CIPFA The Chartered Institute of Public Finance & Accountancy

Discussion Paper DP/2013/1
A Review of the Conceptual Framework for Financial Reporting

response to discussion paper

14 January 2014

the people in public finance

CIPFA, the Chartered Institute of Public Finance and Accountancy, is the professional body for people in public finance. Our 14,000 members work throughout the public services, in national audit agencies, in major accountancy firms, and in other bodies where public money needs to be effectively and efficiently managed.

As the world's only professional accountancy body to specialise in public services, CIPFA's portfolio of qualifications are the foundation for a career in public finance. They include the benchmark professional qualification for public sector accountants as well as a postgraduate diploma for people already working in leadership positions. They are taught by our in-house CIPFA Education and Training Centre as well as other places of learning around the world.

We also champion high performance in public services, translating our experience and insight into clear advice and practical services. They include information and guidance, courses and conferences, property and asset management solutions, consultancy and interim people for a range of public sector clients.

Globally, CIPFA shows the way in public finance by standing up for sound public financial management and good governance. We work with donors, partner governments, accountancy bodies and the public sector around the world to advance public finance and support better public services.

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International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
Submitted electronically to www.ifrs.org
January 2014

Dear IASB secretariat

Discussion Paper DP/2013/1

CIPFA is pleased to present its comments on the matters discussed in this Discussion Paper, which have been reviewed by CIPFA's Accounting and Auditing Standards Panel.

General Comments

While CIPFA has an interest in financial reporting generally, we have a specific interest in both public sector and wider not-for-profit reporting. We therefore have a particular interest in issues which would affect the use of IASB standards by these entities.

The IASB is aware that the International Public Sector Accounting Standards Board is developing its own conceptual framework for public sector financial reporting. While this project is not being pursued with a view to 'convergence' with the IASB framework, considerable attention has been paid to avoiding unnecessary divergence from the framework which will inform IFRS development.

We note that the IASB is not currently taking forward the development of the conceptual framework as it relates to not-for-profit entities.

In the 2012 Request for Information *Comprehensive Review of the IFRS for SMEs* the Board explored whether it would be appropriate for the IFRS for SMEs to be applied by these entities, or whether these entities might be publicly accountable and therefore required to use other standards. CIPFA's response to the Request explained our view that neither the main body of IFRS nor the IFRS for SMEs are suitable for not-for-profit entities in their current form, although the UK Financial Reporting Council has developed a standard based on a combination of the two sets of standards and UK specific material which can be applied to such entities.

CIPFA also explained our initial view that it would be helpful for an international standards provider to produce a standard which could be applied to not-for-profit entities, thereby filling a substantial gap. In line with this view CIPFA has consulted with other accountancy bodies, and the UK and Ireland Consultative Committee of Accountancy Bodies (CCAB) has sponsored research to determine to what extent there is a demand for standards to meet the specific needs of the not-for-profit sector. The results of this research have yet to be analysed, and the role of the IASB and possible revival of Phase G of the IFRS framework have not been explored. However, given the significant interactions between entities in all sectors, CIPFA would in any case wish to see reporting developed which was as comparable as possible, with as little unnecessary divergence as possible, having regard to the different economic characteristics of the sectors and the differing needs of relevant stakeholders. While financial statements and other financial reporting might have substantial differences, we would expect that at a conceptual level there would be much more similarity. Against this background, we strongly support the IASB's decision to recommence work on its Conceptual Framework, given that the existing framework is out of date, as it is helpful not only to the Board in its standard setting processes but also to preparers in understanding the principles behind individual standards. A clear framework is beneficial when determining how best to apply IFRS to entities in sectors which they were not principally designed for, and will also help other standard setters such as the International Public Sector Accounting Standards Board to avoid unnecessary differences in their frameworks and standards.

Responses to the Questions for Respondents

Responses to the questions in the exposure draft are attached in an annex to this letter.

CIPFA is generally supportive of the proposals, except in the area of Measurement, where we consider that the discussion is not at sufficient depth, and mainly has the effect of justifying the current position and dismissing other approaches. Regardless of the final position reached on this aspect of the framework, it is essential that this topic is discussed at proper depth.

If you have any questions about this response, please contact Steven Cain (e:steven.cain@cipfa.org, t:+44(0)20 7543 5794).

I hope this helps the Board in its development of an improved framework.

Yours faithfully

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ANNEX

Responses to Questions for Respondents

Section 1 Introduction

Question 1 Paragraphs 1.25–1.33 set out the proposed purpose and status of the Conceptual Framework. The IASB's preliminary views are that: (a) the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs; and (b) in rare cases, in order to meet the overall objective of financial reporting, the IASB may decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. If this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard. Do you agree with these preliminary views? Why or why not?
(a) CIPFA agrees that the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs. (b) CIPFA agrees that in order to meet the overall objective of financial reporting, the IASB may in rare cases decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. CIPFA also agrees that if this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard. This is particularly important where the Board has rejected an apparently conceptually superior treatment for practical reasons or, for example, to reduce the risk that financial reporting is manipulated or distorted. Furthermore, we suggest that it would be helpful if the read across from the Conceptual Framework to standard setting should be made obvious in all subsequent standard setting.

Section 2 Elements of financial statements

Question 2 The definitions of an asset and a liability are discussed in paragraphs 2.6–2.16. The IASB proposes the following definitions: (a) an asset is a present economic resource controlled by the entity as a result of past events. (b) a liability is a present obligation of the entity to transfer an economic resource as a result of past events. (c) an economic resource is a right, or other source of value, that is capable of producing economic benefits. Do you agree with these definitions? Why or why not? If you do not agree, what changes do you suggest, and why?
CIPFA agrees with the proposed definitions.
Question 3 Whether uncertainty should play any role in the definitions of an asset and a liability, and in the recognition criteria for assets and liabilities, is discussed in paragraphs 2.17–2.36. The IASB's preliminary views are that: (a) the definitions of assets and liabilities should not retain the notion that an inflow or outflow is 'expected'. An asset must be capable of producing economic benefits. A liability must be capable of resulting in a transfer of economic resources. (b) the Conceptual Framework should not set a probability threshold for the rare cases in which it is uncertain whether an asset or a liability exists. If there could be significant uncertainty about whether a particular type of asset or liability exists, the IASB would decide how to deal with that uncertainty when it develops or revises a Standard on that type of asset or liability. (c) the recognition criteria should not retain the existing reference to probability. Do you agree? Why or why not? If you do not agree, what do you suggest, and why?
CIPFA agrees with the proposed definitions. We agree that the definitions and the recognition criteria should not refer to probability or related notions as there are cases - for example some derivatives - where an asset or liability should be recognised irrespective of the probability of an inflow or an outflow. We would also note that in order to provide useful information on assets held by not-for-profit entities, it will be necessary to take a view of 'economic benefit' which encompasses the capacity to provide services to individuals or communities; alternatively, if 'economic benefit' is interpreted more narrowly, it will be necessary to have regard to the service potential of assets held by not-for-profit entities, in line with the formulation used by the IPSASB for public sector assets.

Question 4 Elements for the statement(s) of profit or loss and OCI (income and expense), statement of cash flows (cash receipts and cash payments) and statement of changes in equity (contributions to equity, distributions of equity and transfers between classes of equity) are briefly discussed in paragraphs 2.37–2.52. Do you have any comments on these items? Would it be helpful for the Conceptual Framework to identify them as elements of financial statements?
CIPFA agrees with the proposed definitions of income and expense, although we would note that in other frameworks, such as the UK Statement of Principles for Financial Reporting, these are considered to correspond to the movements in ownership interest (or equity) rather than the movements in assets. We appreciate that these items mirror each other. It is less clear to us that additional elements are required for the other financial statements.

Section 3 Additional guidance to support the asset and liability definitions

Question 5 Constructive obligations are discussed in paragraphs 3.39–3.62. The discussion considers the possibility of narrowing the definition of a liability to include only obligations that are enforceable by legal or equivalent means. However, the IASB tentatively favours retaining the existing definition, which encompasses both legal and constructive obligations—and adding more guidance to help distinguish constructive obligations from economic compulsion. The guidance would clarify the matters listed in paragraph 3.50. Do you agree with this preliminary view? Why or why not?
CIPFA agrees with this preliminary view.
Question 6 The meaning of 'present' in the definition of a liability is discussed in paragraphs 3.63–3.97. A present obligation arises from past events. An obligation can be viewed as having arisen from past events if the amount of the liability will be determined by reference to benefits received, or activities conducted, by the entity before the end of the reporting period. However, it is unclear whether such past events are sufficient to create a present obligation if any requirement to transfer an economic resource remains conditional on the entity's future actions. Three different views on which the IASB could develop guidance for the Conceptual Framework are put forward: (a) View 1: a present obligation must have arisen from past events and be strictly unconditional. An entity does not have a present obligation if it could, at least in theory, avoid the transfer through its future actions. (b) View 2: a present obligation must have arisen from past events and be practically unconditional. An obligation is practically unconditional if the entity does not have the practical ability to avoid the transfer through its future actions. (c) View 3: a present obligation must have arisen from past events, but may be conditional on the entity's future actions. The IASB has tentatively rejected View 1. However, it has not reached a preliminary view in favour of View 2 or View 3. Which of these views (or any other view on when a present obligation comes into existence) do you support? Please give reasons.
CIPFA is also minded to reject View 1 for the reasons set out by IASB at 3.96, but we have not developed a consensus in favour of View 2 or View 3.
Question 7 Do you have comments on any of the other guidance proposed in this section to support the asset and liability definitions?
CIPFA has no further comments to make on the other guidance.

Section 4 Recognition and derecognition

Question 8 Paragraphs 4.1–4.27 discuss recognition criteria. In the IASB's preliminary view, an entity should recognise all its assets and liabilities, unless the IASB decides when developing or revising a particular Standard that an entity need not, or should not, recognise an asset or a liability because: (a) recognising the asset (or the liability) would provide users of financial statements with information that is not relevant, or is not sufficiently relevant to justify the cost; or (b) no measure of the asset (or the liability) would result in a faithful representation of both the asset (or the liability) and the changes in the asset (or the liability), even if all necessary descriptions and explanations are disclosed. Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?
CIPFA agrees that assets and liabilities should not be recognised if doing so does not provide relevant information, or information that is not sufficiently relevant to justify the cost of doing so. The Conceptual Framework should also provide indicative guidance on when recognition might not result in relevant information. This might include consideration of lack of reliability of measurement and low probability of inflow or outflow of economic benefits.
Question 9 In the IASB's preliminary view, as set out in paragraphs 4.28–4.51, an entity should derecognise an asset or a liability when it no longer meets the recognition criteria. (This is the control approach described in paragraph 4.36(a)). However, if the entity retains a component of an asset or a liability, the IASB should determine when developing or revising particular Standards how the entity would best portray the changes that resulted from the transaction. Possible approaches include: (a) enhanced disclosure; (b) presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations, to highlight the greater concentration of risk; or (c) continuing to recognise the original asset or liability and treating the proceeds received or paid for the transfer as a loan received or granted. Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?
CIPFA broadly agrees with the IASB preliminary view.

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

Question 10 The definition of equity, the measurement and presentation of different classes of equity, and how to distinguish liabilities from equity instruments are discussed in paragraphs 5.1–5.59. In the IASB's preliminary view: (a) the Conceptual Framework should retain the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities. (b) the Conceptual Framework should state that the IASB should use the definition of a liability to distinguish liabilities from equity instruments. Two consequences of this are: (i) obligations to issue equity instruments are not liabilities; and (ii) obligations that will arise only on liquidation of the reporting entity are not liabilities (see paragraph 3.89(a)). (c) an entity should: (i) at the end of each reporting period update the measure of each class of equity claim. The IASB would determine when developing or revising particular Standards whether that measure would be a direct measure, or an allocation of total equity. (ii) recognise updates to those measures in the statement of changes in equity as a transfer of wealth between classes of equity claim. (d) if an entity has issued no equity instruments, it may be appropriate to treat the most subordinated class of instruments as if it were an equity claim, with suitable disclosure. Identifying whether to use such an approach, and if so, when, would still be a decision for the IASB to take in developing or revising particular Standards. Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?
CIPFA agrees the general point that equity should be defined as a residual interest. This is also very important for not-for-profit entities and public sector bodies, where there will often be no 'equity instruments' as that term is generally understood.

Section 6 Measurement

General comments

It is particularly important that this material is properly discussed. Consideration of measurement issues has been a key feature in the development of revised standards over the last ten years, relating to business combinations, provisions and contingent liabilities, financial instruments and several other standards. The Canadian Accounting Standards Board promoted discussion with a research paper on *Measurement on Initial Recognition*, and IASB held round tables on Measurement in 2007. The Board has of course also progressed a joint project with FASB on Fair Value, which addressed more specific issues in developing a consistent notion of fair value in IAS and IFRS; in so doing the Board may have effected a change in the conceptual context of standard setting, reducing the role of measures of current value based on replacement cost.

Against this background, while we appreciate that the Board is seeking to develop a revised Framework in a timely fashion, we are concerned that the material on Measurement is not of sufficient depth to sustain a proper conceptual discussion. We have some concerns that the material mainly supports current practices with only cursory justification, but might be seen as dismissive of wider practice. The treatment of 'deprival value' is particularly unfortunate; in the short space afforded to measurement in this paper, the Board might have done better to concentrate on the role of replacement cost in measurement. As it is, neither this more general topic nor the specific case of deprival are properly considered. This seems curious given the relationship between replacement cost and entry prices, the latter seeming to be accepted without much discussion.

Question 11

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

(a) the objective of measurement is to contribute to the faithful representation of relevant information about:

(i) the resources of the entity, claims against the entity and changes in resources and claims; and

(ii) how efficiently and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.

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

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

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

(i) for a particular asset should depend on how that asset contributes to future cash flows; and

(ii) for a particular liability should depend on how the entity will settle or fulfil that liability.

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

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

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

CIPFA generally agrees with the above insofar as measurement applies to balances and flows relating to profit seeking entities and activities. A more rounded discussion may be necessary for wider types of entity.

Question 12 The IASB’s preliminary views set out in Question 11 have implications for the subsequent measurement of assets, as discussed in paragraphs 6.73–6.96. The IASB’s preliminary views are that: (a) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, cost-based measurements normally provide information that is more relevant and understandable than current market prices. (b) if assets contribute directly to future cash flows by being sold, a current exit price is likely to be relevant. (c) if financial assets have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information. (d) if an entity charges for the use of assets, the relevance of a particular measure of those assets will depend on the significance of the individual asset to the entity. Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.
CIPFA agrees with assertions (b) and (c), that is - for assets which contribute directly to future cash flows by being sold, a current exit price is likely to be relevant - for financial assets which have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information. We do not agree with assertion (a), given that the references to ‘cost-based’ measurements are historical and exclude current measures such as replacement cost. As time passes, historical cost information may become increasingly irrelevant, and assets with similar capacity to contribute to operations purchased at different times may be reported on very differently. More generally, we would note that the measurement of assets held by not-for-profit entities needs to produce useful information in situations where assets contribute to cash flows only in the most general sense, for example, by encouraging donations in order to allow the continuation of services provided for the benefit of individuals or communities. In this context, we again find view (a) too narrow. Subject to these comments, CIPFA agrees with assertion (d)

Question 13

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

(a) cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms.

(b) a cost-based measurement will normally provide the most relevant information about:

(i) liabilities that will be settled according to their terms; and

(ii) contractual obligations for services (performance obligations).

(c) current market prices are likely to provide the most relevant information about liabilities that will be transferred.

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

CIPFA broadly agrees with these preliminary views.

Question 14

Paragraph 6.19 states the IASB's preliminary view that for some financial assets and financial liabilities (for example, derivatives), basing measurement on the way in which the asset contributes to future cash flows, or the way in which the liability is settled or fulfilled, may not provide information that is useful when assessing prospects for future cash flows. For example, cost-based information about financial assets that are held for collection or financial liabilities that are settled according to their terms may not provide information that is useful when assessing prospects for future cash flows:

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

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

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

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

CIPFA broadly agrees with these preliminary views.

Question 15

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

General comments are provided at the start of this section.

Section 7 Presentation and disclosure

Question 16 This section sets out the IASB's preliminary views about the scope and content of presentation and disclosure guidance that should be included in the Conceptual Framework. In developing its preliminary views, the IASB has been influenced by two main factors: (a) the primary purpose of the Conceptual Framework, which is to assist the IASB in developing and revising Standards (see Section 1); and (b) other work that the IASB intends to undertake in the area of disclosure (see paragraphs 7.6–7.8), including: (i) a research project involving IAS 1, IAS 7 and IAS 8, as well as a review of feedback received on the Financial Statement Presentation project; (ii) amendments to IAS 1; and (iii) additional guidance or education material on materiality. Within this context, do you agree with the IASB's preliminary views about the scope and content of guidance that should be included in the Conceptual Framework on: (a) presentation in the primary financial statements, including: (i) what the primary financial statements are; (ii) the objective of primary financial statements; (iii) classification and aggregation; (iv) offsetting; and (v) the relationship between primary financial statements. (b) disclosure in the notes to the financial statements, including: (i) the objective of the notes to the financial statements; and (ii) the scope of the notes to the financial statements, including the types of information and disclosures that are relevant to meet the objective of the notes to the financial statements, forward-looking information and comparative information. Why or why not? If you think additional guidance is needed, please specify what additional guidance on presentation and disclosure should be included in the Conceptual Framework.
CIPFA broadly supports the IASB's preliminary views on presentation. While this is less far reaching than similar work on presentation in financial reporting being carried out by the International Public Sector Accounting Standards Board (IPSASB), it is arguably less necessary to produce a wider framework for IFRS at this stage; in contrast, the IPSASB is developing a range of wider reporting products for which a framework which considers wider financial reporting is particularly relevant. We suggest however that the Board should at a later date revisit this subject in the context of wider financial reporting.

Question 17
Paragraph 7.45 describes the IASB's preliminary view that the concept of materiality is clearly described in the existing Conceptual Framework. Consequently, the IASB does not propose to amend, or add to, the guidance in the Conceptual Framework on materiality. However, the IASB is considering developing additional guidance or education material on materiality outside of the Conceptual Framework project. Do you agree with this approach? Why or why not?
CIPFA broadly agrees with this approach. Additional guidance on the application of materiality to disclosures is an important part of changing behaviour in this area and, in line with the comments at 7.47(d), it is particularly important to encourage preparers and auditors to avoid over-disclosure of information which impairs understandability.

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

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

Question 19 The IASB's preliminary view that the Conceptual Framework should require a total or subtotal for profit or loss is discussed in paragraphs 8.19–8.22. Do you agree? Why or why not? If you do not agree do you think that the IASB should still be able to require a total or subtotal profit or loss when developing or amending Standards?
Based on our understanding of the perspective of private sector preparers, we can see that there is a demand for such a total or subtotal. However, our main concerns are with wider categories of reporting, and some adaptation of profit based figures is likely to be necessary. For public sector and public benefit sector purposes we will still be interested in distinguishing between some form of 'surplus' which is e.g. in some sense more reliable or relevant, and other apparent changes to ownership interest. Given this, we have no comments to make on the construction or definition of a profit total or subtotal.
Question 20 The IASB's preliminary view that the Conceptual Framework should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss, ie recycled, is discussed in paragraphs 8.23–8.26. Do you agree? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss? Why or why not? If you do not agree, how would you address cash flow hedge accounting?
CIPFA has no comments to make on this.
Question 21 In this Discussion Paper, two approaches are explored that describe which items could be included in OCI: a narrow approach (Approach 2A described in paragraphs 8.40–8.78) and a broad approach (Approach 2B described in paragraphs 8.79–8.94). Which of these approaches do you support, and why? If you support a different approach, please describe that approach and explain why you believe it is preferable to the approaches described in this Discussion Paper.
CIPFA has no comments to make on this.

Section 9 Other issues

Question 22 **Chapters 1 and 3 of the existing Conceptual Framework** Paragraphs 9.2–9.22 address the chapters of the existing Conceptual Framework that were published in 2010 and how those chapters treat the concepts of stewardship, reliability and prudence. The IASB will make changes to those chapters if work on the rest of the Conceptual Framework highlights areas that need clarifying or amending. However, the IASB does not intend to fundamentally reconsider the content of those chapters. Do you agree with this approach? Please explain your reasons. If you believe that the IASB should consider changes to those chapters (including how those chapters treat the concepts of stewardship, reliability and prudence), please explain those changes and the reasons for them, and please explain as precisely as possible how they would affect the rest of the Conceptual Framework.
Stewardship CIPFA would prefer to articulate the objectives of financial reporting in terms of 'accountability' rather than 'stewardship', as this term more clearly applies to wider classes of entity. In CIPFA's view, providing accountability is a primary objective of financial reporting, and should be reflected in the Conceptual Framework as a separate objective. Accountability should be equal in prominence to the objective of providing information which is decision-useful We note that the Basis for Conclusions states "The Board did not intend to imply that assessing prospects for future cash flow or assessing the quality of management's stewardship is more important than the other." In our view, including a separate accountability objective would provide greater clarity, but not fundamentally change the content of the framework. **Reliability** The Board indicated in its joint IASB FASB consultation in 2006 that the term 'reliability' is not well understood or consistently understood, and that for this reason, the framework should be articulated in terms of 'faithful representation'. In CIPFA's response to the 2006 consultation we outlined our concern that the replacement of 'reliability' with 'faithful representation' does not improve clarity, and may also introduce changes of substance and permit the inclusion of figures in primary statements which would be considered insufficiently reliable under current reporting conventions. The subsequent redrafting of revised Chapters of the framework has focussed on faithful representation, and it has become clear that our concerns are partially ameliorated by requiring that information which incorporates a degree of variability and uncertainty be accompanied by information explaining the nature of the variability and uncertainty. However, as far as we can tell the concept of reliability (or perhaps 'unreliability') is still embedded in the framework, inasmuch as it is considered that if financial information incorporates too great a degree of variability it will not be sufficiently relevant to provide useful information (whether for decision-making or accountability purposes). In our view this is still very cryptic and unclear, and the Board has not succeeded in providing an explanation which is significantly better than the previously problematic discussion of 'reliability'.

Whether or not the Board retains its focus on 'faithful representation', in our view there is a need to make it clear that financial information needs to be be sufficiently reliable for the purpose it is being used for, having regard to related disclosures on the variability of the information. This is essential not just for preparers of financial information, but also for auditors. While regulators are currently focussing on the *scepticism* of auditors, the requirement for scepticism is effectively a requirement to deal with the risk that information provided by management is insufficiently reliable, whether due to management misrepresentation or error, or innate variability.

Prudence

As noted by the Board, the term 'prudence' is used in a number of ways.

While CIPFA does consider that it would be helpful for some additional emphasis to be given to exercise caution when making estimates and judgements under conditions of uncertainty, we are not sure that it would be best to capture this using the term 'prudence'.

As the Discussion Paper explains, some interpretations of prudence incorporate conservatism and reject the notion of neutrality, preferring instead to mitigate perceived risks of misstatement. CIPFA does not support this approach, at least for the purposes of the Conceptual Framework. As an aspirational document, the framework should value items in financial statements and related financial reporting in a neutral and unbiased way, using the best available estimates of their value. We can see that in certain circumstances it may be appropriate to counter perceived sources of bias in financial reporting, and that this might require an asymmetric approach to measurement to be undertaken. However, this should only be used to counterbalance the risk of systematic bias, and this is better considered as a matter for individual standards, having regard to the specific features of the relevant reporting environment

We also have some concerns that the term 'prudence' is quite an old one, and may be associated with some approaches to accounting which are now deprecated under more modern conceptual frameworks. In particular, some forms of 'matching' which have the effect of smoothing results without regard to overall economic substance may be justified on the basis of 'prudence'.

Given the above, we are inclined to support the principle of prudence, but suggest that this should be through improving the description of neutrality.

Question 23 **Business model** The business model concept is discussed in paragraphs 9.23–9.34. This Discussion Paper does not define the business model concept. However, the IASB's preliminary view is that financial statements can be made more relevant if the IASB considers, when developing or revising particular Standards, how an entity conducts its business activities. Do you think that the IASB should use the business model concept when it develops or revises particular Standards? Why or why not? If you agree, in which areas do you think that the business model concept would be helpful? Should the IASB define 'business model'? Why or why not? If you think that 'business model' should be defined, how would you define it?
CIPFA generally agrees with the business model concept, and indeed this might be extended to reflect the wider 'operational model' of entities which do not operate as profit seeking businesses. The fact that public sector entities use a different operational model is one of the reasons that some IFRS cannot be sensibly implemented by public sector entities without additional interpretation or guidance. Having said this, we would hope that in applying the business or operational model concept to the development of individual standards, it will be possible in each case to concentrate on key aspects of the model to determine appropriate reporting on a principled basis, rather than generating a proliferation of different accounting treatments for different models.

Question 24 **Unit of account** The unit of account is discussed in paragraphs 9.35–9.41. The IASB's preliminary view is that the unit of account will normally be decided when the IASB develops or revises particular Standards and that, in selecting a unit of account, the IASB should consider the qualitative characteristics of useful financial information. Do you agree? Why or why not?
CIPFA agrees that the choice of the unit of account will normally be made when the IASB develops or revises particular standards. However, it would be helpful if there were some discussion of the criteria or process which might be followed when determining the unit of account, reflecting, for example, that estimates or other measurements of aggregates or portfolios might be more reliable than measurements of disaggregated items, and that this in turn impacts upon the qualitative characteristics of financial information based on different units of account.
Question 25 **Going concern** Going concern is discussed in paragraphs 9.42–9.44. The IASB has identified three situations in which the going concern assumption is relevant (when measuring assets and liabilities, when identifying liabilities and when disclosing information about the entity). Are there any other situations where the going concern assumption might be relevant?
CIPFA generally agrees with the discussion in paragraphs 9.42-9.44 insofar as these apply to the main category of entities for which IFRS are designed. Furthermore, we would note that the public sector contexts in which going concern is evaluated may be different to those which are normally considered by IFRS appliers, but for accounting purposes we would normally expect these to relate to the matters described at paragraph 9.43.
Question 26 **Capital maintenance** Capital maintenance is discussed in paragraphs 9.45–9.54. The IASB plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised Conceptual Framework largely unchanged until such time as a new or revised Standard on accounting for high inflation indicates a need for change. Do you agree? Why or why not? Please explain your reasons.
In line with our comments on Question 12 in respect of measurement or valuation of assets, CIPFA considers that the issue of changing prices and costs is an important issue and would warrant more attention in the Conceptual Framework. It is not merely an issue for highly inflationary economies, but can become significant for any assets or liabilities held over a long period of time. Even moderate inflation has a significant cumulative effect, and specific price changes as well as general price changes need to be considered.