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Proposed Statement of Financial Accounting Concepts No. 8, Conceptual Framework for Financial Reporting, Chapter 4: *Elements of Financial Statements* (File Reference No. 2020-500)

Dear Ms. Salo:

We appreciate the opportunity to comment on the Proposed Statement of Financial Accounting Concepts No. 8, Conceptual Framework for Financial Reporting, Chapter 4: *Elements of Financial Statements*, issued by the Financial Accounting Standards Board (FASB or Board).

We support the Board's efforts to provide a framework that includes concepts for the Board's use in developing financial accounting and reporting guidance and believe that a properly developed conceptual framework could be helpful. In that context, we have the following suggestions for the Board as it finalizes this chapter and continues its efforts on other chapters of the conceptual framework.

Highlight the hierarchy status of the conceptual framework included in the Codification

We support the Board's efforts to acknowledge in the preface of the proposed chapter that Concepts Statements are not authoritative. We recommend that the FASB continue to highlight the hierarchy contained in Accounting Standards Codification (ASC or Codification) 105-10-05-2 in future updates to the conceptual framework and in other communications, including educational material. Some entities may first consider the Concepts Statements when the accounting and reporting for a transaction or event is not specified in a US GAAP topic without first evaluating whether to analogize to other US GAAP guidance for similar transactions or events. That is, the FASB should consistently emphasize that when guidance for a transaction or event is not specified in an authoritative US GAAP topic, an entity first must consider accounting principles for similar transactions or events in other authoritative US GAAP topics before considering non-authoritative guidance (e.g., Concepts Statements, IFRS).

Consideration of the IASB's conceptual framework

We acknowledge that the FASB's project on revising the conceptual framework began as a joint project with the International Accounting Standards Board (IASB) to revise and converge their conceptual frameworks, which resulted in FASB Concepts Statement No. 8, Conceptual Framework for

Financial Reporting, Chapter 1, *The Objective of General Purpose Financial Reporting*, and Chapter 3, *Qualitative Characteristics of Useful Financial Information*.

With this acknowledgment as context, we suggest that the FASB reflect on its project plan and next steps. The reason we suggest this is the IASB has a fully developed conceptual framework that could serve as a starting point for the FASB's conceptual framework and that would provide benefits for the FASB.

First, this approach could reduce the time and resources needed to complete the FASB's conceptual framework project. Second, a substantially converged framework would increase the chances that the IASB and FASB would reach similar outcomes during the standard-setting process. We acknowledge that a fully converged conceptual framework may not be possible due to differences in regulatory environments (e.g., the definition of "material" in the FASB's conceptual framework is the same as the definition used by the Securities and Exchange Commission and the Public Company Accounting Oversight Board and is not converged with the definition in the IASB's conceptual framework).

Interaction of the proposed chapter and presentation concepts

The proposed chapter includes definitions for key elements in the financial statements but does not provide a framework for how transactions that meet those definitions should be presented in the financial statements. We understand that the FASB intends to address presentation concepts in a separate chapter.

With this in mind, we agree that distinguishing revenues from gains and expenses from losses is a matter for presentation concepts, not element concepts. For example, as noted in paragraph BC4 of Accounting Standards Update No. 2017-05, *Other Income — Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*, because there is little economic difference between the sale of real estate to a customer and the sale of real estate to a noncustomer, the recognition and measurement guidance should be the same, and the only difference should relate to the presentation of the profit or loss in the statement of comprehensive income. Therefore, we believe the Board should apply presentation concepts to decide how elements of comprehensive income should be presented in the statement of comprehensive income.

Further, we recommend that the Board emphasize in the finalized chapter that any changes to the definitions of revenues, gains, expenses and losses should not affect an entity's previous conclusions on the presentation of those types of transactions.

Basis of recognition for liabilities

We believe that the proposed chapter helps clarify for standard-setting purposes that a constructive obligation may meet the definition of a liability, even though it is not legally enforceable. We agree with the Board, as it describes in paragraph E54 of the proposed chapter, that overly narrow interpretations of what is an obligation could exclude significant actual obligations of an entity, while too-broad interpretations effectively nullify the definition of a liability.

With respect to this matter, we recommend that the Board clarify how it intends to evaluate the difference between a constructive obligation and a legal obligation when it is considering standard-setting alternatives. For example, recent accounting standards (e.g., ASC 606, *Revenue from Contracts with Customers*; ASC 842, *Leases*) require a legally enforceable contract (instead of a constructive obligation) to exist before related assets and liabilities are recognized. We believe that the Board should apply the definition of a liability consistently across its standard-setting projects, where possible. However, when the Board takes a different approach in a particular standard-setting project, it should explain its reasons in the Basis for Conclusions.

References to the Concepts Statements in the ASC

We note that the Board currently has a project on its agenda to remove references to the Concepts Statements from the ASC. We acknowledge that the FASB states in this proposal that it expects that most assets and liabilities that met the definition of an asset or liability in FASB Concepts Statement No. 6, *Elements of Financial Statements*, will continue to qualify as assets or liabilities under the definitions in the proposed chapter. We recommend that the Board complete its project on removing references to the Concepts Statements from the ASC before issuing a final chapter, or at the same time a final chapter is issued, because our experience indicates that changes in the language used in the ASC may result in unintended changes to accounting conclusions.

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We would be pleased to discuss our comments with the Board or its staff at your convenience.

Very truly yours,

Ernst + Young LLP