



European Financial Reporting Advisory Group

**ED/2015/3 Conceptual Framework for Financial Reporting**

**Feedback to constituents – EFRAG Comment Letter**

**February 2016**

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## Introduction

### Objective of this feedback statement

This feedback statement summarises the main comments received by EFRAG on its Document for Public Consultation in response to the IASB’s Exposure Draft ED/2015/3 *Conceptual Framework for Financial Reporting* (the ‘ED’) and explains how those comments were considered by EFRAG in its discussions on its final comment letter.

### Background to the Exposure Draft

Following its Agenda Consultation 2011, the IASB decided to restart its work on the Conceptual Framework and published a Discussion Paper on 18 June 2013. The aim of the Discussion Paper was to obtain initial views and comments on important issues that the IASB would consider as it developed an Exposure Draft of a revised Conceptual Framework.

After considering the comments received in response to the Discussion Paper, the IASB published the ED on 29 May 2015. The ED included proposals for the Conceptual Framework on:

- The objective of general purpose financial reporting;
- Qualitative characteristics of useful financial information;
- Financial statements and the reporting entity;
- The elements of financial statements;
- Recognition and derecognition;
- Measurement;
- Presentation and disclosure; and
- Concepts of capital and capital maintenance.

### EFRAG’s Document for Public Consultation

EFRAG published a document for public consultation on the proposals on 8 July 2015. On 8 November 2015 EFRAG updated the Document for Public Consultation to include its preliminary views. The Document for Public Consultation welcomed that the IASB had initiated a project on improving the IASB Conceptual Framework. EFRAG was, however,

concerned that the Conceptual Framework as developed in the ED would not provide the clarity that is deemed necessary. Particularly, EFRAG did not think that the ED provided the expected guidance on how to select a measurement basis and for the reporting of performance, including what should be reported in profit or loss and when.

The Document for Public Consultation supported the proposal in the ED to give more prominence to the objective of stewardship and the re-introduction of prudence. EFRAG was, nevertheless, of the view that more needed to be done in those areas.

EFRAG disagreed with the ED that measurement uncertainty should be dealt with as part of relevance, and thought that the term ‘reliability’ should be re-introduced and replace ‘faithful representation’.

### Comments received from constituents

28 comment letters were received from constituents and considered by EFRAG in its discussions. These comment letters are available on the EFRAG website.

EFRAG received comment letters from the following:

<b>Table 1: Total respondents by type</b>	
Associations of financial statements users	3
Auditors and associations of accountants	3
Enforcers and authorities	1
Individuals	1
National Standard Setters	9
Preparers and preparer organisations	11
	<b>28</b>

The respondents to EFRAG’s draft comment letter are listed in the appendix.

## Outreach events

From July to November 2015, EFRAG and National Standard Setters held outreach events, in coordination with the IASB staff and interested organisations.

The following table shows the locations where the outreach activities were conducted:

**Table 2: Outreach event locations and dates**

Europe (Brussels) User event	1 July 2015
France (Paris)	14 September 2015
Norway (Oslo)	16 September 2015
Spain (Madrid)	21 September 2015
The Baltic states (Vilnius)	23 September 2015
Europe (Brussels)	23 September 2015
Poland (Warsaw)	30 September 2015
The Netherlands (Amsterdam)	5 October 2015
Finland (Helsinki)	14 October 2015
Italy (Milan) User event	22 October 2015
Italy (Rome)	30 November 2015

At the outreach events, selected issues from the ED were presented, followed by a presentation of EFRAG's Document for Public Consultation. The aim of the events was to:

- Stimulate the Conceptual Framework debate within Europe;
- Obtain the views of constituents who may otherwise not submit a comment letter; and
- Learn whether the preliminary position set out in EFRAG's draft comment letter were shared by European constituents.

Separate feedback statements from each of the outreach events can be found on the [EFRAG website](#).

In addition to the events listed in the table above, EFRAG was also represented at the following events on the Conceptual Framework:

- An event organised by the Financial Reporting Council (FRC) and the ICAEW Financial Reporting Faculty on 3 September 2015 in London.
- An event organised by the Accounting Standards Committee of Germany, the Austrian Financial Reporting and Accounting Committee (AFRAC) and the Swiss GAAP FER Foundation on 14 September 2015 in Frankfurt.

When this feedback statement refers to views of constituents, it refers to the 27 comment letters received and to comments reflected in the feedback statements from the outreach events.

## EFRAG's comment letter

EFRAG published its comment letter on the ED on 23 December 2015.

The main differences between the Document for Public Consultation and the comment letter are explained in the following paragraphs.

- The comment letter included additional information on what information the assessment of management's stewardship would require. Several constituents expressed uncertainty about this the implications of including the objective of assessing management's stewardship in the Conceptual Framework, and EFRAG accordingly decided to provide its view on the issue.
- EFRAG's Document for Public Consultation presented the view that where preparers tend to converge and oppose to some IASB proposals because, in their view, the outcome would not be a meaningful depiction of the entities' financial position and/or performance, the IASB should, if it would confirm its preliminary decisions, explain how and why meaningful information will be provided. Some constituents thought that this indicated that EFRAG considered the views of preparers more important than the views of, for example, accountants. This was not the intention of EFRAG. EFRAG accordingly replaced the wording by stating that if preparers consider that the information resulting from a

Standard is useful for them, it could indicate that information resulting from a Standard is useful for users.

- In relation to prudence, EFRAG noted that some constituents thought that prudence would eliminate the use of fair value. EFRAG accordingly decided to state in its comment letter that prudence should not stop the use of fair value measurement in appropriate circumstances or the recognition of fair value gains in financial statements.
- In its document for public consultation, EFRAG argued that the term 'reliability' should be reintroduced and replace the term 'faithful representation'. Constituents had mixed views on this issue. While EFRAG acknowledged that there were good arguments for replacing 'faithful representation' with 'reliability', it decided not to suggest this in its comment letter. EFRAG thought that the main issue would be the content of the term rather than the name of it. EFRAG thought that no matter whether the term 'reliability' or 'faithful representation' would be used, it should include measurement uncertainty.
- In its document for public consultation, EFRAG had suggested guidance on when it would be useful to recognise executory contracts and when it would not. Some constituents did not agree with this guidance. EFRAG therefore decided not to include the suggestion in its comment letter. Instead EFRAG asked the IASB to develop such guidance.
- On the unit of account, EFRAG decided to reflect a comment from some of its constituents that the unit of account should be established in conjunction with developing recognition and measurement guidance for that unit of account – not after as the ED could suggest.
- In its document for public consultation, EFRAG broadly agreed with the principles on recognition suggested in the ED. Based on the comments from constituents, EFRAG assessed, and stated in its comment letter, that the guidance proposed would be insufficient to ensure consistent standard setting. EFRAG's comment letter also clarified that EFRAG did not support the inclusion of a probability recognition threshold in the revised

Conceptual Framework. However, EFRAG considered that the Conceptual Framework could acknowledge that such a threshold would be useful in particular Standards.

- Similar to its comments on recognition, EFRAG also assessed, based on the comments from constituents, that it was uncertain whether the guidance proposed would be sufficient to ensure consistent standard-setting in the future.
- Based on the comments on its Document for Public Consultation, EFRAG assessed that the categorisation of measurement bases as either historical cost measurements or current value measurements might not always be straightforward and asked in its comment letter for some more discussion on this in the Conceptual Framework.
- Together with its document for public consultation, EFRAG issued the Bulletin *Profit or loss versus OCI* for consultation. The Bulletin outlined how a distinction could be made between profit or loss and OCI based on the business model. The responses to the Bulletin were mixed. Most constituents thought that the business model had an important role to play when distinguishing between profit or loss and OCI, but other factors should also be considered. EFRAG decided to reflect this view in its comment letter. EFRAG did therefore not include any suggestions on how to distinguish between profit or loss and OCI in its comment letter.
- Some constituents did not think the statement of cash flows was given sufficient prominence in the ED. EFRAG agreed and reflected that view in its comment letter.
- EFRAG also agreed with constituents who thought that more guidance on when note disclosures should be provided should be included in the Conceptual Framework.

## Chapters 1 and 2 - The objective of general purpose financial reporting and the qualitative characteristics of useful financial information

### Question 1(a) – Stewardship

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG welcomed the greater prominence given to the assessment of management's stewardship in the ED. EFRAG, however, disagreed with the ED that the objective of assessing management's stewardship should be included in a general objective of providing useful information to support decisions involving buying, selling or holding equity and debt instruments, and providing or settling loans and other forms of credit. EFRAG believed that existing investors could need information for the assessment of stewardship that would supplement the information useful to decisions on buying, selling or holding equity and debt instruments. EFRAG's Document for Public Consultation included a question to constituents on whether the group of users, the ED focused on, was appropriately identified.

##### *Constituents' comments*

Some constituents welcomed the inclusion of stewardship.

One constituent, however, did not agree with including 'stewardship'. The constituent thought that the main objective of financial reporting should be to provide 'decision useful' information. The constituent noted that 'stewardship' focused on contracting issues between the management and the owners of the entity (stockholders) and other corporate governance related issues. Accounting requirements should not focus on the contracting use of financial information, i.e. providing relevant information with the capability of impacting contracting decisions between management and owners of the entity. Another constituent thought that the IASB should require relevant information about stewardship through disclosures instead of having stewardship as a separate objective that could be in conflict with providing information useful for buying, holding and selling decisions.

#### EFRAG's response to constituents' comments

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EFRAG noted the general support for reintroducing 'stewardship' in the Conceptual Framework. EFRAG also noted that constituents were split on whether stewardship should be considered as part of the information needed for buying, holding and selling decisions. EFRAG, however, disagreed with the arguments for considering stewardship as part of the information needed for buying, holding and selling decisions. EFRAG agreed that measuring assets and liabilities at fair value could also be relevant for the assessment of stewardship, but EFRAG did not consider this to be an argument for including stewardship as part of the information needed for buying, holding and selling decisions.

First of all, EFRAG did not think that fair value in all cases would result in the most useful information for buying, holding and selling decisions.

Secondly, although the use of fair value could provide information about some aspects of stewardship, it might be that historical cost would provide useful information on other aspects.

EFRAG also did not find the arguments that splitting the objectives could result in conflicts and confusion. If the two objectives were to conflict in some cases, EFRAG thought that it was better to make that explicit instead of hiding it.

EFRAG acknowledged that including 'stewardship' as an objective in the Conceptual Framework could potentially conflict with other objectives. However, EFRAG noted that different types of users could also have different information needs for their assessment of providing capital to an entity depending on, for example, whether they were lenders or shareholders. EFRAG considered that the idea of general purpose financial reports is that they should be able

Some constituents agreed with the ED that information necessary for the assessment of stewardship was part of the information needed for making decisions on buying, holding and selling. Some of the reasons provided were:

- Although some considered that measuring assets and liabilities at fair value was only relevant for making decisions on buying, holding and selling, it was also useful for assessing the stewardship of management.
- Splitting the objectives of providing information for buying, holding and selling decisions and with assessing stewardship could in certain circumstances result in conflicts.
- Introducing an additional primary objective could be confusing.

One constituent thought that the information needed for making decisions on buying, holding and selling was part of the information needed for the assessment of stewardship.

Some constituents thought that the assessment of stewardship should be separated from the objective of providing information for buying, holding and selling decisions. The reasons provided were that additional or different information could be needed for the assessment of stewardship compared with the information needed for making buying, holding and selling decisions.

Some constituents thought that providing useful information for the assessment of stewardship could conflict with the objective of providing information for buying, holding and selling decisions. One of the reasons provided was that the assessment of stewardship requires more prudence in the form of accounting conservatism. Another reason was that measurement at, for example, fair value was more important for serving the needs for decisions on buying, holding and selling than for the assessment of stewardship.

Some constituents provided their views on how to deal with the conflict. Some of the views provided were:

- When a measurement basis would be relevant for buying, holding and selling decisions, but not relevant for the assessment of stewardship, another measurement basis could be selected that would be relevant for the assessment of stewardship and at the same time provide information relevant for buying, holding and selling decisions.

to provide useful information to many different users that would not be in a position to demand specific information. In that regard, EFRAG also noted that many shareholders (minority shareholders) would not be in a position to require special reports of the management. However, they could still have a say in choosing the management. EFRAG therefore maintained its preliminary position that financial statements should provide information for assessing stewardship.

Although EFRAG acknowledged that in some cases the information that would be most useful for providing information on certain aspects of stewardship could be different from the information that would provide the most useful information for aspects of some users' buying, holding and selling decisions, it did not think the Conceptual Framework should present two competing objectives. EFRAG thought that the objective of general financial statements was to provide useful information and that would include providing information useful for assessing management's stewardship and information useful for making buying, holding and selling decisions. EFRAG thought that in most cases it would be possible to provide information that would be useful for both assessing management's stewardship and for buying, holding and selling decisions.

EFRAG noted that a study it had sponsored together with ICAS (*Professional investors and the decision usefulness of financial reporting*) showed that financial statements were relatively more important for the assessment of management's stewardship than for buying, holding and selling decisions. EFRAG did therefore not agree with the comments that the assessment of stewardship should be considered secondary to buying, holding and selling decisions.

As some constituents were uncertain about how the objective of providing information for the assessment of stewardship included in the ED would affect standard setting, EFRAG decided to include its view on this in its comment letter in response to the ED. EFRAG's description of the role of stewardship focused on both forward-looking and backward-looking information. EFRAG did not agree with the comment that providing information for the assessment of stewardship should only focus on information with

- The objective of providing information useful for buy-hold-sell decisions should have priority over the objective of providing information useful for assessing stewardship as an entity could choose to publish customised reports in addition to the general financial reports, to allow specific stakeholders to assess stewardship. One constituent thought that instead of including stewardship as a separate objective, it should be included as an enhancing objective of financial reporting of a lower rank. Another constituent, however, disagreed with these views stating that the objective of stewardship should at least be of the same importance as the decision usefulness objective.

Some constituents were uncertain about how the objective of providing information for the assessment of stewardship included in the ED would affect standard setting and they thought this needed to be clarified. The clarification should include whether the concept of stewardship included both the short-term and the long-term investment perspectives and what additional information the inclusion of 'stewardship' would result in. Some constituents noted that it was difficult to translate 'stewardship' into local languages and it was therefore important that the term could be properly understood.

Some constituents also provided their views on how the IASB could clarify the term. Some of the suggestions and views expressed were:

- The IASB should consider clarifying that the concept of stewardship is called 'accountability' in some jurisdictions.
- The concept of stewardship needs to encompass a broad range of backward-looking as well as forward-looking information, such as information about management remuneration.
- It should result in financial statements that better reflect risk management and how management is running its business in the financial statements.
- Stewardship should be more broadly defined than in the ED and should consider how management has complied with its commitments.
- It should encompass the business model and strategic objectives set by management and that represent appropriately specific management decisions.

confirmatory value. EFRAG also disagreed that stewardship would lead to a rejection of current cost as an appropriate measurement basis. EFRAG noted that stewardship was both about considering what the management had done in a given period (confirmatory value) and about how it had positioned the entity for the future (forward-looking information).

EFRAG agreed with the comment that preparers should not be considered more important than, for example, auditors and regulators. EFRAG therefore clarified its position by stating that if preparers consider that the information resulting from a Standard is useful for them, it could indicate that information resulting from a Standard is useful for users and vice versa.

EFRAG noted that the ED, when discussing understandability, identified that users should have a reasonable knowledge of accounting. Consequently, EFRAG did not agree with the comment that this characteristic had been removed in the ED.

EFRAG agreed with the comment that primary users could have conflicting information needs. However, the task of general purpose financial statements would be to address these different needs as far as possible and within the limits of what financial statements can provide information about.



- It should only focus on financial reporting as general purpose financial reports cannot provide all the necessary information that users might require. Accordingly, it should be explained that the objective of stewardship could be achieved only partially through financial reporting.
- It should state that financial statements should report on past transactions and events and the information should focus on having confirmatory value. It should thus lead to a reclusion of current cost as an appropriate measurement basis.
- It should address the potential conflict of interest between the managers and owners of an entity that make information about stewardship and accountability necessary.

One constituent proposed to strengthen EFRAG's argument on stewardship by referring to the shareholders as a group that have the objective to potentially change the management.

One constituent thought that although the objective of stewardship is now part of the Conceptual Framework, it is important that this is not deemed to give the IASB any mandate to broaden the scope of its sphere of action to other aspects of financial communication or governance outside what is currently understood to be general purpose financial reporting.

On the question included in EFRAG's Document for Public Consultation on which users should be considered as the primary users, some thought that the primary users of financial information were correctly identified in the ED.

Some constituents thought that 'primary users' should include more types of users than in the ED. One of the reasons provided was that the public has an interest in how companies operate and perform. It may be that the financial statements should not include information for these user groups, but the annual report including the management report and management commentary should include such information if relevant. If the Conceptual Framework continued to focus only on financial information, it might mean that financial information under IFRS would become less relevant for the capital markets in the future.

Some constituents thought that the management should be considered a user in order to reduce the use of non-GAAP measures. One of the constituents thought that the IASB did not give sufficient credit to the significant efforts and

costs incurred by preparers dedicated to developing ERP systems and governance processes which align internal with external reporting, and to build a common language within the reporting entity in order to ensure common understanding of all internal KPIs.

On the other hand, one constituent disagreed that preparers should be considered as a user group. The constituent noted that management has access to all the information from the company and they can get additional information. Therefore, they should not be considered as users of financial statements on the same footing as the external users, because they do not only rely on the financial statements.

One constituent also expressed that considering the management as a user would cause conflicts of interests.

One constituent disagreed with EFRAG's proposal that where preparers 'converge' in opposing a proposal from the IASB, the IASB should be under a special responsibility to respond to their views. The constituent thought that there seemed to be no good reason to privilege preparers in this way relative to other groups who express views on the IASB's proposals (for example, regulators or auditors). The constituent thought that if the IASB receives comments on its proposals that indicate a strong body of opinion opposed to them, it should explain why, if it stands by the proposals, it has decided to do so. This should be the case regardless of the source of the opposing views.

Another constituent thought that EFRAG's statement on the role of preparers was useful.

One constituent understood that EFRAG did not think that potential investors, lenders and other creditors would qualify as primary users of financial statements.

One constituent thought that internal users should also be considered but in case of conflicting objectives, external (primary) users' objectives should take prominence over internal users' objectives.

One constituent noted that the idea that users should have a reasonable knowledge of accounting was deleted from the ED. The constituent disagreed with this.

Some constituents expressed the view that primary users could have conflicting information needs. For example, some believed that the notion of

'prudence' would be more closely aligned with the interests of creditors and long-term investors, than with the interests of shareholders and short-term investors.

One constituent considered that long-term investors should be specifically mentioned in the Conceptual Framework and that society at large should be considered as a 'user' of general purpose financial reporting.

## Question 1(b) – Prudence

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG welcomed that the ED re-introduced prudence and with the judgement of the IASB in the Basis for Conclusions that prudence may lead to asymmetry in the recognition of assets/income and liabilities/expenses without introducing any undesirable bias in financial reporting. These conclusions should, however, be acknowledged in the Conceptual Framework itself. Also, prudence should not be made subservient to neutrality. Finally, the Conceptual Framework should focus on how prudence should affect standard setting rather than the behaviour of preparers of financial statements.

#### *Constituents' comments*

Some constituents expressed general support for the comments included in EFRAG's Document for Public Consultation on prudence.

Some constituents did not support including a reference to prudence in the Conceptual Framework. Some of the reasons provided were:

- Prudence would conflict with neutrality.
- Prudence was not needed as appropriate financial reporting would result when the other qualitative characteristics were met.
- A cautious approach to asset and liability recognition in a specific period might result in an overstatement of profit in a future period.
- The concept was given a new meaning in the ED, and it is not a good idea to take a well-known concept and give it a new meaning.

Some constituents, on the other hand, agreed with including an explicit reference to prudence.

Some constituents agreed with the ED to include prudence in the description of neutrality. Some of the reasons provided were:

- It would ensure that prudence would not be misused as a motive for systematic misstatements.

### EFRAG's response to constituents' comments

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EFRAG agreed with the comments that asymmetry is reflected in some current standards. EFRAG considered that in these cases asymmetry results in useful information. EFRAG was therefore in favour of including a specific reference in the Conceptual Framework to the possibility of having asymmetry.

EFRAG agreed also with the comment that stakeholders in some cases perceive that overstating assets is a more serious offence than understating them. That was the reason why asymmetry should sometimes be introduced.

EFRAG noted that it was not in favour of introducing asymmetric prudence as an overarching principle. In many cases using the same principles for recognising and measuring assets and liabilities would result in the most useful information. This would, for example, generally be the case for financial assets and liabilities. However, EFRAG thought that if the possibility of asymmetry was not generally discussed in the Conceptual Framework, it would be difficult to introduce it in relation to recognition and measurement. EFRAG therefore preferred to have asymmetric prudence discussed in relation to the qualitative characteristics in the Conceptual Framework.

While EFRAG agreed that asymmetry could potentially impact recognition and measurement, EFRAG thought the issue could not only be considered in the sections about recognition and measurement of elements of financial statements as suggested by one constituent. As a result of its pervasiveness, EFRAG thought that the issue had to be addressed when discussing the qualitative characteristics.

EFRAG did not think that the introduction of asymmetric prudence in Standards was in conflict with neutrality, as EFRAG did not think that information resulting from such guidance would increase the

- Prudence is necessary for achieving neutrality of financial reporting by counterbalancing the inherent optimistic assumptions of management (e.g. when making estimates).
- Prudence is directly linked to neutrality. When management is being prudent (on its judgements and estimates) in an environment of uncertainty, then it is also being neutral.

Some disagreed with including prudence in the description of neutrality. A reason stated by some constituents was that including prudence in neutrality would give the notion a meaning different from how most people interpreted it (see below).

Some constituents supported the view included in EFRAG's Document for Public Consultation that asymmetric prudence should be discussed in the Conceptual Framework (and not only in the Basis for Conclusions). Some of the reasons provided were:

- 'Asymmetric prudence' is already reflected in many standards, for example, IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* where assets and liabilities were treated asymmetrically in terms of recognition.
- Stakeholders perceive that overstating assets is a more serious offence than understating.
- Asymmetric prudence seems more consistent with the EU Accounting Directive.
- The proposal in the ED does not give any sense of direction.
- 'Good news' that is reported before it is reasonably assured may be disregarded and, if it is not confirmed by subsequent events, undermines the credibility of financial reporting. In contrast, the market needs reassurance that all 'bad news' is reflected in financial statements. Even if bad news is already public, a prudent account of it provides confirmatory value.

One constituent noted that although asymmetric prudence should be discussed in the Conceptual Framework, it should not stop the use of fair value

probability that financial information will be received favourably or unfavourably by users.

EFRAG noted that constituents were split on the issue of whether prudence should be considered to be an element of neutrality or not. EFRAG noted that the arguments for including 'prudence' in 'neutrality' were primarily based on the assumption that 'prudence' should be applied by preparers. EFRAG agreed with the constituents who thought that the Conceptual Framework should explain how prudence should be considered in standard setting. EFRAG thought that the status of the Conceptual Framework made it a less effective tool for affecting the behaviour of preparers than guidance in Standards. In addition, EFRAG noted that if the application of prudence would be left to preparers, it would possibly be applied in an inconsistent manner given the different views on its meaning.

EFRAG agreed with the comments that the manner in which the ED explained prudence did not result in any guidance (and accordingly that the ED defined 'prudence' differently from how it was normally understood). As explained above, EFRAG thought that the description of prudence in the Conceptual Framework should acknowledge the possibility of asymmetry. EFRAG did not think that such a description of prudence would be related to neutrality, although it would not be in conflict with neutrality either.

EFRAG agreed with the comment that an acknowledgement of asymmetric prudence in the Conceptual Framework, should not stop the use of fair value measurement in appropriate circumstances or the recognition of fair value gains in financial statements.

EFRAG agreed with the comment that information that would enable users to understand whether management was taking more risks than shareholders were comfortable with would be useful. EFRAG, however, did not consider that the application of prudence would result in this information. The re-introduction of the objective of assessing stewardship would be more related to this objective,

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measurement in appropriate circumstances or the recognition of fair value gains in financial statements.

Some constituents were against including asymmetry as an overarching concept. The reasons provided were that it would introduce bias into standard setting where it would be assumed that gains and losses and assets and liabilities would be treated differently in all circumstances. These constituents, however, noted that, asymmetry may be appropriate in particular situations.

Some constituents did not think the Conceptual Framework should refer to asymmetric prudence at all. One of these constituents thought that a reference to asymmetric prudence would potentially allow asymmetric recognition and measurement, and that was not desirable. If the IASB were to introduce asymmetric recognition in a specific standard, it should be properly explained and justified in the basis for conclusions. Another of these constituents thought that there could be valid reasons for having asymmetric requirements in Standards. The constituent thought that this outcome would be achieved by the proposal in the ED, as the IASB would have to depart from the Conceptual Framework, and provide the necessary explanations for doing so, when introducing asymmetric prudence in a Standard.

Some constituents thought that the issue of asymmetry should be considered in relation to recognition and measurement of elements of financial statements.

Some constituents did not think the ED provided any clear directions in relation to prudence. One of these constituents noted that the ED's description of prudence did not provide any information as there was no benchmark to assess whether assets or liabilities were understated or overstated. Another constituent was concerned that a lack of clarity in the Conceptual Framework would result in questions arising in the future during standard setting.

One constituent agreed with the ED that prudence should be defined as caution when making judgements under conditions of uncertainty.

Some constituents thought that the ED defined 'prudence' differently from how it was normally understood.

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although EFRAG did not think that financial statements on their own could provide all the information needed by users on this issue.

Some constituents thought prudence normally meant ‘conservatism’.

One constituent thought that prudence was a broader concept that could help users to assess stewardship and understand whether management was taking more risks than shareholders would be comfortable with.

One constituent considered that the aim of the principle of prudence was to ensure that cash flows (negative or positive) were reported in the financial statements, as predictable as possible - that is, the cash flows that are most likely to occur would be reported.

One constituent thought that the prohibition to distribute unrealised profits in many jurisdictions should be considered when explaining prudence.

One constituent supported how EFRAG described prudence but would be concerned with a more explicit notion of asymmetric prudence beyond what was suggested as this could be misinterpreted as a move towards standards that would be more asymmetric than is currently the case, and so should be avoided.

One constituent thought that the Conceptual Framework should explicitly state that prudence should apply not only to measurement but also to recognition and presentation.

One constituent disagreed with EFRAG and thought that prudence should be directed towards preparers in order to counteract their positive bias.

Another constituent thought that prudence should be directed both towards preparers and standard setters.

However, some constituents thought that the definition of prudence should focus on how the guidance would be applied during standard setting.

One constituent noted that the definition of prudence included in the ED would not be compatible with the requirements in IFRS 3 *Business Combinations* on the recognition of a gain in a bargain purchase.

## Question 1(c) – Substance over form

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG welcomed the reintroduction of 'substance over form' but thought the distinction between 'legal substance' and 'legal form' should be more clearly explained.

#### *Constituents' comments*

One constituent explicitly agreed with EFRAG's response in the Document for Public Consultation.

Some constituents welcomed the reintroduction of 'substance over form'.

One constituent did not think the reintroduction was necessary. The constituent explained that the concept was useful 20 years ago, when assets were only recognised if legally owned. Today most people knew that assets in financial statements could be different from assets in accordance with local laws.

Some agreed with the ED. The reasons provided were:

- If information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance and economic reality and not merely their form or appearance.
- Substance over form is necessary for a series of separate, but related, contracts being considered together for accounting purposes.

However, some thought that additional guidance/clarification was needed. The issues raised were:

- The explanation in the ED might be misunderstood as suggesting that the legal form could never reflect the substance of an economic arrangement.
- It was unclear whether 'substance' refers to economic substance or the contractual terms and conditions as some current standards (IFRS 10

### EFRAG's response to constituents' comments

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EFRAG noted that constituents, like EFRAG, generally supported the reintroduction of 'substance over form'. Like EFRAG, some constituents, however, thought that additional clarification was needed on the role of legal form or substance.



*Consolidated Financial Statements and IFRS 11 Joint Arrangements*) seem to focus heavily on the legal form.

- Some constituents may have acquired a different understanding of the predominance of economic phenomena over legal form from some recent developments. For example, via IFRS 11 could be perceived as relying much more on legal form than on the economic substance and purpose of joint arrangements.
- The difference between legal substance and legal form is not clear.

Other constituents did not think that additional guidance was needed as:

- The concepts of legal form as opposed to economic substance were broadly established in practice.
- The concept seemed self-evident.
- The concept just stated that preparers have to do what the Standards tell them to do.

Some constituents thought that the economic substance could not be considered independently from the legal aspects. One of these constituents was particularly concerned about shares in co-operatives.

Some constituents thought that further consideration needed to be given to how 'substance over form' interacts with accounting based on financial instrument contracts as the SPPI test seemed only to be based on the contractual terms and, for example, not legislative provisions that are not specific contractual terms of the financial instrument.

## Question 1(d) – Measurement uncertainty

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG disagreed that measurement uncertainty should be an element of 'relevance'. The Conceptual Framework should provide the opportunity of gaining a better understanding of what the boundary of a reliable measurement should be. Acknowledgment of the trade-off between relevance and reliability should remain. Further, it should be clear that uncertainty plays a role in both recognition and measurement.

#### *Constituents' comments*

Some constituent agreed with the ED that measurement uncertainty should be considered as part of 'relevance'. One of the arguments provided was that measurement uncertainty traditionally had been a part of reliability. However, as this had been replaced by 'faithful representation' measurement uncertainty should be considered in relation to 'relevance' as it did not affect 'faithful representation'.

Other constituents thought that measurement uncertainty should be considered part of 'reliability' or 'faithful representation'. Some of the arguments provided were:

- There is a trade-off between relevance and reliability. It is vital that this trade-off is made clear in the Conceptual Framework. The treatment of measurement uncertainty as an aspect of relevance does not emphasize the trade-off enough.
- Relevant information is always relevant irrespective of the degree of measurement uncertainty. What changes is the reliability of the measurement and hence the usefulness of the information and the way it can be used.

One constituent thought that uncertainty, instead of being included in relevance or faithful representation, should be considered as an underlying constraint when discussing the qualitative characteristics and the

### EFRAG's response to constituents' comments

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EFRAG noted that constituents were split on the question of whether measurement uncertainty should be considered as part of 'relevance' or as part of 'reliability' or 'faithful representation'. EFRAG acknowledged that the issue might not affect future Standards, but for the standard-setting process, EFRAG preferred measurement uncertainty to be considered as part of 'reliability' or 'faithful representation' for the reasons provided by constituents supporting this approach and for the reasons included in EFRAG's Document for Public Consultation.

EFRAG had some sympathy for the comment that uncertainty should be considered as an underlying constraint when discussing the qualitative characteristics. On balance, however, EFRAG preferred it being considered as part of the qualitative characteristics. One reason was that EFRAG did not consider it as a constraint that would apply to disclosures. Another reason was that EFRAG thought that it was important to have measurement uncertainty reflected in the assessment of faithful representation when assessing the trade-off between relevance and faithful representation. EFRAG considered that measurement uncertainty was often a matter of degree. Sometimes, therefore more measurement uncertainty could be accepted if the information provided would be more relevant, than if the information provided would be characterised by less measurement uncertainty.

EFRAG agreed with the comment that the impact on measurement uncertainty could be explained in the chapters on recognition and measurement. EFRAG, however, still thought that it was important to mention measurement uncertainty as something that affects the qualitative characteristic 'faithful representation'.

EFRAG noted that some constituents did not agree with the view expressed in EFRAG's Document for Public Consultation that the boundary of a reliable measurement should be further explained.

Conceptual Framework should then elaborate further on existence and measurement uncertainty in the relevant chapters.

Another constituent thought that instead of highlighting measurement uncertainty in Chapter 2 of the Conceptual Framework, it would be more helpful and understandable to give more prominence about measurement uncertainty and its implication as part of the recognition and measurement guidance.

A third constituent thought that the Conceptual Framework should deal more generally with uncertainties, which in addition to measurement uncertainty would include existence uncertainty.

Some constituents agreed with EFRAG that the effects of uncertainty should not be restricted to measurement issues but should also be considered in decisions about recognition and, perhaps, presentation.

One constituent thought that the discussion on measurement uncertainty should be clearly linked to the measurement guidance in the Conceptual Framework.

Some constituents disagreed with the view expressed in EFRAG's Document for Public Consultation that the boundary of a reliable measurement should be further explained. One of these constituents noted that as there was a trade-off between measurement uncertainty and other factors that make information relevant that will vary from case to case, a more specific explanation of the boundary of a reliable measurement would not benefit the Conceptual Framework.

Similar to the view expressed in EFRAG's Document for Public Consultation, one constituent disagreed with the idea that almost any estimate could qualify as a faithful representation, provided that "the reporting entity has properly applied an appropriate process, properly described the estimate and explained any uncertainties that significantly affect the estimate".

In its document for public consultation, EFRAG had stated that it accepted that a model that is acknowledged as widely used by market practice was a reliable basis for the price of a complex derivative. One constituent understood that EFRAG therefore meant that a model that is not widely used by market participants necessarily lacks linkage with economic reality. The constituent disagreed with this as any pricing model must be

EFRAG agreed with the argument that there was a trade-off between measurement uncertainty and other factors in each case. EFRAG, accordingly acknowledged that sometimes a given level of measurement uncertainty would be more acceptable than in other cases. EFRAG, however, still thought it would be relevant to have an indication about how uncertain a measurement should be before the resulting information would not be considered useful. EFRAG thought that this was particularly important as the ED could give the impression that as long as the uncertainty would be explained, any estimate could qualify as a faithful representation. Similar to one of the constituents, EFRAG would disagree with this.

EFRAG's Document for Public Consultation did not state that a model that is not widely used by market participants necessarily lacks linkage with economic reality. EFRAG, however, observed that its comment was interpreted in that manner. EFRAG therefore decided to clarify its position in relation to its comment in the Document for Public Consultation on the pricing of complex derivatives.

EFRAG noted that one constituent was concerned that the support that EFRAG gave to 'asymmetric prudence' would mean that it would sometimes be appropriate to recognise fair value losses on complex derivatives, but not fair value profits. EFRAG decided to clarify that it was not its view that asymmetric prudence should be an overarching principle. In some cases, it would make sense to use it – for example in relation to contingent assets and liabilities. In other cases, such as in the case of financial instruments, it would not make sense.

linked with economic reality, otherwise it would be of no use as a model. However, as all dealers develop their own models a particular model may not be widely used. While there will often be similarities between the different models, making use of similar mathematical techniques, such models will usually not be exactly the same. The constituent accordingly thought that the term 'widely used' was unhelpful as it implied that most market participants used the same models, and it begged the question as to how much of a variation from the norm would still count as 'widely used'..

One constituent noted that EFRAG thought that prudence had an important role to play in relation to measurement uncertainty. The constituent was concerned that this, given the support that EFRAG gave to 'asymmetric prudence' would mean that it would sometimes be appropriate to recognise fair value losses on complex derivatives, but not fair value profits. The constituent thought that it would never be relevant or useful not to record a trading portfolio at fair value just because the measurement of some of the instruments in the portfolio would be less reliable.

## Question 1(e) – Relevance and faithful representation

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG supported the Conceptual Framework continuing to identify relevance and faithful representation (or reliability) as the two fundamental qualitative characteristics of useful financial information. The Document for Public Consultation asked constituents whether they preferred the term 'reliability' or 'faithful representation'.

#### *Constituents' comments*

Some constituents agreed explicitly with the ED and the view expressed in EFRAG's consultation document that relevance and faithful representation (or reliability) should be the two fundamental qualitative characteristics of useful financial information.

On whether the term 'reliability' or 'faithful representation' should be used some constituents preferred the term 'faithful representation'. Some of the arguments provided were:

- As a concept, faithful representation is easier to understand.
- The label 'reliability' could be confusing.
- Faithful representation is a wider concept than 'reliable', as set out in BC 2.24 to the ED.
- 'Faithful representation' better describes what should be achieved in reporting.
- Reliability is a part of 'faithful representation' as reliability only relates to clerical accuracy.

Other constituents preferred to use the term 'reliability'. Some of the reasons provided were:

- Reliability includes the notion that the information 'can be depended upon by users' and to have such a reference within a fundamental characteristic would help inform both entities and the IASB's thinking

### EFRAG's response to constituents' comments

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EFRAG noted that there were arguments both in favour and against changing from using 'faithful representation' back to using 'reliability'. EFRAG therefore decided not to suggest any changes on this although EFRAG could see some merits in reintroducing the term 'reliability'.

in respect of the use of Level 3 fair value measurements. These can faithfully represent values but may not be reliable.

- It would give greater emphasis on the importance of measurement certainty.
- The reason for the change from ‘reliability’ to ‘faithful representation’ seems to have been that ‘reliability’ was not correctly understood by all. However, it is better to provide additional clarification and to keep the notion than to introduce a new notion.
- The term ‘reliability’ better reflects the trade-off between relevance and reliability.

In addition, some constituents thought that reliability should be defined as in the 1989 Conceptual Framework. The reason provided was that there is no alternative concepts for which greater consensus about the meaning could be achieved.

On the trade-off between relevance and faithful representation/reliability one constituent suggested the following approach:

- If the information is not relevant, then it should not be used either in the financial statements or in the notes.
- If the information is relevant, then depending upon the degree of measurement uncertainty it should be used:
  - In the financial statements if sufficiently reliable (with a secondary distinction between the net income and OCI); or
  - In the notes to the financial statements, if less reliable.

One constituent questioned the decision to select faithful representation and relevance as the fundamental qualitative characteristics. The constituent expressed the view that information could not be relevant if it was not faithfully representational.

One constituent thought that ‘faithful representation’ should include the notion that the information can be depended upon by users, which was part of the term ‘reliability’.

## Chapter 3 – Financial statements and reporting entities

### Question 2 – Description and boundary of a reporting entity

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG agreed with the ED that a reporting entity is not necessarily a legal entity and that an entity can prepare both individual and consolidated financial statements. EFRAG disagreed with including a statement that consolidated financial statements are more likely to provide useful information than unconsolidated financial statements. Finally EFRAG considered that it would be beneficial to have further explained in the Conceptual Framework what the implications of applying the entity approach would be. EFRAG's consultation document included a question to constituents on whether they agreed that there was no urgent need to justify the choice of control as the basis for consolidation from a conceptual perspective.

##### *Constituents' comments*

Some constituents agreed that a reporting entity is not necessarily a legal entity but can be a part of a legal entity or a group of legal entities.

Some constituents agreed with EFRAG that the Conceptual Framework should not include a general statement that consolidated financial statements are more likely to provide useful information than unconsolidated financial statements. One constituent thought that the Conceptual Framework should explain that there are two possible set of accounts with different purposes.

One constituent welcomed the reference to combined financial statements.

Some constituents thought that the Conceptual Framework should provide more guidance on which combinations of entities could constitute a reporting entity that could legitimately prepare combined financial statements. The following guidance/criteria were suggested for when combined financial statements could be prepared:

- The economic activities of the portions must be objectively distinguishable from the rest of the entity (i.e. supported by evidence) and the financial information about these portions of the entity must have

#### EFRAG's response to constituents' comments

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Based on the comments received, EFRAG decided to state in its comment letter that the Conceptual Framework should not include a general statement that consolidated financial statements are more likely to provide useful information than unconsolidated financial statements. Such a statement was also included in EFRAG's Document for Public Consultation.

EFRAG did not agree that the Conceptual Framework should provide guidance on which combination of entities could constitute a reporting entity. EFRAG considered that this was a decision that the jurisdictions that have adopted IFRS could make on an individual basis.

EFRAG agreed with the comment that the Conceptual Framework could state it was for-profit entities. However, EFRAG thought that this could be done in the introduction to the Conceptual Framework rather than in the section on the financial statements and the reporting entity. EFRAG noted that the section on the reporting entity described what a reporting entity was. It did not provide any guidance on the necessary characteristics reporting entities should have in order to prepare financial statements in accordance with IFRS. For the same reason EFRAG did not think that the discussion on the going concern assumption should be moved to the section.

EFRAG did not observe a general request from constituents to justify the choice of control as the basis for consolidation. EFRAG accordingly decided not to include such a request in its comment letter.

EFRAG agreed with the comment that paragraph 3.25 of the ED (the requirement to disclose how users may obtain the consolidated financial statements of an entity) should not be included in the

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the potential to be useful in making decisions about providing resources to these portions of the entity.

- A reporting entity should be a circumscribed area of economic activity and its economic activities can be objectively distinguished from those of other entities and from the economic environment in which the entity exists.
- The entities should currently be under common control.
- The entities should have a common management.
- The entities should have common services.
- The entities should have a stable contractual relationship.

Some constituents found the discussion about defining the boundaries of an entity through direct and indirect control confusing. One of these constituents suggested that the Conceptual Framework should instead explain separate financial statements and consolidated financial statements.

One constituent urged the IASB to revisit its guidance in the ED and define better the boundaries of the reporting entity.

One constituent thought that the IASB could further complete the characterisation of the reporting entity by stating clearly in the main body of the Conceptual Framework that the reporting entity is considered to be a for-profit entity.

One constituent considered it more appropriate to include the going concern assumption of the reporting entity in paragraph 3.10 of the ED as part of the description of the reporting entity chapter (and not as part of the role of financial statements as drafted in the ED) as it seemed to be a characteristic of the reporting entity rather than the financial statements.

On the need to justify the choice of control as the basis for consolidation, some constituents agreed with EFRAG's position.

Some constituents thought that the Conceptual Framework should include a discussion on the concept of control and why control – exclusive control – should be the underlying principle for the definition of the reporting entity. One of these constituents thought this could impact the use of the equity method.

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Conceptual Framework as it would seem more beneficial to include such specific guidance in a Standard.

EFRAG noted that several constituents thought that the statement of cash flows was not given sufficient prominence in the Conceptual Framework. EFRAG accordingly included a comment on this in its comment letter (see below).

EFRAG noted that constituents had different views about the entity approach. EFRAG considered that these different opinions could stem from different views of the implications of the statement in the ED that financial statements should be prepared “from the perspective of the entity as a whole”. EFRAG therefore decided to recommend that the IASB should better explain what it meant by this statement. Based on how EFRAG interpreted the term, EFRAG thought for some types of information a proprietary approach would be more useful than the entity approach suggested. This could, for example, be the case for information to assess the management's stewardship. EFRAG, however, also expected that the IASB's equity/liability project could provide further insight about this issue.



One constituent thought that the IASB should have explored the possibility of introducing a coherent definition of control in the Conceptual Framework, but did not think it should be considered at this stage as it would delay the project.

One constituent thought that the distinction between the entity view and the proprietary views of financial statements was not very useful for the choice of accounting methods in individual Standards. The constituent therefore thought the wording should be reconsidered not to give the impression that what in accounting theory is referred to as the entity view was the preferred approach. On the other hand, another constituent thought the Conceptual Framework should refer more explicitly to the 'entity theory of accounting' as such reference would explain the focus on the investors in the parent entity and the fact that minority interest is presented as part of equity in the consolidated financial statements.

One constituent disagreed with EFRAG that for some types of information a proprietary approach might be useful.

Some constituent was concerned that financial statements should be prepared from the perspective of the entity as a whole without further analysis or explanation about the implications of this approach.

One constituent thought that it would be beneficial to have further explained in the Conceptual Framework what the implications of the entity approach were.

Some constituents had similar views as EFRAG on the use of the terms 'direct' and 'indirect' control.

One constituent thought that different levels of involvement between entities (e.g. joint control) should be explained and explored in the Conceptual Framework.

Some constituents considered that stating that an entity should provide information about how to obtain the consolidated financial statements of an entity is something that could be done on a standards level – not at the level of the Conceptual Framework.

Some constituents thought that when the ED states what financial statements consist of (paragraph 3.6 of the ED) it should also mention the statement of cash flows and the statement of changes in equity as these are important statements.

One constituent thought that Conceptual Framework should more clearly explain the distinction between general and special purpose financial statements.

Some constituents thought that the Conceptual Framework should include a discussion of equity-accounted entities in consolidated or separate financial statements.

One constituent stated that most users of consolidated financial statements have a parent company approach, the constituent thus supported the ED that information about an entity should not be collected from the entity's parent, but from (consolidated) financial statements of the entity.

## Chapter 4 – The elements of financial statements

### Question 3 – Definitions of elements

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG initially supported the proposed definitions, but noted that it would do further testing. EFRAG disagreed with removing the description of revenue and with stating that if one party has a liability another party has an asset. The public consultation document included a question to constituents on whether they agreed that the asset/liability approach leads to more robust and consistent financial reporting than a pure matching approach.

##### *Constituents' comments*

Some constituents generally agreed with the proposed definitions.

However, some constituents were uncertain about the effects of the new definitions and thought that the IASB should further explore the implications of the proposed changes. One constituent thought the IASB should analyse the possible consequences of the proposed changes in their entirety on a broad set of potential rights and obligations that are currently not recognised in the financial statements.

One constituent saw more risks than advantages in changing the definitions and one constituent did not think that the existing definition of liabilities should have been changed before the project on liabilities and equity instruments would be finalised.

Some constituent was concerned that the proposed definitions would result in many more items meeting the definitions.

Some constituents thought that the notion of 'control' would be better included as a recognition criteria instead of in the definition of an asset. Another constituent thought that the notion of risks and rewards should have been considered instead of the notion of control.

Some constituents agreed with EFRAG that it was not useful to state that if one party has an obligation to transfer an economic resource, another party

#### EFRAG's response to constituents' comments

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EFRAG noted that some constituents generally agreed with the proposed definitions, but that other constituents were uncertain about the implications.

EFRAG agreed with the ED that control should be considered as part of the definition of an asset or a liability instead of being included in the recognition criteria. EFRAG thought that it would be inefficient to first consider whether something is an asset or a liability and then, as a second step, consider whether it is an asset or a liability of the entity. However, EFRAG thought it could be clarified - as it was in the IASB's Discussion Paper preceding the ED - that the definitions were of 'an asset of an entity' and 'a liability of an entity'.

EFRAG noted that there was some support for its concern about including a statement in the Conceptual Framework that if one party has a liability another party has an asset.

EFRAG did not think it was necessary to define cash flows conceptually. EFRAG thought it was more efficient to define this term in the standard on cash flow statements for the purpose of that Standard.

EFRAG agreed that, by including 'control' in the definition of an asset, only economic resources controlled by an entity would be recognised in the financial statements. EFRAG was, however, not concerned about this. It noted that 'control' was considered important in some of the IASB's recent Standards. Accordingly, focusing on control would reflect the IASB's current thinking.

EFRAG agreed to some extent with the comment that there should be a default approach which would require all the rights related to an individual physical asset to be treated as a single asset. Instead of introducing a default approach, EFRAG thought that the

(or parties) has a right to receive that economic resource. Some of the reasons provided were:

- It might cause confusion among the different users of the framework and might result in unintended consequences, as it is not well explained or supported.
- It is debatable whether an asset can be controlled by the society at large, and therefore, it is arguable whether an asset would always exist.
- The ED is inconsistent as it says that an asset could be held by the society at large but that a right that is identical to those held by all other parties is not an economic resource. Accordingly, the society at large cannot have an asset.

One constituent was concerned about assets arising from another party's constructive obligations as a result of saying that if one party had a liability another had an asset.

Some constituents thought that it was useful to specify that if one party has a liability another party has an asset. One of these constituents argued that the connection between an asset and a liability was vital.

Some constituents were concerned about considering each right as a separate asset as suggested in the ED, as this could result in future Standards reflecting a very high level of granularity. One constituent noted that there should be a default approach which would require all the rights related to an individual physical asset to be treated as a single asset, unless there are clear and compelling reasons to disaggregate the rights from each other as part of a standards-level approach.

Among the comments that were only raised by one or a few constituents were:

- Cash flows should be defined conceptually.
- The definitions should not link the definitions and financial statements. By linking the definitions of elements to the financial statements, the ED without any justification determines that control is a recognition criterion.
- The term 'rights' is expanded from its commonly accepted meaning.
- The definition of a resource should consider the organisational design of an entity.

guidance on the unit of account should be written in a manner that would generally result in such an outcome.

EFRAG considered that the 'past event' was an important element of the guidance included in the ED on when an obligation would be present. Accordingly, EFRAG agreed with the comment that it was not necessary to refer directly to the past event in the definition of a liability.

EFRAG was not in favour of defining either a claim or equity positively. This could result in some items "falling in between" two definitions or meeting the definitions of two elements.

EFRAG could see some merits in dealing with the role of financial statements in Chapter 1 of the Conceptual Framework. EFRAG, however, noted that Chapter 1 was dealing with financial reporting (and not only financial statements). EFRAG could therefore also see some benefits in keeping the discussion about financial statements separate. EFRAG therefore decided not to discuss the issue in its comment letter.

EFRAG did not consider the IASB to be the appropriate source of guidance on non-financial aspects of economic activities. Therefore, EFRAG did not think that the Conceptual Framework should consider non-financial aspects of economic activity.

Contrary to the view of one of the constituents, EFRAG agreed with the ED in stating that "rights to access public goods [...] are not economic resources for the entity if similar rights are available without significant cost". EFRAG understood the term 'cost' in a broad sense, and thought it was reasonable to exclude items that are freely available to everyone (in unlimited quantities) from being assets of an entity. EFRAG also noted that such public goods could not be controlled by the entity.

EFRAG agreed with the comment that the change from 'expected' to 'having the potential to' could result in many interpreting the definitions more broadly than currently, as 'expected' may have been interpreted as 'more likely than not' by some constituents.

- The reference to ‘past event’ in the definition of liability is not necessary as the concept of a ‘present obligation’ is the most important feature.
- The opposite of assets (e.g. a claim) should also be defined.
- An asset should be defined as a present economic resource controlled by the entity.
- Equity should be defined positively.
- Both liabilities and equity should be defined positively.
- Contributions of equity and distributions of equity should be defined as elements as only elements that meet the definition of an element can be recognised in the financial statements.
- The definition of a liability would require the probability threshold for recognition being explicitly included.
- The reference to ‘expected’ should not be removed from the definition, as something from which future cash flows could not be expected was not an asset
- The discussion on the role of financial statements belonged in Chapter 1.
- The Conceptual Framework should consider non-financial aspects of economic activity.
- The Conceptual Framework should not state that “rights to access public goods [...] are not economic resources for the entity if similar rights are available without significant cost”. This wording seemed to imply that the significance of cost plays a role in determining whether something should be considered as an asset, i.e. should be considered of having the potential to produce economic benefits.
- Contrary to what paragraph BC4.17 of the Basis for Conclusions states, changing the term ‘expected’ to ‘having the potential to’ would have an impact.
- Items that are recycled to profit or loss from OCI would not meet the definitions of income and expenses.

EFRAG acknowledged that income and expenses could be defined based on changes in equity rather than changes in assets and liabilities. Income could thus, for example, be defined as an increase in equity that results from an increase in assets or a decrease in liabilities other than from contributions from equity participants. EFRAG also acknowledged that some would perceive such a definition to be theoretically more correct than the definition proposed in the ED. On the other hand, EFRAG assessed that the fact that income and expenses were defined based on changes in assets and liabilities rather than in equity had not caused many problems when setting standards. As EFRAG had welcomed a pragmatic approach to the revision of the Conceptual Framework, it accordingly decided not to ask for income and expenses being defined based on changes in equity.

EFRAG considered whether the focus should be on matching instead of on assets and liabilities. For the reasons explained in its Document for Public Consultation, EFRAG thought that the asset/liability approach leads to more robust and consistent financial reporting than a pure matching approach. On the other hand, EFRAG also thought that the matching principle was important in order to provide useful information about an entity’s performance. EFRAG therefore suggested in its comment letter, that the IASB should consider situations where guidance in Standards would not result in useful matching of expenses with related income. In those cases, the IASB should carefully assess whether the information provided would be relevant. EFRAG nevertheless agreed with the comment that the Conceptual Framework should not allow for assets and liabilities that do not meet the definitions being recognised in the financial statements. If the IASB in a particular case would consider that the asset/liability approach would not result in relevant information, it would have to deviate from the principles of the Conceptual Framework. This would require the IASB to explain in the Basis for Conclusions why deviating from the Conceptual Framework was necessary in the particular case.

- Income and expenses should have been defined positively referring to the activities carried out by the entity.
- The reference to “other source of value” which was included in the Discussion Paper preceding the ED should have been kept as it was otherwise difficult to consider know-how as an asset. On the other hand, another constituent thought that it was an improvement not to refer to “other source of value” which made the definition too broad.
- The definitions of assets and liabilities should be derived from the definition of performance.
- The term ‘economic benefits’ should be defined in a manner that would exclude recognition of own shares, or shares of a parent entity which only investment is the investment in the reporting entity.

One constituent disagreed with EFRAG’s consultation document that a liability should be recognised for costs related to a restructuring when the entity has initiated and is committed to a restructuring.

One constituent thought that it would be useful to include paragraph BC4.16(a) of the Basis for Conclusions in the Conceptual Framework itself. The paragraph specified that it is not sufficient that the economic benefits may arise in the future. Those economic benefits must arise from some feature that already exists within the economic resource.

Some constituents supported the view included in the Document for Public Consultation that the asset/liability approach leads to more robust and consistent financial reporting than a pure matching approach.

One constituent did not agree with the asset/liability approach and noted that matching was an important principle as the asset/liability approach did not provide a conceptual basis for cash flow hedge accounting. Similarly, another constituent thought that the ED did not sufficiently acknowledge the importance of the ‘matching principle’.

One constituent thought that income and expenses could be defined as increases/decreases in *recognised* assets/liabilities that result in increase/decrease in equity other than those relating to distributions to holders of equity claims. Similarly another constituent thought that income should be defined as an increase in equity (not an increase in assets or decrease in

EFRAG agreed with the comments that revenue should be defined in the Conceptual Framework for the reasons explained in its Document for Public Consultation.

liabilities) and expenses are a decrease in equity (not a decrease in assets or an increase in liabilities). One constituent thought that it was more important to defined equity than assets and liabilities as this would provide the best guidance for what to recognise.

Some constituents thought that no asset or liability should be recognised that does not meet the definition of an asset or liability.

Some constituents thought that the description of revenue should have been retained or that the Conceptual Framework should define what the meaning of the line item would be. The reasons provided were:

- The link with IFRS 15 *Revenue from Contracts with Customers* (this issue was also explained in EFRAG's Document for Public Consultation).
- As currently defined the elements are too focused on balance sheet elements and hence do not give the necessary conceptual underpinning for the statement of profit or loss and the statement of comprehensive income.
- Defining revenue could be helpful in establishing concepts of financial performance and profit.

One constituent did not think it was necessary to describe revenue in the Conceptual Framework as long as income was defined.

One constituent agreed with the alternative views presented by Suzanne Lloyd and Patrick Finnegan and considered that the Conceptual Framework should have provided the Financial Instruments with Characteristics of Equity project with the conceptual starting point, rather than the project subsequently leading to changes in the Conceptual Framework.

One constituent had some issues with the equity section as the constituent found it unclear whether it was a description of equity in unconsolidated financial statements or consolidated financial statements as:

- Information about restrictions on particular components of equity (legally, regulatory or other) only seemed relevant in unconsolidated financial statements.

- There could be differences in what would be useful information from dividing equity into more than one class of equity in unconsolidated financial statements vs. consolidated financial statements.

The constituent noted that equity in consolidated financial statements (and equity in unconsolidated financial statements, when the parent applies the equity method for measuring investments in subsidiaries, joint ventures and associates) includes the share of equity in joint ventures and associates, where the parent does not control the distribution of dividends.

Some constituents thought that 'income' and 'expenses' should only be used for items that constitute net income because this is what is currently and commonly understood by users (other changes should be recognised as a movement in another asset or liability or in OCI). Another constituent had a similar view and thought the terms 'gains' and 'losses' should be used instead of 'income' and 'expenses' for all non-owner changes in assets and liabilities. The terms 'income' and 'expenses' could then be used for a subset of the gains and losses.



## Question 4 – Present obligation

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its consultation document, EFRAG generally agreed with how the ED described a 'present obligation' and a constructive obligation. However, EFRAG was concerned that the guidance was not sufficiently clear. As a result EFRAG sought to collect further input during the comment period.

#### *Constituents' comments*

Some constituents explicitly agreed with EFRAG's approach.

Some constituents were uncertain about the consequences of the proposed definition of a liability and thought the proposal should be further tested.

The uncertainty seemed particularly to relate to:

- The concept of 'practical ability to avoid'.
- What qualifies as a 'past event' that gives rise to a liability.
- What the qualifier 'significant' and 'economic consequence significantly more adverse' would mean in "avoid transfer would cause significant business disruption or would have economic consequences significantly more adverse than the transfer itself".
- How the definition would affect what would be equity (e.g. because the settlement and subsequent issuance of new bonds could prevent economic consequences that are significantly more adverse or because a co-operative's charter contained a right to refuse redemption, which in practice is rarely, if ever, exercised).

One constituent had similar concerns with levies calculated based on more factors as EFRAG did in its Document for Public Consultation.

Some constituents thought the IASB should further explore the impact on:

- Levies.
- The application of the acquisition method under IFRS 3.
- Restructuring plans.

### EFRAG's response to constituents' comments

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EFRAG noted that many constituents were uncertain about the consequences of the definition of a liability and the supporting guidance.

EFRAG sought further input on the definitions of assets and liabilities in its questionnaire on these. EFRAG would provide the IASB with the results of this additional input.

EFRAG noted that some constituents did not agree with EFRAG's position on when a restructuring obligation should be recognised. EFRAG, however, noted that it had consulted its User Panel on the issue, and had based its views on this input. EFRAG therefore decided not to change its view on this issue.

- Repairs and maintenance (including the impact of “no practical ability to avoid transfer”).

Some constituents agreed with the ED. Some constituents did not.

One constituent thought a liability was generally defined too narrowly (for example, where an entity could avoid paying bonus to an employee but this would not be beneficial in the long run), although there could be instances when it might be defined too broadly and would result in expenses relating to a later period being recognised. The constituent suggested defining three categories of liabilities: legally enforceable obligation, constructive obligations and certain other planned future outflows arising from past events. The third category would be intended to cover liabilities related to expenses such as levies, bonuses and some pension costs that are incurred in earning the income of the reporting period, but that do not necessarily give rise to what can be regarded as a ‘present obligation’, in the ordinary sense of these words, at the balance sheet date.

Another constituent thought that an obligation would exist where any action that is practicably available to the entity is more adverse, even by a small amount, than the transfer itself, rather than ‘significantly’ more adverse. In addition, an obligation that an entity has the practical ability to avoid through its future actions is a present obligation until that action is taken, however, the practical ability should be reflected in its measurement. Where the future action involves no transfer of economic benefit, the liability would be measured at nil.

One constituent did not think that the point at which an entity has ‘no practical ability’ to avoid a transfer would necessarily coincide with the accounting period that ought to reflect the benefits received. Unless expenses would be recognised as they accrued, the income statement would give less useful information, both for assessing performance during the period and for forecasting future performance.

One constituent did not think that an entity receives benefits from all transactions. The constituent suggested that the Conceptual Framework should discuss items such as levies and taxes that come into the category of non-reciprocal transactions, but which are important features of business activity.

Some constituent suggested to use the term 'no realistic alternative' instead of "no practical ability to avoid".

One constituent was concerned that a liability for a levy should be recognised for the period it would take to cease operating in the market, which may be more than one year. Another constituent thought that guidance on a liability seemed like an attempt to address issues related to levies rather than an attempt to provide conceptual guidance.

One constituent thought that the proposed definitions did not result in a useful outcome for deposit guarantee schemes as the constituent thought the expenses to these should be distributed evenly over a calendar year. Another constituent did not think that the proposed guidance would result in useful information for co-operatives in relation to their shares. This constituent did therefore not support the proposal.

One constituent thought the IASB had to further consider the relationship to economic compulsion. Another thought that some of the guidance on economic compulsion included in the Basis for Conclusions should also be included in the Conceptual Framework.

One constituent was concerned that some constructive obligations that were currently recognised would not meet the definition of liabilities and would therefore not be recognised (e.g. it was not clear that there would be economic consequences for not reinstating environmental damage in the absence of a legal requirement).

One constituent disagreed with EFRAG and did not prefer to recognise unannounced restructuring provisions due to the considerable degree of judgement involved.

One constituent noted that some of the specific examples in IAS 37 would not be in line with the proposed guidance in the ED.

One constituent thought that the IASB should consider adding a specific discussion on non-reciprocal transactions (e.g. transactions with the government) in the Conceptual Framework.

One constituent thought that an obligation to refrain from an activity could also give rise to a liability (e.g. a non-compete contract).

## Question 5 – Other guidance on the elements

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its consultation document, EFRAG disagreed with how the ED dealt with executory contracts. EFRAG was uncertain about whether the discussion on the unit of account provided sufficient guidance for the IASB and thought that the unit of account for measurement decisions and recognition decisions should generally be the same.

#### *Constituents' comments*

##### Executory contracts

On the guidance on executory contracts, some constituents generally agreed with the ED. Some constituents did not.

One constituent thought that the guidance was confusing and seemed inconsistent with IAS 32 *Financial Instruments: Presentation*.

One constituent thought that the guidance on executory contracts should be included in the unit of account guidance as it was primarily a unit of account issue.

Some constituents thought that the guidance was better explained in the Basis for Conclusions than in the ED. One of these constituents noted that the ED gave the impression that there could be further, unspecified, criteria which come into play and could result in an executory contract's being recognised even when not onerous.

One constituent agreed with EFRAG that the proposed guidance was difficult to understand.

Some constituents did not agree with EFRAG's suggestion to consider whether entering into a contract was a core transaction. One constituent noted that entering into a contract, as opposed to fulfilling it, was not a core transaction for derivatives dealers. Nor was fulfilling a contract a core transaction for a supplier of goods or services and entering into the contract

### EFRAG's response to constituents' comments

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#### Executory contracts

EFRAG noted that some constituents disagreed with the suggestion included in its Document for Public Consultation that the treatment of executory contracts should depend on whether entering into a contract was a core transaction or not. EFRAG accordingly decided not to include this suggestion in its comment letter.

EFRAG, however, thought that it was important that some guidance would be included in the Conceptual Framework to prevent executory contracts that were currently not recognised being recognised in the future. EFRAG assessed that the current practice on executory contracts worked well and did not see any reason to change this.

EFRAG agreed that it could be argued that, at inception of a contract, rights and obligations would have equal value. However, EFRAG noted that this would not necessarily be the case after the inception.

EFRAG did not think that day one gains and losses on executory contracts generally resulted in useful information. EFRAG therefore decided not to change the view expressed in the Document for Public Consultation on the relationship between initial and subsequent measurement.

EFRAG noted that some constituents thought the guidance on executory contracts was better explained in the Basis for Conclusions accompanying the ED. EFRAG agreed with this view. However, as EFRAG thought that the guidance needed to be revised in order to have a more robust basis for not recognising most types of executory contracts, it did not recommend the Basis for Conclusions to be reflected in the Conceptual Framework.

was not. The constituent thought that the concept of a core transaction was new and could result in confusion. Instead, a constituent suggested that the Conceptual Framework should state that if the exchange is neither favourable nor unfavourable to the entity, the contract is recognised at a net zero (or not recognised)

One constituent did not agree with EFRAG that initial and subsequent measurement of an executory contract had to be the same.

One constituent did not agree with EFRAG as the constituent considered an executory contract to be an asset or a liability and it seemed odd if it should only be recognised if it was onerous. As a derivative should be recognised, it seemed natural to also recognise an executory contract regardless of whether it would be an asset or a liability. Similarly, one constituent saw no reason to separate executory contracts that were equally unperformed from the definitions of elements. Rights to receive goods or services and obligations to perform work were the same regardless of whether cash had been transferred and those rights and obligations could not be excluded from the resources and claims, if the financial information is to be complete, the constituent argued. The constituent acknowledged that rights and obligations in equally unperformed contracts were interdependent as was stated in the ED, but they could not be separated and therefore constituted a single right or obligation.

On the other hand, a constituent thought that the Conceptual Framework should state that executory contracts should not be recognised unless onerous. The constituent believed this would be in accordance with prudence and the realisation principle).

One constituent note that at the inception of a contract rights and obligations have equal value and consequently should not be recognised in the financial statement.

#### Unit of account

Some constituents generally agreed with the guidance in the ED on the unit of account. Others thought the guidance needed further development.

One constituent thought that the Conceptual Framework should establish the principle that the same unit of account should be used for both recognition and

#### Unit of account

Based on its test of the guidance on the unit of account, which was included in EFRAG's Document for Public Consultation, EFRAG agreed with the constituents that thought better guidance was needed on the issue.

EFRAG also agreed with the comment that the unit of account for recognition should be the same as the unit of account for measurement.

On the other hand EFRAG did consider that it could be useful to have information about certain aspects of a particular asset or liability or a group of assets and liabilities provided in the notes to the financial statements. Similarly, EFRAG thought that different assets could be grouped for presentation in the financial statements. EFRAG therefore agreed with the ED (and not with the constituent) that a selected unit of account may need to be aggregated or disaggregated for presentation or disclosure.

EFRAG agreed with the comment that the unit of account should not be established after developing recognition and measurement guidance for that unit of account.

measurement or, that when the unit of account was defined at a different level for recognition and measurement within a standard, the IASB should include its rationale and justification in the Basis for Conclusions.

Some constituents disagreed with the ED that a selected unit of account may need to be aggregated or disaggregated for presentation or disclosure purposes.

One constituent believed that the unit of account may also have impact on the existence of an asset or liability, and should not be assessed in relation to only recognition and measurement (pensions and rate-regulated activities were mentioned as examples by the constituent).

One constituent thought that the unit of account should be developed before developing recognition and measurement guidance for that unit of account.

One constituent was concerned that there could be conflicts between what was proposed in the ED and the US guidance on how to determine the unit of account in the oil industry.

## Chapter 5 – Recognition and derecognition

### Question 6 – Recognition criteria

#### EFrag's tentative views and constituents' comments

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##### *EFrag's Document for Public Consultation*

In its consultation document, EFRAG broadly agreed with the guidance on recognition. However, in some areas EFRAG was concerned that the guidance proposed was insufficient to ensure consistent standard setting in the future.

##### *Constituents' comments*

Some constituents (generally) agreed with the ED.

Some constituent agreed with removing the recognition criteria of the current Conceptual Framework, but thought they should be replaced with more rigorous guidance, than that proposed in the ED.

One constituent thought the guidance was unclear and was uncertain about the consequences. This constituent thought that the IASB should explore the possible consequences of the criteria for preparers developing an accounting policy in accordance with paragraphs 10 – 11 of IAS 8. The constituent was concerned that the guidance could, in some circumstances, lead to recognition of a broad range of assets and/or liabilities that were not covered by individual Standards. The constituent thought that there should be additional guidance on when recognising an asset - where there was low probability of an inflow or an outflow - would not result in relevant information..

Another constituent had similar views in relation to uncertainties more generally. This constituent thought that the Conceptual Framework should include some recognition criteria related to the uncertainties mentioned in the ED (existence uncertainty, uncertainty about inflows or outflows and measurement uncertainty). The constituent believed that these uncertainties could be so serious that recognition of an item would be neither relevant nor faithfully representative. The constituent therefore agreed with EFRAG that there should be more substantive guidance on the matter. Another constituent thought, that the discussion on measurement uncertainty should be included within the section on faithful representation.

#### EFrag's response to constituents' comments

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EFrag noted that some constituents thought that different types of uncertainties should affect recognition and the guidance in the ED was not clear on this issue. EFRAG agreed with these comments.

EFrag considered whether the Conceptual Framework should include recognition criteria similar to the current Conceptual Framework (recognition thresholds). EFRAG could see some merits in this, but was concerned that there would be too many departures from those criteria in standard setting for the criteria to be sufficiently conceptual for a Conceptual Framework. EFRAG therefore agreed with a constituent that did not support a general use of the probability thresholds, but thought that the Conceptual Framework could state that the threshold could be appropriate in Standards. EFRAG, however, also assessed that the guidance included in the ED would not be sufficient to establish a consistent basis for recognition.

In relation to the comment on the recognition of stand-ready obligations, EFRAG noted that under current practice these would sometimes be recognised as part of a related asset. This could, for example, be the case when an entity purchased an asset including a general warranty that the asset would be fit for purpose.

EFrag thought that the three dimensional view model presented by one constituent dealt with more than recognition. The model also seemed to deal with performance reporting and presentation. EFRAG thought that this was one of the models that could be considered in the forthcoming debate about performance reporting. However, as it was just one out of several models that could be further explored, EFRAG decided not to make an explicit reference to the model in its comment letter.

One constituent thought that low probability of existence could not only be an indicator of non-relevance, as stated in the ED, it would be an indicator of non-relevance.

Some constituents preferred the probability threshold included in the current Conceptual Framework. The reasons provided were:

- The suggested criteria required too much judgement.
- Assets and liabilities should not be recognised when their realisation and the amount at which they expect to be realised were very uncertain.
- Users of financial statements were interested in the probable consumption of resources, not in financial data which report elements that remain highly improbable of realisation.
- Using judgement to determine whether a recognition threshold had been met was simpler and more reliable than making the judgements necessary to determine a measurement based on all reasonably possible expected outcomes.
- An approach that imposed the systematic tracking, collecting, and processing of information for recognising elements with a remote likelihood of occurrence did not pass the overall cost/benefit objective.

One constituent was concerned that without recognition criteria, assets arising from the stand-ready obligation of another party should be recognised and measured even though it would be very uncertain what the measurement would be.

Some constituents did not support a general use of the probability thresholds, but thought that the Conceptual Framework could state that the threshold would be an appropriate mechanism in particular standards to operationalise professional judgement as to whether a present obligation or an economic resource existed, i.e. to operationalise existence uncertainty in light of cost/benefit considerations.

One constituent disagreed with using 'control' as the basis for recognition

Some constituents came with alternative suggestions for recognition criteria.

EFRAG was not in favour of stating in the Conceptual Framework that a measurement reliability criterion would be fulfilled more often for financial instruments than for non-financial operating liabilities. EFRAG did not consider such a criterion to be sufficiently conceptual without explaining the special characteristics of financial instruments that would result in the reliability criterion being met more often for these than for non-financial operating liabilities.

EFRAG agreed with the comment that it should be highlighted more prominently that items that fails the recognition criteria still might need to be disclosed where information about these items provides relevant information to users.

EFRAG also agreed with the comment that the cost-constraint should not be mentioned particularly in relation to recognition as it is pervasive to all areas.

EFRAG noted that one constituent was uneasy with a principle of not recognising a present obligation that was subject to a high degree of measurement uncertainty, as lenders and creditors would be interested in knowing that retained earnings would not be available for distribution. EFRAG, however, thought that if the measurement uncertainty would be high, lenders and creditors could be misled by a specific number in the financial statements, as this figure would not reflect the related uncertainty surrounding its estimation.

In relation to the comment included in EFRAG's Document for Public Consultation on how to avoid accounting mismatches, EFRAG noted that its proposal would not conflict with the definitions of elements. The proposal would provide guidance on when it would be relevant to recognise an asset or a liability and/or how to measure these. The proposal included in EFRAG's Document for Public Consultation would thus provide additional guidance, but not be in conflict with the principles included in the Conceptual Framework.



One constituent suggested a starting point for a model for recognition based on a three dimensional view of the entity's controlled resources and present obligations:

- The resources and present obligations recognised in the financial position where the net position represent the undistributed earnings and contributions from owners.
- Resources and present obligations from contracts that are unperformed (the net position does not represent earnings, but committed future net cash flows). Such information could provide useful information if presented in a collective statement in the notes.
- Other controlled resources and present obligations, not included in any of the above (most of the items included here are those that are difficult to measure and information about them would in many cases be provided in a narrative form if found relevant to disclose, since the values could be debated indefinitely).

The dimensions would be different for entities with different business models.

One constituent thought that when both the probability and the amount could be measured reliably, then an asset or a liability could be recognised even if the outcome would not be probable (not more likely than not). Measurement reliability should be assessed in relation to different kinds of assets and liabilities and the Conceptual Framework should state that the measurement reliability criterion would be fulfilled more often for financial instruments than for non-financial operating liabilities.

One constituent thought that the Conceptual Framework should state the principle that all assets controlled by an entity and all liabilities resulting in a present obligations for the reporting entity as a result of a past event should be recognised. However, exceptions to this principle should also be formulated.

One constituent thought that it should be highlighted more prominently that items that fail the recognition criteria might still need to be disclosed where information about these items provide relevant information to users.

One constituent disagreed with mentioning the cost-constraint as a separate element of the recognition criteria as it was pervasive to all areas. Another constituent was uncertain about whether the cost constraint should be assessed only when an item first arises, or whether it should be assessed on an ongoing basis. A third constituent thought that it should be clarified that preparers could not use the cost constraint as an excuse for not recognising an asset or a liability.

One constituent thought that the discussion should note that recognition was a continuous process, as the cost constraint may delay recognition up to a certain point in time.

One constituent thought it was inconsistent that the ED stated (paragraph 5.18) that even if the probability of an inflow or outflow of economic benefits was low, recognition of an asset or a liability might provide relevant information and at the same time stating that (paragraph 5.19) it in some cases it would not be useful to recognise assets and liabilities with very low probabilities of inflows and outflows of economic benefits.

One constituent was uneasy with a principle of not recognising a present obligation that was subject to a high degree of measurement uncertainty. If the existence of a present obligation was certain and an outflow of significant economic resources was probable, the constituent thought that an amount in any case should be reserved in the financial position as it would be in the interest of lenders and creditors that retained earnings in equity would not be available for distribution. However, only 'most likely amounts' should be recognised.

One constituent did not agree with EFRAG that the definitions of elements, recognition and measurement could be set aside in order to avoid an accounting mismatch.

## Question 7 – Derecognition

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its consultation document, EFRAG agreed with the guidance derecognition suggested in the ED.

#### *Constituents' comments*

Some constituents (generally) agreed with the ED (and hence EFRAG).

Although generally agreeing with the proposal, one constituent believed that the Conceptual Framework should explicitly refer to the "risk and rewards" notion instead of using new terms like "positive or negative variations". Similarly another constituent thought that the reason for not derecognising an asset should be the continued exposure to risks and rewards, rather than the fact that the asset must or may be reacquired. A third constituent thought that the Conceptual Framework should better articulate the distinction between control and risk and rewards.

One constituent thought that the Conceptual Framework should recognise the potential conflict between 'risks and rewards' and 'control' and that resolution of this conflict should be addressed at a standard level.

Some constituents disagreed with EFRAG's response as they thought that derecognition requirements should mirror the recognition criteria.

One constituent thought the notion of substance over form should be introduced in relation to derecognition.

One constituent agreed with the approach of the ED that the Conceptual Framework should not be definitive but solutions should be developed at the standards level. However, the constituent thought that the IASB should then compare the conclusions in these areas across standards and be clear why there are the same or different.

### EFRAG's response to constituents' comments

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EFRAG noted that constituents broadly agreed with the ED and hence the response provided in EFRAG's Document for Public Consultation. After considering the comments in relation to recognition, EFRAG, however, became uncertain about whether the guidance in relation to derecognition would also be insufficient as a basis for consistent future standard setting.

EFRAG did not agree with the comment that there should be a direct reference in the Conceptual Framework to 'risks and rewards' instead of 'positive or negative variations'. EFRAG thought that 'positive or negative variations' captured the concept of 'risks and rewards' and at the same time provided more guidance on what the concept meant.

## Chapter 6 – Measurement

### Question 8 – Measurement bases

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG broadly agreed with the categorisation proposed in the ED and with the ED's description of the information provided by each of the measurement bases. However, EFRAG thought that the Conceptual Framework should consider the possible use of market-consistent measurement bases other than fair value.

##### *Constituents' comments*

Some constituents explicitly stated general support for EFRAG's comments. One of these constituents did, however, not understand the section on the description of the information provided by each of the measurement bases included in EFRAG's Document for Public Consultation.

Some constituents (generally) agreed with the ED.

However, some constituents did not think that dividing between 'historical cost' and 'current value' was the best approach. One noted that it resulted in current cost being discussed under the heading of historical cost. A better division would be between entry values and exit values. One constituent did not agree that current cost should be discussed under the heading of historical cost. Another noted that these were the two extremes and therefore not helpful for the explanation of existing measurement approaches in current IFRS.

Some constituent also thought that the Conceptual Framework should deal with more complex measurement bases such as 'lower of cost and net realisable value' and 'lower of cost and recoverable amount'. A constituent noted that the 'historical cost' basis used a current exit value, such as fair value or net realisable value or value in use.

Another constituent thought that the Conceptual Framework should provide an underlying rationale for historical cost measurement, consider the implications of changing prices and address issues such as deprival value, current cost and cost of release.

#### EFRAG's response to constituents' comments

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EFRAG noted that there was general support for the proposals included in the ED and hence the view expressed in EFRAG's Document for Public Consultation.

On the comment that a dividing between 'historical cost' and 'current value' was not the best approach, EFRAG noted that it did not agree that such a division would result in current cost being discussed under the heading of historical cost. EFRAG acknowledged that this was the case in the ED (and it followed from how the measurement bases were explained in the Discussion Paper preceding the ED), but EFRAG did not think it was a result of the division. It was rather a result of how the ED considered 'historical cost'. EFRAG, however, thought that the Conceptual Framework should consider exit values and entry values and decided to keep that comment in its comment letter. Based on the comments received, EFRAG also acknowledged that in some cases it was difficult to assess whether a measurement basis should be considered a 'historical cost' measurement basis or a 'current value'. EFRAG accordingly decided to ask the IASB for clarification in these circumstances.

EFRAG agreed with the comments that the Conceptual Framework should also address more complex measurement bases such as 'lower of cost and net realisable value'.

For the reasons explained in its Document for Public Consultation, EFRAG thought that the Conceptual Framework should discuss market based measures other than those presented in the ED.

EFRAG agreed with the comment that up and down movements in the market might not at all influence future cash flows. That was why EFRAG considered that the business model should be taken into account when deciding on the most useful measurement basis.

One constituent did not support EFRAG's comments on the need for alternative market based measures other than those presented in the ED. On the other hand, one constituent supported EFRAG's comments on transactions costs.

Some constituents did not agree with the characteristics the ED assigned to the different measurement bases. One constituent did not think that fair value had either predictive value or confirmatory value. The constituent argued that fair value was measured as a hypothetical market participant might measure the item. Market participants and the markets move up and down depending on a lot of things that might not influence the future cash flows of the entity.

In relation to fair value, one constituent also thought that it should not be explained as the price that *would* be received or paid, but as the price that *may* be received or paid. The participant thought that this would be a logical consequence of re-introducing prudence. 'Would' reflected the idea that an estimate could be neutral.

One constituent thought that the following disadvantages of current value should also be mentioned:

- Recognising unrealised gains can be considered less prudent.
- Fair value results in fluctuations in earnings not driven by the management's actions in the period.
- Fair value may not be relevant if the management has no current intentions to dispose an asset.
- It may be highly uncertain that an estimated fair value represents the price an entity would actually receive in a transaction, as eventually the price is the result of negotiations, where many factors are unpredictable.

One constituent thought that the following advantages of historical cost should also be mentioned:

- The deferral of gains until realised is a prudent approach, when an asset is not readily realisable, or the management has no current intentions to dispose an asset.

EFRAG also agreed with the comment that fair value could be a hypothetical market measure. EFRAG thought that it was therefore important to consider faithful representation when selecting a measurement basis.

EFRAG did not agree with changing the explanation of fair value from the price that *would* be received to the price that *may* be received. EFRAG agreed that the measure would only reflect a value that might have been received. Nevertheless for standard setting purposes 'may' was a too broad term. When setting standards the aim should be to try to reflect what would have been received.

EFRAG did not think that it could be argued that recognising unrealised gains could be considered imprudent following the explanation of prudence included in the ED.

EFRAG also did not agree with a general statement that fair value resulted in fluctuations in earnings not driven by the management's actions. EFRAG thought that it would often depend on an entity's business model whether or not the fluctuations in earnings would reflect the management's actions in the period. EFRAG also noted that some fluctuations in fair value could be hedged. The fair value changes would accordingly reflect management's actions (decision to hedge or not to hedge).

EFRAG agreed with the comment that fair value might not necessarily be relevant if the management had no intentions to dispose of an asset. This would be resolved if the business model would be considered when selecting a measurement basis. EFRAG acknowledged that the business model was not the same as the management's intent. EFRAG was not comfortable about letting management's intent determine how to account for various items.

EFRAG did not think the Conceptual Framework should provide guidance on whether the equity method is a historical cost or a current value measurement. EFRAG thought this was too specific an issue to be considered in the Conceptual Framework.

- If the view is that fair value increases the comparability between entities, the opposite can be said for historic cost: it reveals the differences.

One constituent noted that there had never been a proper debate in Europe on the use of fair value versus cost or other measurement bases, and thought that EFRAG should lead such a debate.

One constituent agreed with EFRAG that it should be explained when own credit changes would be relevant and thought this issue should be highlighted in EFRAG's comment letter by including the issue in the box summarising EFRAG's answer to the question.

One constituent thought that, without prejudice to the future decision whether the equity method was a measurement method or a consolidation technique, the Conceptual Framework should clarify whether it would be a current value measurement base or a historical cost measurement base.

Some constituents had comments on the table in the ED that summarised the information provided by different measurement bases. One thought it should be clarified as it could, for example, be confusing that the description of the historical cost refers to "recoverable" cost. This could give the impression that the measure referred to the amount that could be recovered from the asset, which might be understood as a current value measure.

Some constituents did not believe that table 6.1 should be included at all. One noted that it was too summarised and therefore not suitable for a conceptual framework. However, the constituent thought that the advantages and disadvantages of the different measurement bases should be presented in a table. Another constituent thought the table could be included but needed to be complemented by a more detailed explanation.

Some constituents shared EFRAG's view that the cash-flow based measurement techniques should not be considered as a separate measurement basis. One constituent, however, thought that it should be clarified that the cash-flow based measurement technique could be used for both types of current value measures.

One constituent thought that it was difficult to distinguish amortised cost from current value.

EFRAG noted that some constituents had difficulties when reading Table 6.1. EFRAG therefore agreed that some aspects with the table could be clarified. EFRAG did not consider the table to be too summarised to be useful for the Conceptual Framework.

EFRAG did not think that the term 'amortised cost' should be used instead of 'historical cost'. EFRAG thought that the term 'historical cost' was broader than 'amortised cost'. 'Amortised cost' was used for financial assets, but, for example, not in relation to property, plant and equipment.

Some constituents thought that the term 'amortised cost' should be used instead of 'historical cost'.

## Question 9 – Factors to consider when selecting a measurement basis

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document, EFRAG thought that the ED did not provide sufficient guidance on what measurement bases are useful for reporting financial position and what are useful for reporting performance; when to select between market-consistent and entity-specific measurement bases; and when customisation of measurement bases could be useful. However, it was suggested that the IASB could build on the description of different measurement bases to determine the necessary guidance. The consultation document included a question to constituents on what aspects should help the IASB when the different factors listed in the ED would conflict.

#### *Constituents' comments*

One constituent agreed explicitly with the factors EFRAG thought the Conceptual Framework should provide answers on.

Some constituents generally agreed with the ED on proposed factors to be considered when selecting a measurement basis, but more constituents did not think that the ED provided sufficient guidance on the selection of measurement bases and when a customised measurement basis would be relevant.

One constituent explained that the guidance was insufficient because of the lack of a specific description of the linkage between the measurement bases and the factors to be considered when selecting a measurement basis, and the lack of guidance on the relative importance of each of the factors.

Some constituents noted that the ED did not further analyse what information meets the qualitative characteristics from the perspectives of the statement of financial position and the statement(s) of performance.

One constituent thought that the fundamental building blocks for addressing measurement were missing (e.g. when entity-specific value should be used instead of a market value and if the amount should be discounted, and if so, what discount rate should be used and whether this should take credit risk into account).

### EFRAG's response to constituents' comments

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EFRAG noted that relatively many constituents did not consider the guidance included in the ED sufficient. EFRAG agreed with this.

EFRAG did not think the solution would be to decide on a default measurement. The feedback that the IASB had received in response to its discussion paper preceding the ED showed that constituents preferred a mixed measurement approach. EFRAG thought that a default measurement approach would conflict with this.

EFRAG could probably see a use for fair value for assets and liabilities other than those that are readily realisable (as suggested by one constituent). For example, if certain assets are used as an economic hedge of a long-term liability.

Similar to EFRAG, some constituents thought that the Conceptual Framework should explain how the relative importance of the two factors that affects relevance (the manner in which assets and liabilities contribute to future cash flows and the characteristics of the assets and liabilities) should be assessed.

EFRAG noted that while some constituents thought that the manner in which assets and liabilities contribute to future cash flows / the business model was the most important factor to consider, other constituents thought that both the manner in which assets and liabilities contribute to future cash flows and the characteristics of the assets and liabilities were important. Based on this, EFRAG decided not to include a recommendation on what to do in case the two factors conflict.

EFRAG agreed with the comment that the implications of the proposals included in the ED for accounting for agricultural activity were unclear. As, the guidance was considered insufficient, there were many other areas where the implications would be unclear.



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Some constituents thought that the guidance included in the Discussion Paper could have been more useful.

Whereas some constituents asked for more guidance, one constituent did not want the Conceptual Framework to tie the hands of the IASB on the selection of appropriate measurement bases when it is preparing standards.

One constituent thought that the factors specific to initial measurement that were discussed in the ED were too detailed for the Conceptual Framework.

Some constituents provided suggestions for how the section could be improved.

One constituent thought that the measurement guidance would be more practical if there was a single measurement basis that would be used by default. One constituent thought that default measurement should be historical cost as, in most cases, a cost-based measurement would be preferable as it provided the most useful information for the statement of profit or loss.

Similarly, one constituent found that fair value should only be used as measurement basis for assets that are readily realisable.

One constituent thought that the section could be improved by including that the relevance of the selected measurement basis to performance reporting is enhanced by its linkage to how cash flows are generated by the business activities.

Similar to EFRAG, some constituents thought that the Conceptual Framework should explain how the relative importance of the two factors that affects relevance (the manner in which assets and liabilities contribute to future cash flows and the characteristics of the assets and liabilities) should be assessed..

Some constituents thought the manner in which assets and liabilities contribute to future cash flows / the business model was the most important factor to consider, but not the only factor. However, other constituents thought that both the manner in which assets and liabilities contribute to future cash flows and the characteristics of the assets and liabilities were important.

One constituent thought, in relation to stewardship, that the choice of measurement basis may depend on whether users need to assess past or future management performance.

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and EFRAG decided that it would not mention agricultural activity specifically in its comment letter.

EFRAG agreed with the constituent that disagreed with paragraph 6.57 of the ED.

EFRAG did not want to restrict the use of measurement at current value for non-financial assets to limited types of assets. However, it could be that useful guidance for the selection of measurement bases would have this effect, and EFRAG would support the development of more useful guidance for the selection of measurement bases.

One constituent thought that the implications for accounting for agricultural activity were unclear.

One constituent did not agree with paragraph 6.57 of the ED that an estimate can be a faithful representation if it is described as being an estimate and if the nature and limitations are explained and if no errors have been made. The constituent thought that in certain circumstances, the estimation of a fair value is so difficult and arbitrary (in Level 3 fair value measurement for example) that it is questionable whether such an estimate should always be used for the financial statements, even if very extensive disclosure is provided.

One constituent thought that the measurement of current value for non-financial assets based on discounted cash-flow models was too widely accepted (e.g. the impairment test of goodwill). It should be restricted to limited types of assets.

## Question 10 – More than one relevant measurement basis

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document, EFRAG disagreed with considering the use of different measurement bases as an exception as, in some cases, reflecting the business model in measurement will lead to different measurement bases used for the statement of financial position and the statement of profit or loss.

#### *Constituents' comments*

One constituent agreed explicitly with EFRAG that there are cases where one measurement base is relevant and that these cases should not be referred to as an exception.

Some constituents also agreed that sometimes more than one measurement basis would be needed. Some of the arguments provided were:

- The current uses of OCI provides useful information.
- More relevant information is provided by using a current value measurement basis in the statement of financial position and a different measurement basis to determine the related income or expenses in the statement of profit or loss.

One constituent noted that OCI should not be regarded as a facilitator for the use of a dual measurement, but should be taken as a trigger for the IASB to re-examine and confirm that the measurements selected were really the most relevant. The IASB should also consider whether it would not be better to provide information in the notes rather than to use two different valuations on the balance sheet and in profit or loss.

Similarly, other constituents thought that in most cases only one measurement bases should be used. Arguments provided were:

- There are costs associated with reporting double measures.
- Different measurements could confuse users.

### EFRAG's response to constituents' comments

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EFRAG noted that its Document for Public Consultation perhaps expressed a too positive attitude towards the use of different measurement bases in the statement of profit or loss and the statement of financial position considering the comments of constituents.

As EFRAG agreed with the ED that use of a current value could not be relevant for the statement of profit or loss, if it was not relevant for the statement of financial position, EFRAG decided to describe its position similar to one of its constituents. That is, the same measurement should be applied for the statement of profit or loss and the statement of financial position. However, income and expenses arising from the chosen measurement basis may be analysed into their component parts in the statement of profit or loss and OCI where this provides useful information.

EFRAG decided not to address how often it would be useful to separate the different components. The answer to that question would depend on what information the statement of profit or loss (and the statement of financial position) should present. The answer to that question might also answer the question whether disclosure of amounts based on an alternative measurement basis in the notes would be sufficient.

Some constituents did not support the idea of using different measurement bases for financial position and profit and loss. Reasons provided were:

- It would be difficult to understand and OCI would become even more incomprehensible to management and many users.
- It seems to be just a convenient mechanism for simultaneously applying different views about the appropriate measurement basis for a particular item, in order to reconcile those who take opposing views as to the primacy or importance of the statement of financial position or the income statement.
- Amortised cost would provide more useful balance sheet information for debt financial instruments held within a business model with an objective of both collecting and selling than fair value through OCI.

One of these constituents, however noted that income and expenses arising from the chosen measurement basis may, nonetheless, be analysed into their component parts in the statement of profit or loss and OCI where this provides useful information. And this analysis might be driven by different measurement bases, although other factors might drive disaggregation, as they do, for example, with defined benefit pension accounting. A routine disconnection between the statement of financial position and the statement of profit or loss should, however, not be acceptable.

Some constituents thought that before additional guidance could be provided on when it would be relevant to use different measurement bases the purpose of the statement of profit or loss and statement of OCI had to be clearly defined.

One constituent disagreed with EFRAG that it may provide the most useful information to measure assets and liabilities at current values in the statement of financial position but to record fair value gains and losses in OCI rather than in profit or loss. The constituent disagreed with the current requirements in IFRS 9 on fair value through OCI (but had accepted it as a compromise). The constituent thought that it was misleading to report fair value gains and losses, even in OCI, which were unlikely to be realised through sale. For instruments where fair value information would be useful, it should be provided in the notes.

One constituent thought that the Conceptual Framework should provide guidance on when the disclosure of amounts based on the alternative measurement basis in the notes would be sufficient.

## Chapter 7 – Presentation and disclosure

### Question 11 – Objective and scope of financial statements and communication

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its public consultation document, EFRAG agreed with the proposals included in the ED on the objective and scope of financial statements and communication. However, it was thought that the IASB should consider how to distinguish between presentation and disclosure.

##### *Constituents' comments*

Some constituents generally agreed with the ED (and hence EFRAG's response).

Some constituents agreed with EFRAG's Document for Public Consultation that the IASB should consider how to distinguish between 'presentation' and 'disclosure'.

Some constituents thought that greater prominence should be given to the statement of cash flows in paragraph 7.2 of the ED which discussed what the financial statements should provide information about. Similarly, one constituent suggested another term than financial performance should be used when referring to the income statement only as the cash flow statement was also important for assessing performance.

Some constituents thought that the objective of each statement should be specified, and one constituent suggested the following objectives:

- Statement of net income is dedicated to depicting the performance of the entity over a specific period, showing the consequences of the management's actions in using the entity's resources and discharging its responsibilities.
- Statement of financial position is dedicated to providing a picture of the entity's economic resources (assets) and claims/potential claims of third parties on these resources (liabilities), as generated by its past performance and to be used in its future performance.

#### EFRAG's response to constituents' comments

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Based on the comments received, EFRAG decided to keep the comment that the Conceptual Framework should distinguish between 'presentation' and 'disclosure'.

EFRAG agreed with the comments that greater prominence should be given to the statement of cash flows in the Conceptual Framework.

EFRAG also agreed that it would be a good idea to specify the objective of each financial statement. EFRAG, however, thought that this would be part of the work with defining/describing what performance, profit or loss and/or OCI is. EFRAG, accordingly, thought it was too early to either support or reject the objectives suggested by one of the constituents.

EFRAG thought that the ED made clear that entity-specific information is more useful than 'boilerplate' language. It did not consider that it was necessary to comment on how the ED considered 'boilerplate' language in its comment letter.

EFRAG considered that it would neither help the IASB in its future standard setting nor constituents in applying the Conceptual Framework through the reference in IAS 8 to state the relationship between profit or loss, OCI and total comprehensive income. EFRAG accordingly decided not to include such a recommendation in its comment letter.

EFRAG thought that it would sometimes be useful to provide certain information about transactions and events that have occurred after the end of the reporting period. It could, for example, be relevant to inform about essential assets that existed on the balance sheet date that have been lost (e.g. as a result of a natural disaster). EFRAG agreed with the comment that the Conceptual

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One constituent thought that the objective of presentation of financial statements should also be to clarify the linkage between the primary financial statements.

One constituent thought that it should be clarified (paragraph 7.18 of the ED) that 'boilerplate' language is not useful and the Conceptual Framework should therefore not give the impression that in some circumstances it could be useful.

One constituent thought the relationship between profit or loss, OCI and total comprehensive income should be mentioned in the Conceptual Framework.

Some constituents disagreed that primary financial statements should provide certain information about transactions and events that have occurred after the end of the reporting period (paragraph 7.6 of the ED). The constituents believed this contradicted the clarification that forward-looking information was generally provided outside the financial statements, for example in the management commentary. Another constituent thought that the Conceptual Framework should more clearly describe when such information would be necessary.

One constituent did not think the guidance in the ED was particularly useful.

One constituent suggested that the description about the content and components of financial statements would be better placed in Chapter 3 *Financial statements and the reporting entity*.

One constituent thought it would be useful to establish separate objectives for the primary financial statements and the notes to help determine the content of each. This constituent also thought that the boundary of financial statements and that between the primary financial statements and the notes should be clarified.

One constituent was concerned that because more items would meet the definitions of assets and liabilities, more disclosures had to be provided as disclosures should also be provided for assets and liabilities that would not be recognised.

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Framework could more clearly describe when such information would be necessary.

EFRAG agreed that the IASB could consider whether the description about the content and components of financial statements were better placed in Chapter 3 of the Conceptual Framework.

## Question 12 – Description of the statement of profit or loss

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document, EFRAG supported the description of the statement of profit or loss proposed in the ED. However, it recommended that the IASB clarify what it means by 'return on an entity's economic resources'. The Document for Public Consultation asked for constituents' views on the dissenting opinions presented in the Basis for Conclusions accompanying the ED.

#### *Constituents' comments*

Some constituent supported the proposed definition of the statement of profit or loss included in the ED. One constituent noted that they had never seen any users using comprehensive income as a starting point to assess the performance of a group.

Some constituents thought that the IASB had failed to define 'profit or loss' or 'performance' or the objective of profit or loss in a manner that would make the description useful for standard setting.

One constituent suggested stating that the purpose of profit or loss is to depict the return that an entity has made on its economic resources in reflecting the business activities pursued by the entity and management's stewardship of the entity's resources during the period.

One constituent thought that the IASB should better articulate the notion of performance from the perspective of equity investors.

One constituent, however, thought it would be difficult to define performance given the many past attempts and one constituent could accept that the issue would be treated in a separate research project.

Some constituents provided suggestions for how to improve the guidance.

One constituent thought that the description could be improved by stating explicitly that profit or loss measures financial performance for the period.

One constituent thought it would be easiest to define what OCI was or what 'realised income' should mean.

### EFRAG's response to constituents' comments

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EFRAG noted that the lack of a clear definition of 'profit or loss' or performance generally resulted in lack of guidance on what should be reported in OCI and how to select the most useful measurement basis in a given situation. EFRAG therefore thought it was essential that the IASB would decide on these even though it would be difficult. In the view of EFRAG, the IASB should consider the business model to ensure that performance would not be reported in a manner that did not reflect an entity's business model. Although the business model should be one of the factors to consider, it would also be relevant to consider other factors.

Some constituents suggested that the IASB should consider to distinguish between profit or loss and OCI based on what income and expenses are realised. EFRAG, however, decided not to include such a suggestion in its comment letter as it did not think that a pure focus on realisation would provide useful information. Such a model would, for example, result in impairment losses not being reported until they are realised.

EFRAG did not think the Conceptual Framework should define distributable reserves. EFRAG considered that company law should regulate how much an entity can distribute.

EFRAG did not consider it beneficial to include the description of profit or loss in Chapter 6 of the Conceptual Framework. Chapter 6 in the Conceptual Framework is about measurement and EFRAG did not think a discussion about what should be reported in OCI would fit well into that discussion.

EFRAG's comments on the use of the 'matching principle' are provided in the comments related to Question 3.



One constituent suggested the following criteria for the recognition of elements in profit or loss for the period:

- Items recognised in net income, should be economically linked to the current period, using the ‘matching principle’ as a basis.
- If the application of the matching principle leads to the deferral of elements which do not satisfy the definition of an asset or a liability, then these could be recognised in OCI (such as, for example, a cash flow hedge).
- Items related to future cash-flows should be presented in net income only if they can be forecasted and the flows are probable (i.e. they have the potential to be realised and the value to be recognised should be close to what will actually be realised in the future). Where cash flows could be certain of being realised but at an amount that could be different from that reported in the statement of financial position, the amount certain of being realised would be recognised in profit or loss and the difference in OCI.
- Moreover, probability should be assessed in the light of the business model of the entity. Applying this approach to the profit or loss account, OCI would include the changes in the value of assets and liabilities for which the probability of the realisation of the future cash flows is still too low. This would thus include those elements referred to in the Discussion Paper preceding the ED as ‘transitional items’. Certain items referred to as ‘bridging items’ in the Discussion Paper would also qualify for this category when the amounts used for the balance sheet are not sufficiently certain of occurring for them to be recognised in profit or loss.

In its Document for Public Consultation, EFRAG asked for constituents views on the alternative views presented by two IASB members in the Basis for Conclusions accompanying the ED.

Some constituents disagreed with the dissenting views. The reason provided was that informational output of income disaggregation may be unduly complicated and difficult to comprehend. The cost of providing the information can therefore not be justified in terms of information usefulness. A better approach would not be to replace the use of OCI with disaggregation within the profit or loss account.

Some constituents, however, supported the dissenting views, as it was thought that it was necessary to define financial performance or specify the characteristics of income and expenses that require the presentation in OCI. If this is not done, the IASB is in effectively the same position that it is now. One constituent supported the alternative views of IASB members to define performance and only have one statement.

One constituent thought that the alternatives should be further examined. The constituent thought that one factor that is relevant to the discussion about persistence and different predictive values is the way that income and expenses contribute to future cash flows.

One constituent thought the Conceptual Framework should define distributable reserves.

One constituent thought that the IASB should also evaluate whether the financial statements should provide information that disaggregates the gains and losses between realised and unrealised.

One constituent thought that the section should include a reference to the business model as this was considered a key factor when considering defining what should constitute net income.

Some constituents had a similar comment as in EFRAG's Document for Public Consultation in relation to the use of the word 'return'.

One constituent suggested covering the discussion of profit or loss vs. OCI in Chapter 6 as part of performance measurement of the period.

## Question 13 – Reporting items of income or expenses in other comprehensive income

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its Document for Public Consultation, EFRAG disagreed with the IASB's proposal that profit or loss should be "as inclusive as possible", as this would mean that 'profit or loss' could not be retained as a primary measure of performance from the view point of European Constituents. EFRAG's public consultation document asked for constituents views on the dissenting views expressed in the ED and on whether the concepts used in the Discussion Paper preceding the ED ('bridging items'; 'mismatched remeasurements' and 'transitory remeasurements') should be included in the Conceptual Framework.

#### *Constituents' comments*

Some constituents thought that the proposals in the ED represented a step forward.

Some constituents agreed with the approach of the ED that the Conceptual Framework should not be definitive but solutions should be developed at the standards level. One of these constituents concluded that after years of debate and research, there was no single solid concept to justify the existence of all OCI items. The constituent therefore supported the very pragmatic approach of the IASB. Another of these constituents supported the IASB's approach, but thought that the IASB should compare its decisions about OCI across standards and be clear why it had reach similar or different conclusions.

Some constituents, however, thought that the uses of OCI needed to be explained further in the Conceptual Framework.

Some constituents thought that a definition of performance would be the first building block for developing a robust and clear basis for distinguishing between items that should be recognised in profit or loss and items that should be recognised in OCI. One constituent, however, thought that it would be difficult to defined financial performance.

One constituent thought that it might be more efficient to defer the development principles on the use of OCI to a separate project and to

### EFRAG's response to constituents' comments

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EFRAG noted that many constituents did not find the guidance included in the ED on the use of OCI satisfactory. EFRAG agreed with this.

In its Bulletin *Profit or loss versus OCI*, EFRAG had presented a model illustrating what items should be reported in OCI following one alternative of applying the business model. EFRAG noted that although many constituents thought that the business model should play a role when deciding what items should be reported in OCI, most of these constituents also thought that other factors should be considered. EFRAG decided to reflect this in its comment letter.

EFRAG also noted that constituents generally did not think that, many more items than currently should be reported in OCI, although there were a few exceptions. Some thought that OCI should be abolished. EFRAG accordingly considered whether to remove its opposition to the statement in the ED that profit or loss should be "as inclusive as possible". EFRAG, however, thought that without having clearer principles for what profit or loss should represent, the IASB could not state that profit or loss should be as inclusive as possible. EFRAG would, however, not reject a definition or description of profit or loss that would result in fewer items than currently being reported in OCI.

EFRAG noted that some users use OCI, but many considered it complex. EFRAG could therefore see merits in reporting everything in profit or loss as suggested by some constituents. EFRAG, however, also noted that it should be possible for many different types of users with different needs to use general purpose financial statements. Further, the same user may need information about different aspects of an entity. EFRAG thought that OCI might be useful for this purpose. From a cost/benefit perspective it would be sensible to use OCI instead of preparing different sets of financial statements useful for different purposes. EFRAG also thought that

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eventually update the Conceptual Framework based on the outcome of such project.

Some constituents provided suggestions for what should be reported in profit or loss.

One constituent thought that inflows and outflows which arise from the business model should be classified within profit or loss and other movements should be reported within OCI. Such a direct link back to the business model should result in companies making fewer adjustments to their reported results when discussing them with analysts.

Some constituents thought that OCI could be used for unrealised gains. This could help users understanding performance and the entity's capability to distribute dividends.

One constituent thought that OCI should be restricted to items that neither help to measure the current year's performance nor help to estimate future performance. The list might typically include only: gains on the revaluation of property, plant and equipment (PPE); gains on the sale of PPE, except where they are in substance corrections of accumulated depreciation; foreign currency translation adjustments on foreign subsidiaries; actuarial gains and losses on a defined benefit pension scheme; and fair value gains and losses on effective hedges.

One constituent thought that the use of OCI should be restricted to a limited number of cases in which either (1) a different measurement basis is judged appropriate for measuring income and expenses in profit or loss, compared with that best suited to the measurement of the asset or the liability in the statement of financial position; or (2) there is a mismatch in the recognition basis for different but economically related transactions.

One constituent thought that OCI should be defined as a link between net income and statement of financial position, especially for items recognised in financial statements but for which the probability of realisation is too low for them to be recognised in profit or loss. Reasons for such low probabilities of realisation could be:

- Realisation depends upon a further action or decision by the entity's management.

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the complexity of OCI would be significantly reduced by having clear principles for what it would represent. EFRAG therefore decided not to recommend that all income and expenses be reported in profit or loss.

EFRAG acknowledged that it might be possible to make the statement of profit or loss more useful by categorising income and expenses different from how it is done today. Such changes to the presentation might, however, not solve everything. What was special about OCI was the recycling. EFRAG thought that in some cases, for example in relation to cash flow hedges, it did result in useful information to report fair value changes in the statement of financial position, but including these changes in the statement of profit or loss at a later stage.

- The amount recognised in the balance sheet does not have a high probability of being realised at that value in the context of the business model.

One constituent felt that the IASB should move away from the discussion about the distinction between profit or loss and OCI and focus instead on providing more insights on the relevant attributes of performance, such as what income and expenses are recurring, realised, uncertain and/or related to operating activities.

Some constituents thought that the IASB should move completely away from OCI, as they did not think that OCI should exist

One of these constituent thought OCI could be avoided by measuring more items at cost, by recognising certain or probable future transactions that are hedged, by recognising actuarial gains and losses in the statement of profit or loss and by reporting translational adjustments directly in equity.

Some constituents commented on the statement in EFRAG's Document for Public Consultation that profit or loss should be as inclusive as possible.

One constituent did not think there would be any contradictions in both saying that the statement of profit or loss should be as inclusive as possible and not consider including items in OCI as an exception from a general rule.

Some constituents thought that the OCI presentation should not be considered as a rare exception but as a valid accounting approach. Therefore, the existence of OCI presentation should not be disqualified in an inappropriate and biased way in the Conceptual Framework. An option to use OCI could reduce artificial volatility.

One constituent even preferred to see OCI extended to include revaluations gains and losses of investment properties.

In its Document for Public Consultation, EFRAG asked for constituents views on the alternative views presented by two IASB members in the Basis for Conclusions accompanying the ED.

Some constituents did not support the alternative views. One of these constituents preferred a broader approach than suggested in the alternative views.

Some constituents supported the dissenting views.

Some constituents commented on the role of the business model. One constituent thought that the nature of business activities should be one of the factors that should be considered when distinguishing between items that should be reported in profit or loss and items that should be recognised in OCI. However, it should not be the only determining factor.

Another constituent supported the business model approach when deciding whether income and expenses should be reported in profit or loss or OCI.

Some constituents commented on whether the concepts used in the IASB Discussion Paper preceding the ED should be used. Some constituents preferred how the OCI was dealt with in the Discussion Paper. One constituent explained that it would enhance the usefulness of the Conceptual Framework to describe the general categories of the uses of OCI.

One constituent thought that profit or loss should be presented in one statement, together with OCI. This would ease the analysis of all components related to performance, including those gains and losses that were reported in OCI.

## Question 14 - Recycling

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document EFRAG noted that a principle (rather than a rebuttable presumption) should be set that no income and expense should be permanently excluded from the statement of profit or loss.

#### *Constituents' comments*

Some constituents agreed with EFRAG or had similar views. Some constituents supported the proposal of the ED.

Some constituents thought that all items reported in OCI should be recycled. The reason provided was that all cash flows should ultimately be recognised in the profit and loss account as an element of cost or income. This is the test of the relevance of profit and loss, the realisation of the cash flows being the ultimate proof of performance and it was considered to be important to strengthen the position of accrual accounting. One constituent noted that failure to identify a basis for recycling should be used as an argument for not recognising items in OCI in the first place.

One constituent thought that all fair value gains and losses that are recorded in OCI should eventually be recycled to profit or loss. On the other hand, some constituents thought that changes in fair value reported in OCI should never be recognised in any other period than when the change occurred. Similarly, one constituent did not think that actuarial gains or losses on pensions be considered as part of net income.

One constituent thought that the IASB should articulate the circumstances in which recycling would be considered to be relevant. The constituent thought that the business model should be considered when distinguishing between profit or loss and OCI and noted that this would mean that recycling would be considered to reflect the following circumstances:

- A change in value is realised.
- When a change in business model makes the realisation of the value recognised in OCI probable.

### EFRAG's response to constituents' comments

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EFRAG agreed with the constituents that thought that in principle all items recognised in profit or loss should be recycled based on the arguments of those constituents. EFRAG thought that sometimes it could provide useful information to recycle fair value changes that had occurred in previous periods. This would, for example, be relevant in relation to cash flow hedges.

EFRAG acknowledged that cost/benefit considerations could be one reason not to recycle. EFRAG, however, did not consider it useful to specify this in the Conceptual Framework. EFRAG thought that the cost constraint was pervasive. If it was mentioned in relation to some issues, it could give the impression that the constraint should only be considered in relation to these.

EFRAG thought that an 'OCI balance sheet' would be more confusing than a statement of OCI in relation to the statement of profit or loss. EFRAG understood that such a balance sheet, for example, would include negative values for assets that were measured at a fair value higher than cost in the statement of financial position but at cost in the statement of profit or loss. EFRAG, however, acknowledged that for some purposes it could be relevant to have the totals of items not recognised in profit or loss. EFRAG, however, thought that it would be more useful to provide such information in the notes to the financial statements and did not think this issue should be addressed in the Conceptual Framework.

- When the reason for recognition in OCI is no longer met.

Some constituents thought that the only items that should be recycled should be fair value gains and losses on effective hedges.

One constituent thought that recycling should only be possible if it related to performance. The constituent could not understand why gains and losses related to pension liabilities could not be recycled.

Some constituents thought that without a clear definition of performance or profit or loss it was not possible to provide a view on recycling.

One constituent thought that, generally, all income and expenses that are recognised in OCI should be recycled through profit or loss when presenting the performance of the period. Exceptions should only be introduced based on cost/benefit constraints (not because it would enhance relevance).

One constituent thought that it was not sufficiently clear from the ED when the proposed presumption could be rebutted as the reference to the enhancement of relevance was too vague to be operationalised.

One constituent thought that the IASB should further explore and clarify the implications of the proposals in the ED for items such as defined benefit obligations and investments in equity instruments classified at fair value through OCI.

One constituent suggested introducing an 'other comprehensive balance sheet' which would result in the reflection of two measures for a single item in the balance sheet, without affecting the income statement.

One constituent noted that users did not understand OCI.



## Chapter 8 – Concepts of capital and capital maintenance

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document EFRAG included a question to its constituents on whether the existing chapter on capital maintenance should be kept in the Conceptual Framework.

#### *Constituents' comments*

Some constituents thought that this chapter was outdated and misleading. It should accordingly be deleted if there would be no plans to update or properly link it to the rest of the Conceptual Framework.

However, some constituents thought the chapter should be retained.

One constituent thought that the chapter should be removed as part of the measurement and performance discussion, a description should be included about the underlying assumption regarding nominal capital maintenance when developing or revising future standards. The constituent thought this was a fundamental component of measurement guidance on performance.

One constituent thought that the Conceptual Framework should clarify that the IFRS financial reporting was based on the concept of financial capital maintenance.

### EFRAG's response to constituents' comments

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EFRAG noted that there were arguments both in favour and against removing Chapter 8 from the Conceptual Framework.

The IASB had not included a question on the issue in the ED and most of the comment letters EFRAG had received did not present a view on the issue. EFRAG was accordingly uncertain about the views of its constituents on the issue and decided not to address the issue in its comment letter in response to the ED.

## Other issues

### Question 15 - Effects of the proposed changes to the Conceptual Framework

#### EFRAG's tentative views and constituents' comments

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##### *EFRAG's Document for Public Consultation*

In its public consultation document EFRAG agreed with the status of the Conceptual Framework. As EFRAG assessed that the ED did not provide clear directions for future standard-setting activities, EFRAG did not think that the effect analysis included in the ED was particularly helpful. The consultation document included a question on whether constituents agreed with the status of the Conceptual Framework and that the review should not automatically result in any changes to Standards.

##### *Constituents' comments*

On the status of the Conceptual Framework some constituents generally agreed with the ED (and hence EFRAG).

One constituent mentioned that it was important that the Conceptual Framework should be stable and not change very often, and one constituent was concerned about the fact that Standards may override the principles established in the Conceptual Framework.

One constituent noted that conflicts between the Conceptual Framework and existing Standards should be assessed by the IASB. The IASB should consider whether it would need to add the Standard to its active agenda and to address the conflict on a timely basis.

One constituent thought that the status of the Conceptual Framework should be stronger so that future standards should be in conformity with the Conceptual Framework

On the assessment of the implications, some constituents assessed that the list of inconsistencies in paragraphs BCE.1 – BCE.31 of the ED was incomplete as it, for example, lacked the assessment of the existence of the category of equity instruments measured at fair value through OCI. One constituent thought that the IASB should develop an exhaustive list of all inconsistencies between current Standards and interpretations and the revised Conceptual Framework.

#### EFRAG's response to constituents' comments

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EFRAG noted that there was broad support for the status of the Conceptual Framework.

EFRAG agreed with some of the issues that constituents thought had been overlooked by the IASB in its effects analysis. EFRAG, however, thought the most important point to address was that it was not possible to assess whether current Standards and interpretations would be in conflict with the guidance included in the ED because the guidance was so vague.

Some constituents did not think the IASB analysis of the effects was sufficiently thorough. One constituent thought that there could also be implications for IAS 37, and IAS 32 in relation to puttable options. Another constituent thought that, in addition, the following issues existed:

- Inconsistencies carried forward as regards whether deferred tax assets and liabilities based on temporary deductible or taxable differences meet the definition of assets and liabilities.
- Future inconsistencies as regards the contractual service margin in the insurance contract project as to whether it meets the definition of a liability.
- Potential impacts on standards such as IAS 19 and IFRS 11.

Another constituent thought that the analysis should also have identified requirements that, although considered by the IASB to be consistent with the concepts proposed in the ED, currently are explained using different concepts in the Basis for Conclusions.

One constituent thought that the guidance in the ED was too detailed for a Conceptual Framework.

One constituent thought that the IASB should test how it could apply the proposals in a standard-setting context and the definitions, recognition criteria and profit or loss/distinction should be filed-tested by entities.

## Question 16 – Business activities

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document, EFRAG welcomed the role the business model should play in measurement, in identifying different measurement bases for the statement of financial position and the statement of profit or loss, and in selecting the unit of account. However, EFRAG thought that the ED limited the role of the business model in measurement without stating why and how it would be limited, and the ED did not consider the role it could play in recognition. Furthermore, EFRAG thought that the term 'business model' that had been introduced with IFRS 9 *Financial Instruments* should be retained and described for financial reporting purposes.

#### *Constituents' comments*

Some constituents agreed with the ED.

Some constituents thought that the nature of an entity's business activities had an important role.

One constituent believed that financial statements could only be meaningful for investors and other users of financial statements if relevant standards would allow an entity to reflect how it conducts its business. This constituent noted that the notion 'business model' rather than 'business activities' was very important for accounting for insurers because insurers applied different asset-liability management strategies in which insurance liabilities and guarantees and their related assets were managed together as a business model according to the insurance contract liability profile to meet obligations towards policyholders.

Similarly one constituent thought that the business model should be the determining factor when selecting a measurement basis and when deciding what should be reported in profit or loss versus OCI.

One constituent thought that the discussion of business activities in the ED omitted a general reference to the importance of the perspective in the discussion of the objectives of financial reporting.

Some constituents did not think the ED adequately addressed the importance of the business model. One of these constituents thought that the Conceptual

### EFRAG's response to constituents' comments

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EFRAG noted, that there was very limited support for having the business model being the main driver for, for example, how to distinguish between profit or loss and OCI. However, there was general support for the view that the business model should have a role to play together with other factors. Based on this EFRAG followed the view expressed by one constituent that standards should not be made in a manner that would generally result in entities not being able to reflect their business models in the financial statements.

EFRAG also noted that constituents were uncertain about how to interpret the terms 'business activities' and 'business model'. EFRAG therefore decided to keep its comment that the IASB should describe this in the Conceptual Framework.

Framework should include a separate section in the chapter on qualitative characteristics relating to the business model. The constituent thought it had a role to play in recognition, unit of account, measurement and presentation. Other constituents thought that it should play a role in all aspects of financial reporting.

Other constituents thought that the role of the business activities should play a more limited role. One constituent noted that the Conceptual Framework would lose significance if divergent principles were applied concurrently depending on the business model.

One constituent thought that the nature of business activities should be only one of the considerations used for standard-setting activities.

In direct response to the view expressed in EFRAG's Document for Public Consultation, one constituent did not agree that the business model should lead all reporting issues. However, the constituent was open to support a conceptual debate on the issue. The constituent did not agree that the Conceptual Framework should retain the business model as used in IFRS 9. However, the constituent thought that there might be a role for higher conceptual thinking than was used in IFRS 9.

One respondent thought that the business model concept was important and should be considered when deciding on measurement. However, the term should not be used in the Conceptual Framework due to the difficulty in making a robust definition that would contribute further to the development of individual Standards.

One constituent mentioned that it would not support including a definition of the term 'business model' in the framework, as it did not expect this to achieve anything.

One constituent thought that the Conceptual Framework would benefit from a better description of when it would be appropriate to refer to the business model when developing individual Standards. In addition, one constituent thought that the IASB should be more specific and describe more clearly how the consideration of business activities would affect the development or revision of future IFRS. The current proposal was not considered to be of great help to the IASB.

One constituent thought that the general discussion on the role of the business activities was important as the nature of entity's business activities plays different roles in different aspects of financial reporting.

One constituent thought that the business model had a role to play but did not agree with how it was applied in IFRS 9 and the idea of the business model would need more analysis and debate.

One constituent did not agree with the IASB that the nature of an entity's business activities did not have an impact on recognition. It thought that the recognition requirements in IAS 39 / IFRS 9 on regular-way transactions was an example of where it had an impact.

Some constituents commented on how they interpreted the term.

One constituent interpreted the concept of the 'business model' as meaning that the financial statements faithfully reflected the company's activity

One constituent thought that the notion 'business model' was orientated towards a value-creation model and one possible description would be, "the strategy applied by the entity to manage its resources and obligations in order to create value". Instead of trying to define some specific business models, the constituent proposed that the IASB should work on the key characteristics of business models that could be of interest for accounting purposes (such as, for example, the length of the activity cycle, the use of inputs and outputs, the types of risks related to the activity, and the degree of certainty in the generation of cash flow). The similar key characteristics were identified by another constituent.

One constituent thought that beyond the business model that should be reflected in the accounting model, other specific managerial "intention" should also be considered. On the other hand, one constituent preferred to use the term 'business activities' instead of 'business model' as the nature of an entity's 'business activities' could be distinguished by a matter of fact, as opposed to just an opinion, management intent or arbitrary judgements on pre-defined business models. Another constituent thought that the term 'business activities' had the same meaning as 'business model' – but preferred the term 'business activity'.

## Question 17 – Long-term investment

### EFRAG's tentative views and constituents' comments

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#### *EFRAG's Document for Public Consultation*

In its public consultation document EFRAG thought that the ED provided insufficient guidance on the unit of account, measurement and presentation in order to be helpful to reflect long-term investment business models. Where financial reports genuinely provide information that is necessary to make decisions to buy, hold and sell and to assess the management's stewardship EFRAG thought that it is not necessary to differentiate among investors on the basis of their investment horizon.

#### *Constituents' comments*

Some constituents agreed with the IASB's conclusions on long-term investments.

Some constituents agreed with the ED if their comments to other parts of the ED were considered (comments that were not directly related to long-term investments) or if the IASB would provide sufficient guidance on how to measure the long-term investments (or liabilities) of entities whose business activities include long-term investment and whether such entities should report changes in the carrying amount of those investments (or liabilities) in the statement of profit or loss or OCI.

One constituent agreed with EFRAG that it would be unnecessary to distinguish between the information needs of long- and short-term investors. However, the constituent did not agree that the Conceptual Framework required additional guidance on long-term investment business models.

Some constituents thought it was necessary to have a clear and explicit commitment to consider the characteristics of long-term oriented business models such as the insurance business when developing or revising particular Standards.

### EFRAG's response to constituents' comments

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EFRAG noted that constituents were generally unconcerned about not addressing the needs of long-term investors and the business model of long-term investors in a more specific manner in the Conceptual Framework. EFRAG therefore decided to maintain the view it had expressed in the Document for Public Consultation.

## Additional issues

### EFRAG's tentative views and constituents' comments

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Some constituents provided some general comment or comments on issues in addition to those addressed in the ED.

Some of the comments related to how the ED was structured. One constituent thought the structure of the Conceptual Framework could be improved and be more logical, and on a more detailed level one constituent thought that the fundamental principle of materiality should be established once for all in the Conceptual Framework and then not be repeated.

Some constituents thought the wording could be more consistent and precise. Some constituents noted that the ED mentioned 'resources' when discussing stewardship. However, other parts of the chapter referred to 'economic resources'. One noted that terms like 'may', 'in some cases', 'normally' were not suitable for a framework, unless it is explained more clearly in which cases something shall apply and when deviations from the normal are defensible. A similar comment was made by one constituent in relation to the use of 'sometimes', 'in some cases' and 'in some circumstances', particularly in the measurement section of the ED.

One constituent thought that the IASB should clarify at the conceptual level the relationship between the terms 'material' and 'significant' and one constituent thought that the different probability terms used in IFRS should be clarified.

Some constituents were concerned about the lack of guidance on the distinction between equity and liabilities, particularly as this issue caused many practical problems. One constituent thought that the work on the IASB FICE project should be reflected in the Conceptual Framework, when the project was finalised.

Some constituents made general comments about areas where they considered there was insufficient guidance in the ED. One noted that the ED would not prevent endless discussions on fundamental questions. Another

### EFRAG's response to constituents' comments

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EFRAG noted that some constituents thought that the structure of the Conceptual Framework could be improved. Some constituents provided specific comments on how different parts of the proposed Conceptual Framework could be structured. These comments are considered in the sections above.

EFRAG agreed with the comment that the wording in the ED was too vague. It decided to reflect the comments of constituents who thought it should be made more consistent and precise in its comment letter.

Although EFRAG thought it could be useful to have the relationship between 'material' and 'significant' explained and the different probability terms clarified, it did not think this should be done in the Conceptual Framework.

EFRAG shared the concern of constituents about the lack of guidance on the distinction between equity and liability. However, EFRAG thought that the issue had to be considered together with the IASB project on financial instruments with characteristics of equity as it should be compatible with the relevant guidance that would be set on standards level on this issue. EFRAG therefore thought it would be most efficient to consider the issue in a separate project and then update the Conceptual Framework at a later date. EFRAG was aware that this could result in other changes to the Conceptual Framework at that time.

As previously noted, EFRAG agreed with the general comments that the ED provided insufficient guidance on many topics.

EFRAG also agreed with the constituents who thought it would be useful to include a reference to the true and fair view in the Conceptual Framework.

EFRAG agreed with the observation that the IASB for the current revision had not investigated all different kinds of paths towards more useful information. EFRAG, however, noted that such research would take many years. EFRAG did not think that the



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constituent was concerned that a lack of clarity in the Conceptual Framework would result in questions arising in the future during standard setting.

Some constituents thought that the Conceptual Framework should include a reference to the true and fair view and explain the concept thoroughly and develop the relation to the qualitative characteristics of useful financial information.

One constituent was concerned that alternative paths towards more useful information to users in financial reports were not sufficiently analysed and discussed.

Some constituent thought that the ED included too many different perspectives. The constituents considered that the Conceptual Framework should be clearer on to whom it was addressed for (e.g. standard setter or public as a whole) or what parts were address to who.

One constituent was concerned about the increased use of 'control' by the IASB without being properly substantiated.

One constituent was concerned that the principles had become more complicated. Preparers would prefer to make the judgements on the basis of more simplified and conceptual principles.

One constituent noted that at this time the Conceptual Framework need not be modified to take dynamic risk management into account, but would not want future progress on the accounting for macro hedging activities to be constrained by what is written in the Framework. The constituent thought that it would be helpful if the Conceptual Framework recognised that this issue needed further consideration, which should be undertaken when developing the future standard, in the same way as the ED deals with the classification of equity instruments.

One constituent expressed the view that it was very difficult to reach a common understanding of the key principles and that the need for pragmatism was important.

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research was unimportant, but considered that there were some problems with the current Conceptual Framework that needed to be fixed within a shorter timeframe. EFRAG therefore agreed with the IASB's pragmatic approach for the current review of the Conceptual Framework.

For the same reason, EFRAG accepted the increased use of 'control' as it did reflect the thinking in the current standard setting of the IASB.

EFRAG agreed that the Conceptual Framework should take dynamic risk management into account when the work on this issue would be finalised. EFRAG, however, noted that it could take some time before the IASB could finalise its thoughts about this issue and accordingly decided not to include a comment on this in its comment letter.

EFRAG acknowledged that the moral hazard problem had a role to play in relation to accounting. EFRAG did not think it was essential to mention this in the Conceptual Framework.

EFRAG did not think the Conceptual Framework should provide guidance on whether combined financial statements could be prepared in compliance with IFRS and whether financial statements could be compliant with IFRS if the reporting entity is not going concern. EFRAG thought that such guidance would be better placed in a standard considering the status of the Conceptual Framework. EFRAG therefore decided not to include further comments on this in addition to what it noted in relation to Question 2.

One constituent thought that the problem of moral hazard should be mentioned in the Conceptual Framework.

One constituent thought that the Conceptual Framework should provide guidance on whether combined financial statements could be prepared in compliance with IFRS and whether financial statements could be compliant with IFRS if the reporting entity was not a going concern. Another constituent was concerned that as a result of how the going concern was explained there was a risk that disclosures about material uncertainties relating to going concern were inadequate. A third constituent thought the IASB should better explain what role the term should play.

One constituent thought that the Conceptual Framework should explicitly require the IASB to consider potentially existing linkages between particular Standards when performing standard setting activities.

One constituent thought that the Conceptual Framework should only focus on financial statements rather than financial reporting as a whole.

One constituent thought that a re-exposure of the ED would be necessary. The revised ED should include the concepts for performance reporting and this could have an impact on other aspects of the ED. Also the constituent thought that the impact of the proposed changes should appear more clearly.

One constituent thought that the language of the Conceptual Framework should be strengthened so that all negative consequences of accounting choices would be taken into account when setting Standards. The constituent thought that the Conceptual Framework could give the impression that accounting choices would only affect comparability. The constituent thought that it would also affect understandability.

## **Appendix – List of comment letters**

### **National Standard Setters**

Accounting Standards Committee of Germany  
Autorité des norms comptables (ANC)  
Danish Accounting Standards Committee  
Dutch Accounting Standards Board  
Financial Reporting Council  
Instituto de Contabilidad y Auditoría de Cuentas (ICAC)  
Norwegian Accounting Standards Board  
Polish Accounting Standards Committee  
Swedish Financial Reporting Board

### **Enforcers and authorities**

European Securities and Markets Authority

### **Financial statements users and user associations**

Eumedion  
The European Federation of Financial Analysts Societies (EFFAS)  
French Society of Financial Analysts

### **Preparers and preparer organisations**

ACTEO AFEP MEDEF  
A.P. Møller – Mærsk  
BUSINESSEUROPE  
Confederation of Swedish Enterprise  
European Banking Federation  
Fédération Bancaire Française  
German Banking Industry Committee  
German Insurance Association (GDV)  
Insurance Europe  
International Swaps and Derivatives Association  
Quoted Companies Alliance

### **Auditors and associations of accountants**

The Institute of Chartered Accountants in England and Wales (ICAEW)  
The Institute of Chartered Accountants of Scotland (ICAS)  
Federation of European Accountants

### **Individuals**

Denise Silva Ferreira Juvenal