Government of **Western Australia**
School Curriculum and Standards Authority

Syllabus Support Materials

Conceptual Framework for Financial Reporting

Accounting and Finance

General Year 12

Acknowledgement of Country

Kaya. The School Curriculum and Standards Authority (the Authority) acknowledges that our offices are on Whadjuk Noongar boodjar and that we deliver our services on the country of many traditional custodians and language groups throughout Western Australia. The Authority acknowledges the traditional custodians throughout Western Australia and their continuing connection to land, waters and community. We offer our respect to Elders past and present.

Background

In May 2019, the Australian Accounting Standards Board (AASB) released the *Conceptual Framework for Financial Reporting (*the *Conceptual Framework)*, effective from 1 January 2020, which replaces the *Framework for the Preparation and Presentation of Financial Statements*. From January 2020, the *Conceptual Framework* supersedes:

- the Framework for the Preparation and Presentation of Financial Statements (July 2004)
- Statement of Accounting Concepts SAC 1 Definition of the Reporting Entity (August 1990).

The purpose of the *Conceptual Framework* is to describe the objectives of, and the concepts for, general purpose financial reporting. This assists:

- the AASB to ensure that the Australian Accounting Standards (Standards) they develop are based on concepts which are consistent across all Standards. The consistency in these Standards brings transparency, accountability and efficiency to Australian financial markets
- preparers to develop accounting policies that are consistent when no Standard exists for a particular item or when there is a choice of accounting policies within a Standard
- all individuals to understand and interpret the Standards.

The *Conceptual Framework*, however, is not a Standard issued by the AASB; nothing in the *Conceptual Framework* overrides any Standard or requirement within a Standard.

Implementation timeline

All teachers of the School Curriculum and Standards Authority (the Authority) Accounting and Finance courses must implement the changes resulting from the *Conceptual Framework* from the beginning of 2020 as related to each Year 11 and Year 12 General Accounting and Finance course syllabus.

The following support materials have been provided by the Authority to highlight the significant changes as a result of this new and revised Conceptual Framework. Teachers will need to refer to the Conceptual Framework for more details regarding these changes and other items in the syllabus. The Conceptual Framework can be accessed via the following link:
https://aasb.gov.au/pronouncements/conceptual-framework/.

Definition of the elements of financial statements

Students should be capable of, but not limited to, defining, classifying and describing elements of financial statements as per the *Conceptual Framework*

The elements are defined in the *Conceptual Framework* (*CF*) as follows:

- 'An asset is a present economic resource controlled by the entity as a result of past events.' (*CF*, 4.3)
- 'An economic resource is defined as a right that has the potential to produce economic benefits.' (*CF*, 4.4)
- The three aspects of the definition of an asset are:
  - right
  - potential to produce economic benefits
  - control. (*CF*, 4.5)
- 'A liability is a present obligation of the entity to transfer an economic resource as a result of past events.' (*CF*, 4.26)
- The three criteria that must exist for a liability to exist are:
  - 'the entity has an obligation
  - the obligation is to transfer an economic resource
  - the obligation is a present obligation that exists as a result of past events.' (*CF*, 4.27)
- 'Equity is the residual interest in the assets of the entity after deducting all its liabilities.' (*CF*, 4.63)
- 'Income is increases in assets, or decreases in liabilities, that result in increases in equity, other than those relating to contributions from holders of equity claims.' (*CF*, 4.68)
- 'Expenses are decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims.' (*CF*, 4.69)

Recognition criteria

Students should be capable of, but not limited to, defining and recognising whether assets, liabilities, income and expenses should be recognised in financial statements as per the *Conceptual Framework*.

The *Conceptual Framework* states that, 'Only items that meet the definition of an asset, a liability or equity are recognised in the statement of financial position. Similarly, only items that meet the definition of income or expenses are recognised in the statement(s) of financial performance. However, not all items that meet the definition of one of those elements are recognised.' (*CF*, 5.6)

The *Conceptual Framework* outlines that, 'An asset or liability is recognised only if recognition of that asset or liability and of any resulting income, expenses or changes in equity provides users of financial statements with information that is useful, (*CF*, 5.7) i.e. with:

(a) relevant information about the asset or liability and about any resulting income, expenses or changes in equity; and

(b) a faithful representation of the asset or liability and of any resulting income, expenses or changes in equity.' (See CF, 5.12–5.25)

The *Conceptual Framework* also states that, 'Even if an item meeting the definition of an asset or liability is not recognised, an entity may need to provide information about that item in the notes.' (*CF*, 5.11)

For the purposes of the Year 12 General Accounting and Finance course, the factors determining the recognition criteria for relevance and faithful representation of assets and liabilities will be limited to the following:

Relevance

As defined in the qualitative characteristics of the *Conceptual Framework*, 'Relevant financial information is capable of making a difference in the decisions made by users. Information may be capable of making a difference in a decision even if some users choose not to take advantage of it or are already aware of it from other sources.' (*CF*, 2.6)

According to the *Conceptual Framework*, an asset or liability may not be recognised if:

- 'it is uncertain whether or not the asset or liability exists; or
- an asset or liability exists, but the probability of an inflow or outflow of economic benefits is low.' (CF, 5.12)

Faithful representation

As defined in the qualitative characteristics of the *Conceptual Framework*, 'To be useful, financial information must not only represent relevant phenomena, but it must also faithfully represent the substance of the phenomena that it purports to represent' (*CF,* 2.12) and 'To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral and free from error.' (*CF*, 2.13)

According to the *Conceptual Framework*, for an asset or liability to be recognised it must be measured. The level of measurement uncertainty associated with the asset or liability may impact whether a faithful representation can be provided of the item. Measurement uncertainty is defined as 'uncertainty that arises when monetary amounts in financial reports cannot be observed directly and must instead be estimated.' (*CF*, page 60) Measurement requires the elements to be able to be quantified in monetary terms. To be able to quantify or measure with certainty, the business must select a measurement basis, i.e. either historical cost or current value (current value includes fair value, value in use/fulfilment value or current cost).

Sample questions

The following questions and marking keys are provided as examples of questions that demonstrate knowledge, understanding and application of the *Conceptual Framework*, specifically the changes outlined in this document.

Question 1 **(3 marks)**

An asset is defined as a present economic resource controlled by the entity as a result of past events. Explain how a business determines if an item is an economic resource and therefore can be classified as an asset.

Description	Marks
Explains an economic resource	3
Describes an economic resource	2
States a fact about an economic resource	1
Total	**/3**
Answer could include, but is not limited to	
As per the *Conceptual Framework,* an economic resource is a right that has the potential to produce economic benefits. Rights that have the potential to produce economic benefits can take many forms, including rights to: • receive cash from another party • receive goods or services from another party • exchange economic resources with another party on favourable terms • physical objects (e.g. property, equipment, inventories) • use intellectual property.	

Question 2 **(5 marks)**

Define an expense and provide an example to explain how it meets the definition as per the *Conceptual Framework*.

Description	Marks
Defines an expense	2
Provides a partial definition of an expense	1
Subtotal	**/2**
Explains how the expense meets the definition	3
Outlines how the expense meets the definition	2
Provides an example of an expense	1
Subtotal	**/3**
Total	**/5**

Answer could include, but is not limited to

The *Conceptual Framework* defines expenses as 'decreases in assets, or increase in liabilities, that result in decreases in equity, other than those relating to distributions to owners.'

An example of an expense is wages; it meets the definition as follows:

- decreases in assets, or increase in liabilities – if the wages have been paid, they decrease cash (asset) or if owing, they increase liabilities (accrued expense)
- result in decreases in equity – equity can be reduced by decreasing profit, wages will act to decrease the profit made by the business
- other than those relating to distributions to owners – the wages are paid to the employees of the business, not the owners.

Question 3 **(6 marks)**

Bunyip Ltd is a mining company that has been exploring for minerals in a remote area of Australia. A recent accident at the site has caused some chemicals to leak into the soil at a site that the company leases from the landowners.

The landowners have just successfully sued the company and, as a result, the company must pay for damages awarded to the owners of $3,000,000.

Determine if Bunyip Ltd needs to recognise the $3,000,000 compensation in its financial statements, which are due to be finalised and published this week. Include in your response reference to the definitions and recognition criteria as per the *Conceptual Framework.*

Description	Marks
Identifies that the compensation should be recognised as a liability in the financial statements	1
Subtotal	**/1**
With reference to the definition of liabilities as per the *Conceptual Framework*	
Defines a liability	2
Provides a partial definition of a liability	1
Subtotal	**/2**
With reference to the recognition criteria for liabilities as per the *Conceptual Framework*	
Explains the recognition criteria for a liability	3
Outlines the recognition criteria for a liability	2
States a fact about the recognition criteria for a liability	1
Subtotal	**/3**
Total	**/6**
Answer could include, but is not limited to	

For the $3,000,000 compensation:

- the amount should be recognised as a liability in the financial statement
- the cost meets the definition of a liability
- as per the *Conceptual Framework*, a liability is defined as 'a present obligation of the entity to transfer an economic resource as a result of past events.'
- as per the *Conceptual Framework*, a liability is recognised only if recognition of that liability and any resulting expenses or changes in equity provides users of financial statements with information that is useful, i.e. with:
  - relevant information about the liability and any resulting expenses or changes in equity
  - a faithful representation of the liability and any resulting expenses or changes in equity.'

Acknowledgement

Australian Accounting Standards Board. (2022). *Conceptual Framework for Financial Reporting.* Retrieved September 2024, from https://aasb.gov.au/pronouncements/conceptual-framework/.