

Statement of Financial Accounting Concepts No. 8

As Amended

December 2021

Conceptual Framework for Financial Reporting

Chapter 1, *The Objective of General Purpose
Financial Reporting*

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Chapter 1, *The Objective of General Purpose
Financial Reporting*

Financial Accounting Standards Board

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Statements of Financial Accounting Concepts

The Conceptual Framework is intended to set forth fundamental concepts that will be the basis for development of financial accounting and reporting standards. The fundamentals are the underlying concepts of financial accounting—concepts that guide the selection of transactions and other events and circumstances to be accounted for; their recognition and measurement; and the means of summarizing and communicating them to interested parties. Concepts of that type are fundamental in the sense that other concepts flow from them and repeated reference to them will be necessary in establishing, interpreting, and applying accounting and reporting standards.

The Conceptual Framework is a coherent system of interrelated objectives and fundamental concepts that prescribes the nature, function, and limits of financial accounting and reporting and that is expected to lead to consistent standards. It is intended to serve the public interest by providing structure and direction to financial accounting and reporting to facilitate the provision of unbiased financial and related information. That information helps capital and other markets to function efficiently in allocating scarce resources in the economy and society. Establishment of objectives and identification of fundamental concepts will not directly solve financial accounting and reporting problems. Rather, objectives give direction, and concepts are tools for solving problems.

The Board itself is likely to be the most direct beneficiary of the guidance provided by Concepts Statements. They will guide the Board in developing accounting and reporting standards by providing the Board with a common foundation and basic reasoning on which to consider merits of alternatives. However, knowledge of the objectives and concepts the Board will use in developing new standards also should enable those who are affected by or interested in generally accepted accounting principles (GAAP) to understand better the purposes, content, and characteristics of information provided by financial accounting and reporting. That knowledge is expected to enhance the usefulness of, and confidence in, financial accounting and reporting.

Concepts Statements are not part of the *FASB Accounting Standards Codification*[®], which is the source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities (Topic 105, Generally Accepted Accounting Principles). Rather, Concepts Statements describe concepts that will be considered in developing future financial reporting standards and, in due course, should serve as a basis for evaluating existing guidance and standards.

The Board recognizes that in certain respects current GAAP may be inconsistent with what might be derived from the objectives and fundamental concepts set forth in Concepts Statements. However, a Concepts Statement does not (a) require a change in existing GAAP; (b) amend, modify, or interpret the Accounting Standards Codification; or (c) justify either changing existing generally accepted accounting and reporting practices or interpreting the

Accounting Standards Codification based on personal interpretations of the objectives and concepts in the Concepts Statements.

Because a Concepts Statement does not establish GAAP, it is not intended to invoke application of Rule 203 of the Rules of Conduct of the Code of Professional Ethics of the American Institute of Certified Public Accountants (or successor rules or arrangements of similar scope and intent).*

A Concepts Statement may be amended, superseded, or withdrawn by appropriate action under the Board's *Rules of Procedure*.

Accrual Accounting and Related Concepts

Items that qualify under the definitions of elements of financial statements and that meet criteria for recognition and, therefore would be measured, are accounted for and included in financial statements by using accrual accounting procedures. Accrual accounting and related concepts are significant for understanding and considering several aspects of the Conceptual Framework. The following paragraphs define or describe significant financial accounting and reporting concepts that are used in the Conceptual Framework.

Transactions, Events, and Circumstances

The Conceptual Framework uses the phrase *transactions and other events and circumstances affecting an entity* to describe the sources or causes of changes in assets, liabilities, and equity or net assets. An event is a happening of consequence to an entity. It may be an internal event that occurs within an entity, or it may be an external event that involves interaction between an entity and its environment, such as a transaction with another entity. A transaction is a particular kind of external event, namely, an external event involving a transfer of something of value between two (or more) entities. The transaction may be either an exchange in which each participant both receives and sacrifices value, such as purchases or sales of goods or services, or a nonreciprocal transfer in which an entity incurs a liability or transfers an asset to another entity (or receives an asset or cancellation of a liability) without directly receiving (or giving) value in exchange. Nonreciprocal transfers contrast with exchanges (which are reciprocal transfers) and include, for example, impositions of taxes, gifts, contributions given or received, and thefts.

Circumstances are a condition or a set of conditions that develop from an event or a series of events that may occur almost imperceptibly and may converge in random or unexpected ways to create situations that might otherwise not have

*Rule 203 prohibits a member of the American Institute of Certified Public Accountants from expressing an opinion that financial statements conform with generally accepted accounting principles (GAAP) if those statements contain a material departure from an accounting principle promulgated by the Financial Accounting Standards Board, unless the member can demonstrate that because of unusual circumstances the financial statements otherwise would have been misleading.

occurred and that might not have been anticipated. To see the circumstance may be fairly easy, but to discern specifically when the event or events that caused it occurred may be difficult or impossible. For example, a debtor going bankrupt or a thief stealing gasoline may be an event, but a creditor facing the situation in which its debtor is bankrupt or a warehouse facing the fact that its tank is empty may be a circumstance.

Accrual Accounting

Accrual accounting attempts to record the financial effects on an entity of transactions and other events and circumstances in the periods in which those transactions, events, and circumstances occur. Accrual accounting thus provides information about an entity's assets and liabilities and changes in them that cannot be obtained by accounting for only cash receipts and outlays. Accrual accounting includes using accrual, deferral, and allocation procedures, the result of which is the recognition of revenues, expenses, gains, and losses in periods that depict an entity's performance during a period instead of merely listing its cash receipts and outlays. Thus, the recognition of revenues, expenses, gains, and losses dependent upon increments or decrements in assets and liabilities is the essence of using accrual accounting to measure the performance of entities.

Accrual, Deferral, and Allocation (Including Amortization)

Accrual is the accounting process of recognizing assets or liabilities and the related changes in revenues, expenses, gains, losses, or equity for amounts expected to be received or paid, usually in cash, in the future. Common examples of accruals include purchases and sales of goods or services on account and not-yet-paid interest, rent, wages and salaries, and taxes.

Deferral is concerned with past cash receipts and payments—and with prepayments received or paid; deferral is the accounting process of recognizing a liability resulting from a current cash receipt (or the equivalent) or an asset resulting from a current cash payment (or the equivalent) with deferred recognition of related revenues, expenses, gains, or losses. Recognition of those related elements is deferred until the obligation underlying the liability is partly or wholly satisfied or until the economic benefit underlying the asset is partly or wholly used or lost. Common examples of deferrals include prepaid expenses and customer deposits.

Allocation is the accounting process of assigning or distributing an amount according to a plan or a formula. Allocation includes amortization, which is the accounting process of reducing an amount by periodic payments or write-downs. Common examples of allocations include (a) assigning manufacturing costs to production departments or cost centers and to units of product to determine "product cost," (b) apportioning the cost of a "basket purchase" to the individual assets acquired on the basis of their relative market values, and (c) spreading the cost of an insurance policy or a building to two or more accounting periods. Expenses resulting from the use of assets are normally allocated to the periods of their estimated useful lives (the periods over which they are expected to provide

benefits) by a “systematic and rational” allocation procedure. Other costs also are recognized as expenses in the period in which they are incurred because the period to which they otherwise relate is indeterminable or not worth the effort to determine.

Amortization is also a form of allocation. The cost of an asset is said to be amortized (depreciated) by assigning a portion of the cost over the benefit period of the asset. Amortization also refers to the allocation of payments made or received on debt instruments between interest earned or paid and the principal that is reduced by periodic payments.

A major difference between accrual accounting and accounting based on cash receipts and outlays is the timing of recognition of revenues, expenses, gains, and losses. Investments by an entity in goods and services for its operations or other activities commonly do not all occur in the same period as revenues or other proceeds from selling the resulting products or providing the resulting services. Several periods may elapse between the time cash is invested in raw materials or fixed assets, for example, and the time cash is received from collecting the sales price of products from customers. A report showing cash receipts and cash outlays of an enterprise for a short period (such as a statement of cash flows) cannot indicate how much of the cash received is return *of* investment and how much is return *on* investment and, thus, cannot indicate whether or to what extent an enterprise is successful or unsuccessful. Similarly, goods or services that a not-for-profit entity provides gratis to beneficiaries commonly result from using goods or services acquired with cash received and spent in earlier periods. A report showing cash receipts and outlays of the entity for a short period cannot tell much about the relationship between the goods or services provided and the resources used to provide them and, thus, cannot indicate to what extent an entity is successful or unsuccessful in carrying out its service objectives. Cash receipts in a particular period largely may reflect the effects of the activities of a business entity or a not-for-profit entity in earlier periods, while many of the cash outlays may relate to the entity’s activities and efforts expected in future periods.

In most entities, transactions or events occur that result in simultaneous recognition of revenue and one or more expenses that result directly and jointly from the same transactions or other events. For example, a sale of a product or merchandise involves revenues from the receipt of cash or a receivable and expense for the sacrifice of a product or merchandise sold to the customer. If all assets and liabilities are recorded from the transaction, recognition of revenues and expenses in the same period is achieved by applying the asset and liability definitions.

Many expenses, however, are not related directly to particular revenues but can be related to a period on the basis of transactions or events occurring in that period or by allocation. Some costs that cannot be related directly to particular revenues are incurred to obtain benefits that are exhausted in the period in which the costs are incurred.

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Conceptual Framework for Financial Reporting

CHAPTER 1: THE OBJECTIVE OF GENERAL PURPOSE FINANCIAL REPORTING

Introduction

OB1. The objective of general purpose financial reporting forms the foundation of the Conceptual Framework. Other aspects of the Conceptual Framework—a reporting entity concept; the qualitative characteristics of, and the constraints on, useful financial information; elements of financial statements; recognition, measurement; presentation; and disclosure—flow logically from the objective.

Objective, Usefulness, and Limitations of General Purpose Financial Reporting

OB2. The objective of general purpose financial reporting¹ is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the entity. Those decisions involve buying, selling, or holding equity and debt instruments and providing or settling loans and other forms of credit.

OB3. Decisions by existing and potential investors about buying, selling, or holding equity and debt instruments depend on the returns that they expect from an investment in those instruments; for example, dividends, principal and interest payments, or market price increases. Similarly, decisions by existing and

¹Throughout this Conceptual Framework, the terms *financial reports* and *financial reporting* refer to *general purpose financial reports* and *general purpose financial reporting* unless specifically indicated otherwise.

potential lenders and other creditors about providing or settling loans and other forms of credit depend on the principal and interest payments or other returns that they expect. Investors', lenders', and other creditors' expectations about returns depend on their assessment of the amount, timing, and uncertainty of (the prospects for) future net cash inflows to the entity. Consequently, existing and potential investors, lenders, and other creditors need information to help them assess the prospects for future net cash inflows to an entity.

OB4. To assess an entity's prospects for future net cash inflows, existing and potential investors, lenders, and other creditors need information about the resources of the entity, claims against the entity, and how efficiently and effectively the entity's management and governing board² have discharged their responsibilities to use the entity's resources. Examples of such responsibilities include protecting the entity's resources from unfavorable effects of economic factors such as price and technological changes and ensuring that the entity complies with applicable laws, regulations, and contractual provisions. Information about management's discharge of its responsibilities also is useful for decisions by existing investors, lenders, and other creditors who have the right to vote on or otherwise influence management's actions.

OB5. Many existing and potential investors, lenders, and other creditors cannot require reporting entities to provide information directly to them and must rely on general purpose financial reports for much of the financial information they need. Consequently, they are the primary users to whom general purpose financial reports are directed.

OB6. However, general purpose financial reports do not and cannot provide all of the information that existing and potential investors, lenders, and other creditors need. Those users need to consider pertinent information from other sources, for example, general economic conditions and expectations, political events and political climate, and industry and company outlooks.

OB7. General purpose financial reports are not designed to show the value of a reporting entity; but they provide information to help existing and potential investors, lenders, and other creditors to estimate the value of the reporting entity.

OB8. Individual primary users have different, and possibly conflicting, information needs and desires. The Board, in developing financial reporting standards, will seek to provide the information set that will meet the needs of the maximum number of primary users. However, focusing on common information

²Throughout this Conceptual Framework, the term *management* refers to *management and the governing board of an entity* unless specifically indicated otherwise.

needs does not prevent the reporting entity from including additional information that is most useful to a particular subset of primary users.

OB9. The management of a reporting entity also is interested in financial information about the entity. However, management need not rely on general purpose financial reports because it is able to obtain the financial information it needs internally.

OB10. Other parties, such as regulators and members of the public other than investors, lenders, and other creditors, also may find general purpose financial reports useful. However, those reports are not primarily directed to these other groups.

OB11. To a large extent, financial reports are based on estimates, judgments, and models rather than exact depictions. The Conceptual Framework establishes the concepts that underlie those estimates, judgments, and models. The concepts are the goal towards which the Board and preparers of financial reports strive. As with most goals, the Conceptual Framework's vision of ideal financial reporting is unlikely to be achieved in full, at least not in the short term, because it takes time to understand, accept, and implement new ways of analyzing transactions and other events. Nevertheless, establishing a goal towards which to strive is essential if financial reporting is to evolve so as to improve its usefulness.

Information about a Reporting Entity's Economic Resources, Claims, and Changes in Resources and Claims

OB12. General purpose financial reports provide information about the financial position of a reporting entity, which is information about the entity's economic resources and the claims against the reporting entity. Financial reports also provide information about the effects of transactions and other events that change a reporting entity's economic resources and claims. Both types of information provide useful input for decisions about providing resources to an entity.

Economic Resources and Claims

OB13. Information about the nature and amounts of a reporting entity's economic resources and claims can help users to identify the reporting entity's financial strengths and weaknesses. That information can help users to assess the reporting entity's liquidity and solvency, its needs for additional financing, and how successful it is likely to be in obtaining that financing. Information about priorities and payment requirements of existing claims helps users to predict how

future cash flows will be distributed among those with a claim against the reporting entity.

OB14. Different types of economic resources affect a user's assessment of the reporting entity's prospects for future cash flows differently. Some future cash flows result directly from existing economic resources, such as accounts receivable. Other cash flows result from using several resources in combination to produce and market goods or services to customers. Although those cash flows cannot be identified with individual economic resources (or claims), users of financial reports need to know the nature and amount of the resources available for use in a reporting entity's operations.

Changes in Economic Resources and Claims

OB15. Changes in a reporting entity's economic resources and claims result from that entity's financial performance (see paragraphs OB17–OB20) and from other events or transactions, such as issuing debt or equity instruments (see paragraph OB21). To properly assess the prospects for future cash flows from the reporting entity, users need to be able to distinguish between both of these changes.

OB16. Information about a reporting entity's financial performance helps users to understand the return that the entity has produced on its economic resources. Information about the return the entity has produced provides an indication of how well management has discharged its responsibilities to make efficient and effective use of the reporting entity's resources. Information about the variability and components of that return also is important, especially in assessing the uncertainty of future cash flows. Information about a reporting entity's past financial performance and how its management discharged its responsibilities usually is helpful in predicting the entity's future returns on its economic resources.

Financial Performance Reflected by Accrual Accounting

OB17. Accrual accounting depicts the effects of transactions, and other events and circumstances on a reporting entity's economic resources and claims in the periods in which those effects occur, even if the resulting cash receipts and payments occur in a different period. This is important because information about a reporting entity's economic resources and claims and changes in its economic resources and claims during a period provides a better basis for assessing the entity's past and future performance than information solely about cash receipts and payments during that period.

OB18. Information about a reporting entity's financial performance during a period, reflected by changes in its economic resources and claims other than by obtaining additional resources directly from investors and creditors (see paragraph OB21), is useful in assessing the entity's past and future ability to generate net cash inflows. That information indicates the extent to which the reporting entity has increased its available economic resources, and thus its capacity for generating net cash inflows through its operations rather than by obtaining additional resources directly from investors and creditors.

OB19. Information about a reporting entity's financial performance during a period also may indicate the extent to which events such as changes in market prices or interest rates have increased or decreased the entity's economic resources and claims, thereby affecting the entity's ability to generate net cash inflows.

Financial Performance Reflected by Past Cash Flows

OB20. Information about a reporting entity's cash flows during a period also helps users to assess the entity's ability to generate future net cash inflows. It indicates how the reporting entity obtains and spends cash, including information about its borrowing and repayment of debt, cash dividends or other cash distributions to investors, and other factors that may affect the entity's liquidity or solvency. Information about cash flows helps users understand a reporting entity's operations, evaluate its financing and investing activities, assess its liquidity or solvency, and interpret other information about financial performance.

Changes in Economic Resources and Claims Not Resulting from Financial Performance

OB21. A reporting entity's economic resources and claims also may change for reasons other than financial performance, such as issuing additional ownership shares. Information about this type of change is necessary to give users a complete understanding of why the reporting entity's economic resources and claims changed and the implications of those changes for its future financial performance.

Application of the Objective of General Purpose Financial Reporting to Not-for-Profit Entities³

OB22. The Board has concluded that it is not necessary to develop an independent conceptual framework for any particular category of

³This guidance was incorporated into this chapter from FASB Concepts Statement No. 4, *Objectives of Financial Reporting by Nonbusiness Organizations*.

nongovernmental entities (for example, not-for-profit entities or business enterprises). Rather, the Board's goal is to develop an integrated conceptual framework that has relevance to all entities and that provides appropriate consideration of any different reporting objectives and concepts that may apply to only certain types of entities. Consideration of the characteristics of not-for-profit entities set forth in paragraphs OB23–OB28 will be useful in helping to identify areas that may require unique treatment.

OB23. The major characteristics that distinguish a not-for-profit entity from a business enterprise typically include:

- a. Receipts of significant amounts of resources from resource providers that do not expect to receive either repayment or economic benefits proportionate to resources provided
- b. Operating purposes that are other than to provide goods or services at a profit or profit equivalent
- c. Absence of defined ownership interests that can be sold, transferred, or redeemed or that convey entitlement to a share of a residual distribution of resources in the event of liquidation of the entity.

These distinguishing characteristics result in (a) certain types of transactions that are largely, although not entirely, absent in business enterprises, such as contributions and grants, and (b) the absence of transactions with owners, such as issuing and redeeming equity interests or paying dividends.

OB24. The degree to which not-for-profit entities possess the characteristics in paragraph OB23 varies significantly, ranging from entities with predominantly not-for-profit characteristics to entities with characteristics that are much closer overall to those of a business enterprise. Both not-for-profit entities and business enterprises obtain resources in exchange transactions in markets. Both obtain labor, materials, and facilities or their use by paying for them or agreeing to pay for them in the future. Both may borrow funds through bank loans, mortgages, or other direct loans or through issuing debt securities to creditors that commonly may evaluate and compare the risks and returns of securities of both not-for-profit entities and business enterprises. Financial reporting for not-for-profit entities should provide information to lenders and other creditors.

OB25. The objective of general purpose financial reporting for not-for-profit entities also includes providing useful financial information to other existing and potential resource providers, such as members, donors, and grantors, in making rational decisions about the allocation of resources to those entities. However, members, donors, and grantors that provide resources to not-for-profit entities do so for reasons different from those of owners of business enterprises. Many not-for-profit entities obtain significant resources from resource providers that either expect no economic benefits or expect benefits received not to be proportionate to the resources provided. Those resources are often provided for noneconomic

reasons in furthering the purpose and goals of a not-for-profit entity, such as for charitable, cultural, educational, economic, humanitarian, political, religious, or social reasons.

OB26. Despite those different reasons, resource providers of all entities look to information about economic resources, obligations, net resources, and changes in them for information that is useful in assessing the amounts, timing, and uncertainty of the (prospects for) future net cash flows to the entity.

OB27. Resource providers focus on indicators of entity performance and information about management stewardship. For example, mandates such as restrictions imposed by donors on the use of provided resources give managers a special responsibility to ensure compliance. Information about the extent to which those mandates of a not-for-profit entity were fulfilled or departures from those mandates is important in assessing how well managers have discharged their stewardship responsibilities. In particular, members, donors, and grantors are interested in whether the activities of an entity are consistent with its stated objectives and their directives.

OB28. Existing and potential users of the information provided by financial reporting by a particular not-for-profit entity share a common interest in information about the services provided by the not-for-profit entity and its efficiency and effectiveness in providing those services as a basis for determining its ability to continue to provide those services. Resource providers, such as members, donors, and grantors, may be interested in that information as a basis for assessing how well an entity has met its objectives and whether to continue support. Information about an entity's service efforts in accomplishing its mission is useful in assessing the performance of a not-for-profit entity and in making resource allocation decisions.

This Concepts Statement was adopted by the unanimous vote of the five members of the Financial Accounting Standards Board:

Robert H. Herz, *Chairman*
Thomas J. Linsmeier
Leslie F. Seidman
Marc A. Siegel
Lawrence W. Smith

Paragraphs OB22–OB28 were incorporated from FASB Concepts Statement No. 4, which was adopted by members of the Financial Accounting Standards Board in 1980.

APPENDIX A: BASIS FOR CONCLUSIONS FOR CHAPTER 1

Introduction

BC1.1 This basis for conclusions summarizes considerations of the Financial Accounting Standards Board (the Board) in reaching the conclusions in Chapter 1, *The Objective of General Purpose Financial Reporting*. It includes reasons for accepting some alternatives and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC1.2 The Board developed this chapter jointly with the International Accounting Standards Board (IASB). Consequently, this basis for conclusions also includes some references to the IASB's literature.

Background

BC1.3 The Board began the process of developing the objective of financial reporting by reviewing its own framework and concepts as well as those of other standard setters. In July 2006, the Board published for public comment a Discussion Paper on this topic. That same paper also was published by the IASB. The Board and the IASB received 179 responses. In its redeliberations of the issues on this topic, the Board considered all of the comments received and information gained from other outreach initiatives. In May 2008, the Board and the IASB jointly published an Exposure Draft. The Boards received 142 responses. The Board reconsidered all of the issues. This document is the result of those reconsiderations.

General Purpose Financial Reporting

BC1.4 Consistent with the Board's responsibilities, the Conceptual Framework establishes an objective of financial reporting and not just of financial statements. Financial statements are a central part of financial reporting, and most of the issues that the Board addresses involve financial statements. Although the scope of FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises*, was financial reporting, the other FASB Concepts Statements focused on financial statements. The scope of the IASB's *Framework for the Preparation and Presentation of Financial Statements*, which was published by the IASB's predecessor body in 1989 (hereinafter called *Framework* (1989)), dealt with financial statements only. Therefore, for both Boards the scope of the Conceptual Framework is broader.

BC1.5 Some constituents suggested that advances in technology may make general purpose financial reporting obsolete. New technologies, for example the use of eXtensible Business Reporting Language (XBRL), may make it practicable in the future for reporting entities either to prepare or to make available the information necessary for different users to assemble different financial reports to meet their individual information needs.

BC1.6 To provide different reports for different users or to make available all of the information that users would need to assemble their own custom-designed reports would be expensive. Requiring users of financial information to assemble their own reports also might be unreasonable because many users would need to have a greater understanding of accounting than they have now. Therefore, the Board concluded for now that a general purpose financial report is still the most efficient and effective way to meet the information needs of a variety of users.

BC1.7 In the Discussion Paper, the Board used the term *general purpose external financial reporting*. *External* was intended to convey that internal users such as management were not the intended beneficiaries for general purpose financial reporting as established by the Board. During redeliberations, the Board concluded that this term was redundant. Therefore, this chapter uses *general purpose financial reporting*.

Financial Reporting of the Reporting Entity

BC1.8 Some respondents to the Exposure Draft said that the reporting entity is not separate from its equity investors or a subset of those equity investors. This view has its roots in the days when most businesses were sole proprietorships and partnerships that were managed by their owners who had unlimited liability for the debts incurred in the course of the business. Over time, the separation between businesses and their owners has grown. The vast majority of today's businesses have legal substance separate from their owners by virtue of their legal form of organization, numerous investors with limited legal liability, and professional managers separate from the owners. Consequently, the Board concluded that financial reports should reflect that separation by accounting for the entity (and its economic resources and claims) rather than its primary users and their interests in the reporting entity.

Primary Users

BC1.9 The objective of financial reporting set out in paragraph OB2 refers to existing and potential investors, lenders, and other creditors. The description of the primary users in paragraph OB5 refers to existing and potential investors, lenders, and other creditors who cannot require reporting entities to provide information directly to them. Paragraph OB10 states that "regulators and

members of the public other than investors, lenders, and other creditors” may find information in general purpose financial reports useful but clearly states that those are not the parties to whom general purpose financial reports are primarily directed.

BC1.10 Paragraph 9 of the *Framework* (1989) stated that users included “present and potential investors, employees, lenders, suppliers and other trade creditors,” (and later added advisers in the discussion of investors’ needs) all of which are intended to be encompassed by the phrase in paragraph OB2. Paragraph 9 of the *Framework* (1989) also included a list of other potential users such as customers, governments and their agencies, and the public, which is similar to the list in paragraph OB10 of those who may be interested in financial reports but are not primary users.

BC1.11 Paragraph 10 of the *Framework* (1989) stated that “as investors are providers of risk capital to the entity, the provision of financial statements that meet their needs will also meet most of the needs of other users that financial statements can satisfy,” which might have been read to narrow the focus to investors only. However, paragraph 12 explicitly stated that the objective of financial statements is to provide information “that is useful to a wide range of users in making economic decisions.” Thus, the *Framework* (1989) focused on investors’ needs as representative of the needs of a wide range of users but did not explicitly identify a group of primary users.

BC1.12 FASB Concepts Statement 1 referred to “present and potential investors and creditors and other users in making rational investment, credit, and similar decisions” (paragraph 34). It also stated that “major groups of investors are equity securityholders and debt securityholders” and “major groups of creditors are suppliers of goods and services who extend credit, customers and employees with claims, lending institutions, individual lenders, and debt securityholders” (paragraph 35). One difference in emphasis from the *Framework* (1989), which emphasized providers of risk capital, is that Concepts Statement 1 referred to “both those who desire safety of investment and those who are willing to accept risk to obtain high rates of return” (paragraph 35). However, like the *Framework* (1989), Concepts Statement 1 stated that the terms investors and creditors “also may comprehend security analysts and advisors, brokers, lawyers, regulatory agencies, and others who advise or represent the interests of investors and creditors or who otherwise are interested in how investors and creditors are faring” (paragraph 35).

BC1.13 Paragraphs OB3, OB5, and OB10 differ from the *Framework* (1989) and Concepts Statement 1 for two reasons—to eliminate differences between the *Framework* (1989) and Concepts Statement 1 and to be more direct by focusing on users making decisions about providing resources (but not to exclude advisors). The reasons are discussed in paragraphs BC1.15–BC1.24.

Should There Be a Primary User Group?

BC1.14 The Discussion Paper and the Exposure Draft proposed identifying a group of primary users of financial reports. Some respondents to the Exposure Draft said that other users who have not provided and are not considering providing resources to the entity, use financial reports for a variety of reasons. The Board sympathized with their information needs but concluded that without a defined group of primary users, the Conceptual Framework would risk becoming unduly abstract or vague.

Why Are Existing and Potential Investors, Lenders, and Other Creditors Considered the Primary Users?

BC1.15 Some respondents to the Discussion Paper and the Exposure Draft suggested that the primary user group should be limited to existing shareholders or the controlling entity's majority shareholders. Others said that the primary users should be existing shareholders and creditors and that financial reports should focus on their needs.

BC1.16 The reasons why the Board concluded that the primary user group should be the existing and potential investors, lenders, and other creditors of a reporting entity are:

- a. Existing and potential investors, lenders, and other creditors have the most critical and immediate need for the information in financial reports and many cannot require the entity to provide the information to them directly.
- b. The Board's and the IASB's responsibilities require them to focus on the needs of participants in capital markets, which include not only existing investors, but also potential investors and existing and potential lenders and other creditors.
- c. Information that meets the needs of the specified primary users is likely to meet the needs of users both in jurisdictions with a corporate governance model defined in the context of shareholders and those with a corporate governance model defined in the context of all types of stakeholders.

BC1.17 Some respondents expressed the view that the specified primary user group was too broad and that it would result in too much information in the financial reports. However, *too much* is a subjective judgment. In developing financial reporting requirements that meet the objective of financial reporting, the Boards will rely on the qualitative characteristics of, and the cost constraint on, useful financial information to provide discipline to avoid providing too much information.

Should There Be a Hierarchy of Users?

BC1.18 Some respondents to the Exposure Draft who supported the composition of the primary user group also recommended that the Board should establish a hierarchy of primary users because investors, lenders, and other creditors have different information needs. However, the Board observed that individual users may have information needs and desires that are different from, and possibly conflict with, those of other users with the same type of interest in the reporting entity. General purpose financial reports are intended to provide common information to users and cannot accommodate every request for information. The Board will seek the information set that is intended to meet the needs of the maximum number of users in cost-beneficial ways.

Information Needs of Other Users Who Are Not within the Primary User Group

Management's Information Needs

BC1.19 Some constituents questioned the interaction between general purpose financial reporting and management's needs. The Board stated that some of the information directed to the primary users is likely to meet some of management's needs but not all of them. However, management has the ability to access additional financial information, and consequently, general purpose financial reporting need not be directed explicitly to management.

Regulators' Information Needs

BC1.20 Some constituents said that maintaining financial stability in capital markets (the stability of a country's or region's economy or financial systems) should be an objective of financial reporting. They stated that financial reporting should focus on the needs of regulators and fiscal policy decision makers who are responsible for maintaining financial stability.

BC1.21 Other constituents opposed establishing an objective to maintain financial stability. They said that financial statements should present the economic reality of the reporting entity with as little bias as possible but that such a presentation is not necessarily inconsistent with a financial stability objective. By presenting economic reality, financial statements could lead to more informed

decision making and, thereby, support financial stability even if that is not the primary aim.⁴

BC1.22 However, advocates of a financial stability objective had a different outcome in mind. They did not encourage the Board to require reporting entities to provide information for use by regulators and fiscal policy decision makers. Instead, they recommended that the Board consider the consequences of new financial reporting standards for the stability of the world's economies and financial systems and, at least at times, assign greater weight to that objective than to the information needs of investors, lenders, and other creditors.

BC1.23 The Board acknowledged that the interests of investors, lenders, and other creditors often overlap with those of regulators. However, expanding the objective of financial reporting to include maintaining financial stability could at times create conflicts between the objectives that the Board is not well equipped to resolve. For example, some may take the view that the best way to maintain financial stability is to require entities not to report or to delay reporting some changes in asset or liability values. That requirement almost certainly would result in depriving investors, lenders, and other creditors of information that they need. The only way to avoid conflicts would be to eliminate or deemphasize the existing objective of providing information to investors, lenders, and other creditors. The Board concluded that eliminating that objective would be inconsistent with its basic mission, which is to serve the information needs of participants in capital markets. The Board also noted that providing relevant and faithfully represented financial information can improve users' confidence in the information and, thus, contribute to promoting financial stability.

Usefulness for Making Decisions

BC1.24 Both the Board's and the IASB's previous frameworks focused on providing information that is useful in making economic decisions as the fundamental objective of financial reporting. Those frameworks also state that financial information that is useful in making economic decisions would also be helpful in assessing how management has fulfilled its stewardship responsibility.

BC1.25 The Discussion Paper that led to this chapter stated that the objective of financial reporting should focus on resource allocation decisions. Although most respondents to the Discussion Paper agreed that providing useful information for decision making was the appropriate objective, they said that

⁴One group expressing that view was the Financial Crisis Advisory Group (FCAG). The FCAG comprised approximately 20 senior leaders with broad experience in international financial markets and an interest in the transparency of financial reporting information. The FCAG was formed in 2009 to advise the Board and the IASB about the standard-setting implications of the financial crisis and potential changes in the global regulatory environment.

investors, lenders, and other creditors make other decisions that are aided by financial reporting information in addition to resource allocation decisions. For example, shareholders who vote on whether to retain directors or replace them, and on how members of management should be remunerated for their services, need information on which to base their decisions. Shareholders' decision-making process may include evaluating how management of the entity performed against management in competing entities in similar circumstances.

BC1.26 The Board agreed with these respondents and noted that, in most cases, information designed for resource allocation decisions also would be useful for assessing management's performance. Therefore, in the Exposure Draft leading to this chapter, the Board proposed that the objective of financial reporting is to provide financial information about the reporting entity that is useful to present and potential investors, lenders, and other creditors in making decisions in their capacity as capital providers. The Exposure Draft also described the role financial statements can have in supporting decisions related to the stewardship of an entity's resources.

BC1.27 The Exposure Draft discussed the *Objective of Financial Reporting* and *Decision Usefulness* in separate sections. The Board combined those two sections in this chapter because usefulness in making decisions is the objective of financial reporting. Consequently, both sections addressed the same points and provided more detail than was necessary. Combining those two sections resulted in eliminating the separate subsections on usefulness in assessing cash flow prospects and usefulness in assessing stewardship. The Board did not intend to imply that assessing prospects for future cash flow or assessing the quality of management's stewardship is more important than the other. Both are important for making decisions about providing resources to an entity, and information about stewardship also is important for resource providers who have the ability to vote on, or otherwise influence, management's actions.

BC1.28 The Board decided not to use the term *stewardship* in this chapter because there would be difficulties in translating it into other languages. Instead, the Board described what stewardship encapsulates. Accordingly, the objective of financial reporting acknowledges that users make resource allocation decisions as well as decisions as to whether management has made efficient and effective use of the resources provided.

The Objective of Financial Reporting for Different Types of Entities

BC1.29 The Board also considered whether the objective of general purpose financial reporting should differ for different types of entities. Possibilities include the following:

- a. Smaller entities versus larger entities

- b. Entities with listed (publicly traded) debt or equity financial instruments versus those without such instruments
- c. Closely held entities versus those with widely dispersed ownership.

BC1.30 External users of financial reporting have similar objectives, irrespective of the type of entities in which they invest. Therefore, the Board concluded that the objective of general purpose financial reports is the same for all entities. However, cost constraints and differences in activities among entities sometimes may lead the Board to permit or require differences in reporting for different types of entities.

Information about a Reporting Entity's Resources, Claims against That Entity, and Changes in Resources and Claims

The Significance of Information about Financial Performance

BC1.31 A longstanding assertion by many constituents is that a reporting entity's financial performance as represented by comprehensive income and its components is the most important information.⁵ Concepts Statement 1 (paragraph 43) stated:

The primary focus of financial reporting is information about an enterprise's performance provided by measures of comprehensive income and its components. Investors, creditors, and others who are concerned with assessing the prospects for enterprise net cash inflows are especially interested in that information.

In contrast, the *Framework* (1989) considered information on the reporting entity's financial position and financial performance of equal importance.

BC1.32 To be useful for decision making, financial reports must provide information about a reporting entity's economic resources and claims and the change during a period in economic resources and claims. A reporting entity cannot provide reasonably complete information about its financial performance (as represented by comprehensive income, profit or loss or other similar terms) without identifying and measuring its economic resources and the claims. Consequently, the Board concluded that to designate one type of information as the primary focus of financial reporting would be inappropriate.

⁵Concepts Statement 1 referred to *earnings and its components*. However, FASB Concepts Statement No. 6, *Elements of Financial Statements*, substituted the term *comprehensive income* for the term *earnings*. The latter term is reserved for a component of comprehensive income.

BC1.33 In discussing the financial position of an entity, the Exposure Draft referred to *economic resources and claims on them*. The chapter uses the phrase *economic resources of the reporting entity and the claims against the reporting entity* (see paragraph OB12). The reason for the change is that, in many cases, claims against an entity are not claims on specific resources. In addition, many claims will be satisfied using resources that will result from future net cash inflows. Thus, while all claims are claims against the entity, not all are claims against the entity's existing resources.

Financial Position and Solvency

BC1.34 Some constituents have suggested that the main purpose of the statement of financial position should be to provide information that helps assess the reporting entity's solvency. The question is not whether information provided in the financial reports should be helpful in assessing solvency; clearly, it should. Assessing solvency is of interest to investors, lenders, and other creditors, and the objective of general purpose financial reporting is to provide information that is useful to them for making decisions.

BC1.35 However, some have suggested that the statement of financial position should be directed towards the information needs of lenders, other creditors, and regulators, possibly to the detriment of investors and other users. To do so would be inconsistent with the objective of serving the common information needs of the primary user group. Therefore, the Board rejected the notion of directing the statement of financial position (or any other particular financial statement) towards the needs of a particular subset of users.

Incorporation of Concepts Statement 4

BC1.36 FASB Concepts Statement No. 4, *Objectives of Financial Reporting by Nonbusiness Organizations*, was released in 1980 and addressed the objectives of financial reporting to nonbusiness organizations. Since Concepts Statement 4's release, the Conceptual Framework and standard setting have evolved. As a result, there were inconsistencies and redundancies in Concepts Statement 4, making it outdated and in need of reevaluation. Concepts Statement 4 used the term *nonbusiness organizations*, which the FASB has since replaced with the term *not-for-profit entities*. The scope of Concepts Statement 4 included state and local governmental units. The Governmental Accounting Standards Board (GASB) was established as the authoritative accounting standard-setting body for U.S. state and local governments in 1984 and began releasing its own Concepts Statements in 1987.

BC1.37 The Board decided to reevaluate the outdated Concepts Statement 4 and supersede it in order to improve the framework and avoid inconsistencies with the release of Chapter 4, *Elements of Financial Statements*, and Chapter 7, *Presentation*, of FASB Concepts Statement No. 8, *Conceptual Framework for Financial Reporting*. The Board concluded that the integrated Conceptual

Framework should be relevant to all entities and it is not necessary to retain a separate objective of financial reporting for not-for-profit entities consistent with paragraphs BC1.29 and BC1.30 of this chapter. As a result, the Board decided to incorporate language from Concepts Statement 4 discussing the areas that may require any different reporting objectives with minor editing and to add them to this chapter.

APPENDIX B: AMENDMENTS TO THE CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING

B1. FASB Concepts Statement No. 8, *Conceptual Framework for Financial Reporting*, Chapter 8: *Notes to Financial Statements*, is amended as follows:

- a. Paragraph D9 is amended as follows:

As indicated in paragraph OB3 of Chapter 1, investors and creditors allocate resources on the basis of their expectations about returns from their investments, loans, or other forms of credit. The parties noted in paragraph OB2 (along with contributors to not-for-profit ~~organizations~~ entities) are referred to throughout this chapter as users of financial statements (or users).

- b. Paragraph D14 is amended as follows:

~~Paragraph 30 OB28 of FASB Concepts Statement No. 4, *Objectives of Financial Reporting by Nonbusiness Organizations* Chapter 1, *The Objective of General Purpose Financial Reporting*, of this Concepts Statement, states:~~

~~Present Existing and potential users of the information provided by financial reporting by a particular ~~nonbusiness organization~~ not-for-profit entity share a common interest in information about the services provided by the ~~nonbusiness organization~~ not-for-profit entity and its efficiency and effectiveness in providing those services as a basis for determining, and its ability to continue to provide those services.~~

The users noted above are different from current and potential lenders or other creditors because lenders and other creditors are generally most interested in assessing cash flows to themselves.

- c. Paragraph D26 is amended as follows:

The FASB establishes financial accounting and reporting standards for public and private companies and not-for-profit ~~organizations~~ entities that follow generally accepted accounting principles (GAAP). Subsets of these entities might be required to include general purpose financial

statements in SEC filings or other regulatory reports. The Board attempts to avoid requiring information in notes that entities are otherwise required to provide, for example, in SEC filings or other regulatory reports. However, there may be valid reasons why the Board at times considers requiring disclosure of information in notes when an entity provides similar or identical information in other forms of communication. For example, some entities whose users would find the information useful may not be subject to the requirement to provide it in any other form of communication. Also, the form of communication in which the information is provided may not be required every period or may not be as timely as the financial statements and notes. Finally, the information provided in that other form of communication may not be as complete or subject to the same degree of scrutiny and verification as information in financial statements.

- d. Paragraph D59 is amended as follows:

Many business entities provide significantly different products or services, otherwise engage in varied activities such as operating in different geographical areas with different effects on prospects for cash flows to users, or may manage different portions of the consolidated entity separately or differently. Similarly, some not-for-profit ~~organizations~~ entities provide more than one type of service or otherwise engage in more than one type of activity. Information such as a description of each of those portions (for example, segments) and some indication of assets, liabilities, and results of operations is a candidate for disclosure.