

CHAPTER 2

Conceptual Frameworks for Financial Reporting

LEARNING OBJECTIVES

- 2-1. Explain the role of a conceptual framework for financial reporting and the reasons for having conceptual frameworks.
- 2-2. Explain the rationale for each of the eight major components of these frameworks and synthesize these components into an integrated whole.
- 2-3. Apply the conceptual frameworks in IFRS and ASPE to specific circumstances and evaluate the trade-offs among different concepts within the frameworks.
- 2-4. Describe the standard setting environment in Canada.

OVERALL APPROACH

The overall objective of financial reporting is to provide useful information to financial statement users. When determining what is useful, we need to consider what information is important to financial statement users. Conceptual frameworks help to identify and organize concepts that are important.

Conceptual frameworks are an important set of foundational concepts in intermediate financial accounting. Many of the terms, concepts, and principles covered in this chapter provide a foundation for upcoming chapters. Students often struggle with this chapter because conceptual frameworks are a set of *concepts* rather than concrete objects.

This chapter builds on the ideas of supply and demand for information as discussed in Chapter 1. This chapter describes conceptual frameworks (there is more than one such as one for IFRS, one for ASPE) as business plans that lay out the demand for financial information and how accounting should supply information that responds to that demand.

Since supply and demand should be second nature to accounting / business students, this linkage makes conceptual frameworks understandable. Another benefit of portraying conceptual frameworks as business plans is that doing so makes apparent that more than one framework can be valid, and that these frameworks are not set in stone—they can and do change over time.

KEY POINTS

The chapter focuses on the concept of **supply and demand for information** as discussed in Chapter 1. The chapter focuses the discussion using the conceptual framework in

IFRS. Exhibit 2-7 (page 42) provides a comparison of the conceptual frameworks in IFRS and ASPE.

Similar to many other business situations, it is useful to separately analyze the demand and the supply. From the standpoint of accounting standard setters and financial statement preparers, the demand for information is external and largely out of their control. The supply side, on the other hand, is more directly managed by accountants.

The diagrams in Exhibits 2-1, 2-2, and 2-3 convey this separation and other logical connections among the eight major components of the IFRS Framework. In particular:

- The five supply side components are encased in an arrowhead pointing toward demand to show the need to have supply meet demand.
- Constraints can be thought of as limits, so the diagrams position them at the top. Meanwhile, underlying assumptions are positioned naturally at the bottom.
- Constraints and assumptions are positioned on the periphery; while they are important considerations, they are not at the “core” of what accountants do. The core involves the elements of the financial statements, recognition, and measurement.

Once the IFRS Framework has been introduced in the context of supply and demand, the remaining details of the framework flow naturally.

Section D of this chapter, beginning on page 43, provides a description of the standard setting process in Canada and includes articles that provide an alternate perspective of the global convergence of accounting standards. In this context, it is important to distinguish a publicly accountable enterprise from a private enterprise, particularly because the latter term has a more restrictive meaning in accounting than in business and economics.

Some instructors may find the assumption of the financial capital maintenance concept worthy of additional exploration, and the Appendix to this chapter (Section F, pages 50-52) does so with a detailed numerical example.

USE OF END-OF-CHAPTER PROBLEMS AND CASES

In addition to lectures, discussion of some of the end-of-chapter problems and cases will help students apply the concepts. The following table identifies all of problems and cases that can be used in class, and problems and cases that can be used for homework assignments. (Depending on the time allocation between lectures and questions, it may not be feasible to cover all of the suggested items.)

Table 2-1:
Summary of learning objectives, chapter content, and suggested problems and cases

L.O. number	Learning objective	Pages	Suggestions for in-class discussion	Suggestions for assignments
2-1.	Explain the role of a conceptual framework for financial reporting and the reasons for having conceptual frameworks.	28-30	P2-1	
2-2.	Explain the rationale for each of the eight major components of these frameworks and synthesize these components into an integrated whole.	30-40	P2-3 P2-8 P2-9 P2-11	P2-2 P2-4 P2-5 P2-6 P2-7 P2-10
2-3.	Apply the conceptual frameworks in IFRS and ASPE to specific circumstances and evaluate the trade-offs among different concepts within the frameworks.	40-43	P2-12 P2-14	P2-13 P2-15 P2-16 P2-17 P2-18 P2-19
2-4.	Describe the standard setting environment in Canada.	43-50	P2-20 P2-22	P2-21 P2-23 P2-24 P2-25
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Case 2 involves the application of the IFRS conceptual framework, and in particular, a good understanding of the elements of financial statements. Many students will readily grasp the issues on the asset side of the transaction (because the case explicitly refers to the receivables), but rarely will they see the other side relating to the liabilities.

Case 5 is a practical question that looks at a public company that is considering whether to acquire a private company. Students are asked to consider the reporting requirements for a private company and to explain the qualitative characteristics that will help to meet the needs of the financial statement users.