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EXTRACT FOR AASB MEETING

6 June 2014

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans

IASB Discussion Paper DP/2013/1
***A Review of the Conceptual Framework for Financial Reporting*:**
Supplementary Paper to AASB's Submission

As mentioned in paragraph 31 of the Australian Accounting Standards Board's (AASB's) submission dated 11 February 2014 on the abovenamed IASB Discussion Paper (DP), to help IFRS Foundation staff classify the views in that submission, the AASB attaches a supplementary paper setting out its responses to the specific matters for comment in the DP. The attached supplementary paper also makes a number of suggestions that might be of assistance to IFRS Foundation staff in developing Board papers relating to the IASB Exposure Draft (ED) for a revised IASB Conceptual Framework.

These AASB responses to the specific matters for comment in the DP include, in addition to noting the preliminary views/proposals in the DP with which the AASB agrees:

(a) summaries of, or cross-references to, the AASB's serious concerns, and other highly significant concerns, set out in the AASB's submission on the DP, attributed to the pertinent specific matters for comment;

(b) the AASB's concerns with the DP that are not highlighted in the AASB's submission. Those additional concerns are less significant than the concerns expressed in the AASB's submission, and were omitted from the submission in the interests of retaining focus on the more important matters; and

(c) suggestions for clarifying or otherwise improving the conceptual discussion in the DP.

The supplementary paper also includes, on pages 111 – 112, the AASB's comments on some issues raised (explicitly or implicitly) by the DP and that were not the subject of a specific matter for comment.

Some specific issues commented on

In relation to paragraphs (b) and (c) above, some AASB views that were not expressed or fully explored in the AASB's submission and are set out in the attached supplementary paper are that:

(a) 'control' should be excluded from the definition of an asset, and 'past events' should be excluded from the definitions of an asset and a liability (see paragraphs S7 – S8; and S9 – S11 and S14 – S15, respectively, of the attached paper);

(b) in relation to the definition of an 'economic resource' in the DP, all economic resources are rights. Adopting that view could simplify the conceptual guidance on economic resources (see paragraphs S16 – S19 of the attached paper);

(c) the guidance in the DP dealing with executory contracts and other forward contracts lacks conceptual foundation, and a suggestion that the IASB discusses contractual rights and obligations in greater depth in the Exposure Draft developed from the DP (see paragraphs S61 – S64 of the attached paper);

(d) most of the examples in paragraph 4.26 of the DP should be characterised as examples of when, because of uncertainty, it might be infeasible to *faithfully represent* a measure of an asset or a liability. (The DP characterises all of the examples in paragraph 4.26 as examples of when recognition of an asset or a liability might not provide *relevant* information.) The AASB also considers that the ability to faithfully represent a measure of an asset or a liability should (unlike relevance and cost-benefit) be assessed on an entity-specific basis (see paragraphs S68 – S83 of the attached paper and paragraphs A5 – A13 of the attachment thereto);

(e) the IASB should clarify its preliminary view in paragraph 4.25(b) of the DP that an entity need not, or should not, recognise an asset or a liability if (among other things) no measure of that asset or liability would faithfully represent changes in that asset or liability (see paragraphs S84 – S89 of the attached paper);

(f) in the DP's discussion of measurement, inventories seem to be arbitrarily classified as 'held for use' rather than 'held for sale'. In addition, the AASB considers that whether, in concept, an asset should be measured at (historical) cost or a current value should not depend on whether that asset is 'held for use' or 'held for sale'. This is explained in paragraphs S160 – S164 of the attached paper;

(g) in the DP's discussion of measurement, it is confusing for 'other cash-flow-based measurements' to be put on an apparently equal ranking with cost, fair value and other current market prices. This concern is an example of the comment in the AASB's submission on the DP that the DP "inappropriately elevate[s] measurement methods to the status of measurement attributes", and is explained in paragraphs S171 – S176 of the attached paper;

(h) in relation to the presentation of profit or loss and other comprehensive income (including recycling), the examples of 'mismatched remeasurements' discussed in the DP do not provide convincing reasons for recognising particular items of income or expense in OCI and subsequently recycling them into profit or loss (the AASB's reasons for this view are explained in paragraphs S217 – S232 of the attached paper);

(i) stewardship (or accountability) should not be given greater emphasis in the IASB Conceptual Framework's discussion of the objective of general purpose financial reporting. Nevertheless, the AASB's comments include a suggestion that the 'objective' should refer to "making *and evaluating* decisions about providing resources to the entity". Adding those words in italics might make more apparent the link between providing financial information for stewardship/accountability and for meeting the 'resource allocation decisions' objective (a detailed explanation of the AASB's reasons for this view is provided in paragraphs S236 – S253 of the attached paper);

(j) it would be inappropriate to reintroduce 'reliability' to the IASB Conceptual Framework (a detailed explanation of the AASB's reasons for this view is provided in paragraphs S254 – S264 of the attached paper);

(k) 'prudence' should not be reintroduced to the IASB Conceptual Framework (a detailed explanation of the AASB's reasons for this view is provided in paragraphs S265 – S270 of the attached paper); and

(l) the 'business model' concept might be appropriate for financial reporting, but only in particular contexts (see paragraphs S281 – S307 of the attached paper).

We would be pleased to respond to any requests for elaboration of the AASB's comments.

If you have any queries regarding matters in the attached supplementary paper on IASB DP/2013/1, please contact me or Jim Paul (jpaul@aasb.gov.au).

Yours sincerely

Kevin Stevenson
Chairman and CEO

AASB Supplementary Paper on IASB DP/2013/1

The AASB's response to the Specific Matters for Comment on the DP

The paragraphs in this paper are numbered with an 'S' to signify the nature of these comments as a supplement to the AASB's submission (dated 11 February 2014) on IASB DP/2013/1. Where these supplementary comments relate to comments made in the AASB's submission, they are cross-referenced. As mentioned in the covering letter to this supplement, some of the comments below are on matters not commented on in that AASB submission.

[*Paragraphs S1 – S128 omitted from this extract*]

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 of the Discussion Paper. 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?

(a) The objective of measurement

S129 As indicated in paragraph 12 of its submission on the DP, the AASB agrees with the preliminary view relating to the measurement objective in paragraph 6.35(a) of the DP [repeated in Question 11(a)]. The AASB also considers that, consistently with paragraph OB3 of the IASB Conceptual Framework, the measurement objective should be strengthened by stating that a key objective of measurement concepts should be to identify measurement bases or attributes that provide the most useful information for predicting the entity's future cash flows.

S130 As indicated in paragraphs 13 – 14 of its submission on the DP, the AASB considers that:

(a) in addition to specifying the measurement objectives referred to in paragraph S129 above, the Conceptual Framework should include measurement concepts that (if applied at a standards level) would result in measurements possessing the following qualities:

(i) the amounts can meaningfully be added, subtracted and compared; and

(ii) their economic significance, individually and collectively, is capable of being understood; and

(b) to achieve the goals in (a) above and help achieve the measurement objectives referred to in paragraph S129 above, an ideal concept of 'wealth' needs to be identified. The wealth embodied in an entity's assets is their capability to contribute (directly or indirectly) to generating cash inflows to the entity; the reduction in wealth embodied in an entity's liabilities is the reduction they cause in the entity's capability to generate cash inflows.

S131 As indicated in paragraphs 17 – 18 of its submission on the DP, the AASB considers that:

(a) operating capability is the concept of wealth most useful for achieving the objective of financial reporting, including the provision of information useful for predicting the entity's future cash flows (see paragraph S134 below for an elaboration); and

(b) historical cost-based measurements would not achieve the objective (mentioned in paragraph S129 above) that measurements should provide the most useful information for predicting the entity's future cash flows, except when those measurements do not differ materially from current market entry prices.

S132 These comments in paragraphs S129 – S131 above are elaborated on in paragraphs 12 – 19 of the AASB's submission on the DP.

(b) Single measurement basis for all assets and liabilities

S133 As indicated in paragraph 11 of its submission on the DP, the AASB strongly disagrees with the preliminary view in paragraph 6.35(b) of the DP that a single measurement basis for all assets and liabilities may not provide the most relevant information for users of financial statements.

S134 As indicated in paragraphs A18 – A20 of Appendix A to its submission on the DP, the AASB observes that the mixed-measurement requirements in IFRSs presently lack coherence, and considers there is a pressing need for a single conceptual measurement model (based on an explicitly identified ideal concept of wealth) to provide a foundation for developing consistent measurement requirements. As noted in paragraph S131(a) above, the AASB's preferred measurement model adopts an operating capability concept of wealth. As indicated in paragraph 15(b) of the AASB's submission on the DP, an entity's 'operating capability' represents its ability, at any given time, to carry out its activities at the scale determined by its then-existing resources, both monetary and non-monetary. Using an operating capability concept of wealth, the entity's recognised economic resources and present obligations, and recognised changes in those resources and obligations resulting from the entity's operations, are measured in terms of the specific prices currently relating to them, i.e. their current cost. Specifically:

(a) recognised assets are generally measured at the amounts the entity would currently need to pay to acquire them[1]; and

(b) recognised liabilities are generally measured at the current cost of the assets the entity expects to consume in extinguishing those liabilities (e.g. by providing promised goods and services to customers)[2]. In the case of outstanding loans, these amounts would be the present value of loans discounted at a current borrowing rate.

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1 More particularly, recognised assets would be measured at the lower of their current cost and recoverable amount. For assets used in sustainable cash-generating operations, current cost would be lower than recoverable amount. Therefore, current cost would generally be the measurement basis used under an operating capability concept of wealth.

2 More particularly, recognised liabilities would be measured according to their least costly mode of extinguishment, which would be determined as the lowest of: (1) the present value of the resources required to fulfil the obligation; (2) the amount that the entity would have to pay to cancel the obligation; and (3) the amount that the entity would have to pay to transfer the obligation to a third party. For financial liabilities such as loans payable, those three amounts should seldom differ significantly. For those non-financial liabilities in respect of which those three amounts differ significantly, the lowest amount would generally be the fulfilment value referred to in (1) above. The fulfilment value of a non-financial liability (such as a performance obligation or a provision) would incorporate the risk-adjusted estimated cash flows for the entity to fulfil the obligation, reflecting the entity's likely mode of fulfilling the obligation (i.e. using contractors, internal resources or a combination of both). In that sense, the current cost of a liability would be the current cost of the assets the entity expects to consume in extinguishing the liability, or (e.g. in relation to financial liabilities) an amount that does not differ significantly from the current cost of those assets.

S135 As indicated in paragraph 11 of the AASB's submission on the DP, the DP does not explore the possibility that a single measurement basis (or model) could allow for practical standards-level compromises while providing consistent conceptual direction in improving measurement. Appendix C to the AASB's submission on the DP illustrates how the AASB's preferred measurement model (see paragraph S134 above) might be modified for application in IFRSs without radical changes to those Standards at this stage.

S136 These comments in paragraphs S133 – S135 above are elaborated on in paragraphs 11, 15 and A18 – A26 of the AASB's submission on the DP.

(c) Considering what information a measurement would produce in both the statement of financial position and the statement(s) of profit or loss and OCI

S137 The AASB is unsure of the underlying purpose of Question 11(c). The AASB notes that, on the face of it, Question 11(c) rephrases the measurement objective referred to in Question 11(a). Therefore, the AASB questions whether a different question is really being asked in Question 11(c). The AASB's comments in paragraphs S138 – S140 below address the literal wording of Question 11(c) and not any different question. The AASB's comments in paragraphs S141 – S144 below address the question the AASB thinks is possibly, although not literally, being asked in Question 11(c).

S138 In relation to the preliminary view in paragraph 6.35(c) of the DP that, when selecting the measurement [basis] 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, the AASB considers that an ideal concept of wealth would, if applied at a standards level:

(a) result in the provision of useful information for assessing the entity's assets, liabilities, equity, income and expenses—as reported in the statement of financial position and the statement(s) of profit or loss and OCI[3] (this view is consistent with the AASB's agreement with the measurement objective in the preliminary view in paragraph 6.35(a) of the DP, noted in paragraph S129 above); and

(b) identify the measurement basis (bases) that provides the most useful information for predicting the entity's future cash flows. Information useful for this purpose is provided in both the statement of financial position and the statement(s) of profit or loss and OCI.

S139 One of the key benefits of identifying an ideal concept of wealth—which the AASB advocates in paragraph 14 of its submission on the DP—is that the measurement of recognised assets and liabilities (and thus equity) and of changes in recognised assets and liabilities (including income and expenses) would be coherent. This would avoid the concern expressed in paragraph 6.15 of the DP, which

3 In making this comment, the AASB is not expressing a view on whether profit or loss and OCI should be reported separately, or, in particular, reported separately in the manner discussed in Section 8 of the DP. The AASB's comments on those aspects are provided separately in paragraphs S212 – S233 below.

Question 11(c) seems to address, that "Selecting measurements by considering either the statement of financial position alone or the statement(s) of profit or loss and OCI alone will not usually produce the most relevant information for users of financial statements."

S140 The AASB does not rank either the statement of financial position or the statement(s) of profit or loss and OCI as more important than the other. Consistent with this, the AASB considers that adopting operating capability as an ideal concept of wealth and thus generally measuring assets at their current cost (as noted in paragraph S134 above) would yield the benefits of an ideal concept of wealth mentioned in paragraphs S138(a) and S138(b) above in relation to information in both the statement of financial position and the statement(s) of profit or loss and OCI. In that regard, paragraph B128 of Appendix B to the AASB's submission on the DP illustrates the ways in which measuring assets at their current cost would provide useful information to investors and creditors.

S141 Rather than the literal meaning of Question 11(c), to which paragraphs S138 – S140 above respond, the question the AASB thinks is possibly being asked by Question 11(c) is whether either or both of the following propositions is agreed with:

(a) in some circumstances, a particular measurement basis that provides useful information about an asset or a liability (e.g. a current market price) should not be identified as conceptually appropriate because it does not provide useful information in the statement(s) of profit or loss or OCI (e.g. because changes in that current market price would result in excessive volatility in income or expense, whether recognised in profit or loss or in OCI); or

(b) in some circumstances, an entity should "[use] one measure in the statement of financial position and [use] a different measure to determine the amounts recognised in profit or loss (presenting the difference between the two measures in OCI)" [paragraph 6.76(b) of the DP]. The difference between the two measures would be a 'bridging item' recognised in OCI under paragraphs 8.55 – 8.60 of the DP.

S142 An example of where the issue in paragraph S141(a) above potentially arises is the DP's discussion of the subsequent measurement of assets held for use. Regarding assets held for use, paragraph 6.79 of the DP emphasises the relevance (in the IASB's view) of (historical) cost-based measurements in respect of the amounts of income and expenses reported, without explicitly commenting on whether (historical) cost-based measurements are relevant for measuring such assets in the statement of financial position. Paragraph 6.79 of the DP could be construed as indicating that, regardless of how relevant current market prices might be for measuring such assets in the statement of financial position, the greater relevance (in the IASB's view) of historical cost than current market prices to the measurement of income and expenses means historical cost should be adopted as the measurement basis for such assets in both the statement of financial position and the statement(s) of profit or loss and OCI.

S143 An example of where the issue in paragraph S141(b) above potentially arises is, as described in paragraph 8.57 of the DP, where specified debt instruments are measured at fair value in the statement of financial position, but measured at amortised cost to determine the amounts recognised in profit or loss (with the difference being treated as a 'bridging item' recognised in OCI).

S144 The AASB would disagree with the proposition implicit in either of the possible questions in paragraphs S141(a) and S141(b) above. In relation to those paragraphs, the AASB considers that the same measurement basis should be used for an asset or a liability recognised in the statement of financial position and changes in that asset or liability recognised in the statement(s) of profit or loss and OCI. Any implications of remeasurements of assets or liabilities for assessing the entity's financial performance should be dealt with as matters of presentation and disclosure, within a presentation approach to income and expenses that (as advocated in paragraph A48 of the AASB's submission on the ED) is based on a multi-faceted disaggregation of those elements. Thus, the implications of a measurement basis for reporting aspects of financial performance should not, in concept, preclude adopting a relevant measurement basis for the statement of financial position. In addition, as indicated in paragraph A63 of Appendix A to its submission on the DP, the AASB strongly disagrees with adopting the concept of 'bridging items'.

S145 The AASB also considers it is not apparent how the lead-in of paragraph 6.35 of the DP relates to the preliminary view in paragraph 6.35(c). That is, it is not apparent to the AASB how consideration of the objective of financial reporting and the qualitative characteristics led to that preliminary view. The AASB considers there should be a clear articulation of the progression from the objective of financial reporting and the qualitative characteristics to the preliminary view in paragraph 6.35(c) of the DP.

(d) How investors, creditors and other lenders are likely to assess how an asset or liability of that type will contribute to future cash flows

S146 As mentioned in paragraph S129 above, the AASB considers that a key objective of measurement concepts should be to identify the measurement basis (bases) that provides the most useful information for predicting the entity's future cash flows. In that context, the AASB agrees, but only in a very limited sense (see paragraphs S148 – S149 below) with the preliminary view in paragraphs 6.16 and 6.35(d) of the DP, as reproduced in Question 11(d), that:

> "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:
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> (a) for a particular asset should depend on how that asset contributes to future cash flows; and
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> (b) for a particular liability should depend on how the entity will settle or fulfil that liability."

S147 Under the AASB's preferred concept of wealth (operating capability), assets and liabilities are generally measured at current cost (see paragraph S134 above). In relation to the preliminary view quoted in paragraph S146 above:

(a) whilst the current costs of assets do not explicitly measure the cash inflows those assets would generate, those measures are considered by the AASB to be the most useful to users for making predictions of the entity's future cash flows (for an elaboration, see paragraphs 17, B119 and B128 of the AASB's submission on the DP); and

(b) the current costs of liabilities explicitly reflect the cash outflows (or other consumptions of resources) expected to be incurred in extinguishing[4] those liabilities using the least costly mode of extinguishment. Those cash outflows (or other resource consumptions), in turn, reflect *how* the entity expects to extinguish the liability, subject to the constraints mentioned in the footnote to paragraph S134(b) above.

S148 However, the AASB notes that, in illustrating the preliminary view quoted in paragraph S146 above, paragraphs 6.16(a) and 6.16(b) of the DP indicate that "how an asset or a liability … will contribute to the entity's future cash flows" includes whether assets contribute *directly* or *indirectly* to the entity's future cash flows. As indicated in paragraphs 19 and B90 of its submission on the DP, the AASB strongly disagrees with the statements in paragraphs 6.16, 6.78 – 6.80 and 6.83 of the DP that the selection of a measurement for a particular asset should differ according to whether that asset is expected to contribute *directly* or *indirectly* to the generation of future cash flows. This view of the AASB is articulated in more detail in the AASB's comments on parts (a), (b) and (d) of Question 12 on the DP (see paragraphs S156 – S165 below), because views on the pertinence of whether an asset is expected to contribute *directly* or *indirectly* to the entity's future cash flows to the identification of a relevant measure of that asset are explicitly sought in those parts of Question 12.

S149 In addition, the AASB notes that the reason for the preliminary view in paragraph 6.35(d) of the DP that "the selection of a measurement for a particular liability should depend on how the entity will settle or fulfil that liability" is given (in paragraph 6.16(c) of the DP) that "current market prices may not provide the best indication of the ultimate cash outflows arising from the liability"[5]. That reason seems to focus on whether to use current market prices or historical (amortised) cost to measure liabilities. In contrast, although (as indicated in paragraph S147(b) above), the AASB's preferred measurement basis for liabilities (i.e. current cost) reflects how the entity expects to extinguish (settle or fulfil) its liabilities using the least costly mode of extinguishment, reflecting that aspect is pertinent to which current market prices (entry or exit) to use to measure liabilities, and not whether to use current market prices or historical (amortised) cost to measure liabilities. As is indicated in paragraphs 18 and A34 of its submission on

4 This Paper uses 'extinguish' to encompass the terms 'settle or fulfil' used in paragraph 6.35(d) of the DP.

5 Paragraph 6.16(c) of the DP gives an example of current market prices for a non-derivative liability with fixed cash flows varying even though the expected cash flows do not.

the DP, the AASB considers that historical cost (or amortised historical cost) is not in concept a relevant measurement basis for assets or liabilities.

(e) The number of different measurements used

S150 The AASB disagrees with the preliminary view in paragraph 6.35(e) of the DP because it considers that identifying an ideal concept of wealth (see paragraph S130(b) above) should render redundant the question of how many measurement bases might be appropriate. Identifying an ideal concept of wealth would limit the number of measurement bases to very few. Some concepts of wealth (for example, operating capability) can involve more than one measurement basis. Provided the concept of wealth is coherent, it should not matter how many measurement bases its adoption would entail.

S151 Paragraph 6.23 of the DP says the reason for the preliminary view in paragraph 6.35(e) of the DP that: "the number of different measurements used should be the smallest number necessary to provide relevant information" is that: "The more measurements that are used … the harder it is to understand how those measurements interact to depict the entity's financial position and financial performance." The AASB has the following concerns with this reason for the preliminary view (and, therefore, with the preliminary view itself):

(a) it implies understandability is a constraint on the reporting of information that meets the fundamental qualitative characteristics of relevance and faithful representation, although Chapter 3 of the IASB Conceptual Framework makes no such statement (i.e. Chapter 3 of the IASB Conceptual Framework describes understandability as an *enhancing* characteristic);

(b) it implies information is not understandable, or is less understandable, if it is difficult to understand. This implies the enhancing qualitative characteristic of understandability is 'easy to understand', which is a higher threshold than that used in Chapter 3 of the IASB Conceptual Framework. In contrast, the Basis for Conclusions on that Chapter says:

> "understandability … enables users to comprehend the information and therefore make it useful for making decisions."
> (paragraph BC3.40); and
>
> "Classifying understandability as an enhancing qualitative characteristic is intended to indicate that information that is difficult to understand should be presented and explained as clearly as possible." (paragraph BC3.42);

(c) measurements interact best to depict the entity's financial position and financial performance if they reflect an ideal concept of wealth and an ideal concept of economic income (see the comments in paragraphs A29 – A30 in Appendix A to the AASB's submission on the DP). However, the DP does not propose identifying an ideal concept of wealth and an ideal concept of economic income; and

(d) paragraph 4.25 of the DP sets out a preliminary view that, as an exception to the preliminary view in paragraph 4.24 that an entity should recognise all its assets and liabilities, "the *Conceptual Framework* should state that the IASB might decide in developing or revising particular Standards that an entity need not, or should not, recognise an asset or a liability … (b) if no measure of the asset (or the liability) would result in a faithful representation of the asset (or the liability) and of changes in the asset (or the liability), *even if all necessary descriptions and explanations are disclosed*" (emphasis added). The AASB thinks that, for consistency with the implication in paragraph 4.25 of the DP that all necessary descriptions and explanations should be disclosed in order to enable an item to meet the fundamental qualitative characteristic of faithful representation, all necessary descriptions and explanations should be provided before concluding that assets or liabilities measured on a particular basis should not be recognised or disclosed.

S152 Having regard to the concerns in paragraph S150 above, the AASB also considers it is not apparent how the lead-in of paragraph 6.35 of the DP relates to the preliminary view in paragraph 6.35(e). That is, it is not apparent to the AASB how consideration of the objective of financial reporting and the qualitative characteristics led to that preliminary view. The AASB considers there should be a clear articulation of the progression from the objective of financial reporting and the qualitative characteristics to the preliminary view in paragraph 6.35(e) of the DP.

(f) The benefits and costs of a particular measurement

S153 Whilst the AASB agrees with the DP discussing (in paragraphs 6.30 – 6.34) how the cost constraint might be applied when choosing measurement concepts, the AASB disagrees with reiterating the cost constraint as a preliminary view in paragraph 6.35(f) of the DP, given that the cost constraint applies to all financial information by virtue of Chapter 3 of the IASB Conceptual Framework. To be consistent, it would seem logical to state that a particular measurement needs to meet each of the qualitative characteristics of financial information, and to name each of those characteristics—however, the AASB would consider this unnecessary. In addition, explicitly referring to the cost constraint (but not each of the qualitative characteristics) in the preliminary views on measurement might be construed as indicating the IASB considers the cost constraint to be a more important consideration than the qualitative characteristics. The AASB would not support such a message.

S154 The AASB also considers it is not apparent how the lead-in of paragraph 6.35 of the DP relates to the preliminary view in paragraph 6.35(f). That is, it is not apparent to the AASB how consideration of the objective of financial reporting and the qualitative characteristics led to that preliminary view. The AASB considers there should be a clear articulation of the progression from the objective of financial reporting and the qualitative characteristics to the preliminary view in paragraph 6.35(f) of the DP.

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 of the Discussion Paper. 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.

S155 The AASB strongly disagrees with these preliminary views in Question 12. The AASB’s specific response to parts (a) – (d) of the question is set out integrally in paragraphs S156 – S168 below, with grouping of comments in common to some parts of the question.

(a), (b) & (d) How assets contribute to future cash flows

S156 The AASB’s comments in paragraphs S157 – S165 below relate collectively to parts (a), (b) and (d) of Question 12 on the DP.

S157 As indicated in paragraphs 19, A33 and B90 of its submission on the DP, the AASB strongly disagrees with the manner in which paragraphs 6.16, 6.78 – 6.80 and 6.83 of the DP elaborate on the preliminary view in paragraph 6.35(d)(i) of the DP that “the selection of a measurement for a particular asset should depend on how that asset contributes to future cash flows”. Those paragraphs with which the AASB strongly disagrees state that the selection of a measurement for a particular asset should differ according to whether that asset is expected to contribute *directly* or *indirectly* to the generation of future cash flows. In particular, the AASB strongly disagrees with the preliminary views in those paragraphs that:

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

(b) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, (historical) cost-based measurements[6] normally provide information that is more relevant and understandable than current market prices.

S158 As indicated in paragraphs 18 and A34 of its submission on the DP, the AASB considers that, in concept, current values of assets and liabilities would always be more useful than historical cost measurements for meeting the 'resource allocation decision' objective of financial reporting. (Paragraph A36 of the AASB's submission notes examples of findings in academic studies that current values provide more relevant information than historical costs for predicting an entity's future cash flows.) Therefore, the AASB fundamentally disagrees with preliminary views in paragraphs 6.16(b) and 6.79 – 6.80 of the DP that it would provide more relevant information to measure on an historical cost basis assets held to generate cash flows in a particular manner.

S159 These comments in paragraphs S157 – S158 above are elaborated on in paragraphs 19 and B90 – B125 of the AASB's submission on the DP.

Characterisation of inventories as 'held for use'

S160 In addition to the comments in the AASB's submission on the DP referred to in paragraph S159 above, an example of why the AASB considers the preliminary views in paragraphs 6.16, 6.78 – 6.80 and 6.83 of the DP to be conceptually flawed is that inventories seem to be arbitrarily classified as 'held for use' rather than 'held for sale'. This concern is elaborated on in paragraphs S161 – S164 below.

S161 Paragraph 6.80 of the DP says that, although inventories will be sold, they are similar to assets that are used, in that they cannot generate cash flows independently of the other assets of the entity. Paragraph 6.80 asserts (historical) cost-based measurement is more relevant for inventories than for assets that will be sold. Under that argument, inventories would be measured consistently with assets held for use, which paragraph 6.79 of the DP argues should be measured at (historical) cost. One of the arguments in paragraph 6.80 of the DP for (historical) cost-based measurement of inventories is that, unlike with the sale of most commodities or financial instruments, the sale of inventories usually requires the seller to undertake significant activities to locate purchasers [paragraph 6.80(a)]. The AASB rejects that argument because:

(a) differences in the extent of selling activities required for different types of inventory are often a matter of degree, depending on such matters as whether inventory is specialised or generic, the significance of existing customer relationships, and the extent of market competition;

(b) regardless of the amount of selling effort required, the cash inflows from sales of inventories seem to be direct; the need to incur cash outflows in generating those cash inflows does not seem to affect the direct nature of those cash inflows;

[6] As explained in paragraphs B93 – B99 (particularly paragraph B98) of Appendix B to the AASB's submission on the DP, the AASB construes references in the DP to 'cost-based measurements' as meaning historical cost.

(c) in relation to the issue in (b) immediately above, it is unclear whether significant activities to locate purchasers – which are cited in paragraph 6.80(a) of the DP as a reason for (historical) cost-based measurement of inventories – would be considered by the IASB to occur if an entity sells inventories through an agent and:

   (i) the inventories remain controlled by the entity until sold by the agent (i.e. as at the reporting date, the agent has yet to locate purchasers in relation to the entity's own inventories); and

   (ii) the entity pays significant amounts of sales commissions.

   Some might consider that, because the agent – rather than the entity – locates purchasers of the entity's inventories, there are no significant activities yet to be performed by the entity and therefore the inventories should be treated as directly generating cash inflows (i.e. measured consistently with traded commodities, as assets 'held for sale'). Others might consider that, because the entity has yet to incur significant amounts of sales commissions, its inventories should be treated as indirectly generating cash inflows. They would probably consider that paying employees and paying agents in the future to locate purchasers are substantially the same actions, and therefore that inventories should be classified the same way for measurement purposes, regardless of whether they are sold by employees or agents. The AASB considers that this issue illustrates that classifying cash inflows from sales of inventories as 'direct' or 'indirect' according to the amount of selling effort required, and basing the measurement of inventories on that distinction, does not seem to be a robust measurement principle; and

(d) it does not seem to be applied consistently in the DP. That is, paragraph 6.83 of the DP indicates that physical assets, other than inventories, that will be sold should be measured consistently with other assets held for sale, even though their sale might require significant activities to locate purchasers (which, as noted earlier in this paragraph, is an argument used in paragraph 6.80(a) of the DP for not measuring inventories consistently with assets held for sale).

S162 The other reason given in paragraph 6.80 of the DP for (historical) cost-based measurement of inventories is that using current market selling prices could obscure information about the entity's margins on recurring sales of inventories [see paragraph 6.80(b)]. As indicated in paragraphs B93 – B99 of Appendix B to its submission on the DP, the AASB is concerned that the DP appears to treat current market selling price as the only alternative to (historical) cost-based measurements worth considering. As noted in paragraph S134 above, the AASB considers that current cost would generally be the most relevant basis on which to measure assets and liabilities. When inventories are measured at current cost, the concern expressed in paragraph 6.80(b) of the DP about the loss of information about the entity's sales margins should not arise. As indicated in paragraphs 17, B117 – B125 and B128 – B130 of its submission on the DP, the AASB considers that current margins (i.e. the margins between current income and related expenses measured using current input costs) are considerably more relevant for predicting an entity's future margins than are margins based on historical cost measurements of expenses, regardless of whether the assets consumed in generating that income contributed *directly* to the generation of cash inflows by the entity.

S163 The AASB acknowledges that the 'held for use' category of assets discussed in paragraphs 6.79 – 6.82 of the DP includes "assets [that] contribute indirectly to future cash flows by being used in … delivering assets or services that the entity sells" (paragraph 6.78 of the DP). Because inventories are consumed in delivering assets or services to customers, they qualify as 'held for use' assets under that quoted description. However, as a consequence, the distinction between 'held for sale' assets (which paragraph 6.83 of the DP argues should ideally be measured at a current exit price, perhaps after deducting costs to sell) and 'held for use' assets (which, as mentioned in paragraph S161 above, the DP says should be measured at historical cost), seems to lack meaning or substance. Paragraphs 6.78 – 6.85 of the DP seem to imply that the sale of assets generates cash inflows directly but the delivery of assets or services to customers does not, even though the delivery of assets or services is necessary to complete a sale. This seems a very narrow (and, arguably, non-substantive) distinction on which to base significantly different conclusions regarding whether assets should be measured on an historical cost basis or at current market selling prices[7].

S164 The AASB agrees with the implication of paragraphs 6.80 – 6.81 of the DP that, in concept, inventories should not be measured at their current market selling prices. However, this agreement is based on a different reason than those provided in paragraphs 6.80 – 6.81 of the DP. That is, it is based on the AASB's view that an operating capability concept of wealth would be conceptually ideal (and, thus, assets should in concept generally be measured at their current market buying price), and not because of how inventories are classified as either *directly* or *indirectly* contributing to the generation of future cash flows by the entity.

Additional comments on Question 12(d): Assets the use of which the entity charges for

S165 In relation to paragraph 6.94 of the DP, it is unclear to the AASB why the measurement basis considered most relevant in concept for assets held for charging others to use them should depend (in part) on the number of low-value assets composing that category of assets. The AASB acknowledges that, potentially, the greater the number of assets measured using current market prices, the greater the cost of measuring those assets. However, the AASB thinks addressing that cost is a standards-level assessment that should not be considered in identifying the conceptually ideal measurement basis for this category of assets (i.e. 'charge-for-use assets'). Similarly, the AASB notes that holding a large number of low-value assets might cause some of those assets not to warrant being revalued, because such revaluations would be immaterial. Again, the AASB thinks considerations of applying the concept of materiality do not belong in a Conceptual Framework.

7 See the comment in paragraph S162 above regarding the DP appearing to treat current market selling prices as the only alternative to (historical) cost-based measurements worth considering.

(c) Financial assets that have insignificant variability in contractual cash flows and are held for collection

S166 The AASB strongly disagrees with the preliminary view in paragraphs 6.87 – 6.88 of the DP that, 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 about them (as mentioned in the footnote to paragraph S157(b) above, the AASB construes references to 'cost-based measurement' to mean historical cost-based measurement). This strong disagreement arises primarily because, as indicated in paragraph S131(b) above, the AASB considers that, in concept, for any assets or liabilities, (historical) cost-based measurements provide less useful information for investors and creditors than current market prices (particularly current market buying prices).

S167 Paragraphs 6.87 – 6.88 of the DP argue the preliminary view referred to in paragraph S166 above, saying that, for financial assets that have insignificant variability in contractual cash flows and are held for collection, cost-based interest income, along with bad debt expense as estimated by management, is likely to provide relevant information about the effective yield and collectability of those financial assets. However, the AASB considers that measuring such financial assets at current market entry prices would lose none of that information value and would have the advantage of providing current measures of effective yield and collectability.

S168 See also paragraphs S183 – S184 below in the comments on Question 14(b), regarding the significance of the variability of returns to how financial assets would be measured under the AASB's preferred concept of wealth. The AASB's view that current values (specifically, measurement bases that represent operating capability) are, in concept, more relevant than historical cost applies to all assets and liabilities and reflects the AASB's focus on coherent application of its preferred concept of wealth, which is not dependent on whether contractual (or other) cash flows have significant variability.

Question 13

The implications of the IASB's preliminary views for the subsequent measurement of liabilities are discussed in paragraphs 6.97–6.109 of the Discussion Paper. 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.

(a) Liabilities without stated terms

Cash-flow-based measurements

S169 The AASB thinks the revised IASB Conceptual Framework should not include the preliminary view in paragraph 6.99 of the DP that cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms. This is because the AASB considers that:

(a) measurement concepts for all liabilities should, consistent with the comment in paragraph S130(b) above, be based on an identified ideal concept of wealth. Consequently, whether particular liabilities have stated terms should not affect the fundamental measurement concepts for those liabilities; and

(b) 'cash-flow-based measurements' refer to measurement techniques; practical issues regarding a lack of 'stated terms' for some liabilities (and the measurement techniques that should address those practical issues) should be addressed at a standards level only.

S170 In addition, the AASB has the following concerns about the preliminary view referred to in paragraph S169 above and the related discussion in paragraphs 6.51 – 6.54 and 6.110 – 6.130 of the DP. These concerns relate to the general role of 'cash-flow-based measurements' and the application of such measurements to liabilities without stated terms (referred to in paragraph 6.99 of the DP) and contractual liabilities with stated terms but highly uncertain settlement amounts (referred to in paragraph 6.100 of the DP).

General role of 'other cash-flow-based measurements'

S171 The AASB considers the measurement category of 'other cash-flow-based measurements'[8] referred to in paragraph 6.3(b)(iii) of the DP to be potentially confusing when set in contrast to the other categories in paragraph 6.3(b). Putting cash-flow-based measurements on an apparently equal ranking with cost, fair value and other current market prices seems inappropriate because discounted cash flows may be used to estimate fair value (using the 'income approach' in IFRS 13 *Fair Value Measurement*) or other current market prices. It seems important to separate the discussion of measurement bases (such as historical cost, current cost and fair value/current market selling price) from any discussion about measurement techniques or methods (such as discounted cash flows). An example of the lack of clarity of the DP's discussion of cash-flow-based measurements is the discussion of financial assets and financial liabilities in paragraph 6.44 of the DP. The second sentence of paragraph 6.44 of the DP says "amortised cost measurement used for financial assets and financial liabilities could equally well be described as a cash-flow-based measurement …". This concern of the AASB about putting cash-flow-based measurements on an apparently equal ranking with cost, fair value and other current market prices is an example of the comment in paragraph 11 of the AASB's submission on the DP that the DP "inappropriately elevate[s] measurement methods to the status of measurement attributes".

S172 In relation to the concern outlined in paragraph S171 above, the AASB notes that some commentators have criticised the existing IASB Conceptual Framework (paragraph 4.55) for treating 'present value' as a measurement basis [in addition to 'historical cost', 'current cost' and 'realisable (settlement) value']. The AASB notes that giving the above-mentioned category of 'other cash-flow-based measurements' the same ranking as cost, fair value and other current market prices would give rise to the same problem.

S173 Paragraph 6.52 of the DP generally indicates that 'cash-flow-based measurements' are used when neither cost nor a current market price is appropriate or obtainable without excessive cost. However, paragraphs 6.110 – 6.130 of the DP indicate that 'other cash-flow-based measurements' might be determined in different ways (i.e. potentially based on a selection of various factors noted in paragraph 6.112). Because the overall nature of 'other cash-flow-based measurements' is not defined in the DP, the AASB is concerned that the nature of such measurements might not be ascertainable by users of financial statements. The AASB considers it essential that the nature of all measurements of financial statement elements is identifiable by users, and that disclosing the techniques used in a 'cash-flow-based measurement' would not be an adequate substitute for disclosing the nature of that measurement.

S174 The second sentence of paragraph 6.110 of the DP refers to 'custom-designing' cash-flow-based measurements to fit a particular asset or liability, and "creat[ing] new measurements in each new Standard". This raises the spectre of a possible array of new so-called measurement bases or attributes that are:

[8] i.e. cash-flow-based measurements that are neither current market prices nor cost-based (see paragraph 6.51 of the DP).

(a) not underpinned by an explicit concept of wealth or other broad measurement principle; and

(b) limited only by the constraint in paragraph 6.110 of the DP that a 'custom-designed measurement' [basis/attribute] should be understandable and the resulting preliminary view in paragraph 6.35(e) of the DP (as referred to in Question 11(e) above[9]) that "the number of different measurements used should be the smallest number necessary to provide relevant information". The DP does not appear to provide conceptual underpinnings that would assist the IASB to identify relevant 'custom-designed measurements' that are the smallest number necessary.

S175 Paragraph 6.122 of the DP notes differences between cash-flow-based measurements in existing IFRSs. The AASB considers that, without an explicitly stated concept of wealth, it would seem infeasible to remove those inconsistencies without resorting to arbitrary rules.

S176 The second sentence of paragraph 6.127 says: "Entity-specific inputs would be relevant for unique and highly uncertain cash flows …". This statement about using entity-specific inputs (i.e. an 'entity perspective') rather than a 'market perspective' to measure an asset or a liability using a cash-flow-based-measurement seems to focus on the nature of available evidence for the estimated cash-flow-based measurement. The AASB thinks that, instead of being based on the availability of evidence, concepts for measurement bases should be 'objective-based'—e.g. they should reflect a view about whether an 'entity perspective' or a 'market perspective' would provide the most relevant measure of an asset or a liability, regardless of the nature of the available evidence of that measure. This reflects the AASB's view that, consistent with IFRS 13 *Fair Value Measurement*, a best estimate of fair value should be treated as fair value regardless of the nature of the available evidence to support that estimate – in other words, the objective of the estimate, rather than its supportability, should determine the nature of the measurement. To clarify this point, the AASB notes that, in its submission dated 19 July 2006 on the IASB Discussion Paper *Measurement Bases for Financial Accounting – Measurement on Initial Recognition* (November 2005), it disagreed with the proposal in that 2005 DP that an estimate of fair value should be treated as a 'substitute measure' for fair value (and not as 'fair value') in the absence of evidence described in Levels 1 and 2 of the measurement hierarchy proposed in that DP. The AASB is concerned that the above-mentioned comment in paragraph 6.127 of the Conceptual Framework DP, which emphasises the availability of evidence as a criterion for selecting a measurement basis, is more akin to the view in the 2005 DP (that the selection of a measurement basis should not be based only on the objective of the measurement basis) than to the IASB's conclusion, reflected in IFRS 13, that a best estimate of fair value is fair value regardless of limitations on the evidence supporting that estimate[10].

9 See the AASB's comments on that question in paragraphs S150 – S152 above.

10 For the same reason, the AASB disagrees with the words in italics in the following quote from paragraph 6.34 of the DP: "… a highly uncertain estimate will be faithfully represented if it is properly described (for example, *not as a market price but as a highly uncertain estimate of a market price*)".

Using 'other cash-flow-based measurements' for particular liabilities

S177 The general comments in paragraphs S169 – S176 above also apply to the references to using 'cash-flow-based measurements' for particular liabilities in paragraphs 6.99 and 6.100 of the DP. Those references are:

(a) the third and fourth sentences of paragraph 6.99 of the DP indicate that, for liabilities without stated terms, cost-based measurement is not possible, current market prices are likely to be difficult to determine and a cash-flow-based measurement may be the only possible option; and

(b) similarly, paragraph 6.100 of the DP indicates that, for some types of contractual liabilities with stated terms but highly uncertain settlement amounts, cost-based measurement is unlikely to provide relevant information, current market prices may be difficult to determine and a cash-flow-based measurement may provide the most relevant information.

S178 In view of the undefined nature of 'cash-flow-based measurements' in Section 6 of the DP, the nature of the 'cash-flow-based measurements' referred to in paragraphs 6.99 and 6.100 of the DP is unclear. For the reasons in paragraphs S169 – S177 of this paper (and the sentence immediately above), the AASB considers that putting 'cash-flow-based measurements' (measurement techniques) on an apparently equal ranking with measurement bases, and apparently omitting to identify the measurement basis for liabilities without stated terms, is conceptually inappropriate.

(b) Liabilities that will be settled according to their terms, and contractual obligations for services

S179 The AASB disagrees with the preliminary view in paragraphs 6.103 and 6.108 of the DP that an (historical) cost-based measurement will normally provide the most relevant information about liabilities that will be settled according to their stated terms and contractual obligations for services (performance obligations). As indicated in paragraph S131 above, the AASB considers that:

(a) operating capability is the concept of wealth most useful for achieving the objective of financial reporting, including the provision of information useful for predicting the entity's future cash flows; and

(b) historical cost-based measurements would not achieve the objective that measurements should provide the most useful information for predicting the entity's future cash flows, except when those measurements do not differ materially from current market entry prices.

The AASB considers that measurement uncertainties should be disclosed when relevant to users of financial statements, but that those uncertainties do not change the nature of the measurement basis adopted.

S180 Consistent with the AASB view reiterated in paragraph S179 above, the AASB considers that all liabilities should, in concept, be measured at their current cost (see also paragraphs 14 – 18 of the AASB's submission on the DP).

(c) Liabilities that will be transferred

S181 The AASB disagrees with the preliminary view in paragraph 6.107 of the DP that current market prices are likely to provide the most relevant information about liabilities that will be transferred. This is because:

(a) as mentioned in paragraph S162 above, the AASB is concerned that the DP appears to treat current market selling price as the only alternative to (historical) cost-based measurements worth considering. In the context of liabilities, the AASB construes the reference in paragraph 6.107 of the DP to 'current market prices' as referring to the exit prices (i.e. transfer prices) of the liabilities in question;

(b) as indicated in paragraph S180 above, the AASB considers that all liabilities should, in concept, be measured at their current cost (rather than, for example, at their transfer prices: see (a) immediately above); and

(c) the above-mentioned preliminary view in paragraph 6.107 of the DP seems to make the measurement of liabilities "that will be settled by transfer" dependent on management intentions regarding the mode of settlement – the AASB considers instead that measurement bases should reflect an ideal concept of wealth. In addition, the reference in paragraph 6.107 of the DP to liabilities "that *will* be settled by transfer" (emphasis added) seems to presume that entities will know, at the reporting date, the manner in which liabilities will be settled after that date. The AASB observes that this might not be known by the date when the financial statements are authorised for issue, in which case entities would need to predict how the liability will be settled.

S182 The AASB also notes that the rationale for the preliminary view in paragraph 6.107 of the DP that current market prices are likely to provide the most relevant information about liabilities that will be transferred seems inconsistent with the rationale for the preliminary view in paragraph 6.108 of the DP that an (historical) cost-based measurement will normally provide the most relevant information about contractual obligations for services (performance obligations). This is because:

(a) paragraph 6.107 of the DP argues that a current market price (with or without adjustment for transaction costs) is the most relevant measure of a liability that will be settled by transfer because it is an estimate of the cash that will be paid to settle the liability (based on that liability's mode of settlement); but

(b) paragraph 6.108 of the DP argues that an (historical) cost-based measurement will normally provide the most relevant information about performance obligations because of the alleged relevance of margins on historical cost for predicting future margins. However, there is not a direct connection between the historical cost of a performance obligation and the amount of cash that will be paid to settle the performance obligation. Therefore, if the rationale referred to in (a) immediately above were applied to performance obligations, it seems a different preliminary view than that set out in paragraph 6.108 of the DP would be warranted.

Question 14

Paragraph 6.19 of the Discussion Paper 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?

S183 The AASB agrees that (historical) cost-based information about the financial assets and financial liabilities with the features referred to in sub-paragraphs (a) – (c) of Question 14 (e.g. derivatives) [would[11]] not provide information that is useful when assessing prospects for future cash flows. However, the AASB considers that (historical) cost-based measurements of any assets or liabilities would provide less useful information than current values (particularly, as indicated in paragraph S134 above, current costs) for assessing the entity's prospects for future cash flows. This reflects the AASB's focus on coherent application of its preferred concept of wealth (i.e. operating capability), which is not affected by the factors identified in sub-paragraphs (a) – (c) of Question 14.

S184 As indicated in paragraph A17(b) of Appendix A to the AASB's submission on the DP, the AASB observes that the preliminary view that the measurement of financial assets held for collection should significantly depend on the degree of variability of the contractual cash flows (paragraphs 6.19 and 6.89(a) of the DP) contradicts the preliminary view that the measurement of a particular asset should differ according to whether that asset is expected to contribute directly or indirectly to the generation of future cash flows (paragraphs 6.16, 6.78 – 6.80 and 6.83 of the DP) and thus indicates a lack of robustness of the latter preliminary view.

[11] Question 14 uses "may", but the AASB would be more categorical.

S185 Similarly, the AASB observes that the exceptions in paragraph 6.19 of the DP to the preliminary view in paragraph 6.35(d) of the DP that the selection of a measurement for a particular liability (in particular, as noted in paragraph S149 above, the decision whether to measure a liability at historical cost or a current market price) should depend on how the entity will settle or fulfil that liability also indicate a lack of robustness of the latter preliminary view.

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

Measurement of liabilities under the historical cost basis

S186 The AASB notes that the DP does not clarify the meaning of 'cost', and subsequent measurement considerations, in relation to liabilities that are subject to variable or contingent pricing. For example, if a liability subject to variable pricing has previously been recognised, in the IASB's view, would it represent a departure from the historical cost basis to remeasure the liability for changes in the factor(s) that reprice the liability? The AASB recommends addressing this issue in the process of developing an Exposure Draft (ED) of the Measurement chapter of the revised IASB Conceptual Framework.

S187 In addition, the AASB recommends that the ED mentions that a weakness of the historical cost basis is that it does not cater effectively for liabilities specified to be extinguished with non-cash consideration. The value of non-cash consideration the entity is obliged to sacrifice in extinguishing a liability might change between reporting periods. Arguably, the fair value of the non-cash consideration at the time of initially recognising the liability would be treated as the historical cost of the liability and, under the historical cost basis, would not subsequently be remeasured when the fair value of that non-cash consideration changes[12]. However, measuring a liability at an historical value of non-cash consideration:

(a) would not provide relevant information about the burden that the liability represents (and its implications for the entity's future cash flows); and

(b) arguably would not represent faithfully changes in the entity's financial position, because the non-cash consideration has a changing value but is measured as if its value were fixed.

[*Paragraphs S188 – S211 omitted from this extract*]

[12] The liability might be remeasured if it becomes 'onerous'. However, this would be a departure from the strict application of the historical cost concept.

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 of the Discussion Paper.

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?

S212 As indicated in paragraphs 23(a) and 24 of its submission on the DP, the AASB strongly disagrees with the IASB's preliminary view that comprehensive income should necessarily be bifurcated into profit or loss and other comprehensive income (OCI), and that profit or loss (stripped of items presented in OCI) should be treated as providing the primary source of information about an entity's return on its economic resources, because:

(a) the AASB considers it would be conceptually inappropriate to classify continuous variables as if they were discrete. That is, binary classification of economic ('comprehensive') income should not be adopted, given the range of ways in which economic income could (and should) be classified with differentiated implications for predicting the entity's future cash flows;

(b) the notion of OCI is not part of an integrated theory of presentation of financial performance; and

(c) the AASB considers that the DP does not establish a coherent principle for determining when it is more relevant to present an item in OCI rather than in profit or loss. Furthermore, it seems unlikely that such a principle could be developed.

S213 The AASB considers that, rather than adopting a binary classification of economic ('comprehensive') income, the IASB should develop principles for a multi-faceted disaggregation of economic income that facilitate classifying items of economic income (supported by disclosures) according to their different implications for predicting the amount, timing, uncertainty and velocity of future cash flows. In making these predictions, users need information about the volume, direction, pace of change, variability and predictability of changes in the entity's economic resources and claims on the entity's economic resources. In this regard, the distinction between profit or loss and OCI, if made at all, should be a matter of sub-classification of items recognised once (and only once) in the statement of comprehensive income (see the AASB's response to Question 20 below, particularly in paragraphs S215 – S216).

S214 The comments in paragraphs S212 – S213 above are elaborated on in paragraphs 23 – 25 and A44 – A67 of the AASB's submission on the DP.

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 of the Discussion Paper.

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?

General comments

S215 As indicated in paragraphs 23(b) and 26 of its submission on the DP, the AASB:

(a) fundamentally disagrees with 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 recycled to profit or loss in a later period; and

(b) considers that introducing recycling to the Conceptual Framework would represent a significant backward step from the existing Conceptual Framework. This is because the existing Conceptual Framework identifies as elements of financial statements only economic phenomena. Recycling would involve an entity reporting in its financial statements 'events' that are not economic phenomena of the period in which they are reported. It would involve recognising particular economic phenomena (inflows and outflows of economic resources) twice in one component or another of comprehensive income. Recycling items previously recognised in OCI would report as income and expenses in profit or loss items that are not inflows or outflows of economic resources of the period in which they are reported (because those inflows/outflows occurred when they were previously recognised in OCI)[13]. The AASB would regard the weakening of the Conceptual Framework's approach of reporting only economic phenomena affecting an entity as a fundamental flaw.

S216 As indicated in paragraph S213 above, the AASB considers that the distinction between profit or loss and OCI, if made at all, should be a matter of sub-classification of items recognised and presented once (and only once) in the statement of comprehensive income. This view is generally consistent with 'Approach 1' discussed in paragraphs 8.25, 8.27 and 8.29 – 8.31 of the DP.

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13 See the examples in paragraph S220 below.

Mismatched remeasurements (including hedges of forecast transactions)[14]

S217 Although the AASB's submission on the ED commented on the various 'Approaches' to presenting an entity's profit or loss and OCI discussed in Section 8 of the DP, that submission did not comment specifically on 'mismatched remeasurements'[15] (with the exception of commenting in broad terms on hedge accounting: see paragraph S219 below).

S218 The AASB disagrees with the preliminary view in paragraph 8.62 of the DP that, in some cases, an item of income or expense represents a linked set of items so incompletely that recognising that item in profit or loss would provide little relevant information about the return the entity has made on its economic resources during the period and would consequently diminish the understandability and predictive value of the amounts included in profit or loss. The AASB considers that, in concept, rather than excluding an item of income or expense from profit or loss (and including it in OCI) on the grounds of its relationship with an item not recognised during the period, the relationship between that item and the item not recognised during the period should be communicated through note disclosure. (As mentioned in paragraphs A47 – A48 of Appendix A to the AASB's submission on the DP, the AASB would not object to presenting totals for 'profit or loss' and 'OCI' as part of a multi-faceted disaggregation of economic income based on an integrated theory of presentation of financial performance. However, the AASB considers that being a 'mismatched remeasurement' would not be an adequate reason to exclude an item of income or expense from profit or loss.)

Hedges of forecast transactions

S219 The AASB notes that the first example of a 'mismatched remeasurement' given in the DP is a gain/loss on remeasuring a derivative that hedges a forecast transaction. Paragraph 8.63 of the DP notes that, under IFRSs, to the extent that the hedge is effective and qualifies for hedge accounting, the entity reports in OCI the gain/loss on remeasuring the derivative that is determined to be an effective hedge of the 'hedged risk' (as a mismatched remeasurement), and subsequently recycles the gain/loss into profit or loss when the forecast transaction affects profit or loss. However, as mentioned in paragraph A73 of Appendix A to the AASB's submission on the DP, the AASB considers that all forms of hedge accounting should be excluded from the revised IASB Conceptual Framework. The AASB considers that hedge accounting is an accounting response to shortcomings in accounting for economic phenomena (e.g. an accounting mismatch arising from

14 Because the identification and treatment of 'mismatched remeasurements' is not solely related to recycling, the comments in paragraphs S217 – S231 logically belong in the AASB's response to Question 19. However, because cash flow hedge accounting is an example of 'mismatched remeasurements', and Question 20 asks for views on cash flow hedge accounting, the comments in paragraphs S217 – S231 are included in the AASB's response to Question 20.

15 Paragraph A54(c) of Appendix A to the AASB's submission noted that 'mismatched remeasurements' are not commented on in that submission, given the narrow range of items that seem likely to qualify as mismatched remeasurements.

remeasuring one asset or liability but not another[16]) or to hedging an economic exposure that does not relate to a recognised asset or liability (e.g. a hedge of a forecast transaction), and in either case is conceptually inappropriate. This is because:

(a) conceptually, recognised assets and liabilities should be remeasured on a consistent basis and, accordingly, an accounting mismatch should not arise (as indicated in paragraphs S133 – S134 above, the AASB considers that, in concept, all assets and liabilities should be measured under a single current value measurement model that adopts an operating capability concept of wealth); and

(b) hedge accounting, in effect, nets (or offsets) flows of separate economic phenomena (i.e. changes in hedged and hedging items), and thus obscures the effects of the decision to hedge an exposure. This comment (which does not apply to fair value hedges in relation to the gains/losses on hedging instruments, and the gains/losses attributable to the hedged risk of hedged items, recognised simultaneously in profit or loss in accordance with paragraph 6.5.8 of IFRS 9 *Financial Instruments*) is illustrated in the examples of hedges of forecast transactions discussed in paragraph S220 below.

S220 As mentioned at the beginning of paragraph S219 above, paragraph 8.63 of the DP notes that, under IFRSs, for a hedge of a forecast transaction, to the extent that the hedge is effective and qualifies for hedge accounting, the entity reports in OCI the gain/loss on remeasuring the derivative that is determined to be an effective hedge of the 'hedged risk' (as a mismatched remeasurement), and subsequently recycles the gain/loss into profit or loss when the forecast transaction affects profit or loss. Hedges of forecast transactions can, depending on the nature of the transaction, give rise to different accounting treatments under IFRS 9, which involve a different form of netting of economic phenomena. This is explained in (a) and (b) immediately below:

(a) as mentioned in paragraph 8.65 of the DP, recycling would occur in relation to a mismatched remeasurement arising from a hedge of a forecast sale of inventories. For example, if a cumulative loss had been recognised in OCI on the hedging instrument, when the hedged sales occur, that cumulative loss would be reversed in accordance with paragraph 6.5.11(d)(ii) of IFRS 9 by crediting OCI and debiting sales revenue. Thus, the cumulative loss on the hedging instrument arising in periods prior to the sale of the inventories would effectively be netted against the revenue recognised when the inventories are sold. From a disclosure perspective, within comprehensive income, netting does not occur, because the recycling of OCI and the resulting reduction in revenue would be disclosed separately as a

[16] For example, an accounting mismatch would arise if a derivative is measured at fair value through profit or loss under paragraph 4.1.4 or paragraph 4.2.1(a) of IFRS 9 *Financial Instruments* and a loan receivable or payable to which the derivative is related is measured on an amortised cost basis under paragraphs 4.1.1 – 4.1.2 or paragraph 4.2.1 of IFRS 9, even though, economically, both are affected by price changes reflecting changes in economic conditions.

reclassification adjustment under paragraphs 92 – 95 of IAS 1. However, from a recognition perspective, the amounts are effectively netted, inappropriately, because:

(i) the amount of sales revenue (the value of the sales proceeds received or receivable) is reduced by the amount of a different economic phenomenon, i.e. the hedging losses; disclosure of that netting of different economic phenomena does not remedy the fact that sales revenue is understated because the hedging losses (despite having a different character) are embedded within that revenue amount; and

(ii) the hedging losses are recognised in profit or loss when the inventories are sold[17], rather than when they arose (and were initially recognised by remeasuring the hedging instruments). As mentioned in (i) immediately above, the inflow of economic benefits to the entity in the period during which the inventories were sold[18] is the value of the sales proceeds received or receivable. Consequently, the recycling of the cumulative hedging loss from OCI to profit or loss is an accounting entry that does not faithfully represent an economic phenomenon occurring in the period in which the recycling occurs; and

(b) in relation to a hedge of a highly probable forecast purchase of inventories, netting occurs in accordance with paragraph 6.5.11(d)(i) of IFRS 9 when the inventories are initially recognised. If, for example, a cumulative gain was recognised in OCI on remeasuring the hedging instruments before initial recognition of the inventories, this netting occurs in the form of reversing that cumulative gain by debiting OCI and crediting the initial carrying amount of the inventories. This netting reduces the carrying amount of the inventories relative to their spot price when they are initially recognised and, consequently, reduces the amount of expenses recognised in profit or loss when the inventories are sold[19]. The AASB considers these manifestations of netting are conceptually inappropriate because:

(i) the recycling (reversal) of OCI when the inventories are acquired recognises an item of expense (in OCI) although an outflow of economic benefits does not occur when that recycling occurs. At that point, the entity’s wealth remains enhanced to the extent of the cumulative gain on the hedging instruments. However, the financial statements depict the entity as being no better off, because the cumulative amount recognised within comprehensive income has been fully reversed; and

[17] The reversal of the cumulative hedging losses from OCI has the effect that, over time, those losses were not recognised in OCI and were only recognised in profit or loss.

[18] Ignoring the effects of unrelated transactions and other unrelated events.

[19] The recognition principle in IFRSs, noted in the penultimate sentence of paragraph 8.63 of the DP, that gains or losses on the hedging instrument are recycled from OCI into profit or loss when the forecast transaction affects profit or loss, is applied by recognising a reduced expense for ‘cost of inventories sold’ in profit or loss when the inventories are sold.

(ii) effectively netting the cumulative gain on the hedging instrument against the expense recognised in profit or loss when the inventories are sold anticipates part of the 'cost of inventories sold' expense incurred when the inventories are sold, and recognises that expense prematurely as an item of OCI when the inventories were acquired.

The AASB agrees with the following criticism of adjusting the initial carrying amounts of assets or liabilities for the amount of related hedging gains or losses, made by the Financial Instruments Joint Working Group of Standard Setters:

> "Adjusting the recorded amount of a transaction by the amount of a gain or loss on a hedging instrument results in not recording the transaction at the fair value of the consideration given or received. To … 'basis adjust' the amount actually paid for the hedged asset, or received for assuming the hedged liability, has the effect of measuring that asset or liability as if it had been acquired or issued when the hedging instrument was acquired, rather than when the hedged transaction actually took place."[20]

S221 The AASB considers that, conceptually:

(a) remeasuring recognised assets and liabilities on a consistent basis (with full remeasurement of each asset and liability) would faithfully represent the economic events affecting those assets and liabilities each period; and

(b) instead of applying hedge accounting, an entity should disclose by way of note the relationships between items, including relationships between unrecognised and recognised elements.

Other potential examples of mismatched remeasurements identified in the DP

S222 Paragraphs S225 – S231 below discuss potential examples of mismatched remeasurements identified in the DP, other than hedges of forecast transactions (which are discussed in paragraphs S219 – S221 above).

S223 As indicated in paragraphs S212 and S215 above, the AASB strongly disagrees with the preliminary view in paragraph 8.22 of the DP that comprehensive income should necessarily be bifurcated into profit or loss and OCI[21], and fundamentally disagrees with the preliminary view in paragraph 8.26 of the DP that the Conceptual Framework should permit or require items of income and expense previously recognised in OCI to be recycled to profit or loss in a later period. In the context of the AASB's fundamental disagreement with recycling items of OCI into profit or loss, paragraphs S225 – S231 below note the AASB's concerns about the logic of

[20] Financial Instruments Joint Working Group of Standard Setters, *Accounting for Financial Instruments and Similar Items – an Invitation to Comment on the JWG Draft Standard*, December 2000, paragraph 7.11(c).

[21] That is, with profit or loss (stripped of items presented in OCI) treated as providing the primary source of information about an entity's return on its economic resources.

applying the notion of mismatched remeasurements to those potential examples, and about potentially applying that logic to other items of income or expense.

S224 However, given that the AASB disagrees with the fundamental premises upon which the notion of mismatched remeasurements in the DP is based, paragraphs S225 – S231 below do not evaluate whether the items described in the DP as potentially being treated as mismatched remeasurements should be identified as such if that notion were to be incorporated into the revised IASB Conceptual Framework.

Investments in foreign operations

S225 The AASB notes that an example of a 'mismatched remeasurement', given in paragraph 8.64 of the DP, is an exchange gain/loss "resulting when an entity translates an investment in a foreign operation into its presentation currency"[22]. Paragraphs 8.64 and 8.66 of the DP argue that such an exchange gain/loss would be a mismatched remeasurement that should initially be recognised in OCI and then recycled into profit or loss on disposal of the operation because:

(a) the exchange gain/loss does not capture the effect of the change in exchange rates on:

(i) the value of unrecognised assets, particularly goodwill and intangible assets, and therefore provides an incomplete depiction of how the change in exchange rates affected the value of the entity's investment in a foreign operation; and

(ii) the value, expressed in the foreign currency, of non-monetary assets or liabilities that are measured using a (historical) cost-based measurement; and

(b) the cumulative amount of exchange gains/losses at the date of disposal provides relevant information about the cumulative impact of the entity's exposure to foreign currency arising from its foreign activities.

S226 The DP's rationale referred to in paragraph S225(a)(i) above seems similar, in substance, to arguing that changes in the assets and liabilities of a subsidiary should, in consolidated financial statements, be accounted for in a manner that tracks changes in the value of the parent entity's investment in that subsidiary. The AASB disagrees with that argument because the AASB considers that, in concept, the accounting for a particular reporting entity (e.g. the economic entity comprising a

[22] The AASB assumes this quote refers to a more specifically described item in paragraph 32 of IAS 21 *The Effects of Changes in Foreign Exchange Rates*, namely, exchange differences arising on a *monetary item that forms part of* a reporting entity's net investment in a foreign operation. Paragraph 32 of IAS 21 requires such exchange differences to initially be recognised in OCI in the consolidated financial statements of the group reporting entity that includes the foreign operation, and subsequently to be recycled to profit or loss on disposal of the net investment. That is, the AASB assumes paragraph 8.64 refers to characterising such an item of OCI as a 'mismatched remeasurement'.

parent and its subsidiaries) should not be influenced by changes in the value of an investment in an entity within that reporting entity.

S227 The AASB disagrees with the DP's rationale referred to in paragraph S225(a)(ii) above, because the translation of monetary items (on which exchange differences are recognised) and non-monetary items under IAS 21 *The Effects of Changes in Foreign Exchange Rates* is separate and fundamentally different, whereas the DP's rationale referred to in paragraph S225(b) above implies they should be linked. Applying the DP's rationale could imply treating all other exchange differences on monetary items as items of OCI, in conflict with paragraph 28 of IAS 21, which the AASB would not support. In addition, in respect of that rationale, even if non-monetary items forming part of an entity's net investment in a foreign operation were revalued, such a revaluation would not be recognised in profit or loss (nor would the exchange rate change embedded in the revaluation increase/decrease be accounted for separately as an exchange difference). Thus, the AASB perceives the real reason for recognising in OCI exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation is that it results in a form of 'matching', which the AASB regards as an inadequate conceptual reason for OCI classification.

S228 The AASB observes that the argument in paragraph 8.66 of the DP repeated in paragraph S225(b) above seems to be circular and therefore does not seem to add anything to the IASB's reasons referred to in paragraph S225(a) above. In other words:

(a) the AASB thinks the real issue in relation to that argument is why profit or loss should only include the *cumulative* impact of the entity's exposure to foreign currency arising from its foreign activities (when the foreign operation is disposed of) and not each period's impact of that foreign currency exposure; and

(b) the issue referred to in (a) immediately above is addressed implicitly by the IASB's reasons referred to in paragraph S225(a) above and commented on in paragraphs S226 – S227 above.

<u>Changes in financial liabilities designated at fair value through profit or loss</u>

S229 The AASB notes that Table 8.2 on page 169 of the DP indicates that changes in financial liabilities designated at fair value through profit or loss, when attributable to a change in the issuer's own credit risk, could be a mismatched remeasurement that should initially be recognised in OCI and then recycled into profit or loss if the liability is transferred prior to maturity. The reason for initially recognising in OCI changes in particular financial liabilities attributable to changes in the issuer's own credit risk, given in Table 8.2 of the DP, is that:

(a) there is an inverse relationship between an entity's own credit risk and the value of the entity's goodwill; but

(b) the effect on the value of goodwill is not recognised because internally generated goodwill is not recognised.

S230 In relation to the argument noted in paragraph S229 above [and the rationale in paragraph S225(a)(i) above], the AASB is concerned that initially recognising items of income or expense in OCI (as 'mismatched remeasurements') when they arise because they relate to unrecognised internally generated goodwill, and then recycling them into profit or loss if the liability is transferred prior to maturity, would inappropriately:

(a) incorporate a standards-level assumption in the revised IASB Conceptual Framework (i.e. an assumption that a nexus exists between a gain or loss recognised during the period and a change in the value of internally generated goodwill). For example, the DP's argument noted in paragraph S229(a) above seems to disregard the possibility that a deterioration of the entity's own credit risk would be expected by investors to ultimately result in lenders and other creditors accepting partial settlement of amounts the entity owes them, and therefore would not necessarily give rise to a commensurate reduction in the entity's internally generated goodwill; and

(b) set a precedent for classifying a range of expenses (such as salaries of marketing staff and advertising costs) as items of OCI on the basis that they relate to enhancing the entity's unrecognised internally generated goodwill. In other words, basing a classification of an item of income or expense on an omission to recognise corresponding purported effects on internally generated goodwill would not be a robust concept, because applying that rationale to other transactions and events would result in classifications that would be inappropriate and presumably were not intended by the IASB.

S231 For the reasons outlined in paragraphs S217 – S230 above, the AASB considers that the potential examples of 'mismatched remeasurements' identified in the DP do not provide convincing reasons to recognise particular items of income and expense in OCI and subsequently recycle them to profit or loss.

S232 The comments in paragraphs S215, S216 and S219 above are elaborated on in paragraphs 23, 26, A44 and A68 – A74 of the AASB's submission on the DP.

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 of the Discussion Paper) and a broad approach (Approach 2B described in paragraphs 8.79–8.94 of the Discussion Paper).

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.

S233 For the reasons set out in paragraphs S215 – S216 above, the AASB fundamentally disagrees with both of 'Approaches' 2A and 2B to OCI, and considers that, of the three ‘Approaches’ to profit or loss and recycling discussed in Section 8 of the DP, ‘Approach 1’ is the only conceptually appropriate approach.

[*Paragraphs S234 – S316 omitted from this extract*]

Section 9—Other issues

Question 26

Capital maintenance

Capital maintenance is discussed in paragraphs 9.45–9.54 of the Discussion Paper. 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.

S317 As indicated in paragraph B142 of Appendix B to its submission on the DP, the AASB strongly disagrees with the preliminary view in paragraph 9.49 of the DP that the topic of capital maintenance should be addressed at a standards level in the context of accounting for high inflation. This is because the AASB considers that:

(a) concepts of capital maintenance are important regardless of the type of economic environment in which the reporting entity operates (i.e. whether highly inflationary or otherwise);

(b) every measurement basis adopted for the various elements in a set of financial statements, and the treatment of any changes in the carrying amounts of those elements, implicitly reflects concepts of capital and capital maintenance. The AASB thinks it is preferable to have explicit coherent concepts of wealth and changes in wealth (‘capital’ and ‘capital maintenance’) than implicit and potentially conflicting concepts for those matters; and

(c) for the reasons in (a) and (b) immediately above, the issue is so pervasive that it should be addressed in the Conceptual Framework rather than a standards-level project.

S318 As indicated in paragraph B146 of Appendix B to the AASB’s submission on the DP, the AASB’s concerns in paragraph S317 above are not allayed by the proposal in paragraph 9.50 of the DP to retain the existing Conceptual Framework’s discussion of concepts of capital maintenance largely unchanged until any project on accounting for high inflation indicates a need for change. This is because the discussion of concepts of capital maintenance in the existing Conceptual Framework is descriptive and does not indicate which concept of capital maintenance is conceptually ideal.

S319 These comments in paragraphs S317 – S318 above are elaborated on in paragraphs B142 – B148 of the AASB's submission on the DP.

[*Paragraphs S320 – S326 and A1 – A13 omitted from this extract*]