Grant Thornton
An instinct for growth™

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH

Grant Thornton International Ltd
Grant Thornton House
22 Melton Street
London NW1 2EP

17 November 2015

Submitted electronically through the IFRS Foundation website (www.ifrs.org)

ED/2015/3 Conceptual Framework for Financial Reporting

Grant Thornton International Ltd is pleased to comment on the International Accounting Standards Board's (the Board) Exposure Draft ED/2015/3 'Conceptual Framework for Financial Reporting' (the ED). We have considered the ED, as well as the accompanying draft Basis for Conclusions.

We believe that the ED builds successfully on the preceding Discussion Paper and also represents a considerable improvement on the existing Conceptual Framework. We congratulate all concerned on producing a very well-written and coherent document in a relatively short period of time.

We also agree with most of the proposed changes, subject to various detailed comments.

Our most significant comments relate to the following areas.

Prudence

We welcome the re-introduction of the notion of prudence in Chapter 1. However, we consider that the actual wording proposed will not provide useful or meaningful guidance for future standard-setting purposes.

We do agree that, when an entity applies IFRS, the exercise of prudence does not permit the deliberate understatement of assets and income or the overstatement of liabilities and expenses. However, we also believe that an 'asymmetric' notion of prudence is and should continue to be a feature of standard-setting decisions.

Equity

We support the proposal to define equity as a residual for the time being. However, we also suggest that this approach results in the amounts reported as, or within, equity having very limited information value. Accordingly, we encourage it to consider other approaches to defining equity that might result in more useful information as the applicable research project progresses.

Other comprehensive income (OCI)
We support the continued possibility of presenting certain types of income or expense within OCI, at least for the time being. However, although we acknowledge that developing a robust conceptual distinction between profit and loss and OCI might not be practical as part of this project, we do think some more work is needed before issuing a revised Conceptual Framework. This is because we doubt that the discussion in the ED will be sufficient to assist the Board in its future standard-setting decisions about the use of OCI and about recycling. We therefore think that, as a minimum, some discussion of those factors that might contribute to, or detract from, the relevance of profit or loss should be developed to assist the Board in making the necessary judgements.

However, we also believe that the profit and loss versus OCI distinction is a 'blunt instrument' as a means of distinguishing different categories of performance. We therefore welcome the Board's decision to restart a research-level project on performance reporting (the 'Primary Statements' project), and hope that this might lead to the distinction becoming redundant or less important in due course.

Our responses to the ED's Invitation to Comment are set out in the Appendix.

****

If you have any questions on our response, or wish us to amplify our comments, please contact our Global Head of IFRS, Andrew Watchman (andrew.watchman@gti.gt.com or telephone + 44 207 391 9510).

Yours sincerely,

Kenneth C. Sharp

Kenneth C Sharp
Global Leader - Assurance Services
Grant Thornton International Ltd

Responses to Invitation to Comment questions

Question 1 - Proposed changes to Chapters 1 and 2

Do you support the proposals:

(a) to give more prominence, within the objective of financial reporting, to the importance of providing information needed to assess management's stewardship of the entity's resources;
(b) to reintroduce an explicit reference to the notion of prudence (described as caution when making judgements under conditions of uncertainty) and to state that prudence is important in achieving neutrality;
(c) to state explicitly that a faithful representation represents the substance of an economic phenomenon instead of merely representing its legal form;
(d) to clarify that measurement uncertainty is one factor that can make financial information less relevant, and that there is a trade-off between the level of measurement uncertainty and other factors that make information relevant; and
(e) to continue to identify relevance and faithful representation as the two fundamental qualitative characteristics of useful financial information?

Why or why not?

We support the proposed amendments relating to the substance of an economic phenomenon (item (c)) and the continued identification of relevance and faithful representation as the fundamental qualitative characteristics of useful financial information (item (e)). We have no further comments on those proposals.

Our responses to the questions on stewardship (item (a)), prudence (item (b)) and measurement uncertainty (item (d)) are set out below.

Stewardship

We support the changes proposed to Chapter 1 to give greater prominence to the role of stewardship. We also agree with the ED's articulation of this concept as the provision of information that helps users to assess management's stewardship of the entity's economic resources.

We acknowledge that information that is useful for assessing future cash flow prospects will usually also be useful for stewardship decisions. However, we believe that a specific focus on stewardship would have some effect on the Board's future standard-setting decisions. In particular we believe that information on the sources and uses of cash is particularly important for stewardship purposes. We also think that a more explicit focus on stewardship could influence future standard-setting decisions in areas such as the selection of a measurement basis.

We also welcome the acknowledgment (in paragraph 1.22 of the ED) that "information about management's discharge of its responsibilities is also useful for decisions by existing investors, lenders and other creditors who have the right to vote on or otherwise influence management's actions". We believe that the role of financial statements in helping shareholders and other investors to decide whether and how to use their rights to intervene should be acknowledged in the Conceptual Framework.

We have previously called for stewardship to be reinstated as a distinct objective of financial reporting. However, we feel that the ED's proposals to increase the prominence of stewardship address our immediate concerns.

Prudence

We welcome the proposed inclusion of an explicit reference to the notion of prudence. However, we consider that the proposed wording at paragraph 2.18:

- inappropriately defines 'prudence' as synonymous with 'neutrality', which is not its normal meaning and undermines its inclusion in the Conceptual Framework
- fails to acknowledge or reflect the practical application of prudence-type concepts in existing standards
- seems to be more of an instruction to preparers in the application of standards than a concept for use in the development of new standards.

For these reasons we do not believe the proposed amendments will provide useful or meaningful guidance for future standard-setting purposes.

We do agree that, when an entity applies IFRS, the exercise of prudence does not permit the deliberate understatement of assets and income or the overstatement of liabilities and expenses. We also agree that, when an entity develops an accounting policy for a transaction or event not specifically addressed by IFRS, a prudence concept should not permit deliberate bias.

Nonetheless, as noted in our response to the 2013 Discussion Paper, we observe that IFRSs include numerous examples of prudence in practice. Examples include different recognition and disclosure thresholds for assets and liabilities (in IAS 37 'Provisions, Contingent Assets and Liabilities), stricter criteria for recognising deferred tax assets than for liabilities, and stricter criteria for internally-generated intangible assets than for externally purchased intangible assets. An example of a more recent application of prudence is the constraint on the recognition of revenue for variable consideration in IFRS 15 'Revenue from Contracts with Customers'. Asymmetry in recognition seems to be accepted in practice when the amount affects profit and loss. Prudence and recognition asymmetry is inherent in the occasional difference between economic elements. For example, it is widely-accepted practice to recognise a liability for an onerous contract or liability based on probability of an economic loss in the future. By contrast, the economic benefits of a favourable contract are typically recognised later – for example when control of a good or service has been transferred, a liability qualifies for derecognition or goods or services purchased have been consumed or sold on.

Given that prudence is a feature of both existing and forthcoming standards, we believe its role in standard-setting should be acknowledged in the Conceptual Framework. Specifically, the Conceptual Framework should acknowledge that, when dealing with a high degree of uncertainty, the Board might take an 'asymmetrical' approach for the inclusion of revenue or other income/gains in the financial statements than for losses or expenses.

Measurement uncertainty

We support the proposed amendments in paragraphs 2.12-13. This is because we agree that there is a trade-off between measurement uncertainty and relevance.

However, we are concerned that this proposed amendment is undermined by the subsequent proposals in Chapter 5 recognition that describe this trade-off in more detail. For example, paragraph 5.21(a) refers to the range of possible outcomes being "extremely wide" and the likelihood of each outcome being "exceptionally difficult to estimate".

In addition, requiring the recognition of items (or use of measurement bases) with a high degree of estimation uncertainty will typically add costs and complexity for preparers, and result in information that is challenging to audit. Experience also suggests that recognition of items with high estimation uncertainty leads to additional disclosures – and thereby contributes to the perceived disclosure problem.

Finally, consistent with our comments above, we think the Conceptual Framework should acknowledge a link between measurement uncertainty and prudence. The proposed discussion does not provide any indication that the Board might take a more cautious approach in the inclusion of revenue or gains under conditions of a high degree of measurement uncertainty.

Relevance

We note that the current definition of relevance is exclusively focussed on future cash flows, wherein information is capable of making a difference when it has predictive or confirmatory value. We encourage the Board to reconsider how consideration of stewardship could affect the current definition of relevance. We believe that the users of the financial statements want information about performance during a period and current cash flows, including cash flow from operations, and investing and financing activities, regardless of predictive or confirmatory value. While these types of issues are considered in the objective of financial reporting, they are not included in the description of relevance, creating a potential disconnect between the objective of financial reporting and the definition of relevant information.

Question 2 - Description and boundary of a reporting entity

Do you agree with:

(a) the proposed description of a reporting entity in paragraphs 3.11–3.12; and
(b) the discussion of the boundary of a reporting entity in paragraphs 3.13–3.25?

Why or why not?

We generally agree with the proposals in Chapter 3, subject to the following comments.

We note that the ED defines 'reporting entity' by reference to 'entity' but does not attempt to define or describe an 'entity'. The term 'entity' is used extensively in IFRSs and the lack of a definition in either the Conceptual Framework or in the Glossary seems unsatisfactory. If the Board has concluded that no such definition is needed, or that a definition is needed but not in the Conceptual Framework, we suggest that the final Basis for Conclusions should discuss the Board's reasoning.

We agree with much of the discussion in paragraphs 3.13–3.25. However, we find the generalisation in paragraph 3.23 difficult to agree with and think that the discussion of consolidated and unconsolidated financial statements should include some material on circumstances in which the latter could be more useful. The most obvious example is the Board's decision to introduce an exception from consolidation for investment entities. Also, if an entity holds a subsidiary with net liabilities there is an argument that the consolidated statements overstate liabilities if the parent is not obliged to stand behind those liabilities. We think the relative usefulness of consolidated and unconsolidated financial statements depends on the perspective of the particular user.

Finally, we think that, if a reporting entity is not a legal entity (or group or combination of legal entities) it is necessary that its assets, liabilities, income and expenses can be identified objectively. Put another way the boundary of the reporting entity should be sufficiently defined to enable the elements that lie inside that boundary to be distinguished from those that lie outside it. In the absence of such a boundary, there would be no basis to identify a group of assets with a common residual interest and the claims (liabilities) against those assets. If the assets do not have a common current or intended residual interest, there can be no equity and, by definition, no income or expense. In such circumstances the financial statements could not be relevant or representationally faithful. For these reasons we suggest that some discussion is needed of the boundary of a reporting entity that is not a legal entity.

Question 3 - Definitions of elements

Do you agree with the proposed definitions of elements (excluding issues relating to the distinction between liabilities and equity):

(a) an asset, and the related definition of an economic resource;
(b) a liability;
(c) equity;
(d) income; and
(e) expenses?

Why or why not? If you disagree with the proposed definitions, what alternative definitions do you suggest and why?

Asset and liability

We agree with the basic definitions of 'asset' and liability' proposed in paragraph 4.4. We note however that the practical effects of these definitions can be assessed properly only in conjunction with other aspects of the Conceptual Framework – in particular the proposed recognition criteria. As stated earlier, a strictly economic perspective may consider items such as the likelihood of future profits or a favourable outcome on a legal case as assets or reductions in a liability earlier than would be appropriate for financial reporting purposes.

In particular, we agree with the reasons set out on BC4.11-17 for removing from these definitions a reference to an 'expected flow' of economic benefits. These changes should also help to reduce certain anomalies whereby, in accordance with current requirements, the existence of assets or liabilities can depend on whether the unit of account is a single item or a group of items.

Equity

We support the Board's tentative decision to continue to:

- maintain a conceptual distinction between liabilities and equity claims
- define equity as a residual (but see our comments below).

We also agree with the Board's reasoning for pursuing the development of improved guidance on how to distinguish financial liabilities from equity instruments in a Financial Instruments with Characteristics of Equity research project instead of in the Conceptual Framework project.

We welcome the Board's decision not to pursue the proposals in the Discussion Paper on enhancing the statement of changes in equity at this time. Although we agreed that those are one potential means of addressing an 'information deficit', we were concerned that preparing the proposed statement could be complex and that any future requirements should be implemented only after detailed field-testing and careful consideration of costs and benefits.

Notwithstanding our support for continuing to define equity as a residual for the time being, we suggest that this approach result in the amounts reported as (or within) equity having rather limited information value. We believe that alternative approaches – either to the definition of equity or to the information provided about its components – could result in more useful information. Another way of thinking about equity is that it provides a record of investment by capital providers and reinvestment in the form of profits less returns to capital providers. Equity, or specific components of equity, can provide information about the ability of the reporting entity to pay dividends in future. Such information seems of obvious relevance to investors concerned about future cash flows from the entity. Information on treasury transactions and the issuance of shares or options as compensation would be an element of stewardship. To dismiss all of this potential information content as a residual understates the importance of equity. As the Board progresses with its research project on the distinction between equity and liabilities, we encourage it to reconsider describing equity as a residual.

Income and expenses

We agree with the proposed definitions, subject to the comments below.

The ED proposes to maintain the existing approach by which income and expenses are defined by reference to changes in assets and liabilities. We agree that this is generally appropriate. However, we suggested in our response to the Discussion Paper that a revised Conceptual Framework should at least acknowledge the role of income- and expense-driven requirements in the recognition of assets and liabilities. We continue to hold that view.

To explain, we observe that some standards are oriented more towards direct measurement of income or expenses than towards recognition and measurement of assets and liabilities. When such standards are applied, assets and liabilities (or at least debits and credits in the statement of financial position) are then measured by reference to the amount of income or expense. The most obvious example of such a standard is IFRS 15; in applying this standard a contract asset is measured based on the amount of revenue recognised, not vice versa. We think this is entirely appropriate. We therefore suggest that the revised Conceptual Framework should include some discussion of income- and expense-oriented standard-setting.

We also question the assertion in paragraph 4.50 that it follows from the definition of income and expenses that transactions with holders of equity claims acting in that capacity do not give rise to income or expenses. The definition of income and expense makes reference only to contributions from and distributions to holders of equity claims. We suggest instead that assessing whether a holder of an equity claim is acting in that capacity in relation to a transaction is relevant to determining whether that transaction is in substance a distribution or contribution.

Reporting the substance of contractual rights and contractual obligations

We support the discussion in paragraphs 4.45 -4.56. We suggest that paragraph 4.54 should also refer to the fact that terms in a contract could be implied through an entity's past practice.

We note that paragraph 4.55 defines the concept of 'commercial substance' as having no discernible effect on the economics. We have no objection to this broad definition and welcome the Board's initiative to provide guidance within the Conceptual Framework. Nonetheless, we note that existing IFRSs apply the concept of substance in different ways. For example:

- the requirements of IAS 16 and IAS 38 on asset exchanges consider the effects on cash flows, which seems broadly consistent with the proposed guidance in 4.55
- IFRS 10's guidance on substantive rights considers the holder's practical ability to exercise its rights, which is consistent with 4.55(b)
- IAS 32's approach to assessing classification of a financial instrument as equity or liability in accordance with the substance of the contractual arrangement can result in liability classification even if a cash outflow would arise only on occurrence of a very unlikely event. This does not necessarily seem consistent with the proposed approach
- IFRS 9 and IAS 32 refer to a concept of 'not genuine' in certain areas. This seems to be a narrower assessment than 'not substantive'. Contractual features that have an effect only in remote circumstances are capable of being 'genuine'. However, IFRS 9 also states that a "cash flow characteristic is not genuine if it affects the instrument's contractual cash flows only on the occurrence of an event that is extremely rare, highly abnormal and very unlikely to occur".

In view of these differences, we think it is important that the Board analyses how the concept of substance is currently applied in finalising this guidance. In particular, we suggest that the concepts of 'remoteness' and 'not genuine' should be considered.

Question 4 – Present obligation

Do you agree with the proposed description of a present obligation and the proposed guidance to support that description? Why or why not?

We agree with the general direction of the proposed description, subject to some detailed comments and clarifications. We explained in our response to the Discussion Paper our reasons for favouring an approach along the lines of View 2 (as described in BC4.55 and in the Discussion Paper).

We note that a reference to 'past events' appears in both the basic definition of a liability and in the definition of a present obligation. We suggest this reference could be removed from the basic definition given that the detailed description of past events follows the description of a present obligation.

Also in 4.31(b), we are concerned that the reference to 'establish the extent of its obligation' might cause confusion. This terminology seems to confuse concepts of existence with measurement. The additional explanation in paragraph 4.37 helps to clarify the Board's intentions but we think the potential for confusion remains. In particular it is not clear how this guidance would relate to situations such as litigation claims or regulatory breaches in which the basis for determining the quantum of damages or penalties is not specified.

Question 5 - Other guidance on the elements

Do you have any comments on the proposed guidance?

Do you believe that additional guidance is needed? If so, please specify what that guidance should include.

We note that existing Standards seem to take a different approach to constructive obligations in the context of financial liabilities. We do not necessarily disagree with this but suggest that a revised Conceptual Framework should acknowledge and explain the reasons for this.

Question 6 - Recognition criteria

Do you agree with the proposed approach to recognition? Why or why not? If you do not agree, what changes do you suggest and why?

We generally agree with the proposed approach to recognition. We think the proposed guidance in the ED is significantly better than that in the 2013 Discussion Paper.

In particular we agree that:

- an asset, liability (etc) should only be recognised if it meets the applicable definition
- not all elements can or should be recognised however
- the assessment of whether or not to recognise an element should take into account relevance, faithful representation and the balance of costs and benefits
- it may not be relevant or cost effective to recognise an element if it is too uncertain whether the asset or liability exists or is separable from goodwill, the probability of an inflow or outflow of economic benefits is low or the level of measurement uncertainty is excessive.

Despite our overall support we continue to find the discussion of the role of 'faithful representation' unhelpful. We agree that an ability to achieve a faithful representation should be a criterion for recognition. However, the discussion in 5.22-23 seems unlikely to be a useful tool in deciding what should and should not be recognised in practice. The discussion should be expanded to include some reference to situations in which achieving a faithful representation may not be possible, or would be possible only at a cost that exceeds the benefits.

We also have a concern over the phrasing in paragraph 5.21(a) that "the range of possible outcomes is **extremely** wide and the likelihood of each outcome is **exceptionally** difficult to estimate" (our emphasis). In our view this discussion seems likely to underplay the role of reliability. We also find this emphasis inconsistent with the manner in which reliability concepts have been applied in IFRS 15 and the forthcoming leasing standard.

Question 7 - Derecognition

Do you agree with the proposed discussion of derecognition? Why or why not? If you do not agree, what changes do you suggest and why?

We generally agree with the proposed approach to derecognition.

We agree that the aim of derecognition guidance should be to depict faithfully the assets and liabilities retained after the transaction or other event, and the resulting change in the entity's assets and liabilities. We would prefer, however, that the final guidance refers to faithful representation of the income and/or expenses that result from the transaction or event as well or instead of the resulting change in assets and liabilities.

We suggest this on the basis that some derecognition requirements in existing standards are driven by the recognition of the related revenue or income. In particular IAS 2 states that when inventories are sold, their carrying amount is recognised as an expense when the related revenue is recognised.

The draft guidance does not refer to the linkage between derecognition of assets and recognition of liabilities. We note that a consequence of transferring an asset in a transaction that 'fails' derecognition is that the proceeds are recognised as a liability. Said differently, deciding on the appropriate accounting treatment for a transfer with a linked transaction depends in part on whether the substance of the overall arrangement is a sale or a financing. We suggest this should be acknowledged in the final guidance.

We welcome the inclusion of a discussion about modification of contracts and the link to derecognition. We also think the discussion in paragraphs 5.34 and 5.35 about whether the new rights and obligations are 'distinct' should be helpful in the context of contracts for non-financial items that are accounted for on a gross basis. We doubt this guidance will be relevant for developing standards-level derecognition guidance for financial assets or liabilities.

We have a concern with regard to paragraph 5.27(b), which refers to not recognising income or expense on the retained component in the context of a partial derecognition. We question how this relates to existing requirements for remeasurement of a retained interest on loss of control of a subsidiary or loss of significant influence (or joint control) over an equity-method investee. In these 'change of status' events the nature of the retained interest is, or is regarded, as substantially different in character to the pre-transfer interest. We also note that existing IFRSs do not provide explicit guidance on some change of status events and, accordingly, entities have developed their own accounting policies for dealing with these. As such, any discussion in the Conceptual Framework will influence the policies that entities adopt and could lead to changes in accounting policies. For these reasons we suggest that the discussion of (non-)remeasurement of retained interests is expanded to include change of status events.

Question 8 - Measurement bases

Has the IASB:

(a) correctly identified the measurement bases that should be described in the Conceptual Framework? If not, which measurement bases would you include and why?
(b) properly described the information provided by each of the measurement bases, and their advantages and disadvantages? If not, how would you describe the Information provided by each measurement basis, and its advantages and disadvantages?

We agree with the broad classification of measurement bases into historical cost and current value. We also largely agree that Section 6 properly describes the information provided by each of the measurement bases, and their advantages and disadvantages.

We would question some of the assertions about the advantages of fair value in terms of comparability. For example, paragraph 6.31 asserts that, when using fair value "identical assets will (subject to estimation error) be measured at the same amount". There are technical reasons why this might not be the case, such as different units of account and access to different markets. There are also practical limitations to comparability when observable prices are not available and unobservable inputs are required (we would not describe the differences that result as "estimation error"). We also note that fair value, and the market participant perspective that underlies it, is a hypothetical concept when applied to assets and liabilities that are not in practice acquired or transferred in the same unit of account.

With regard to liabilities and fair value, we suggest that the discussion of the impact of own credit risk should be expanded (with reference to paragraph 6.24). The impact of changes in own credit risk on reported financial performance should be separately highlighted in Table 1, reflecting the well-aired concerns and past standard-setting action in this area.

Question 9 - Factors to consider when selecting a measurement basis

Has the IASB correctly identified the factors to consider when selecting a measurement basis? If not, what factors would you consider and why?

We generally agree with the proposed factors to consider when selecting a measurement basis, subject to the following comments. We think this discussion represents significant progress in addressing a gap in the existing Conceptual Framework, and is also a significant improvement on the Discussion Paper.

We very much welcome the fact that the proposals refer to:

- cost (paragraph 6.53)
- the importance of considering the information produced in the statement of financial performance as well in the statement of financial position (paragraph 6.53)
- measurement uncertainty (paragraphs 6.55-56)

We also agree that the way in which an asset or a liability contributes to future cash flows should be considered in selecting a measurement basis (paragraph 6.54). That said, we note this guidance is from an asset and liability perspective. We would welcome some discussion of the criteria for selecting a measurement basis from a financial performance perspective.

More generally, we think it would be useful to link the material on information provided by different measurement bases in the different statements (paragraph 6.47) with the discussion on selection. Put another way, what factors (apart from the way in which an asset or a liability contributes to future cash flows) would be considered when determining whether the information provided by each measurement basis contributes to, or detracts from, relevance, representational faithfulness and the enhancing characteristics?

In selecting measurement bases, we think the Conceptual Framework should also discuss disclosure implications. We observe that the greater use of measurements with a high degree of estimation uncertainty (an obvious example being level 3 fair values) tend to result in increased disclosures. In our view a particular measurement basis is less understandable if complex and/or voluminous disclosures are considered necessary to explain the methods and assumptions used in its application.

We are not convinced by the guidance on internally constructed assets in paragraph 6.73, which asserts that fair value information is useful in order to assess the cost-effectiveness of the construction process. We agree with the statement regarding the difficulty of estimating fair value (in addition to the estimation of cost, which would be affected by matters such as whether the asset is funded by debt or equity). We also think the real issue is whether recognition of a gain (or loss) is more relevant on completion of construction or only on sale. Why should a different approach be taken for internally-constructed property, plant & equipment than for inventory?

Question 10 - More than one relevant measurement basis

Do you agree with the approach discussed in paragraphs 6.74–6.77 and BC6.68? Why or why not?

We agree that using different measurement bases for the statement of financial position and the statement of profit or loss can sometimes enhance the usefulness of the financial statements and provide benefits outweighing the costs. We would not describe this as "needed" however (with reference to paragraph 6.74).

We also agree that using a single measurement basis is usually more appropriate.

We question the reference in paragraph 6.75(b) to disclosure in the notes of additional information about the other measurement basis. We acknowledge this exists in some standards but we are not convinced it should be legitimised by the Conceptual Framework at this time. Our preference would be to remove this pending the outcome of work on the boundaries of disclosure in the Principles of Disclosure project.

Question 11 - Objective and scope of financial statements and communication

Do you have any comments on the discussion of the objective and scope of financial statements, and on the use of presentation and disclosure as communication tools?

We agree with the points made in the discussion in paragraphs 7.8–7.18 and with the explanation in BC7.17–BC7.23.

We agree in particular with the statement in 7.17 to the effect that there is a trade-off between flexibility and comparability in terms of presentation and disclosure requirements. In evaluating this trade-off in future standard-setting decisions, we would caution against responding to concerns about disclosure overload by veering too far towards flexibility and discretion. We believe that the financial statements and the related notes should be a reasonably comprehensive source of information that can be utilised by a wide range of users. The first cut at determining relevance lies with the standard-setter that specifies the disclosure requirements. Judgements about the specific relevance of that information should normally be left to the users of the financial statements and their advisors who can select which information to incorporate into their analysis.

Better use of technology, such as standardised XBRL taxonomies, can reduce the cost of accessing and utilising that data. Transferring judgement about the relevance of information to the preparer also could increase the cost of financial reporting by increasing the amount of time and level of expertise required to make disclosure decisions and the risk of adverse regulatory or legal consequences when different judgements are made in the light of subsequent events. We note that some of the most important revelations about the quality of financial reporting come from evaluating information across entities. The ability to conduct meaningful research based on uniform disclosure rules is of value to all investors. So while it is easy to criticise a checklist approach to disclosure, standardised disclosures (in terms of the scope of information provided not the specific content) may be the lowest cost alternative for maximising the usefulness and comparability of financial statements.

We support limiting the guidance in the Conceptual Framework to the underlying concepts. We agree that more detailed guidance on how preparers can improve the effectiveness of their financial statements as a communication tool would be more appropriately provided in standards-level or other guidance.

Question 12 - Description of the statement of profit or loss

Do you support the proposed description of the statement of profit or loss? Why or why not?

If you think that the Conceptual Framework should provide a definition of profit or loss, please explain why it is necessary and provide your suggestion for that definition.

We agree with the proposed discussion as far as it goes. We also agree that it may not be necessary or even feasible to define profit or loss as part of this project.

As noted in our responses to questions 13 and 14, however, we:

- suggest that the Conceptual Framework or its Basis for Conclusions should include some discussion of the factors that might contribute to, or detract from, the relevance of profit or loss. This would provide more help to the Board in making decisions about presenting certain types of income or expense in other comprehensive income (OCI), and on recycling
- believe that profit and loss versus OCI distinction is a 'blunt instrument' as a means of distinguishing different categories of performance. Developing a conceptual basis for the distinction also seems to be an intractable problem. We therefore welcome the Board's decision to restart a research-level project on performance reporting (the 'Primary Statements' project), and hope that this might lead to the distinction becoming redundant or less important in due course.

Question 13 - Reporting items of income or expenses in other comprehensive income

Do you agree with the proposals on the use of other comprehensive income? Do you think that they provide useful guidance to the IASB for future decisions about the use of other comprehensive income? Why or why not?

If you disagree, what alternative do you suggest and why?

The ED's proposals would maintain the use of a profit or loss subtotal along with the possibility of selective use of other comprehensive income (OCI). The ED proposes a rebuttable presumption that income and expenses will be presented in profit or loss, with possible rebuttal (other than for precluded categories) if the use of OCI would enhance the usefulness of the profit or loss subtotal. Overall, we support the continued possibility of using OCI as means to enhance the relevance of profit or loss for the time being.

As acknowledged in BC7.36 (and elsewhere), the ED does not attempt to define OCI or set a clear distinction between profit or loss and OCI. Indeed the ED's proposals seem less specific than those in the 2013 Discussion Paper on the circumstances in which OCI might be used (noting that the DP classified the circumstances for use of OCI into bridging items, mismatched remeasurements and transitory remeasurements). Accordingly, the ED provides neither a conceptual basis for distinguishing profit and loss and OCI nor practical guidance that will be helpful for standard-setting purposes.

While we view this lack of guidance as an unfortunate gap in the proposals, we fully acknowledge the lack of consensus among constituents and other challenges faced by the Board that have led to this situation. Given the seeming intractability of this issue, we believe that a longer-term solution is more likely to be found by developing other ways to enhance the presentation of different components of financial performance. We expand on this comment below.

Pending the outcome of further work on performance reporting, standards-level decisions about OCI would continue to be based on the IASB's judgements about whether recycling would enhance or detract from the relevance of profit or loss. In view of this, we have the following comments:

- although it may not be feasible to 'define' profit or loss at this time, some discussion of those factors that might contribute to, or detract from, the relevance of profit or loss would assist the Board in making the necessary judgements
- while we agree that presentation of income or expenses in profit or loss should be the norm, we do not support a rebuttable presumption in the absence of clearer guidance on the circumstances in which the rebuttal would be appropriate
- we note that the selection of a measurement basis should consider the effects on both financial position and financial performance. Accordingly, if the Board is conspiring a particular measurement basis but is concerned that it might result in information in profit or loss that is not relevant, or detracts from relevance, the use of that measurement basis should be reconsidered.

More broadly, however, we doubt that a profit and loss versus OCI distinction is the best means of providing disaggregated information about financial performance. The downsides of this distinction include that:

- it is a rather 'blunt instrument' in that it mixes quite different types of gain or loss
- OCI is not used consistently (eg some equity investments are measured at FVTOCI but investment properties are measured at FVTPL)
- the Board will continue to come under pressure to utilise OCI as a compromise solution from time to time.

Ultimately we believe there might be better ways to enhance presentation that could result in OCI becoming redundant or less widely used. We therefore welcome the Board's decision to restart a research-level project on performance reporting (the 'Primary Statements' project).

At a more detailed level, we question whether the language in paragraph 7.23 is appropriate. This prohibits rebuttal of the presumption that income and expense are presented in profit or loss for certain types of income or expense. While we agree that presenting the types of income or expense outside profit or loss seems unlikely to enhance the usefulness of that metric, the prescriptiveness of this prohibition also seems inconsistent with the overall tone of the Conceptual Framework and with the judgemental nature of decisions about how to utilise OCI.

Question 14 - Recycling

Do you agree that the Conceptual Framework should include the rebuttable presumption described above? Why or why not?

If you disagree, what do you propose instead and why.

The ED proposes a presumption in favour of recycling that can be rebutted in certain circumstances - for example, in the absence of a clear basis for identifying the period in which the income or expense should be recycled. The ED also proposes that recycling will be required if it enhances the relevance of profit or loss for that period.

We doubt that this guidance would be of much practical help to the Board when making future standard-setting decisions. This is because, consistent with our response to Question 13, the effects of this guidance would depend primarily on the IASB's judgements about whether the relevance of profit or loss would be enhanced by recycling. Without some additional guidance on factors that contribute to or detract from the relevance of profit or loss, those judgements would be made in something of a vacuum.

That said, we appreciate the difficulties and challenges of identifying a clear principle for recycling and understand that it might not be feasible to provide more detailed guidance at this time. If the Board decides to proceed along the lines proposed we would suggest removing the rebuttable presumption in favour of recycling and replacing it with a neutral statement to the effect that recycling will be required if it will enhance the relevance of profit or loss and prohibited if it will not.

We also note that the recycling question is relevant only for certain types of OCI. In certain situations where OCI is used the accounting mechanics automatically result in cumulative OCI reducing to zero over the life of the transaction. We suggest that the text of the Conceptual Framework should refer to this in order to clarify and limit the scope of the recycling guidance.

Decisions about recycling OCI will depend on judgements about 'P&L relevance' and will therefore be subject to the same challenges as decisions about initial presentation in OCI. However, we think there are some distinct conceptual factors that could guide decisions about recycling. These include:

- *realisation*: some argue that a gain or loss becomes relevant, or more relevant, on 'realisation' and would see this as a trigger for recycling. In a similar vein, some argue that profit or loss should provide a record of realised profit over time. While, in general, 'realisation' is not a pervasive concept in IFRS it does seem to have a part to play in decisions about recycling
- *multiple recognition*: we are aware that some commentators do not support recycling based on a view that items of income and expenditure should be reported in financial performance only once. This view is partially expressed in the Alternative View of Mr Cooper and Mr Finnegan at AV7. We note that past standards-level decisions and the ED's proposals implicitly take a different view. We also agree that recycling is consistent with treating profit or loss as the primary measure of financial performance
- *periodic versus cumulative relevance:* judgements about the relevance of profit or loss will be influenced by whether a discrete period view of performance is taken, or a cumulative view. Recycling of a cumulative gain or loss on disposal of an asset that has been measured at fair value through OCI does of course result in the P&L impact being recorded in a single period, while the changes in value have occurred over the holding period.

Although we understand that the IASB does not intend to provide detailed guidance on when reclassification may be appropriate, we believe that some discussion of these factors may help to guide future decisions.

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

Do you agree with the analysis in paragraphs BCE.1–BCE.31? Should the IASB consider any other effects of the proposals in the Exposure Draft?

We agree with the analysis in paragraphs BCE.1–BCE.31, subject to the comments below.

We do not fully agree with the statements in BCE.7(a) concerning inconsistency between IAS 32 *Financial Instruments: Presentation* and the existing Conceptual Framework's definitions and the proposed definitions of liability and equity. We agree that, in general, an obligation to issue an entity's own equity instruments is not a liability by definition since the entity's own equity instruments are not assets of that entity. However, the proposed substance over form guidance also needs to be considered. We think an obligation to issue shares can at least be considered to be a financial liability in substance when the terms of the obligation indicate that the entity is using its own shares as currency. This issue will presumably be considered in the Board's research project.

Question 16 - Business activities

Do you agree with the proposed approach to business activities? Why or why not?

We agree with the discussion in BCIN.28 – BCIN.34.

We consider a business model to be something created to solve a particular class of business problem and create value via a particular profit formula. Differences in business model do not in general seem to us to be an appropriate basis for differences in accounting principles. We suggest that existing applications of the term 'business model', in particular in financial asset classification, in fact focus on the actual or expected outcomes of the entity's business and not on the business model itself.

We do however concur that the manner in which an asset or liability is expected to be used is one factor to consider in selecting a measurement basis and unit of account, and is also relevant for making standard-setting decisions about presentation and disclosure. We support recent research that focuses on the difference between assets whose value is realised in exchange transactions and those whose value is realised in use, usually in conjunction with other assets and liabilities.

Management intent can be relevant. For example, if the reporting entity intends to dispose of productive assets instead of consuming them, we believe that management's intent justifies a change in the measurement basis and prospective accounting up to the point where the value of those assets is realised in an exchange transaction. The criteria for determining when intent could change a measurement basis would most likely be best addressed at the standards level.

We also support the decision not to include a broader discussion of the role of an entity's business model in the revised Conceptual Framework at this time. We think it would be inappropriate to include more pervasive guidance on the role of business model concepts in the absence of a definition of business model and a fuller analysis of how it might affect the IASB's decisions.

Question 17 - Long-term investment

Do you agree with the IASB's conclusions on long-term investment? Why or why not?

We agree with the discussion in BCIN.35 – BCIN.44. We concur that there is no need to include additional guidance in the Conceptual Framework on the information needs of long-term investors for the purpose of future standard-setting.

In this context we also support the recommendations in the June 2014 paper by the 'B20' Panel of six international accounting networks *Unlocking Investment in Infrastructure: is current accounting and reporting a barrier?* This report, to which Grant Thornton contributed, makes a small number of recommendations on the future development of IFRS, including:

- continuing to work with priority on the issuance of a global standard on insurance contracts
- giving further consideration to performance reporting as part of the Conceptual Framework and Disclosure Initiative projects.

However, the B20 report does not identify any particular bias towards short-term investors in existing standards. To the extent that an information gap exists from the perspective of longer-term investors, the report suggests that changes in the broader corporate model are needed to address them.

Question 18 - Other comments

Do you have comments on any other aspect of the Exposure Draft? Please indicate the specific paragraphs or group of paragraphs to which your comments relate (if applicable).

As previously noted, the IASB is not requesting comments on all parts of Chapters 1 and 2, on how to distinguish liabilities from equity claims (see Chapter 4) or on Chapter 8.

The discussion of capital maintenance concepts in Chapter 8, which is carried forward unchanged from the existing Conceptual Framework seems outdated. It is not clear to us that this guidance will be useful as a practical tool when making future standards-setting decisions. We understand that the Board is not requesting comments on this material, but we nonetheless question whether it is appropriate to include this section in the revised Conceptual Framework. The Board's decision to remove the research project on high inflation from the research programme (subject to feedback in the next Agenda Consultation) raises additional doubts as to the usefulness of Chapter 8.

We have no other comments.