Grupo Latinoamericano
de Emisores de Normas
de Información Financiera

Group of Latin American
Accounting Standard Setters

November 25, 2015

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

RE: Exposure Draft ED/2015/3 – Conceptual Framework for Financial Reporting

Dear Board Members:

The "Group of Latin American Accounting Standard Setters"[1] – GLASS welcomes the opportunity to comment on the Exposure Draft ED/2015/3 – Conceptual Framework for Financial Reporting (the "ED").

Due process

The discussions regarding the ED were held within a specified Technical Working Group (TWG) created in June 2015. All country-members had the opportunity to appoint at least one member to participate in this TWG. Each standard setter represented in the TWG has undertaken different tasks in their respective countries (e.g. surveys, internal working groups). All results were summarized, and this summary was the platform for the TWG discussion process.

The TWG discussed the different points of view included in the summary during several conference calls. In those calls the TWG developed a final document on the basis of the agreed-upon responses and the technical points of view of its members. Finally, the TWG document was submitted to and approved by the GLASS Board.

Overall Comments

The following presents some general comments of the ED, plus a summary of the more significant comments included in the attachment:

- In general, we believe the ED is a significant improvement over the existing Conceptual Framework. It is much more comprehensive and should prove to be very useful going forward.
- Some of our constituents believe very strongly that there should be no inconsistencies between the Conceptual Framework and individual standards. They would like to see the IASB commit to working on the elimination of existing inconsistencies and also commit to not issuing future standards or interpretations that conflict with the Conceptual Framework.
- With respect to other comprehensive income (OCI), the majority of our constituents:
  - would like the Board to develop a comprehensive and understandable definition of "other comprehensive income" (OCI) to be included in the definitions of elements of financial statements;
  - disagree with the inclusion of a rebuttable presumption that items of income or expenses included in OCI in one period will be recycled into the statement of profit or loss in some future period. They believe that all components of OCI should be recycled.

[1] The overall objective of the Group of Latin American Accounting Standard Setters (GLASS) is to present technical contributions with respect to all Exposure Drafts issued by the IASB. Therefore, GLASS aims to have a single regional voice before the IASB. GLASS is constituted by: Argentina (Board), Bolivia, Brazil (Vice Chairman), Chile, Colombia (Board), Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico (Chairman), Panama, Paraguay, Peru (Board), Uruguay (Board) and Venezuela (Board).

- Our constituents strongly believe that the Conceptual Framework should define the qualitative characteristics a currency must possess to be used as a unit of measure so that its use results in reliable and useful financial information for users.

Specific comments
Attached please find our specific responses to the questions presented in the ED.

Contact
If you have any questions about our comments, please contact glenif@glenif.org.

Sincerely yours,

Felipe Pérez Cervantes
Chairman
Group of Latin American Accounting Standard Setters (GLASS)

Grupo Latinoamericano de Emisores de Normas de Información Financiera

Group of Latin American Accounting Standard Setters

Attachment

GLASS' Comment Letter on the IASB Exposure Draft on the Conceptual Framework for Financial Reporting

Chapters 1 and 2—The objective of general purpose financial reporting and the qualitative characteristics of useful financial information

Question 1—Proposed changes to Chapters 1 and 2

Do you support the proposals:

(a) to give more prominence, within the objective of financial reporting, to the importance of providing information needed to assess management's stewardship of the entity's resources;

(b) to reintroduce an explicit reference to the notion of prudence (described as caution when making judgements under conditions of uncertainty) and to state that prudence is important in achieving neutrality;

(c) to state explicitly that a faithful representation represents the substance of an economic phenomenon instead of merely representing its legal form;

(d) to clarify that measurement uncertainty is one factor that can make financial information less relevant, and that there is a trade-off between the level of measurement uncertainty and other factors that make information relevant; and

(e) to continue to identify relevance and faithful representation as the two fundamental qualitative characteristics of useful financial information?

Why or why not?

Our constituents had the following comments on the individual proposals mentioned above:

(a) All agreed with giving more prominence to the importance of providing information needed to assess management's stewardship of the entity's resources. However, one country would like the Board to address both the anticipated consequences of explicitly including stewardship as an objective of financial statements and the expected impacts on the development of future accounting standards.

(b) The "Invitation to comment" states that it was decided to reintroduce an explicit reference to the notion of prudence, later described as using "caution when making judgements under conditions of uncertainty". Most of our constituents agree with the reintroduction. However, one country observes that the ED states that "prudence is important for achieving neutrality", and paragraph 2.18 of the ED states that "Neutrality is supported by the exercise of prudence." Some do not believe that neutrality, i.e. a lack of bias, requires prudence, and that the current elements of completeness, neutrality and freedom from error sufficiently support the concept of faithful representation. Accordingly, they argue that the reintroduction of prudence is unnecessary. Others are unclear as to the interaction between prudence, relevance and faithful representation.

(c) All agree that substance overrides form, especially in some of our environments whose accounting conventions are significantly influenced by form-based tax legislation. However, some believe that the term "economic phenomenon" used in paragraph 2.14 of the ED is unclear and requires definition.

(d) All agree that that measurement uncertainty is one factor that can make financial information less relevant and the adequate disclosure is essential.

(e) All agree that relevance and faithful representation are the two fundamental qualitative characteristics of useful financial information.

Chapter 3—Financial statements and the reporting entity

Question 2—Description and boundary of a reporting entity
Do you agree with: (a) the proposed description of a reporting entity in paragraphs 3.11–3.12; and (b) the discussion of the boundary of a reporting entity in paragraphs 3.13–3.25? Why or why not?

Our constituents agree with the proposed description and boundaries of a reporting entity and believe that they will prove useful going forward. They also welcome paragraph 3.17 that allows for the preparation of combined financial statements.

One country believes that given the possibility of an investment in a subsidiary or affiliate for which the entity has an obligation involving unsecured liabilities of the investee, the Board should consider adding "or a liability" at the end of paragraph 3.19.

Chapter 4—The elements of financial statements

Question 3—Definitions of elements
Do you agree with the proposed the proposed definitions of elements (excluding issues relating to the distinction between liabilities and equity): (a) an asset, and the related definition of an economic resource; (b) a liability; (c) equity; (d) income; and (e) expenses? Why or why not? If you disagree with the proposed definitions, what alternative definitions do you suggest and why?

Most of our constituents agree with the elimination of the probability threshold from definitions of an asset and a liability, although some believe that this could result in the modification of several individual standards to achieve consistency. However, one country strongly prefers to retain the existing definitions with their references to "expected" inflows and outflows of economic resources, since it is feared that some preparers may only look to the definitions without adequately studying the guidance on recognition, which could lead to the recognition of assets that may never generate future economic benefits and the recognition of liabilities for many contingencies as currently defined in IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*.

Several of our constituents believe that it is essential for the Board to develop a comprehensive and understandable definition of "other comprehensive income" (OCI) to be included in the definitions of elements of financial statements. They do not believe it is sufficient just to describe when it is appropriate to use OCI. If the Board decides that such a definition is not required, that decision should be explained in the Basis for Conclusions.

Question 4—Present obligation
Do you agree with the proposed description of a present obligation and the proposed guidance to support that description? Why or why not?

Our constituents in general agree with the description of a present obligation but some believe that such definition could be more precise to avoid inconsistent application. Additionally, several constituents expressed difficulty understanding the concept of "no practical ability to avoid" the transfer of an economic resource and would like to see more guidance in this regard.

Question 5—Other guidance on the elements
Do you have any comments on the proposed guidance? Do you believe that additional guidance is needed? If so, please specify what that guidance should include.

There is general agreement with the proposed other guidance on the elements of financial statements. We found the guidance on equity to be useful, although we recognize that there are inconsistencies between such guidance and IAS 32, *Financial Instruments: Presentation*, regarding the distinction between liabilities and equity, as acknowledged in paragraphs BCE.7 and BCE.8. We also found the guidance on reporting the substance of contractual rights and contractual obligations and on the unit of account to be very useful.

However, some of our constituents expressed concern with respect to paragraphs 4.40 to 4.42 on executory contracts. They believe that contracts for the purchase of goods and services that establish an enforceable right and obligation should be recognized as such, as they meet the definitions of an asset and a liability in the ED. They believe there is no conceptual basis for such contracts to be treated in a manner different from financial and lease contracts. In all cases, when a right and an obligation exist, IFRS requires recognition of the corresponding asset and liability, and there is no underlying economic distinction that allows for a different accounting treatment. The characteristics of these contracts do not justify considering these rights and obligations to be an indivisible single asset or liability, other than on the basis of immateriality.

Chapter 5—Recognition and derecognition

Question 6—Recognition criteria

Do you agree with the proposed approach to recognition? Why or why not? If you do not agree, what changes do you suggest and why?

In general our constituents agree with the proposed approach to recognition. However, some would like to see clarification of one of the factors that indicate recognition may not provide relevant information. That factor is when there is only a low probability that an inflow or outflow of economic benefits will result. Paragraphs 5.17 to 5.19 of the ED discuss this factor but never adequately define it. They believe that such factor comes into play particularly when the fair value of the unrecognized asset or liability is immaterial.

Additionally, the same country that strongly prefers to retain the existing definitions of assets and liabilities with their references to expected inflows and outflows of economic resources, as mentioned in our response to Question 3, accordingly also believes that probability, as opposed to relevance, and reliable measurement provide better support for the recognition of elements in the financial statements.

Another country would like to see more guidance with respect to what level of uncertainty is acceptable, to avoid abuses and excessive discretion in interpretation.

Finally, another country believes the Board should emphasize that “off balance sheet” assets and liabilities should be minimized.

Question 7—Derecognition

Do you agree with the proposed discussion of derecognition? Why or why not? If you do not agree, what changes do you suggest and why?

In general our constituents agree with the proposed discussion of derecognition. Nevertheless, one country observes that the 2013 Discussion Paper presented two different approaches for derecognition in those cases when a transaction eliminates some but not all of the rights and obligations contained in an asset (or a liability). Those two approaches are the “control approach” and the “risk-and-rewards approach”. Under the “control approach” an entity derecognizes the entire asset (or liability) and recognizes the retained component as a new asset (or liability), while under the “risk-and-rewards approach” an entity continues to recognize the retained component and derecognizes the component that is not retained. Our constituents would like to see the ED more clearly address when each of the two approaches is most appropriate.

Question 8—Measurement bases

Has the IASB:

(a) correctly identified the measurement bases that should be described in the Conceptual Framework? If not, which measurement bases would you include and why?

(b) properly described the information provided by each of the measurement bases, and their advantages and disadvantages? If not, how would you describe the information provided by each measurement basis, and its advantages and disadvantages?

Our constituents are in general agreement with the measurement bases that have been identified and described in the ED. However, one country believes that current cost-based measurements can provide more relevant information than measurements that are based solely on historical cost. The use of replacement cost, obtained by adjusting historical cost to reflect specific price changes, results in margins that are more relevant than margins derived from historical cost. In the ED, replacement cost is hidden in the historical cost measurement basis discussion. In the opinion of that country, it is necessary to take into account both the ability to predict future cash flows and the cost of obtaining such information, and in most cases the financial statement user's ability to predict future cash flows is improved using replacement cost instead of historical cost.

In the ED it is assumed that the effort to obtain replacement cost is greater than that to obtain historical cost, which is often not the case, and replacement cost is frequently more verifiable than a fair value measurement in the absence of observable data. Using the arguments of greater cost and less verifiability to exclude a particular measurement basis is inconsistent with some standards under which in many more complex situations fair value measurements are used. The country defending replacement cost believes the Conceptual Framework should require selection of the measurement basis that best predicts future cash flows of the entity, giving equal weight to all proposed alternatives, and the individual standards should address the best measurement basis in the particular circumstances.

Other countries believe that the proposed guidance on measurement bases is too restrictive for the preparation of future standards. They are not convinced that all of the different measurement metrics (including, for example, replacement cost and net realizable value) found in existing standards are covered by the proposed guidance.

Question 9—Factors to consider when selecting a measurement basis
Has the IASB correctly identified the factors to consider when selecting a measurement basis? If not, what factors would you consider and why?

Our constituents are in general agreement with the factors identified by the Board for the selection of a measurement basis. However, some countries believe that the importance of the business model, or nature of the business activities, of the entity, which are briefly addressed in paragraph 6.54(a) of the ED, should be given greater emphasis in this selection.

We observe that paragraph 6.69 of the ED that addresses transactions with holders of equity claims indicates that if an entity receives an asset from a holder of an existing or new equity claim, it would normally be appropriate to measure the asset initially at a current value. We believe that this section should clarify that transfers of assets between related parties or entities under common control should not be recorded at current value.

Question 10—More than one relevant measurement basis
Do you agree with the approach discussed in paragraphs 6.74–6.77 and BC6.68? Why or why not?

In general our constituents agree that there can be more than one relevant measurement basis in some cases. However, concern was expressed regarding the complexity of financial information when using different measurement bases in the statement of financial position and the statement of financial performance, with the difference recognized in OCI. Accordingly, they believe the use of different measurement bases in the different statements should be limited and clearly justified in the individual related standard.

Chapter 7—Presentation and disclosure

Question 11—Objective and scope of financial statements and communication
Do you have any comments on the discussion of the objective and scope of financial statements, and on the use of presentation and disclosure as communication tools?

Our constituents agree with the use of presentation and disclosure as communication tools. However, one of our constituents observes that most of the discussion regarding the use of presentation and disclosure as communication tools, in particular the comments on classification and aggregation, only mention the statements of financial position and financial performance, but do not mention the statements of changes in equity or cash flows. The country making this observation believes that all of the basic financial statements should be subject to the same guidance.

One country would like more clarity as to which aspects of presentation and disclosure assist in assessing management's stewardship of the entity's resources.

Question 12—Description of the statement of profit or loss
Do you support the proposed description of the statement of profit or loss? Why or why not? If you think that the Conceptual Framework should provide a definition of profit or loss, please explain why it is necessary and provide your suggestion for that definition.

Our constituents support the proposed description of the statement of profit or loss and agree with the importance of always presenting such a statement. However, several of our constituents expressed uncertainty about renaming the statement of profit or loss, or comprehensive income, as the statement of financial performance. Some are unclear as to how to adequately define "financial performance".

Others would like to see the Board establish a requirement to present a single statement of comprehensive income in all cases and not allow two separate statements, thereby achieving comparability and consistency among reporting entities.

Question 13—Reporting items of income or expenses in other comprehensive
Do you agree with the proposals on the use of other comprehensive income? Do you think that they provide useful guidance to the IASB for future decisions about the use of other comprehensive income? Why or why not? If you disagree, what alternative do you suggest and why?

Our constituents agree with the proposal to restrict the use of OCI to income or expenses (or components of them) that relate to assets or liabilities measured at current values. However, some constituents have difficulty understanding when excluding those income or expenses (or components of them) from the statement of profit or loss would enhance the relevance of the information in that statement for the period. This concern could be alleviated if the Board would develop a comprehensive and understandable definition of OCI to be included in the definitions of elements of financial statements, as mentioned in our response to Question 3 above.

Question 14—Recycling

Do you agree that the Conceptual Framework should include the rebuttable presumption that items of income or expenses included in other comprehensive income in one period will be reclassified into the statement of profit or loss in some future period (recycled), if doing so will enhance the relevance of the information included in the statement of profit or loss for that future period? Why or why not?
If you disagree, what do you propose instead and why?

The vast majority of our constituents disagree with the inclusion of a rebuttable presumption that items of income or expenses included in OCI in one period will be recycled into the statement of profit or loss in some future period. They find it difficult to envision a scenario in which not recycling will enhance the relevance of the information included in the statement of profit or loss for that future period. They believe that if there is no clear basis for identifying the period in which recycling would enhance the relevance of the information in the statement of profit or loss, this indicates that the income or expenses should not be included in OCI.

If an item previously recognized in OCI is not recycled but rather reclassified in some future period from OCI to retained earnings, such item will never be considered in the determination of the earnings per share of the entity. We believe that recycling will always enhance the relevance of the information included in the statement of profit or loss for that future period.

Other questions for respondents

Question 15—Effects of the proposed changes to the Conceptual Framework
Do you agree with the analysis in paragraphs BCE.1–BCE.31? Should the IASB consider any other effects of the proposals in the Exposure Draft?

Our constituents are divided regarding the lack of a commitment by the Board to undertake a project to eliminate existing inconsistencies between existing standards and the ED, together with no commitment to not issue future standards that would create new inconsistencies. Some feel very strongly that there should be no inconsistencies and that over time the Conceptual Framework should take precedence over individual standards. They say over time because they understand the problems that would arise if the Conceptual Framework were to take precedence from one day to the next.

Those that believe that the Conceptual Framework should be more than a tool for the development of future standards believe that if a particular situation arises that was not previously contemplated and results in the need to issue a standard or an interpretation that is not consistent with the Conceptual Framework, in that same standard or interpretation the Board should propose a modification of the Conceptual Framework to achieve consistency. It is clear that there cannot be two different answers to the same question, both of which are correct.

Question 16—Business activities
Do you agree with the proposed approach to business activities? Why or why not?

In general our constituents agree with the proposed approach to business activities, as evidenced by its importance in recently issued IFRS 9, *Financial Instruments*. We refer to its importance in our response to Question 9.

Additionally, many believe that the concept of "business model" is sufficiently understood to be used in place of business activities. In fact, some suggest adding a definition of "business model" to the IFRS Glossary.

Question 17—Long-term investment

Do you agree with the IASB's conclusions on long-term investment? Why or why not?

In general our constituents agree with the IASB's conclusions on long-term investment. We agree that both existing and potential long-term and short-term investors should be considered to be primary users of financial statements. We also agree that the information needs of all primary users are essentially the same, and that it is not the role of accounting standards to encourage or discourage investments that have particular characteristics.

Question 18—Other comments

Do you have comments on any other aspect of the Exposure Draft? Please indicate the specific paragraphs or group of paragraphs to which your comments relate (if applicable).

As previously noted, the IASB is not requesting comments on all parts of Chapters 1 and 2, on how to distinguish liabilities from equity claims (see Chapter 4) or on Chapter 8.

Our constituents have the following additional comments that do not flow from a direct response to the specific questions:

1. Capital maintenance

    - One of our constituents believes there is no benefit to retaining in the Conceptual Framework the concept of physical capital maintenance, which is a measurement alternative not considered in any particular standard.

    - That country believes that only the concept of financial capital maintenance should be retained. Inclusion of the concept of physical capital maintenance only creates confusion, as in the case of preparers and users of financial information who believe that such concept is related to the unit of measure in high inflation environments, which is clearly incorrect as its objective is completely different.

2. Unit of measure

    - Our constituents have expressed serious concern about the failure of the Conceptual Framework to address this issue. They believe the Conceptual Framework should define the qualitative characteristics a unit of measure must possess so that its use results in reliable and useful financial information for users. Common sense tells us that we would not use a unit of measure that changes over time. Accordingly, we should not use a monetary unit of measure that experiences significant changes in value and therefore distorts comparisons between measures made at different points in time, which frequently occurs in the measurement of certain assets and most elements of the statement of income or loss.

    - As the concept of the unit of measure is not addressed in the Conceptual Framework, we refer to the units of measure that are addressed in particular standards, including the functional currency of reporting currency addressed in IAS 21, *The Effects of Changes in Foreign Exchange Rates*. However, IAS 21 does not consider the fact that such units of measure may have characteristics that make them inappropriate as a unit of measure in financial information. The application of IAS 21 often results in the recognition of enormous cumulative translation adjustments in OCI that are impossible to explain on a conceptual basis to the users of financial information. In essence such cumulative translation adjustments represent the cumulative errors resulting from inappropriate currencies used as units of measure.

- IAS 29, *Financial Reporting in Hyperinflationary Economies*, is an example of a mechanism to correct the unit of measure that is not presently considered in the Conceptual Framework. However, as IAS 29 only applies in hyperinflationary environments, which is a very uncommon situation, that standard is rarely applied and consequently poorly understood. Separately we have communicated our concerns to the IASB regarding the modifications to IAS 29 that we believe are required, basically to recognize the effects of inflation in economies with high inflation, not just hyperinflation.

- We believe it is imperative that the Conceptual Framework establish the qualitative characteristics a currency must possess to be used as a functional or reporting currency. It should also establish boundaries to the deviations from such qualitative characteristics to generate the high quality financial information required by users of financial information. The Conceptual Framework should also establish the courses of action to be taken when a currency no longer meets the criteria for a viable unit of measure and accordingly requires adjustment to continue be used.

- Those of us who live in countries with significant instability in the value of our currencies are seriously impacted by the use of unreliable currencies as a unit of measure, and the financial information we prepare under IFRS does not come close to accurately presenting the resources, obligations and performance of an entity.