

THE CHAIRPERSON



Floor 46, One Canada Square,
London E14 5AA UNITED KINGDOM

t: +44(0) 20 7382 1776

f: +44(0) 20 7382 1771

info@eba.europa.eu

www.eba.europa.eu

EBA/2015/D/376

Hans Hoogervorst
Chairman
International Accounting Standard Board (IASB)
30 Cannon Street
London, EC4M 6XH

25 November 2015

Exposure Draft: Conceptual Framework for Financial Reporting

Dear Mr Hoogervorst

The European Banking Authority (EBA) welcomes the opportunity to comment on the IASB's Exposure Draft ED/2015/3: *Conceptual Framework for Financial Reporting* (ED). The EBA has a strong interest in promoting sound and high quality accounting and disclosure standards for the banking and financial industry, as well as transparent and comparable financial statements that would strengthen market discipline.

The EBA welcomes the progress made by the IASB in developing proposals to amend, clarify and update the current Conceptual Framework for Financial Reporting (CF) in light of the responses received on the Discussion Paper: *A Review of the Conceptual Framework for Financial Reporting* (DP) on which the EBA has also commented¹. The revised CF should improve financial reporting by providing a more complete, clear and updated set of concepts for the IASB to consider during the standard-setting process, for the preparers during the implementation of standards, and for the users of financial statements during the interpretation of financial information, without limiting the flexibility to develop a specific treatment in the individual standards.

In line with our previous comments on the DP, the EBA welcomes the reintroduction of the notion of prudence. In addition, we would encourage the IASB to clarify in the main text that not all asymmetry is inconsistent with neutrality as is currently explained in the basis for conclusions (BC2.11 and 2.14).

The EBA would welcome further assessment by the IASB on the impact of the removal of the probability threshold in conjunction with the application of the proposed recognition criteria in ED on the type and amounts of assets and liabilities to be recognised compared to the current standards.

¹<https://www.eba.europa.eu/documents/10180/547248/EBA+Comment+Letter+on+IASB+DP+Conceptual+Framework.pdf>

The EBA agrees with the high-level provisions provided in the ED concerning the statement of profit or loss. However, we would encourage the IASB to continue working on developing a conceptual basis which addresses the definition and the purpose of the statements of profit or loss and other comprehensive income, and the conditions under which recycling should occur, in order to guide the development of future IFRS, even if we also acknowledge the difficulties in doing so. Having an adequate conceptual basis may avoid future discussions when setting new Standards and it may also help users assessing the financial performance of an entity.

Our comments on the ED are set out in the Annex. We have not explicitly addressed the specific questions raised in the ED.

If you have any questions regarding our comments, please do not hesitate to contact us.

Yours sincerely

signed

Andrea Enria

Encls: Annex

Annex

Chapter 2 - Qualitative characteristics of useful financial information

The EBA agrees that if measurement uncertainty is high, an estimate is less relevant than it would be if it were subject to low measurement uncertainty as stated in paragraph 2.13 of the ED. The proposed paragraphs 2.12 and 2.13 of the ED confirm that the use of estimates is an essential part of the preparation of financial information which needs to be properly described and disclosed. The EBA notes that paragraph 2.13 of the ED states that there is a trade-off between the level of measurement uncertainty and *other factors* that make information relevant. However, there are no examples in the ED of what '*other factors*' could be. The EBA considers that additional examples should be introduced into the CF to clarify the nature of '*other factors*' in order to help users and preparers of financial information to understand the trade-off between measurement uncertainty and other factors that make financial information relevant. Additionally, the EBA acknowledges measurement uncertainty as a factor affecting the relevance of financial information but would suggest that the IASB investigates further whether measurement uncertainty may also have a role to play in faithful representation.

In addition, the IASB states in paragraph BC2.25 that “there is much in common between the description of reliability in the pre-2010 framework and the description of faithful representation proposed in the exposure draft”. The EBA considers it would be helpful if the IASB could describe the remaining differences between the concept of reliability (as in the pre-2010 Framework) and the concept of faithful representation (as proposed in the ED) to address the respondents' comments on the use of the term 'faithful representation'.

The EBA acknowledges the decision of the IASB to define primary users strictly. However, banking regulators also rely on financial information to carry out their duties, in particular accounting data is used as a basis for prudential assessments. For this reason, we believe that the IASB should recognise regulators more strongly as users in paragraph 1.10 of the ED as currently it only says that regulators “may also find general purpose financial reports useful”.

Chapter 4—The elements of financial statements

The proposed definition of assets in the ED is similar to the definition in existing CF but with the reference to the 'expected' inflows replaced by the notion of 'has the potential to produce economic benefits'. The EBA has expressed the concern in its previous comment letter on the DP that the revised definition might increase the range or quantum of assets that will need to be assessed against the recognition criteria. Nevertheless, we acknowledge as the IASB explains in

BC4.15 that this concern could be addressed in the recognition criteria instead of in the definitions.

In addition, we would have preferred to have some additional guidance on the distinction between liabilities and equity instruments in the ED. However, we encourage the IASB to explore this issue further in its *Financial Instruments with Characteristics of Equity* research project.

Chapter 5—Recognition and derecognition

The EBA welcomes the additional clarifications in the ED regarding the recognition of items taking into account measurement uncertainty, the probability of the cash flows and if it is uncertain whether these items exist. The proposed approach to recognition is based on the exercise of judgement taking account more than a single criterion for recognising an item, as is mentioned in paragraph 5.14 of the ED, and therefore it should reflect more appropriately the substance of the economic phenomena. However, the EBA would welcome further assessment by the IASB on the impact of the removal of the probability threshold in conjunction with the application of the proposed recognition criteria in ED on the type and amounts of assets and liabilities to be recognised compared to the current standards. For instance, we are concerned about the possible interpretation of paragraph 5.19 of the ED as it refers to ‘very low probabilities of inflows and outflows of economic benefits’ which may therefore broaden substantially the scope of assets being recognised.

In addition, we agree with the IASB’s view in the Basis for Conclusions (BC2.11 and 2.14) that not all asymmetry is inconsistent with neutrality and therefore that in some circumstances accounting policies that treat gains and losses asymmetrically could be selected, if their selection is intended to result in relevant information that faithfully represents what it purports to represent, such as is the case in the current IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, which requires different recognition thresholds for contingent liabilities and contingent assets. However, these are important aspects that the IASB should clarify in the main text of the CF.

Regarding the proposed discussion on derecognition, the EBA welcomes the introduction of general and high-level guidance regarding derecognition of items instead of prescriptive requirements, which may impose unnecessary limitations on the future development of Standards or may have unintended adverse consequences for financial reporting by entities.

Chapter 6—Measurement

The EBA welcomes the explicit explanation in the ED that there is a range of relevant measurement attributes; and also the acknowledgment in the framework that an entity's business model may be relevant to measurement.

The EBA is of the view that the wording of paragraph 6.18 of the ED concerning current cost measurement is not clear and we would appreciate a more thorough explanation of its definition, its classification as historical cost and a clear distinction of it from other measurement basis (for example current value).

Chapter 7—Presentation and disclosure

The EBA welcomes the inclusion of high-level concepts in the ED regarding presentation and disclosure of information in the financial statements and acknowledges the IASB's current work on improving disclosures through the IASB Disclosure Initiative. However, the EBA would appreciate more prominence being given to the role and the status of the accompanying notes to the financial statements. In this regard, paragraph 7.8 of the ED could recognise more prominently the role of the accompanying notes as an additional communication mechanism alongside the statement of financial position and the statement(s) of financial performance.

The EBA agrees with the description of the statement of profit or loss as the primary source of information about an entity's financial performance and the requirement for maintaining presentation of profit or loss as a total or subtotal, as also mentioned in our comment letter on the DP.

The ED sets out when income and expenses should be recognised outside the statement of profit or loss (meaning in the statement of other comprehensive income) and a rebuttable presumption that income and expenses included in the statement of other comprehensive income will have to be recycled to the statement of profit or loss in the future. We would prefer that the IASB provides a conceptual basis to the purpose of the statement of profit or loss and other comprehensive income and the conditions under which recycling should occur, in order to guide the development of future IFRS but we also acknowledge the difficulties in doing so. Having an adequate conceptual basis may avoid future discussions when setting new Standards.