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Theory and practice of the proposed conceptual framework: Evidence from the field

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ABSTRACT

We provide survey evidence of chartered accountants' perspectives on the proposed conceptual framework of the International Accounting Standards Board. Our survey obtains their views on the changes in the definitions of assets and liabilities, recognition criterion, and additional guidance in these areas, as well as issues relating to other comprehensive income, business model-based accounting, and choice of measurement basis. Our field evidence suggests broad consensus with respect to most of these changes. The areas that generate the most disagreement among our respondents relate to the removal of economic benefits in the proposed asset definition, the proposal to remove the minimum probability threshold from the asset recognition criterion, and the use of fair value as a measurement basis for certain difficult to measure assets. Overall, our results provide interesting insights regarding how chartered accountants view the proposed conceptual framework.

1. Introduction

Our study seeks to inform the debate on fundamental shifts in accounting thought in the proposed IASB's Conceptual Framework. We provide field evidence on chartered accountants' opinions with respect to some of these proposed changes. Historically, the role of the conceptual framework in accounting has been the subject of much debate (Macve, 2010). For example, theoretical research on the information perspective is critical of the usefulness of the conceptual framework in negotiating the tension between relevance and reliability of financial information (Christensen, 2010). On the other hand, other scholars strongly advocate the necessity of a conceptual framework in any credible standard-setting endeavor to ensure consistency and to demonstrate technical competency (Boyle, 2010; Macve, 1981, 2010). Regardless of the criticisms, the conceptual framework is a critical component in the architecture of accounting standards, and paradigmatic shifts in this component would impact the accounting of the future.

The conceptual framework presents the purest articulation of the standard setters' views on the fundamental concepts that would guide future accounting standards and practice. Our paper provides evidence of how chartered accountants view the proposed conceptual framework and whether there are differences in opinions between those of chartered accountants and the standard setters. Archival studies typically present *ex post* evidence subsequent to the issuance of a standard, whereas the survey methodology allows us to capture *ex ante* evidence of accountants' views on changes made to accounting concepts as proposed by standard setters. Accountants have their own collective wisdom and familiarity with real-world issues and pressures acquired through years of experience. On that same note, they are conditioned by their experience and may be less imaginative in responding to new situations (Gray, Shaw, & McSweeney, 1981). We expect that there would be differences of opinion between the views of accountants and those of the standard setters. Hence, the proposed conceptual framework presents an excellent opportunity for us to assess the receptivity of accountants to changes in deeply entrenched accounting concepts. The focus of our study is not on a document *per se* but the concepts that undergird the proposals. Hence, this study obtains field evidence on opinions on the conceptual foundations that will shape accounting practice in future.

As the contribution of Asia to the global economy increases, the Asian voice is particularly important to the IASB as it seeks to extend its global reach. Singapore is a leading global financial centre and seeks to position itself as a major accountancy hub. It is English speaking, inherits the British governance and legal infrastructure, and the “Anglo-Saxon” mode of accounting during its colonial period. In the post-independence period of 50 years, Singapore has gone on to establish its own unique identity in establishing high standards of government, education, professional, and business practices. The Global Financial Centres Index ranks Singapore as the fourth most competitive financial centre in the world just behind New York, London, and Hong Kong (Yeandle & Mainelli, 2015). Singapore is also ranked consistently within the top 10 countries in the world in terms of GDP per capita (Knoema, 2015).

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The accounting bodies in Asia have been participating more actively in giving feedback to the IASB on their projects. Collectively, the Asian-Oceanian Standard Setters Group (AOSSG) formed in 2009 has made their views known to the IASB. Singapore is one of the founding members of the AOSSG. Hence, our survey is relevant in capturing views from a group of accountants that is becoming more important in the global economic and accounting landscape.[3]

We solicit views of chartered accountants from Singapore on the proposed revisions to the definitions of assets and liabilities, additional guidance on applying the definitions, proposed guidance on asset and liability recognition and de-recognition, other comprehensive income, business model-based accounting, and measurement basis. Our survey respondents are members of the Institute of Singapore Chartered Accountants (ISCA) with differing seniority levels and employer firm sizes, and they work in a diverse range of industries. Generally, they possess accountancy degrees with at least three years of working experience in accounting and finance positions. To qualify for this survey, they must be chartered accountants with the Institute. We obtain their views through an online survey in collaboration with ISCA.

Our key findings fall in three broad categories. The first category relates to the elements of financial statements. We find some resistance among our respondents with respect to the proposed asset definition. The new asset definition emphasizes economic resource over economic benefits. In addition, the minimum probability threshold as implied in the term “probable” is removed. These proposed changes are perceived as being too radical by some of our respondents. The respondents who disagree with the proposed asset definition mainly have disagreements with respect to the underlying premise that an asset could exist without producing future economic benefits. While they agree with the definition of economic resource as a right capable of producing economic benefits, they disagree with replacing the term “economic benefits” with “economic resource.” They also think that there could be interpretation issues if the proposed asset definition relies on a term that is separately defined. On the other hand, the majority of our respondents agree with the proposed definition of liability. This is because they think that the proposed definition of a liability is simpler and easier to understand, and it places greater weight on the existence of an obligation. Interestingly, our findings thus indicate that our respondents have asymmetric views with regard to the proposed asset and liability definitions despite the fact that both definitions include economic resource as the new operative term.

The second set of results relates to respondents' views on other comprehensive income (OCI). The IASB has explored the need for OCI, the presentation of OCI, and whether OCI should be recycled to profit or loss. Our survey provides evidence that our respondents continue to support the need for OCI to be presented separately from net income. Some expressed the view that OCI tends to be non-operating in nature, and are mainly unrealized income changes. While they recognize that some net income items embody these features, they feel that having OCI separated from net income better represents the reporting entity's financial performance. They also believe that financial statement users have already learned to interpret the financial performance in its current form of presentation since the revised implementation of IAS 1 *Presentation of Financial Statements* that delineates OCI from net income in 2009. Thus, they agree that the IASB should focus on the presentation guidance rather than the definition of OCI. Finally, most of them continue to support the recognition of existing OCI items.[4]

Our final set of results relates to issues regarding business model-based accounting and measurement bases. The IASB's view is that the application of the business model concept in developing accounting standards enhances the relevance of financial statements. Our survey respondents mainly agree that the reporting entity's business model should be used as a basis to determine whether assets and liabilities should be reported at fair value or historical cost, and whether fair value changes should be reported in net income or OCI. They consider fair value to be a more appropriate measurement basis than historical cost for assets and liabilities held for trading purposes, but they consider historical cost to be a more appropriate basis for assets and liabilities held for use within the business or held for passive investment. In the same vein, they think that fair value changes should be recognized in net income for assets and liabilities held for trading but recognized in OCI for assets and liabilities held for use or for passive investment.

2. Overview of issues in the proposed conceptual framework

The IASB's Conceptual Framework for Financial Reporting sets out the concepts that underlie the preparation and presentation of financial statements (IASB, 2015). The existing conceptual framework has its roots in earlier pronouncements that date back to 1989. The conceptual framework serves as guidance to accounting standard development and accounting practices. The standards developed prior to the advent of the conceptual framework are more likely to reflect consensus in practice rather consistent principles. The accounting practices developed at the local level by firms could be subjective and dependent on individual preparer/auditor judgment (McGregor & McCahey, 2013; Zeff, 1999). Hence, standard setters took on the job to develop a conceptual framework to provide a coherent set of concepts and principles so that the accounting standards and practices are consistent. This consistency is needed given the internationalization of company businesses and the political, subjective, and piecemeal practice-oriented development of standards at the local level (Camfferman & Zeff, 2007; Gray et al., 1981).

In July 2013, the International Accounting Standards Board (IASB) issued a discussion paper (DP) on the Conceptual Framework for financial reporting in a move to revise the existing Conceptual Framework (IASB, 2013). The IASB identified a number of problems with the existing framework relating to inadequate coverage of important areas, unclear guidance, and out-of-date principles that fail to reflect the current thinking of the IASB. The DP thus sets out preliminary views on areas that would potentially have a major impact on financial reporting in general. In May 2015, the IASB issued an Exposure Draft on the Conceptual Framework. The Exposure Draft largely retains the positions adopted in the DP. Hence, the result of this study is relevant to the current decisions of the IASB at the time of writing.

Given the long history of the existing framework in accounting thought and practice (Peasnell, 1982; Zeff, 2013), it would be interesting to assess accountants' responses to the various proposed changes in the conceptual framework project. For example, economic interests affect the willingness of different stakeholders to accept changes. Glaum and Mandler (1997) finds German managers are more positively inclined towards the then current German accounting and more negatively towards U.S. GAAP than German academics.[5] The conceptual framework project itself is not immune to political lobbying by various stakeholders (Hines, 1989). The early conceptual framework project was criticized by stakeholders for departures from the accepted accounting practices at that time (Bloom, Collins, Fuglister, & Heymann, 1994). While the conceptual framework has been largely developed from a user perspective with a focus on “decision usefulness” of financial statements (Gassen & Schwedler, 2010; Zeff, 1999), accountants may take different views depending on their incentives. Other studies also provide evidence that accounting standard setters with financial services background are more likely to propose fair value methods in standards (Allen & Ramanna, 2013), and that auditors support

[3] On the other hand, we acknowledge that this is a single country study; hence, the results might differ if the same survey was conducted in a different country.

[4] These OCI items are foreign currency translation difference, fixed asset revaluation reserve, gains/losses on the remeasurement of available-for-sale securities, gains/losses on re-measurements of defined benefit pension plans, and gains/losses on cash flow hedging instruments.

[5] Arguably, academics might be more independent than managers with respect to changes imposed by accounting standards.

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