Mr. Hans Hoogervorst  
Chairman  
International Accounting Standards Board  
30 Cannon Street, London EC4M 6XH  
United Kingdom  

Dear Mr. Hoogervorst,


We support the decision to review the Conceptual Framework and believe that it will improve financial reporting.

Please find below our detailed comments for the questions raised in the DP:

Question 1 - Paragraphs 1.25–1.33 set out the proposed purpose and status of the Conceptual Framework. The IASB’s preliminary views are that:

(a) the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs; and
(b) in rare cases, in order to meet the overall objective of financial reporting, the IASB may decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. If this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard.

Do you agree with these preliminary views? Why or why not?

Generally, we agree to the preliminary views of the IASB. However, we believe that paragraph 1.29 deviates from the principles-based method on which IFRSs are based on. In our opinion, the use of the Conceptual Framework should be allowed equally for both preparers and the IASB and the IASB should not prescribe certain aspects only for the IASB’s use as it develops new or revised IFRSs. Paragraph 1.29 also contradicts IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors (paragraphs 10 and 11) that prescribes that in the absence of an IFRS that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy and in making that judgement, management shall refer to the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Framework. In our opinion, the primary purpose of the revised Conceptual Framework should be to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs, but also to assist entities to develop an accounting policy in the absence of an IFRS that specifically applies to the transaction, other event or condition.

Question 3

Whether uncertainty should play any role in the definitions of an asset and a liability, and in the recognition criteria for assets and liabilities, is discussed in paragraphs 2.17–2.36. The IASB’s preliminary views are that:

(a) the definitions of assets and liabilities should not retain the notion that an inflow or outflow is ‘expected’. An asset must be capable of producing economic benefits. A liability must be capable of resulting in a transfer of economic resources.

(b) the Conceptual Framework should not set a probability threshold for the rare cases in which it is uncertain whether an asset or a liability exists. If there could be significant uncertainty about whether a particular type of asset or liability exists, the IASB would
decide how to deal with that uncertainty when it develops or revises a Standard on that type of asset or liability.

(c) the recognition criteria should not retain the existing reference to probability.

Do you agree? Why or why not? If you do not agree, what do you suggest, and why?

1. We have some concerns regarding the preliminary views of the IASB on uncertainty, as described in paragraph 2.35. We believe that the distinction between existence uncertainty and outcome uncertainty is not clear enough and the IASB should enhance its explanations to that distinction and add examples.

2. Paragraph 2.20 states that "In some rare cases, it is unclear whether an entity has an asset or a liability…..The most obvious example of existence uncertainty is litigation…". We believe that the IASB should further explain in which rare cases it is unclear whether an entity has an asset or a liability. The example in paragraph 2.20 of litigation is not specific enough since litigations are common phenomena in the ordinary course of business of entities. We would appreciate if the IASB would explain the distinction between litigation and other uncertainties that do not prevent recognition of an asset or a liability.

Question 4

Elements for the statement(s) of profit or loss and OCI (income and expense), statement of cash flows (cash receipts and cash payments) and statement of changes in equity (contributions to equity, distributions of equity and transfers between classes of equity) are briefly discussed in paragraphs 2.37–2.52.

Do you have any comments on these items? Would it be helpful for the Conceptual Framework to identify them as elements of financial statements?

The IASB proposes to add to the existing Conceptual Framework, definitions to new elements - cash receipts and cash payments (statement of cash flows) and contributions to equity, distributions of equity and transfers between classes of equity (statement of changes in equity). We believe that the IASB should distinguish between different levels of elements. In our opinion, assets, liabilities, income and expense are primary elements, and all other elements are derived from them. Therefore, all other elements should be secondary elements.
Question 5
Constructive obligations are discussed in paragraphs 3.39–3.62. The discussion considers the possibility of narrowing the definition of a liability to include only obligations that are enforceable by legal or equivalent means. However, the IASB tentatively favours retaining the existing definition, which encompasses both legal and constructive obligations—and adding more guidance to help distinguish constructive obligations from economic compulsion. The guidance would clarify the matters listed in paragraph 3.50. Do you agree with this preliminary view? Why or why not?

1. We agree to the IASB's proposal to include in the definition of a liability both legal and constructive obligations. We notice that the definition of constructive obligation refers to "other parties". We would appreciate if the IASB would clearly state whether other parties include shareholders and whether a distinction should be made between non-controlling shareholders and a controlling shareholder.

2. Paragraph 3.5(b) states that economic resources may take the form of "rights arising from a constructive obligation of another party". We believe the IASB should clearly express its view whether that economic resource is controlled by the other party and whether the other party can direct its use and therefore can recognise it as an asset. In our opinion, the IASB should not allow situations where one party recognises a liability and the other party does not recognise an asset. In addition, it is inadvisable that a situation where two parties recognise the same asset, will be allowed.

Question 6
The meaning of 'present' in the definition of a liability is discussed in paragraphs 3.63–3.97. A present obligation arises from past events. An obligation can be viewed as having arisen from past events if the amount of the liability will be determined by reference to benefits received, or activities conducted, by the entity before the end of the reporting period. However, it is unclear whether such past events are sufficient to create a present obligation if any requirement to transfer an economic resource remains conditional on the entity’s future actions. Three different views on which the IASB could develop guidance for the Conceptual Framework are put forward:
(a) View 1: a present obligation must have arisen from past events and be strictly unconditional. An entity does not have a present obligation if it could, at least in theory, avoid the transfer through its future actions.

(b) View 2: a present obligation must have arisen from past events and be practically unconditional. An obligation is practically unconditional if the entity does not have the practical ability to avoid the transfer through its future actions.

(c) View 3: a present obligation must have arisen from past events, but may be conditional on the entity’s future actions.

The IASB has tentatively rejected View 1. However, it has not reached a preliminary view in favour of View 2 or View 3.

Which of these views (or any other view on when a present obligation comes into existence) do you support? Please give reasons.

We support View 2. Although this view requires the exercise of judgment, we do not believe that it should prevent application of that view, since judgment is required in many other Standards.

Question 7
Do you have comments on any of the other guidance proposed in this section to support the asset and liability definitions?

We believe that there should be one definition of control to all cases, ie control of an individual asset, control of an investee in its entirety etc.

Question 8
Paragraphs 4.1–4.27 discuss recognition criteria. In the IASB’s preliminary view, an entity should recognise all its assets and liabilities, unless the IASB decides when developing or revising a particular Standard that an entity need not, or should not, recognise an asset or a liability because:

(a) recognising the asset (or the liability) would provide users of financial statements with information that is not relevant, or is not sufficiently relevant to justify the cost; or
(b) no measure of the asset (or the liability) would result in a faithful representation of both the asset (or the liability) and the changes in the asset (or the liability), even if all necessary descriptions and explanations are disclosed.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We believe that paragraphs 4.1-4.27 lack clarity. It is unclear whether an entity should recognise all items that meet the definitions of assets and liabilities or an entity should identify all items that meet the definitions of assets and liabilities and recognise only those that are relevant and result in faithful representation.

Paragraph 4.25 states that "In the IASB's preliminary view, the Conceptual Framework should state that the IASB might decide in developing or revising particular standards that an entity need not, or should not, recognise an asset or a liability…". We understand the need to allow the IASB to prohibit recognition of certain assets and liabilities. However, we would appreciate if the IASB could determine the criteria for allowing entities to choose whether or not to recognise an asset or a liability.

**Question 9**

In the IASB’s preliminary view, as set out in paragraphs 4.28–4.51, an entity should derecognise an asset or a liability when it no longer meets the recognition criteria. (This is the control approach described in paragraph 4.36(a)). However, if the entity retains a component of an asset or a liability, the IASB should determine when developing or revising particular Standards how the entity would best portray the changes that resulted from the transaction. Possible approaches include:

(a) enhanced disclosure;

(b) presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations, to highlight the greater concentration of risk; or

(c) continuing to recognise the original asset or liability and treating the proceeds received or paid for the transfer as a loan received or granted.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?
We support the IASB’s approach to derecognise assets when the recognition criteria are no longer met. In our opinion, the IASB should also consider the current approach in IAS 39 which is based on risks and rewards, that is more conservative than the control approach, which is accepted under US GAAP.

From the three possible approaches described above for cases where the entity retains a component of an asset or a liability, we support approach (b).

**Question 10**

The definition of equity, the measurement and presentation of different classes of equity, and how to distinguish liabilities from equity instruments are discussed in paragraphs 5.1–5.59. In the IASB’s preliminary view:

(a) the Conceptual Framework should retain the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities.

(b) the Conceptual Framework should state that the IASB should use the definition of a liability to distinguish liabilities from equity instruments. Two consequences of this are:

(i) obligations to issue equity instruments are not liabilities; and

(ii) obligations that will arise only on liquidation of the reporting entity are not liabilities (see paragraph 3.89(a)).

(c) an entity should:

(i) at the end of each reporting period update the measure of each class of equity claim. The IASB would determine when developing or revising particular Standards whether that measure would be a direct measure, or an allocation of total equity.

(ii) recognise updates to those measures in the statement of changes in equity as a transfer of wealth between classes of equity claim.

(d) if an entity has issued no equity instruments, it may be appropriate to treat the most subordinated class of instruments as if it were an equity claim, with suitable disclosure. Identifying whether to use such an approach, and if so, when, would still be a decision for the IASB to take in developing or revising particular Standards.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?
(a) We agree that the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities, should be retained.

(b) We agree that the definition of a liability should be used to distinguish liabilities from equity instruments and that should be stated clearly in the *Conceptual Framework*.

(c) We agree to the requirements for measuring equity presented in the Discussion Paper. However, we believe that the IASB should develop a Standard that would prescribe measurement requirements for equity instruments and would also refer to issuance of equity instruments, which were not issued at market conditions, to existing shareholders and to transactions with controlling shareholders.

(d) We believe that a *Conceptual Framework* should not address this issue. In our opinion, if the IASB would identify a situation where such an approach should be used, the IASB should use this approach in developing or revising particular Standards.

**Question 11**

*How the objective of financial reporting and the qualitative characteristics of useful financial information affect measurement is discussed in paragraphs 6.6–6.35. The IASB’s preliminary views are that:*  

(a) **the objective of measurement is to contribute to the faithful representation of relevant information about:**  

   (i) the resources of the entity, claims against the entity and changes in resources and claims; and  

   (ii) how efficiently and effectively the entity’s management and governing board have discharged their responsibilities to use the entity’s resources.

(b) a single measurement basis for all assets and liabilities may not provide the most relevant information for users of financial statements;

(c) when selecting the measurement to use for a particular item, the IASB should consider what information that measurement will produce in both the statement of financial position and the statement(s) of profit or loss and OCI;

(d) the relevance of a particular measurement will depend on how investors, creditors and other lenders are likely to assess how an asset or a liability of that type will contribute to future cash flows. Consequently, the selection of a measurement:  

   (i) for a particular asset should depend on how that asset contributes to future cash flows; and
(ii) for a particular liability should depend on how the entity will settle or fulfil that liability.

(e) the number of different measurements used should be the smallest number necessary to provide relevant information. Unnecessary measurement changes should be avoided and necessary measurement changes should be explained; and

(f) the benefits of a particular measurement to users of financial statements need to be sufficient to justify the cost.

Do you agree with these preliminary views? Why or why not? If you disagree, what alternative approach to deciding how to measure an asset or a liability would you support?

We agree to the preliminary views regarding measurement presented in the Discussion Paper.

Question 12

The IASB’s preliminary views set out in Question 11 have implications for the subsequent measurement of assets, as discussed in paragraphs 6.73–6.96. The IASB’s preliminary views are that:

(a) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, cost-based measurements normally provide information that is more relevant and understandable than current market prices.

(b) if assets contribute directly to future cash flows by being sold, a current exit price is likely to be relevant.

(c) if financial assets have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information.

(d) if an entity charges for the use of assets, the relevance of a particular measure of those assets will depend on the significance of the individual asset to the entity.

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.
We agree to the preliminary views regarding the measurement of assets presented in the Discussion Paper. However, in our opinion, the Conceptual Framework is by its nature a more permanent publication than a Standard. Therefore, we believe that the preliminary views presented are too detailed for a Conceptual Framework and that the Conceptual Framework should state that different measurement bases are appropriate for the measurement of assets that contribute directly and indirectly to future cash flows of an entity. The other, more detailed, measurement requirements should be included in a Standard and not in the Conceptual Framework. This view refers also to Questions 13 and 14.

Question 13
The implications of the IASB’s preliminary views for the subsequent measurement of liabilities are discussed in paragraphs 6.97–6.109. The IASB’s preliminary views are that:
(a) cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms.
(b) a cost-based measurement will normally provide the most relevant information about:
   (i) liabilities that will be settled according to their terms; and
   (ii) contractual obligations for services (performance obligations).
(c) current market prices are likely to provide the most relevant information about liabilities that will be transferred.

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

See our view in our comment to question 12 above.

Question 14
Paragraph 6.19 states the IASB’s preliminary view that for some financial assets and financial liabilities (for example, derivatives), basing measurement on the way in which the asset contributes to future cash flows, or the way in which the liability is settled or fulfilled, may not provide information that is useful when assessing prospects for future cash flows. For example, cost-based information about financial assets that are held for collection or financial liabilities that are settled according to their terms may not provide information that is useful when assessing prospects for future cash flows:
(a) if the ultimate cash flows are not closely linked to the original cost;
(b) if, because of significant variability in contractual cash flows, cost-based measurement
techniques may not work because they would be unable to simply allocate interest
payments over the life of such financial assets or financial liabilities; or
(c) if changes in market factors have a disproportionate effect on the value of the asset or
the liability (ie the asset or the liability is highly leveraged).

Do you agree with this preliminary view? Why or why not?

See our view in our comment to question 12 above.

Question 17
Paragraph 7.45 describes the IASB’s preliminary view that the concept of materiality is
clearly described in the existing Conceptual Framework. Consequently, the IASB does not
propose to amend, or add to, the guidance in the Conceptual Framework on materiality.
However, the IASB is considering developing additional guidance or education material on
materiality outside of the Conceptual Framework project.
Do you agree with this approach? Why or why not?

We agree with this approach. We support the IASB’s intention to develop additional guidance on
materiality. In our opinion, the additional guidance should also refer to different terms used
through the IFRSs to describe materiality (significant, material, etc) and the relation between
those different terms.

Question 19
The IASB’s preliminary view that the Conceptual Framework should require a total or
subtotal for profit or loss is discussed in paragraphs 8.19–8.22. Do you agree? Why or why
not? If you do not agree do you think that the IASB should still be able to require a total or
subtotal profit or loss when developing or amending Standards?

We strongly support the arguments set out in paragraph 8.21 and therefore we believe that the
IASB should not retain profit or loss as a total or subtotal.
If the IASB wish to proceed with the requirement for a total or subtotal for profit or loss, we believe that the IASB must set out in the *Conceptual Framework* clear criteria for the distinction between items of other comprehensive income and items of profit or loss and not allow the IASB to reach a conclusion in each particular Standard. We suggest that the distinction between items of other comprehensive income and items of profit or loss should be made according to the principle of realisation, ie if income was not realised (for example, income derived from measuring investment property at fair value) it should not be included in profit or loss.

**Question 20**

The IASB’s preliminary view that the *Conceptual Framework* should permit or require at least some items of income and expense previously recognised in OCI to be recognized subsequently in profit or loss, ie recycled, is discussed in paragraphs 8.23–8.26. Do you agree? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss? Why or why not? If you do not agree, how would you address cash flow hedge accounting?

Since we believe that other comprehensive items are part of the performance of the entity and part of the comprehensive income, we do not support recycling since its meaning is presentation of the same item twice in comprehensive income.

**Question 21**

In this Discussion Paper, two approaches are explored that describe which items could be included in OCI: a narrow approach (Approach 2A described in paragraphs 8.40–8.78) and a broad approach (Approach 2B described in paragraphs 8.79–8.94). Which of these approaches do you support, and why? If you support a different approach, please describe that approach and explain why you believe it is preferable to the approaches described in this Discussion Paper.

We support the narrow approach for items to be included in other comprehensive income and we do not support recycling.
Question 23

Business model

The business model concept is discussed in paragraphs 9.23–9.34. This Discussion Paper does not define the business model concept. However, the IASB’s preliminary view is that financial statements can be made more relevant if the IASB considers, when developing or revising particular Standards, how an entity conducts its business activities.

Do you think that the IASB should use the business model concept when it develops or revises particular Standards? Why or why not? If you agree, in which areas do you think that the business model concept would be helpful?

Should the IASB define ‘business model’? Why or why not? If you think that ‘business model’ should be defined, how would you define it?

Yes, we believe that the IASB should use the business model concept when it develops or revises particular Standards. In our opinion, it is important to distinguish between the business model of an entity (its long term strategies that are evident from its operations and actions) and its management's intentions (which could be reversed by a board of directors' decision) and to avoid using management's intentions when developing or revising particular Standards. Therefore, we believe that the IASB should make an effort to define the 'business model'.

Question 24

Unit of account

The unit of account is discussed in paragraphs 9.35–9.41. The IASB’s preliminary view is that the unit of account will normally be decided when the IASB develops or revises particular Standards and that, in selecting a unit of account, the IASB should consider the qualitative characteristics of useful financial information. Do you agree? Why or why not?

We agree. We believe that the IASB should select the unit of account when it develops or revises particular Standards while taking into account the qualitative characteristics of useful financial information. However, the existence of many units of account (PPE group, segment, discontinued operation, cash generating unit, disposal group etc) increases the complexity of the application of IFRSs. Therefore, in our opinion, the IASB should also seek consistency in determining the unit of account in order to mitigate that complexity and to avoid confusion between different units of account.
Question 26

Capital maintenance

Capital maintenance is discussed in paragraphs 9.45–9.54. The IASB plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised Conceptual Framework largely unchanged until such time as a new or revised Standard on accounting for high inflation indicates a need for change.

Do you agree? Why or why not? Please explain your reasons.

We agree that the IASB should currently include the existing descriptions and the discussion of capital maintenance concepts. See also our other comment 3.
Other comments

1. In our opinion, the Conceptual Framework lacks general principles for the recognition and measurement of transactions between an entity and its equity holders, not in their capacity as equity holders. We believe that one of the general principles should be that these transactions should be measured as all other transactions regardless of the fact they were made with equity holders.

2. The Conceptual Framework does not deal with the recognition of equity instruments. Therefore, currently the recognition of equity instruments depends on meeting the recognition criteria for the corresponding asset. In our opinion, the Conceptual Framework should refer to the recognition criteria of equity instruments and especially to the timing of the recognition of an equity instrument issued but not paid.

3. We believe that while reconsidering the capital maintenance concepts the IASB should make a clear distinction between other comprehensive income and capital maintenance. In our opinion, some items that are currently considered other comprehensive income items are actually part of capital maintenance. For example, revaluation of property, plant and equipment and the translation differences that arise when an entity translates its financial statements from its reporting currency to its presentation currency. These items are not other comprehensive income since they are not related to the entity's performance and therefore should be considered as part of capital maintenance.

We appreciate the opportunity to provide our comments.

Sincerely,

Dov Sapir, CPA, Chairman
Israel Accounting Standards Board