Session 1
The Regulatory and Conceptual framework

Learning Outcome

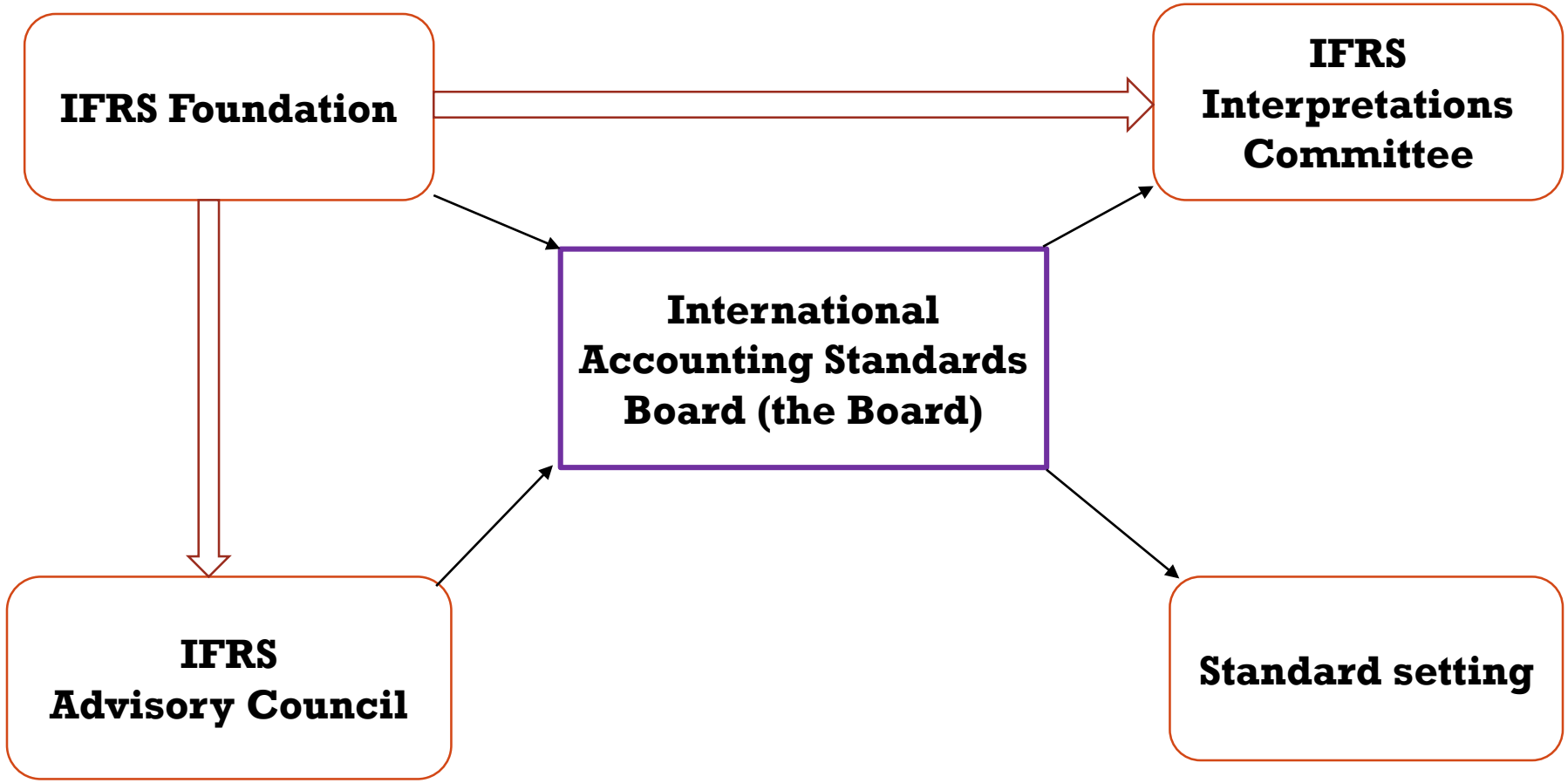
By the end of this session you should be able to:

- explain why a regulatory framework is needed
- distinguish between a principles-based and a rules-based framework
- describe the International Accounting Standards Board's (the Board's) standard
- describe a conceptual framework
- discuss what an alternative system to a conceptual framework might be
- define and discuss fundamental and enhancing qualitative characteristics
- define and explain recognition in financial statements

and answer questions relating to these areas.

Overview

Regulatory framework



Producer: Khotso Moea

The standard setting process

- **International Financial Reporting Standards Foundation (the Foundation)**: responsible for governance of the IFRS Standard setting process
- **International Financial Reporting Standards Board (the Board)**: responsible for setting IFRS Standards
- **IFRS® Interpretations Committee (IFRIC®)**: issues guidance where divergent interpretations have arisen
- **IFRS Advisory Council**: forum for experts to offer advice to the Board.

Why a framework is needed

- to ensure the achievement of relevant and reliable financial reporting in order to meet the needs of users.
- full regulation of financial statement preparation cannot be achieved by accounting standards alone.

Standard setting process

International standard setters

- the Board identifies a subject requiring a new standard
- the Board establishes an Advisory Committee to recommend appropriate treatment
- Exposure Draft is issued for public comment
- having considered comments received, the Board publishes the standard

National standard setters

- committed to a framework of standards based on IFRS Standards
- trend towards harmonisation means national standards are unlikely to be produced that conflict with IFRS Standards

Principles-based V Rules-based Accounting

Principles-based accounting

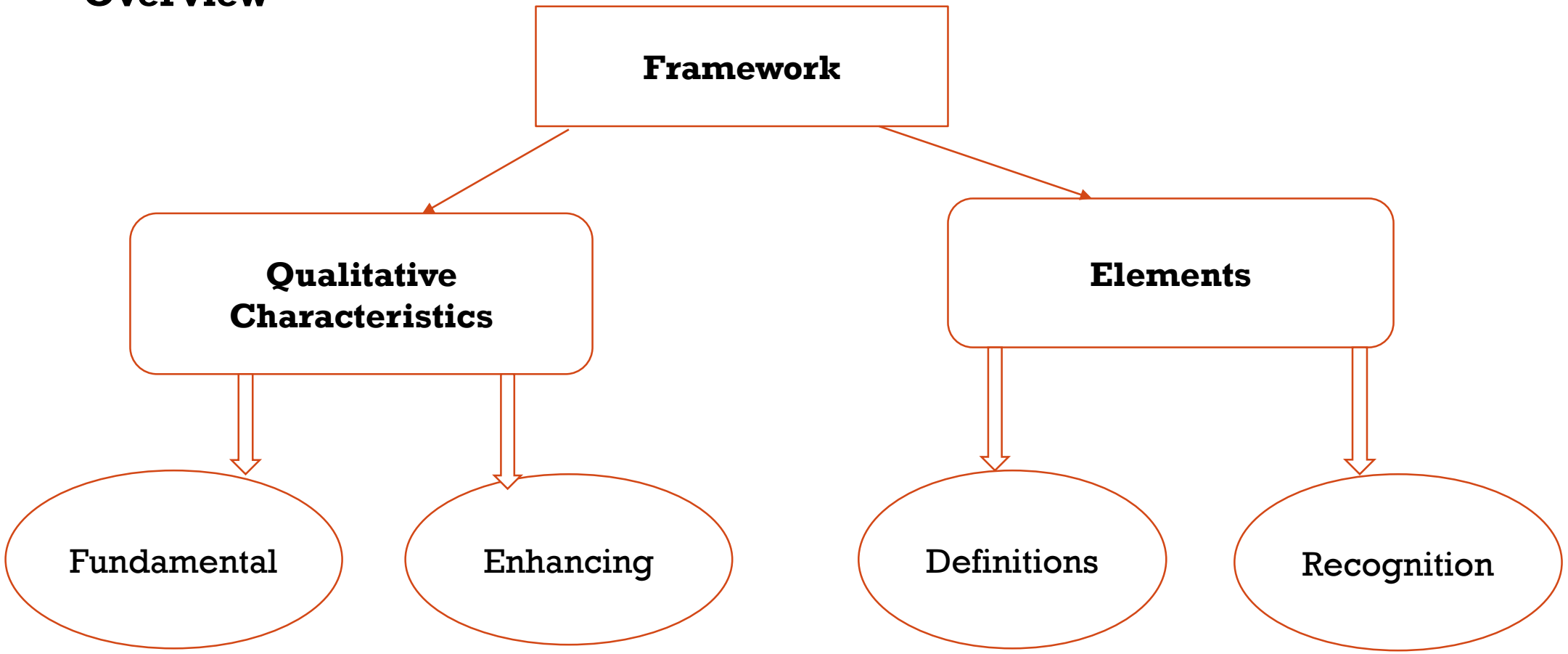
- follows a conceptual framework, such as the Board's Framework
- accounting standards are created based on the conceptual framework

Rules-based accounting

- accounting standards are a set of rules to be followed
- often described as a 'cookbook' approach

The conceptual framework

Overview



Qualitative Characteristics

Fundamental qualitative characteristics

Relevance

Relevant financial information is capable of making a difference in the decisions made by users, i.e. if it has:

- Predictive value; and/or
- Confirmatory value.

Materiality

Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information.

Faithful representation

To be useful, financial information must faithfully represent the phenomena it purports to represent.

A perfect faithful representation would be:

- Complete
- Neutral
- Free from error

Prudence

'The exercise of caution when making judgements under conditions of uncertainty'
(*Conceptual Framework*, para.2.16)

Qualitative characteristics

Enhancing qualitative characteristics

Comparability

Information is more useful if it can be compared with similar information about:

- Other entities; and
- Other periods.

Consistency helps achieve comparability.

Verifiability

Assures users that information faithfully represents the economic phenomena it purports to represent

Verification can be direct or indirect

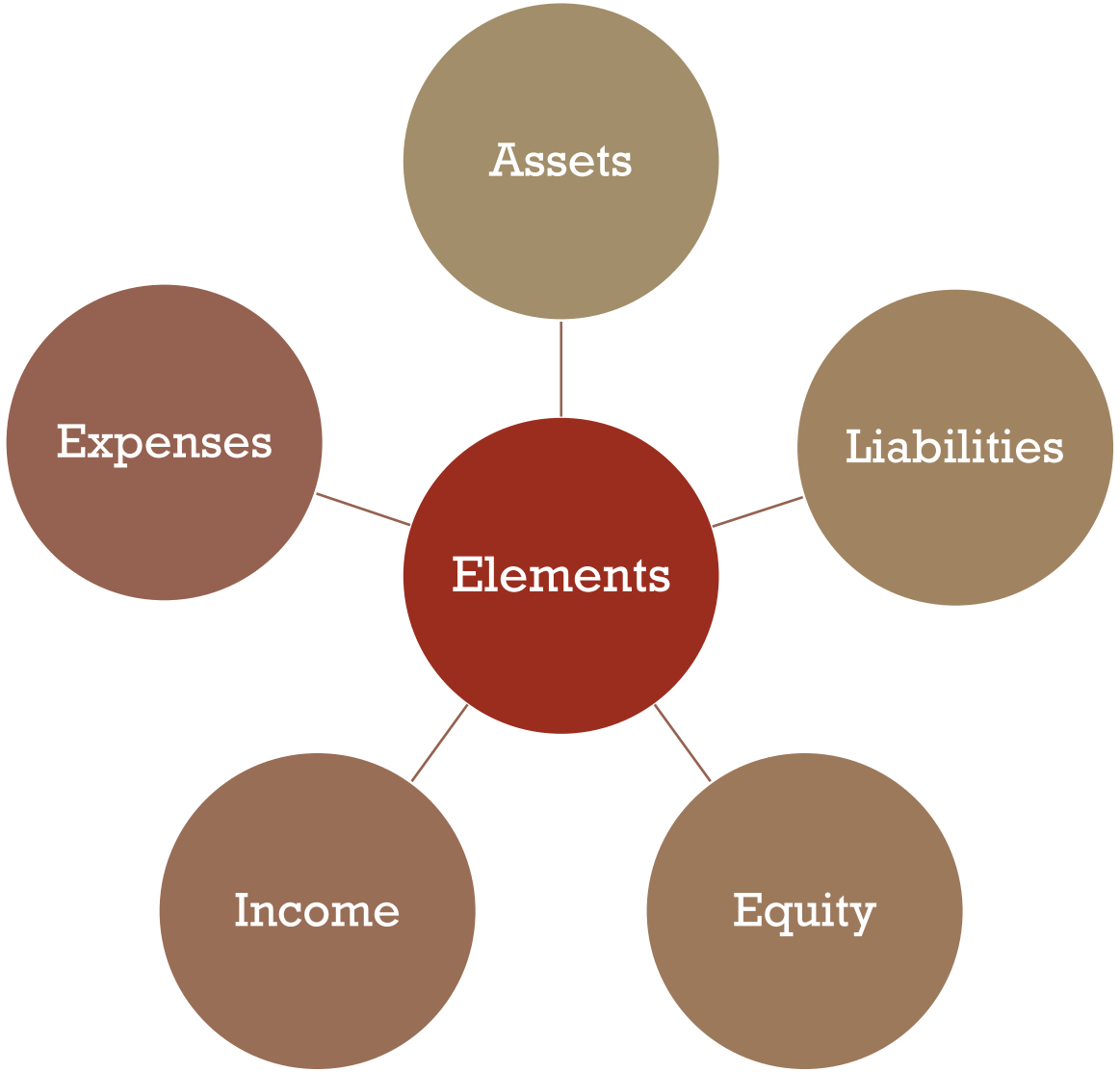
Timeliness

Having information available to decision-makers in time to be capable of influencing their decisions

Understandability

Classifying, characterising and presenting information clearly and concisely

The elements of financial statements



Definitions

Asset

- resource controlled by the entity as a result of past events
- expected to result in an inflow of economic benefit

Liability

- present obligation as a result of a past event
- expected to result in an outflow of economic benefit

Equity

- residual interest in assets after deducting all liabilities

Income

- increases in economic benefits in the form of inflows
- or enhancements of assets or decreases of liabilities

Expenses

- decreases in economic benefits in the form of outflows
- or depletions of assets or incurrences of liabilities

Recognition

In order to be recognised, an item that meets the definition of an element must also meet the following criteria:

- a probable flow of economic benefit is associated with the element
- the element can be measured reliably.

Practice Question

Which of the following best describes the role of the IFRS Advisory Council?

A. To prepare interpretations of IFRS Standards
B. To provide the Board with the views of its members on standard setting projects
C. To promote the use of IFRS Standards amongst its members
D. To select the members of the Board