapters (including how those chapters treat the concepts of stewardship, reliability and prudence), please explain those changes and the reasons for them, and please explain as precisely as possible how they would affect the rest of the Conceptual Framework.

We agree that the qualitative characteristics do not need fundamental reconsideration. The current guidance was subject to due process before it was finalised in 2010. We have provided specific comment below on the areas highlighted in the Discussion Paper.

Stewardship

We recognise the importance that some users ascribe to stewardship. We believe that the concept is adequately explained in Chapter 1 of the Framework in the description of the objective of the financial statements, but we support a more explicit reference to the term 'stewardship' within that description.

Prudence

There is no shared understanding among users, preparers and regulators of what prudence means. Some believe it is caution in making estimates. Others believe that it means a different recognition threshold for assets and liabilities. Others believe that it means 'conservatism'. Including the word in the Framework might result in inconsistent application, and therefore, we do not believe it is appropriate to re-introduce the word 'prudence' into the Framework.

We do, however, agree with the definition of 'prudence' included in the previous Framework. Prudence is including a degree of caution in the exercise of the judgements needed to make estimates under conditions of uncertainty. This definition reflects a degree of caution in the exercise of judgements, but does not reflect, for example, recognition of liabilities that do not exist. We believe that this definition is consistent with the notion of 'neutrality'. An explicit reference in the Framework to the need for caution in decision making, together with enhanced guidance in IAS 1, is likely to address some constituents' concerns while preserving the concept of neutrality.

Caution in making estimates and judgements is sometimes necessary to enhance relevance and faithful representation. Relevant financial information influences the decisions made by users about whether or not they provide resources to the entity, hold them or withdraw them. Natural risk aversion of investors, lenders, creditors and other existing or potential users suggests that any misrepresentation that overstates assets or performance is likely to affect users' decisions more than understatement of assets or performance. Caution is needed in making judgements where uncertainty might result in overstatement of financial position or performance. IAS 1 requires disclosures about significant accounting judgements and sources of estimation uncertainty. These are often the areas in which caution in decision making might enhance relevance.

Reliability

There is no need to replace 'faithful representation' with 'reliability'. Much of the focus for standard setters and preparers of financial information is to represent appropriately the economic substance of balances and transactions. This idea is embedded in the concept of 'faithful representation'.

The term 'reliability' does not intuitively lead to this idea. It is commonly associated with the ideas of 'verifiability' and 'certainty', and perhaps 'auditability'. 'Auditability' is not an appropriate characteristic to consider in the standard-setting process.

Question 23 – Business model

The business model concept is discussed in paragraphs 9.23–9.34. This Discussion Paper does not define the business model concept. However, the IASB's preliminary view is that financial statements can be made more relevant if the IASB considers, when developing or revising particular Standards, how an entity conducts its business activities.
Do you think that the IASB should use the business model concept when it develops or revises particular Standards? Why or why not?
If you agree, in which areas do you think that the business model concept would be helpful?
Should the IASB define 'business model'? Why or why not?
If you think that 'business model' should be defined, how would you define it?

We agree that financial statements can be made more relevant if the IASB considers how an entity conducts its business activities when developing or revising particular standards. The notion of a business model has influenced the guidance in several standards, most recently IFRS 7, IFRS 8, IFRS 9 and IFRS 10. It has been used as a guiding point to determine what is relevant for users of financial information and it should continue to be considered when evaluating relevance in determining recognition and measurement of elements at the standards level. A statement that relevance can be linked to an entity's business activities is sufficient to capture this concept, and so we do not believe that a single definition of 'business model' in the Framework is necessary.

Question 24 – Unit of account

The unit of account is discussed in paragraphs 9.35–9.41. The IASB's preliminary view is that the unit of account will normally be decided when the IASB develops or revises particular Standards and that, in selecting a unit of account, the IASB should consider the qualitative characteristics of useful financial information.
Do you agree? Why or why not?

We agree that the selection of the unit of account should be based on what is most relevant for users and most faithfully represents specific transactions. Defining a unit of account at a conceptual level might not be achievable. The appropriate unit of account depends on the nature of the transaction and should be addressed at the standards level.

The proposals to refine the definitions of assets and liabilities and the objectives of recognition and derecognition emphasise the need for a clear description of the unit of account at the standards level.

We have highlighted some areas of the Framework where the unit of account will significantly affect the outcome of applying the concepts. The Framework should acknowledge this, and the IASB should be clear at the standards level about what unit of account has been selected and why it has been selected.

Question 25 – Going concern

Going concern is discussed in paragraphs 9.42–9.44. The IASB has identified three situations in which the going concern assumption is relevant (when measuring assets and liabilities, when identifying liabilities and when disclosing information about the entity).
Are there any other situations where the going concern assumption might be relevant?

We agree with the description of going concern in the Framework, and we believe that this concept is well understood in practice. However, following the financial crisis, we have seen an increasing number of entities seek to prepare financial statements on a non-going concern basis in compliance with IFRS. The IASB might consider clarifying whether financial statements that are not prepared on a going concern basis can comply with IFRS, provided they apply the concepts in the Framework.

Question 26 – Capital maintenance

Capital maintenance is discussed in paragraphs 9.45–9.54. The IASB plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised Conceptual Framework largely unchanged until such time as a new or revised Standard on accounting for high inflation indicates a need for change.
Do you agree? Why or why not? Please explain your reasons.

We believe that in most cases the IASB considers the financial capital model when setting standards. Capital maintenance within the current Framework appears disconnected from other aspects related to the preparation of financial reporting. The IASB should consider including an explanation of how the concept is considered during standard setting. This explanation might include an explicit statement that it will primarily use the financial capital maintenance concept and that the notion of physical capital maintenance will be used in rare circumstances where it provides more relevant information or faithfully represents a specific set of circumstances.

We agree that the concept of capital maintenance is likely to have limited impact on the current standards and future standard setting. Accounting for inflation is the most relevant topic that is influenced by the concept of capital maintenance. It is sensible to revisit capital maintenance when the accounting for inflation is addressed.