

Policy Statement

**PS 5**  
July 2001

# **The Nature and Purpose of Statements of Accounting Concepts**



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ISSN 1320-2553

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**POLICY STATEMENT PS 5**  
**“THE NATURE AND PURPOSE OF**  
**STATEMENTS OF ACCOUNTING CONCEPTS”**

**Purpose of the Policy Statement**

- 1 The purpose of this Policy Statement is to enunciate the policy of the Australian Accounting Standards Board (AASB) regarding the nature and purpose of Statements of Accounting Concepts. The *Australian Securities and Investments Commission Act 2001*, subsection 227(1)(a), provides that a function of the AASB is to develop a conceptual framework, not having the force of an accounting standard, for the purpose of evaluating proposed accounting standards and international standards. Policy Statement PS 1 “The Development of Statements of Accounting Concepts and Accounting Standards” (forthcoming) documents the procedures the AASB and the Urgent Issues Group (UIG) follow in developing Statements of Accounting Concepts, Accounting Standards and other authoritative pronouncements.
- 2 This Statement supersedes Policy Statement 5 “The Nature and Purpose of Statements of Accounting Concepts” issued by the former Australian Accounting Standards Board and the Public Sector Accounting Standards Board in March 1995.<sup>1</sup>

**Nature of Statements of Accounting Concepts**

- 3 Statements of Accounting Concepts set out the concepts which have been adopted by the AASB in respect of the nature, subject, purpose and broad content of general purpose financial reporting in the private and public sectors. An outline of the conceptual framework is set out in the Appendix to this Statement.

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<sup>1</sup> An outline of the nature and purpose of Statements of Accounting Concepts was originally set out in “Brief Guide to Statements of Accounting Concepts”, issued by the Australian Accounting Research Foundation and by the Accounting Standards Review Board (ASRB) in August 1990, and in ASRB Release 100 “Nature of Approved Accounting Standards and Statements of Accounting Concepts and Criteria for the Evaluation of Proposed Approved Accounting Standards”, issued by the ASRB in August 1990. The Brief Guide, and the comments in ASRB Release 100 on Statements of Accounting Concepts, were superseded by Policy Statement 5 “The Nature and Purpose of Statements of Accounting Concepts”, which was issued in March 1995.

- 4 Statements of Accounting Concepts articulate the AASB's thinking at the time of their development. They are also forward looking and evolving documents. The concepts will be subject to ongoing review as they are tested against practical issues in developing Accounting Standards, and in dealing with emerging issues. Accordingly, Statements of Accounting Concepts will be revised from time to time on the basis of the AASB's experience.

### **Purpose of Statements of Accounting Concepts**

- 5 The primary purpose of Statements of Accounting Concepts is to guide the AASB and the UIG when developing and reviewing Accounting Standards and other authoritative documents. For the AASB, this is consistent with its statutory obligation to develop a conceptual framework, not having the force of an Accounting Standard, for the purpose of evaluating proposed Accounting Standards and international standards.
- 6 Knowledge of the concepts the AASB and UIG use in developing Accounting Standards and other authoritative pronouncements should assist preparers, auditors and other parties with an interest in financial reporting to understand better the general nature and purpose of information reported in general purpose financial reports. The concepts also may provide guidance for preparers and others in analysing new or emerging issues in the absence of applicable Accounting Standards and other authoritative documents.

### **Benefits of a Conceptual Framework**

- 7 The following benefits are intended to result from the development of Statements of Accounting Concepts:
- (a) Accounting Standards should be more consistent and logical, because they are developed in the context of an orderly set of concepts;
  - (b) increased international compatibility of Accounting Standards should occur, because they are developed in the context of a conceptual framework that is similar to the explicit conceptual frameworks used by the International Accounting Standards Board (IASB) and major overseas national standard-setters;

- (c) the AASB should be more accountable for its decisions, because the thinking behind specific requirements should be more explicit, as should any departures from the concepts which may be included in particular Accounting Standards;
- (d) the process of communication between the AASB and its constituents should be enhanced, because the conceptual underpinnings of proposed Accounting Standards should be more apparent when the AASB seeks public comment on them; and
- (e) the development of Accounting Standards and other authoritative pronouncements should be more economical because the concepts developed by the AASB will guide the AASB and the UIG in their decision making.

### **Status of Statements of Accounting Concepts**

- 8 Statements of Accounting Concepts do not override or amend Accounting Standards and other authoritative pronouncements, including UIG Consensus Views.
- 9 Statements of Accounting Concepts do not have legal force for entities reporting under the Corporations Act.
- 10 Some Statements of Accounting Concepts have been given legislative backing in respect of some reporting entities in the public and private sectors through requirements specified in legislation, ministerial directives or other government authority. The level of authority given to Statements of Accounting Concepts by governments and other authorities is a matter for those authorities to determine.
- 11 The status of Statements of Accounting Concepts with respect to members of The Institute of Chartered Accountants in Australia and CPA Australia is identified in Miscellaneous Professional Statement APS 1 "Conformity with Accounting Standards and UIG Consensus Views". Paragraph 21 of APS 1 (June 1995) includes a statement that "By themselves, Statements of Accounting Concepts are not mandatory in the preparation, presentation or audit of a general purpose financial report".

## **Consistency between Accounting Standards and Statements of Accounting Concepts**

- 12 Some Accounting Standards are not consistent with Statements of Accounting Concepts. Subject to work program priorities, the AASB intends to review each Accounting Standard on issue for consistency with Statements of Accounting Concepts. The AASB may decide that some inconsistencies are justified at a particular time, based on:
- (a) an analysis of the costs and benefits of potential or proposed changes to Accounting Standards; and
  - (b) the implications of those changes for the international comparability of Accounting Standards.

Where those differences remain, the concepts concerned indicate the direction toward which the AASB believes future proposed Accounting Standards should ideally be developed.

## **International Comparability**

- 13 The AASB is committed to the process of international convergence and harmonisation to increase the international comparability of financial reporting. In this context, legislation setting out the functions of the Financial Reporting Council requires that, inter alia, it monitor the development of international accounting standards and accounting standards that apply in major international financial centres and provides that the AASB participate in and contribute to the development of a single set of accounting standards for world-wide use. This goal can be achieved more efficiently if standard-setters develop accounting standards using consistent conceptual frameworks. The explicit conceptual frameworks in Australia and in overseas jurisdictions are similar. The AASB supports the reduction of the limited differences between conceptual frameworks and, to this end, will continue to explore with the IASB and overseas standard-setters opportunities for further convergence and harmonisation of conceptual frameworks.

## **APPENDIX**

### **OUTLINE OF CONCEPTUAL FRAMEWORK**

The following outline describes each of the building blocks of the conceptual framework. Figure 1 is a diagrammatic representation of the framework to assist readers in understanding the place of individual Statements of Accounting Concepts (Concepts Statements) within the framework.

The following Concepts Statements have been issued to date:

SAC 1 “Definition of the Reporting Entity”;  
SAC 2 “Objective of General Purpose Financial Reporting”;  
SAC 3 “Qualitative Characteristics of Financial Information”; and  
SAC 4 “Definition and Recognition of the Elements of Financial Statements”.

The following Accounting Theory Monographs have also been issued:

“Measurement in Financial Reporting”; and  
“Reporting on Solvency and Cash Condition”.

### **Definition of financial reporting**

This area of the framework is concerned with delineating the boundaries of financial reporting and, therefore, the scope of Concepts Statements and Accounting Standards and other authoritative pronouncements. It involves consideration of the types of activity or information which should be embraced within the discipline of financial reporting, and consideration of the skills that accountants can reasonably lay claim to, having regard to community expectations.

These considerations are relevant in distinguishing general purpose financial reporting from special purpose financial reporting, determining which parts of a periodic report by an entity would be subject to reporting requirements and audit, considering whether non-financial information (for example, a non-financial performance indicator) has a part to play in financial reporting, and considering whether new areas of reporting (for example, prospective financial information) should be included within financial reporting.



## **Definition of the reporting entity**

This part of the framework is concerned with establishing the criteria for determining those entities which are reporting entities and should, therefore, prepare general purpose financial reports. SAC 1 addresses this aspect of the framework.

## **Objective of general purpose financial reporting**

This part of the framework specifies the broad objective which general purpose financial reporting should seek to serve. It identifies the users of general purpose financial reports, the nature of their information needs and the type of reporting appropriate to those needs, in the context of general purpose financial reports being directed at meeting the common information needs of users. SAC 2 addresses this aspect of the framework.

## **Qualitative characteristics of financial information**

This part of the framework is concerned with the identification of qualitative characteristics which financial information should possess if it is to achieve the objective of general purpose financial reporting. SAC 3 addresses this aspect of the framework.

## **Elements of financial statements: definition and recognition**

Blocks 5 and 6 of the framework deal with the elements of financial statements (assets, liabilities, equity, revenues and expenses). They are concerned with the identification, definition and establishment of criteria for the recognition of the elements that should be included in financial statements if general purpose financial reports are to satisfy:

- (a) the objective of general purpose financial reporting; and
- (b) the qualitative characteristics of financial information.

SAC 4 addresses this aspect of the framework.

## **Measurement**

This part of the framework deals with the bases and techniques for measurement of the elements of financial statements. It explores alternative measurement attributes (historical cost, current cost, current cash equivalent and other alternatives), measurement units (nominal and constant purchasing power dollars) and concepts of capital (financial and physical). This area of the framework involves exploring the relationships between the various concepts, such as the objective of general purpose financial reporting, the qualitative characteristics of financial information, and the manner in which information is displayed in financial reports.

## **Display of financial information**

This level of the framework explores in detail the nature of the information that should be disclosed in general purpose financial reports. As Figure 1 indicates, this will involve identifying the information categories (financial position, performance, etc.) and analysing the components of those categories. This should provide a logical basis for disclosures required by each Accounting Standard and other authoritative pronouncements.

## **Standard-setting policy**

This level of the framework is concerned with the policies that the AASB and the UIG should adopt in relation to the development, structure and application of Accounting Standards and other authoritative pronouncements, and may also influence bodies responsible for developing requirements for the audit of general purpose financial reports.

Block 13 is concerned with whether particular Accounting Standards and other authoritative pronouncements should apply to some or all classes of reporting entity. The issue of differential reporting is more broadly addressed in Level 2 of the framework. Block 14 (Elevation) relates to the level of detail that Accounting Standards and other authoritative pronouncements should contain. This aspect is affected, in part, by the status of Concepts Statements. Block 15 is concerned with the due process for the development of Concepts Statements, Accounting Standards and other authoritative pronouncements, including consideration of whether the same due process should be adhered to in the development of all Concepts Statements, Accounting Standards and other authoritative pronouncements. Block 16 is concerned with whether general purpose financial reports should, for some or all classes of reporting entity, be required to be audited; and, if so, what authority should impose that requirement. Block 17 addresses the length of the period(s) between issuance and application of Accounting Standards and

other authoritative pronouncements, and the provision of transitional arrangements for adoption of particular Accounting Standards and other authoritative pronouncements.

## **Enforcement**

The final level of the framework is concerned with the procedures for monitoring compliance with Accounting Standards and other authoritative pronouncements, and with policies for responses to non-compliance with those Standards and other authoritative pronouncements.

**FIGURE 1**  
**Building Blocks of a Conceptual Framework**  
**for General Purpose Financial Reporting**

