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Framework for the Preparation and Presentation of Financial Statements

The IASB Framework was approved by the IASC Board in April 1989 for publication in July 1989, and adopted by the IASB in April 2001.

This *Framework* sets out the concepts that underlie the preparation and presentation of financial statements for external users.

The *Framework* deals with:

- (a) the objective of financial statements;
- (b) the qualitative characteristics that determine the usefulness of information in financial statements;
- (c) the definition, recognition and measurement of the elements from which financial statements are constructed; and
- (d) concepts of capital and capital maintenance.

The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions. Financial statements prepared for this purpose meet the common needs of most users. However, financial statements do not provide all the information that users may need to make economic decisions since they largely portray the financial effects of past events and do not necessarily provide non-financial information.

In order to meet their objectives, financial statements are prepared on the accrual basis of accounting.

The financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future.

Qualitative characteristics are the attributes that make the information provided in financial statements useful to users. The four principal qualitative characteristics are understandability, relevance, reliability and comparability. In practice a balancing, or trade-off, between qualitative characteristics is often necessary.

The elements directly related to the measurement of financial position are assets, liabilities and equity. These are defined as follows:

- (a) An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.

- (b) A liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.
- (c) Equity is the residual interest in the assets of the entity after deducting all its liabilities.

The elements of income and expenses are defined as follows:

- (a) Income is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.
- (b) Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

An item that meets the definition of an element should be recognised if:

- (a) it is probable that any future economic benefit associated with the item will flow to or from the entity; and
- (b) the item has a cost or value that can be measured with reliability.

Measurement is the process of determining the monetary amounts at which the elements of the financial statements are to be recognised and carried in the balance sheet and income statement. This involves the selection of the particular basis of measurement.

The concept of capital maintenance is concerned with how an entity defines the capital that it seeks to maintain. It provides the linkage between the concepts of capital and the concepts of profit because it provides the point of reference by which profit is measured; it is a prerequisite for distinguishing between an entity's return on capital and its return of capital; only inflows of assets in excess of amounts needed to maintain capital may be regarded as profit and therefore as a return on capital. Hence, profit is the residual amount that remains after expenses (including capital maintenance adjustments, where appropriate) have been deducted from income. If expenses exceed income the residual amount is a loss.

The Board of IASC recognises that in a limited number of cases there may be a conflict between the *Framework* and an International Accounting Standard. In those cases where there is a conflict, the requirements of the International Accounting Standard prevail over those of the *Framework*. As, however, the Board of IASC will be guided by the *Framework* in the development of future Standards and in its review of existing Standards, the number of cases of conflict between the *Framework* and International Accounting Standards will diminish through time.