DIGITAL CFO SOLUTIONS • IFRS SERIES

INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Conceptual Framework

The standard of standards — the foundation upon which every IAS and IFRS is built

BD

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PART I — FOUNDATIONS

What Is the Conceptual Framework?

A shared reference point for every accounting standard — not a standard in itself, but the logic that all standards must answer to.

FOUNDATIONS

The Framework Is Not an Accounting Standard

> *“The Framework provides the general principles upon which the accounting standards themselves are based — it is the standard of all standards.”*

Not Mandatory

It has no authority to override any individual IAS or IFRS requirement.

Sets Principles

It establishes the concepts that underlie the preparation of financial statements.

The Foundation

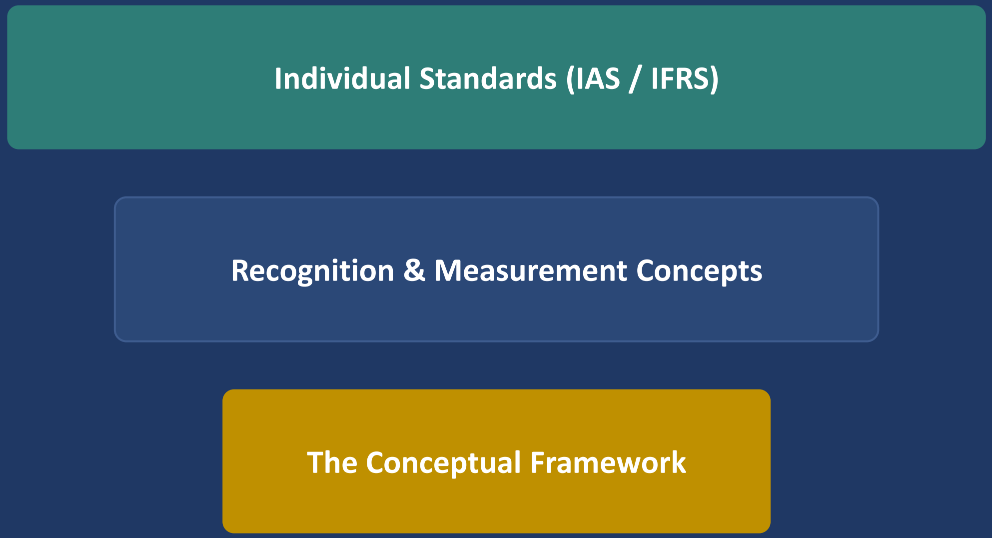
Every standard is built on — and interpreted through — the Framework's logic.

FOUNDATIONS

The Framework Is the Edifice of IFRS

The Conceptual Framework is the edifice upon which International Financial Reporting Standards are built.

It determines how financial statements are prepared, and the information they must contain.



Every layer of IFRS reporting rests on the layer beneath it

PART II — ELEMENTS

Elements of Financial Statements

Five building blocks underpin every financial statement: three describe financial position, two describe financial performance.

ELEMENTS

Two Families, Five Elements

FINANCIAL POSITION

Represented in the Statement of Financial Position

1 **Assets**

Resources controlled with future economic benefit

2 **Liabilities**

Present obligations to transfer resources

3 **Equity**

Residual interest after deducting liabilities

FINANCIAL PERFORMANCE

Represented in the Statement of Comprehensive Income

1 **Income**

Increases in economic benefits during the period

2 **Expenses**

Decreases in economic benefits during the period

ELEMENTS — FINANCIAL POSITION

Assets, Liabilities & Equity (in the SOFP)

Assets

- A right, controlled as a result of a past event
- With the potential to produce future economic benefits

Liabilities

- A present obligation to transfer an economic resource
- Arising from a past event; outflow expected

Equity

- The residual interest in assets
- After deducting all liabilities

Income & Expenses (in the SOCI)

Income

Increases in economic benefits during the accounting period, in the form of inflows or enhancements of assets, or decreases of liabilities — that result in increases in equity, other than contributions from equity participants.

Conceptual Framework

Expenses

Decreases in economic benefits during the accounting period, in the form of outflows or depletions of assets, or incurrence of liabilities — that result in decreases in equity, other than distributions to equity participants.

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PART III — RECOGNITION

Recognition Criteria

An item is recognised only once it meets the definition of an element and satisfies the Framework's two-part test for recognition.

RECOGNITION

When Is an Item Recognised?

Recognition is the process of incorporating an item that meets the definition of an element of the financial statements — and satisfies the criteria below — into the Statement of Financial Position or the Statement of Comprehensive Income.

1 Probable Future Benefit

It is probable that any future economic benefit associated with the item will flow to, or from, the enterprise.

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2 Reliable Measurement

The item has a cost or value that can be measured with reliability.

— Conceptual Framework

Recognition Criteria by Element

Element	Recognised In	When
Asset	Statement of Financial Position	It is probable that future economic benefits will flow to the enterprise, and the asset has a cost or value that can be measured reliably.
Liability	Statement of Financial Position	It is probable that an outflow of resources embodying economic benefits will result from settling a present obligation, and the settlement amount can be measured reliably.
Income	Statement of Comprehensive Income	An increase in future economic benefits related to an increase in an asset, or a decrease in a liability, has arisen and can be measured reliably.
Expenses	Statement of Comprehensive Income	A decrease in future economic benefits related to a decrease in an asset, or an increase in a liability, has arisen and can be measured reliably.

PART IV — FINANCIAL STATEMENTS

Financial Position & Performance

How the accounting equation links the opening and closing Statement of Financial Position through the period's financial performance.

Linking Position and Performance

Opening Statement of Financial Position		Financial Performance		Changes in Equity		Closing Statement of Financial Position
Assets – Liabilities = Equity	+	Income – Expenses	+	Contributions – Distributions	=	Assets – Liabilities = Equity

Every change in equity between two balance sheet dates is explained either by the financial performance for the period (income less expenses), or by transactions with equity holders — contributions received, less distributions paid. Nothing moves equity outside of these two channels.

What Makes Something an Asset?

"An asset is a present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits." — Conceptual Framework

1

Right

A legal or practical right the entity holds

2

Control

The entity can direct the resource's use and obtain its benefits

3

Potential to Produce Benefits

The right can, in some scenario, generate economic value

Two Categories of Right

(a) Rights Corresponding to Another Party's Obligation

- Rights to receive cash
- Rights to receive goods or services
- Rights to exchange resources on favourable terms — e.g. a favourable forward contract or option
- Rights to benefit from another party's obligation if a specified uncertain event occurs

(b) Rights That Do Not Correspond to an Obligation

- Rights over physical objects — e.g. property, plant & equipment, or inventories
- A right to use a physical object, or to benefit from its residual value
- Rights to use intellectual property

How a Resource Produces Benefits

An economic resource is a right that has the potential to produce economic benefits. That potential does not need to be certain, or even likely — only possible.

- **a** Receive contractual cash flows, or another economic resource
- **b** Exchange economic resources with another party on favourable terms
- **c** Produce cash inflows, or avoid cash outflows — by using the resource alone or in combination with others, enhancing other resources' value, or leasing it to another party
- **d** Receive cash or other resources by selling the economic resource
- **e** Extinguish liabilities by transferring the economic resource

ASSETS — CONTROL

Control Links the Resource to the Entity

An entity controls an economic resource if it has the present ability to direct the resource's use and obtain the economic benefits that flow from it.

1. Assessing whether control exists helps identify the economic resource for which the entity accounts
2. Control includes the present ability to prevent other parties from directing the resource's use or obtaining its benefits
3. If one party controls a resource, no other party can also control that same resource

LIABILITIES

What Makes Something a Liability?

"A liability is a present obligation of the entity to transfer an economic resource as a result of past events." — Conceptual Framework

1

Obligation Exists

The entity has an obligation to another party

2

Transfer of Resource

The obligation is to transfer an economic resource

3

Arises From the Past

It is a present obligation as a result of past events

What Is an Obligation?

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An obligation is a duty or responsibility that an entity has no practical ability to avoid.

An obligation is always owed to another party (or parties) — a person, another entity, a group of people or entities, or society at large.

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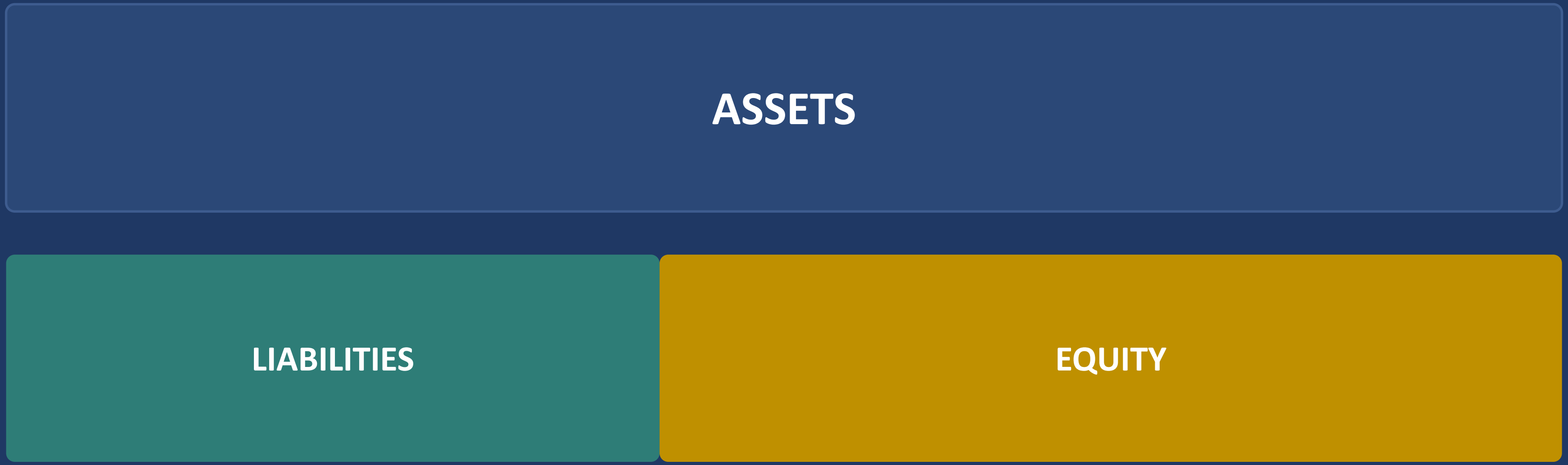
The Residual Interest

"The residual interest in the assets of the enterprise after deducting all its liabilities." — Conceptual Framework



The Statement of Financial Position

The Statement of Financial Position discloses short-term and long-term solvency — the entity's ability to meet its liabilities as they fall due.

Solvency is the availability of cash over the longer term to meet financial commitments as they fall due.

Liquidity is the availability of sufficient funds to meet withdrawals and other financial commitments as they fall due.

Assets = Liabilities + Equity

Assets	What the entity controls
Liabilities	What the entity owes
Equity	What remains for owners

The Statement of Profit & Loss

Depicts the net financial results of the organisation, represented by income and expenses, and includes all items of income and expense recognised in a period.

Income

Increases in assets, or decreases in liabilities, that result in increases in equity — other than contributions from holders of equity claims.

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Expenses

Decreases in assets, or increases in liabilities, that result in decreases in equity — other than distributions to holders of equity claims.

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PART V — QUALITATIVE CHARACTERISTICS

Qualitative Characteristics

The Framework identifies the characteristics that make financial information useful to the primary users of financial statements.

QUALITATIVE CHARACTERISTICS

Fundamental Characteristics

1 Relevance

Information is capable of making a difference to users' decisions. It has predictive value, confirmatory value, or both — and materiality is an entity-specific aspect of relevance.

2 Faithful Representation

Information must faithfully represent the substance of what it purports to represent — complete, neutral, and free from error.

Enhancing Characteristics

1

Comparability

Enables users to identify and understand similarities and differences across entities and periods

2

Verifiability

Different knowledgeable observers could reach consensus that information faithfully represents events

3

Timeliness

Information is available to decision-makers before it loses its capacity to influence decisions

4

Understandability

Information is classified, characterised and presented clearly and concisely

THANK YOU

International Financial Reporting Standards — The Conceptual Framework

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A Career Built on Making IFRS Understandable

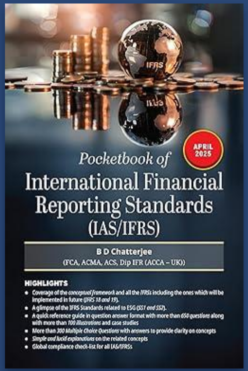
B D Chatterjee is a Chartered Accountant and financial thought leader with over 35 years of global experience spanning corporate finance, accounting standards, financial reporting, business valuation and financial due diligence. As a seasoned CFO, he has led finance functions across major corporations and now heads Digital CFO Solutions, a platform delivering institutional-grade IFRS, US GAAP and valuation workbooks alongside fractional CFO services.

- ✓ Published author of the Pocketbook of IFRS series
- ✓ Teacher and Mentor to finance professionals worldwide
- ✓ Guided thousands through IFRS, US GAAP & valuation transitions

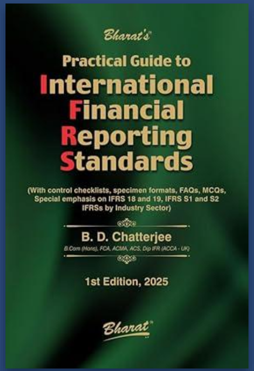
Digital CFO Solutions provides institutional-grade Excel-based CFO workbooks, fractional CFO advisory, and published finance literature on IFRS, US GAAP, business valuation and financial due diligence.

ABOUT THE AUTHOR

Books by B D Chatterjee — IFRS Library

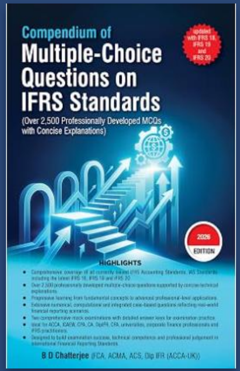


Pocketbook of International Financial Reporting Standards (IAS/IFRS)

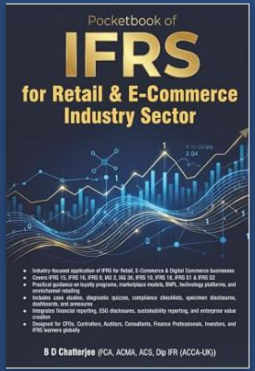


Practical Guide to International Financial Reporting Standards

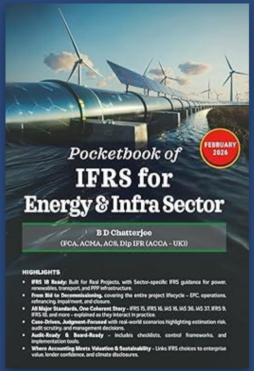
Pocketbook of IFRS 18 — Presentation, Analysis & Industry Applications



Compendium of Multiple-Choice Questions on IFRS Standards



Pocketbook of IFRS for Retail & E-Commerce Industry Sector



Pocketbook of IFRS for Energy & Infra Sector

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