
Przemysław KABALSKI *

Abstract

This paper aims to present the first section of the proposed (by International Accounting Standards Board and Financial Accounting Standards Board) new conceptual framework dealing with the objectives of financial reporting. The author presents and explains the proposed solutions. He places them in a broader context, which facilitates their understanding, critical analysis and forming of an opinion. This paper seeks to contribute to the discussion on the new conceptual framework for financial reporting.

Keywords: International Financial Reporting Standards, financial reporting, users of financial reporting, conceptual framework, capital providers, entity theory, proprietary theory

JEL Classification Codes: M40, M41
Introduction

The International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) are conducting a joint conceptual framework project, which is a major undertaking aimed at developing an improved common conceptual framework for financial reporting. In July 2006, the IASB and the FASB published a discussion paper entitled *Preliminary Views on an Improved Conceptual Framework for Financial Reporting: Objective of Financial Reporting and Qualitative Characteristics of Decision-Useful Financial Reporting Information*. This document was the first of a series of publications prepared jointly by the two boards as part of a joint conceptual framework project (subsequent sections of the project address or will address: definition of financial statement elements, their recognition and de-recognition, initial and subsequent measurement of the elements of financial statements, and the concept of a reporting entity). 179 comments were received in response to the discussion paper. On 29th May 2008 the IASB and the FASB issued an exposure draft entitled *Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information*. The comment period ended on 29th September 2008.

This paper aims to present the first section of the proposed new conceptual framework dealing with the objectives of financial reporting. The author presents and explains the proposed solutions without any attempt at their evaluation either from the theoretical or practical viewpoint. Instead, they are placed in a broader context, which, in the author’s opinion, facilitates their understanding, critical analysis and forming of an opinion. The author also formulates questions and voices concerns which, doubtless, have been and will be raised regarding the proposed solutions, without however providing any answers or venturing any opinions. This paper seeks to contribute to the discussion on the new conceptual framework for financial reporting and, as such, does not attempt to provide an exhaustive description of all the solutions adopted in the project or identify all potential problem areas.

Issues addressed in the preface to the draft, such as reasons for undertaking work to develop an improved converged conceptual framework, the agreed method of

---

1 Naturally, we are not the first (in Poland) to present changes to the conceptual framework for financial reporting. The new framework was discussed, inter alia, in a presentation by A. Jaruga (2007).

2 The term “critical” as used in this paper means based on careful analysis rather than implying a negative perspective.

3 There are two reasons for adopting this approach. First, such was the author’s original conception; and second (and more importantly), the author is aware of the limitations of his knowledge and experience, which dictate caution in formulating definitive answers to fundamental questions in such complex matters.
preparing and introducing amendments, and discussion on the status of the new framework, however interesting, do not come within the scope of this paper.

2. The objective of financial reporting in the proposed new conceptual framework

It is expressly stated in the summary and preface to the new framework that the conceptual framework constitutes an internally consistent system of concepts directly relating to the objective of financial reporting. The financial reporting objective exists to provide a foundation for the framework – all the statements contained in the framework have to relate to it, i.e. have to follow from it logically and support its fulfilment. The objective of financial reporting has also been defined in the preface to the existing IASB Framework, but with less emphasis on its being the foundation of the conceptual basis of financial reporting. It is important to note that inclusion of the objective of accounting in accounting theory (the conceptual framework does constitute accounting theory) is a basic feature characteristic of normative accounting theories (see Szychta, 1996, pp. 77 and 218-224). In this approach to accounting theory, accounting standards are instrumentally subordinated to the objective (or objectives) of accounting. It should be emphasized that the existing FASB and IASB frameworks have always had such a character, but it was not explicitly articulated.

Recognition of the normative character of accounting theory in the new conceptual framework is crucial for a proper understanding (and critical appraisal) of the general and specific provisions of IAS/IFRS. In questioning the validity of specific solutions (approaches, models etc.) prescribed in international accounting standards (e.g. fair value valuation or ex ante reporting), we are de facto questioning the validity of the objective of accounting as defined in the conceptual framework. Criticizing approaches, solutions or models alone seems irrelevant, as they only constitute means (unless the adopted means are insufficiently, or not at all, conformable to the objective).

In the new conceptual framework, the objective of general purpose financial reporting is to provide information that is useful for present and potential equity investors, lenders and other creditors in making decisions in their capacity as capital providers. Thus, primary users of financial reporting information are capital providers. At the same time, information that is useful to capital providers can be useful to other users (those who do not have vested interests in the entity). It should be added that the objective of financial reporting as formulated in the draft framework (and, hence, the whole of the framework) is applicable to business entities in the private sector.

Thus formulated by the IASB and the FASB, the objective of financial reporting is the consequence of their mandate to support efficient functioning of economies
and efficient allocation of resources in capital markets through developing high-quality standards of financial reporting.

Under the proposed conceptual framework, general purpose financial reporting is oriented to the needs of a broad range of users rather than to the needs of one specific group of users. Decision usefulness, as the principal objective, reflects the intention to meet the needs of those users who are not able to obtain information about the entity that is sufficient for their decision making, and therefore have to rely on information provided in financial statements. Although it has not been explicitly articulated in the documents issued by the IASB and the FASB, the purpose of the joint project is to eliminate the problem of so-called information asymmetry. Managers of companies have better access to inside information than do external providers of capital. Unequal access to information is one of the causes of market inefficiency, which in extreme cases can result in its collapse.

In the case of large entities, the problem of information asymmetry is worsened by the fact that it is inherent in the relationship described by the so-called agency theory. This is a relationship between two actors: the agent and the principal. The agent is hired by the principal to act on his behalf for a specified remuneration. He is not, however, an inert, programmable machine, but has a utility function which determines his actions. The agent’s decisions are not always (though from the principal’s point of view they should be) consistent with the principal’s interest. In the case of a company, the management is the agent, and the owner is the principal. Information asymmetry would further strengthen the agent’s tendency towards suboptimal action – seeking maximization of his own short-term benefits at the expense of the owner’s long-term interests. Also, it would make it difficult for the principal to evaluate the agent’s performance (i.e. to what extent his decisions were guided by the principal’s interest). In other words, the management could try to convince the owners that things were fine, that nothing more could be done etc., and the owners, viewing the business from the outside, would not be able to verify such claims. Accounting information can thus contribute to restoring balance in market relations (at least to some degree).

With regard to eliminating or reducing information asymmetry at the business entity level, it is necessary to provide outside stakeholders with information about the entity’s performance. However, it is not enough to provide “some kind of information”. As the management, on account of their being inside the company, has practically unlimited access to all information about the results, directions and prospects of its activity, information asymmetry will only be eliminated when external users can see the entity through the management’s eyes. Therefore,

---
4 A paper famous among economists illustrates this phenomenon with the used car market as an example (see Hendriksen, van Breda, 2002, p.224).
5 The American Accounting Association stated in one of its reports issued in the 1990s that financial information users are oriented to the future, whereas financial reporting in the present form is focused
information communicated to external users should be similar in character (scope, timing, forms) to the information generated by management accounting. It follows logically, then, that there should be convergence between financial accounting and management accounting (which has often been postulated by I. Sobanska in her recent publications [e.g. 2007]).

It should also be noted that the objective as defined in the proposed new conceptual framework relates to financial reporting, which comprises financial statements (its core), but is not limited to them. Such a broad approach to the mode of communicating financial information offers more scope for fulfilment of the IASB and FASB joint project goals. In a document attached to the framework, entitled Basis for Conclusions, which summarises the discussions and arguments leading to the final decision, it was stated among other things that future discussions about the boundaries of financial reporting should address such issues as inclusion of ex ante information and forecasts in financial reporting, and the way in which financial statements are prepared and presented. It affords new scope for discussion about the character of financial reporting. On the one hand, it may raise concerns, especially among conservatives, about what the standard setters might be thinking of next. On the other hand, taking a narrow view of financial accounting would seem to be highly inappropriate in today’s world, where “nothing is as it was yesterday”. This is especially true if accounting still aspires to be a socially useful discipline.

3. Users of financial reporting information in the new conceptual framework

According to the new framework, general purpose financial reporting information is intended to serve the needs of all capital providers, i.e. all stakeholders, not just one particular group (e.g. shareholders). It is pointed out that, from this approach, financial reporting is viewed from the entity perspective. Under the entity theory, a business or other organisation has an identity distinct from its owners, so it has a separate accountability of its own (see Hendricksen, van Breda, 2002, p.761). Economic resources brought into the business entity are the entity’s resources, not the property of those who brought them in. Capital providers can only have claims to the entity’s economic resources. The character of the claims differs between on the past. Although historical information is an indication of future performance, users need more future-oriented information. Many users want to see the company through its managers’ eyes in order to understand their vision and expectations about the company’s future.

6 Quite obviously, external users, such as owners for example, will not need information that is necessary in the daily management of a company, but strategic information will be as important to them as to managers.

7 Convergence of these two areas of accounting means here the use of management accounting methods in the process of preparing information for financial reporting purposes.
different types of capital provider (e.g. the legal standing of shareholders is different from that of creditors), but these differences do not affect the way in which the business entity is viewed. Under the entity theory, financial reporting communicates information about financial resources and about capital providers’ claims to those resources (with no special reference to any particular class of capital provider). Figure 1 presents the entity theory using the terminology adopted in the new conceptual framework project.

![Figure 1: Financial reporting under the entity theory in the new conceptual framework project](source: author's elaboration)

In the Basis for Conclusions appended to the published draft, it was noted, for comparison’s sake, that a different view is taken by the proprietary theory, in which the financial aspects of a business are not accounted for separately from its owner(s). Assets brought in by the owners are still their property. They are not considered as the entity’s assets because it does not have a separate identity of its own. Consequently, lenders and other creditors supply economic resources to the business entity’s proprietor, not to the entity itself. Therefore the claims of lenders and other creditors reduce the owners’ equity in the resources associated with the reporting entity. The accounting equation in the proprietary theory is:

\[
\text{Assets (of the owners)} - \text{liabilities (of the owners)} = \text{Owners' equity (in the entity)}
\]

Under the proprietary theory, financial reporting reflects the assets of the owners, the liabilities of the owners and the net residual owners’ equity in the reporting entity. In this approach, the owner of a business entity is the focus of interest.

The bodies developing the new conceptual framework have decided that the proprietary theory does not reflect the character of the majority of today’s business enterprises constituting reporting entities under IAS/IFRS. They are mostly

---

8 The entity and proprietary theories are two of the three ontological orientations of accounting. Ontology is the philosophical study of the nature of being, existence or reality in general, as well as of the basic categories of being and their relations. With reference to accounting, the starting point of the ontological orientation is defining the object on which the accounting system is circumscribed (see Nowak, 1998, pp. 60-61), i.e. finding answers to the question: what is the object of financial reporting and what is its identity? The third of the ontological conceptions of accounting is the funds theory.
large companies with substance of their own and many different capital providers with limited liability, and they are managed by employed professionals rather than by the owners.

Adoption of one of these two perspectives (entity or proprietary) determines which of the groups of financial information users are regarded as its primary users. In the proprietary theory, attention is focused on shareholders, while in the entity theory all providers of capital (both equity capital and borrowed capital) are considered as being primary users of reporting information. It should be noted that it remains an open question whether adoption of the entity perspective will have any implications for other conceptual aspects or for the particular reporting standards. Some members of the IASB and the FASB are of the opinion that a logical consequence of adopting the entity perspective will be the elimination of alternative solutions regarding elements of financial statements and definition of financial reporting boundaries. Others argue that the entity theory is only useful for proper definition of the main users of financial reporting and does not affect other areas of the new conceptual framework. The IASB and the FASB have decided, temporarily, to suspend deliberation of the possible impact of adoption of the entity theory on the subsequent phases of the project, and to postpone decisions in this respect until discussions have begun during these phases.

An interesting issue to be resolved is whether the entity theory leads to the adoption of other measurement bases than under the proprietary theory. Opinions of accounting theorists vary widely on this issue. Some argue that adoption of a particular theory implies adoption of a specific measurement basis – that the current cost basis of measurement is appropriate for the proprietary theory, while historical cost accounting is more consistent with the entity theory. Others believe that adoption of one of these perspectives (entity or proprietary) does not necessarily have implications for choosing the measurement basis (Hendricksen, van Breda, 2002, p.762).

With regard to the definition of financial reporting users in the conceptual framework project, they are defined as those people who provide capital to an entity in exchange for claims to its assets. On account of those claims they are in the most immediate and critical need of financial information about business entity resources. Capital providers are:

- equity investors,
- lenders,
- other creditors.

All these groups have common information needs. The first two groups need no explaining. The third group comprises other creditors, such as employees whose remuneration payment is deferred (sometimes for many years), suppliers providing goods on credit, or buyers making prepayments for goods or services to be.

EJBE 2009, 2 (4)                                                                                          Page | 101
supplied in the future. If employees, suppliers, buyers and other financial information users provide capital in the form of credit, they can be regarded as capital providers. To sum up, it should be emphasized that, in the new conceptual framework, the main group of financial reporting information users are present and potential equity investors, lenders and other creditors, regardless of the way in which they have obtained or will acquire their interests (claims to the entity’s assets). The main user groups are referred to in the new framework project as capital providers or claimants. In the framework, managers are not considered to be primary addressees of financial reporting. They do need financial information about the entity, but they do not act as capital providers, and neither do suppliers, buyers, employees, government and its agencies, the public and other user groups that are not acting in the capacity of capital providers. Nevertheless, information that meets the needs of capital providers may also be useful for the groups listed above.

The existing IASB framework provides that the users of financial statements include not only investors, lenders and other creditors but also employees, suppliers, customers, governments and their agencies and the public. In a way, investors are given priority as “providers of risk capital to the entity”. It is stated in the framework that the provision of financial statements that meet their needs will also meet most of the needs of other users. Thus, the project introduces an essential change. First, capital providers are named as primary users of financial reporting information. Their need for information about the entity is direct and immediate. Other groups that have a stake in the entity but are not capital providers can also use reporting information. What is more, the information may be equally useful for them as for capital providers. Second, none of the groups of capital providers is given priority, not even verbally – this also refers to those who invest equity capital (equal treatment of equity investors and lenders is consistent with the view that entity theory underlies financial reporting in the new conceptual framework).

The approach adopted in the draft is certain to raise a number of questions. The main object of criticism may be the position of owners (as users of reporting information), which is in no way privileged – this is particularly controversial in the context of today’s management orientation towards maximizing the value of the business to the owners. Such an objection may be raised by the proponents of the privileged position of shareholders (the shareholders’ perspective), i.e. placing them highest in the hierarchy of stakeholders. In this view, a business entity is created by its owners and operates on their behalf, thus the interests of all other persons and groups are of secondary importance. But does equal treatment really impair their interests in any way, even if we accept that their needs are of primary importance? The answer to this question is not at all self-evident. The Basis for Conclusion emphasizes that the statement of equal treatment of all capital providers does not mean that shareholders’ needs are not given due attention; it
only means that, when developing reporting standards, the standard setters seek to meet the information needs of all capital providers.

The provision discussed above may also be questioned from a different standpoint by proponents of the stakeholder perspective, who maintain that financial reporting information should meet the needs of all stakeholders to the same degree. Putting capital providers first is likely to be opposed by supporters of the concept of the social responsibility of corporations, in which the business entity should pursue broad social goals rather than seek only to satisfy the financial interests of the capital providers. Under this approach, a company is accountable not only to the owners, and not even to all capital providers, but also to employees, customers, suppliers and contractors, government and members of the public within their sphere of influence (even global in some cases), and the natural environment. Objections may also be raised on behalf of particular groups of stakeholders on account of their not being included among the primary users of financial information, which might result in treating their information needs as being peripheral in financial reporting (or even ignoring them altogether). This in turn would be detrimental to the interests of this particular group (provided that financial statements are the only publicly available source of information about the entity). An example of a group which might think that their interests were not given due attention in the draft framework are those who are concerned about the natural environment and see a significant role for accounting in its protection.

Another example is those people who are in favour of providing extensive information about an entity’s human resources and their management (in the context of both recognizing human resource development as a key factor of success and protection of employee interests, and to eliminate discrimination based on race, gender, age, etc.). Two questions arise at this point:

a) is the non-inclusion of some major stakeholder groups among primary users of financial statements justified?

b) will it result in the reduction or even omission of information about an entity’s employees or its environmental and social impacts?

If, from a particular viewpoint, we consider it inappropriate to limit primary users of financial statements to capital providers, we should refer to the purpose of financial reporting as stated by the FASB and the IASB in the common conceptual

---

9 In the theory of management, stakeholders are “groups or individuals directly or indirectly interested in an entity’s activity aimed at fulfilling its goals” (Stoner, Freeman, Gilbert, 1997, p.80) Stakeholders are both internal (employees, managers, owners, supervisory board) and external (customers, suppliers, competitors, the public, government and its agencies, and other groups).

10 The issue of responsibility accounting has often been addressed by A. Jaruga (i.a. 1991, pp. 30-31).

11 The requirement to disclose this type of information, recently introduced to EU Directive IV, reflects the significance of this problem to many people and institutions (a corresponding requirement is in art. 49 of the Polish Accounting Act).
framework project. The purpose is to provide capital providers with financial information that will be useful in decision making. The orientation towards capital providers follows logically from both these organisations' mandates – they were set up to support the effective development of economies and the efficient allocation of resources in capital markets. Such objectives as sustainable development, protection of the natural environment or alleviation of social problems, however laudable, are not among their mandatory objectives. Thus, the question about the validity of the approach adopted in the draft framework with regard to primary users of financial statements is in fact a question about the role of the IASB as an accounting regulator (and indirectly about the role of accounting as a practical activity). There seems to be no inconsistency between financial reporting objectives and users as defined in the common framework project and the IASB’s mandatory objective.

As regards the second of the questions formulated above, i.e. the implications of the non-inclusion of some major stakeholder groups among primary users of financial statements, it seems at first sight that it will have a negative effect on the information content in the areas mentioned in the question. On the other hand, we must be aware that information about human resources and their development, and environmental and social impacts, may find its way into financial statements of companies sooner than we expect. To explain this, we must again make reference to the objective of financial reporting, i.e. provision of information that is useful to capital providers in making decisions. As all the elements mentioned above are either key determinants of an entity's success or the main source of opportunities and threats, information about them is very useful to present and potential investors and creditors. It should therefore be included in financial reporting. Many companies are already publishing, along with their financial statements (or in notes to financial statements), information concerning performance in various areas. Among the most notable examples are the reports of the Skandia company concerning its intellectual capital (employees, customer relations, strategic sources of growth, etc.), directed specifically to present and potential investors.
Examples include reports on impacts on the natural environment or society. IAS/IFRS take a favourable view of such reports, as they enhance the usefulness of financial statements. In future, the scope of information on human resources, performance in environmental and social areas, and relations with customers, suppliers and government agencies, published under IAS/IFRS, may increase further. This is because, as has already been emphasised in this paper, the new conceptual framework introduces the concept of financial reporting going beyond the narrow view of financial statements. Thus understood, reporting may comprise, among other things, management reports. The IASB has started work on the so-called Management Commentary, i.e. a narrative report which will provide non-financial and prospective information that is not included in financial statements.

Let us consider for example the guidelines in the Operating and Financial Review issued by the British ASB (Accounting Standards Board) to realise how broad the scope of reporting may become. The ASB recommends that such a report should include information about:

- a) the character of the entity's activity, market characteristics, and competitive, economic and legal environment,
- b) goals and strategy,
- c) development and performance, present and future,
- d) resources, risks, sources of threats and uncertainty, and relations determining the entity's value in the long term,
- e) financial position, present and future,
- f) environmental issues,
- g) employee relations,
- h) social issues.

Naturally, the ASB recommendations set out in the OFR (Operating and Financial Review) are more detailed. For instance, with regard to the natural environment issue, it is prescribed to include information on CO2 emissions and the amount of water used by the entity. It should be noted that the recommendations in the ASB's Operating and Financial Review have an optional, not an obligatory, character – they constitute a model of good practice rather than compulsory requirements. The IASB's standard concerning the Management Commentary is to have a similar status. This does not mean, though, that the optional character of these guidelines will encourage entities to avoid disclosure of such information; on the contrary, it is very likely that entities, competing for equity capital, will readily volunteer this type of information. After all, the pioneers and leaders in publishing such reports, e.g. Skandia, do it of their own initiative and in their own interest (the company is convinced that this will help it to attract “good” investors who expect above average returns in the long term).

It seems reasonable to assume that the more an entity presents extensive and diverse information in its reports, the better will be its competitive position with
regard to raising capital. Thus, the exclusion of employees, government agencies and other groups not acting as capital providers from the class of primary users of financial reporting information does not necessarily result in omission of information important to members of these groups, which might impair their interests. As has already been noted, the purpose of the IASB and FASB activity is to support the development of economies and efficient allocation of resources in capital markets. Provision of decision-useful information is a means of fulfilling this objective. The argument may proceed as follows: information that is useful to capital providers in making sound economic decisions not only satisfies their needs, but also enhances the utility of other market participants (employees, customers, the general public). Let us consider, for instance, a company that is producing consumer goods. Its customers are members of a local community, the great majority of whom have an ecological orientation. If the company were selling goods manufactured via an environmentally harmful process without taking any protective measures, it would not be able to stay in the market. Similarly, investors would not be willing to invest in such a company, as value to the investors is a derivative of value to the customers. If the entity is to keep present investors and attract new ones, it will have to convince them that its activity has a positive effect on the environment. It is certain to publish all relevant details in its financial statements of its own accord, without being mandatorily required to do so. Companies that fail to report on the environmental aspects of their activity will be viewed with a suspicion that their performance in this area is not satisfactory. Therefore, useful financial reporting information (about the entity’s impact on the environment) leads to decisions which are beneficial not only to equity investors but to other stakeholders as well. In other words, useful financial information that is oriented to capital providers’ needs, through a sequence of economic decisions, makes life better for all.

This seems to be a logical conclusion, but it may be questioned in the light of Arrow’s statement that it is impossible to create one utility function that would reflect the needs of all\(^{15}\). If it is so indeed, then it is not in the power of accounting to solve this problem. Even if the new conceptual framework provided that all stakeholders are primary users of financial reporting possessing equal rights, their information needs and interests are not likely to be met to the same degree. It may therefore be a good thing that the new framework gives priority to capital providers, who have the most critical and immediate need for financial information about the entity. Perhaps in this way the objective of financial reporting will not lose its focus – the document Basis for Conclusions shows that this was an important argument for the IASB and the FASB. On the other hand, giving priority

\(^{15}\) Professor K. Arrow, the Nobel prize winner, studied decision theory. An illuminating application of this theory in the context of accounting, and financial information users in particular, is in: Hendriksen, van Breda (2002, pp. 226-227)
Comments on the Objective of Financial Reporting in the Proposed New Conceptual ...

to capital providers does not seem to result in gross infringement of the interests of other user groups.\(^{16}\)

4. Two aspects of decision usefulness of financial reporting

Decisions are made by capital providers on the basis of financial reporting information and they relate to whether and how to allocate their resources within a given entity (whether and how to provide capital to it) and how to protect and enhance their investment. In making such decisions, capital providers are interested in:

1) the entity's ability to generate positive net cash flows, and
2) management's ability to fulfil their stewardship responsibility.

The first of these two aspects of decision usefulness of financial reporting information relates to its usefulness in assessing the entity's ability to generate cash. Capital providers have an immediate interest in the amounts, timing and uncertainty of cash flows from dividends, interest and the sale, redemption or maturity of securities and loans. It is noted at this point in the draft framework that other users of financial reporting are also interested, directly or indirectly, in the entity's ability to generate cash. The boards therefore maintained their view that information that meets the needs of capital providers will also be useful for other groups that are interested in financial information about the entity.

The second aspect of decision usefulness of financial information pertains to management's stewardship responsibility. Management is accountable to capital providers for protection of the entity's economic resources and their effective and efficient use. Management's responsibilities include protection of the entity's assets from the unfavourable influence of economic factors (e.g. price fluctuations, changes in the technological and social environment) and meeting all obligations of the entity arising from law, contracts and other regulations. All these responsibilities are comprised by the stewardship function. The effects of fulfilling the stewardship responsibility by management are significant for present shareholders in making decisions to which they are entitled, such as replacement of the board's members, their remuneration and the method of voting on its policy proposals. Effective performance of the stewardship function generally affects the entity's ability to generate cash, so the effects of management's performance in this respect are also of interest to potential capital providers.

The definition of decision usefulness of information and whether it encompasses assessment of the stewardship function (in addition to or instead of the resource allocation objective) turned out to be controversial in the course of work on the

\(^{16}\) In the Basis for Conclusions it is stated that the entity's social responsibility is an example of information that is interesting to capital providers.
project. In the discussion paper preceding the exposure draft, the IASB and the FASB agreed that reporting information on the management’s performance of the stewardship function should be part of the overall purpose, i.e. provision of information for making resource allocation decisions. It was also decided that eliminating discussion on the stewardship function might wrongly imply that the boards do not think that financial reporting should provide information that is useful in assessing how the management has fulfilled its responsibility to protect and enhance the investments of capital providers. The boards also stated in the discussion paper that formulation of a separate objective relating to the stewardship function might imply that financial reporting should separate the effects of the management’s performance from the effects of events that are beyond its control. It was also noted that those people who think that provision of information for assessment of the stewardship function is an objective broader than decision usefulness are probably confusing financial reporting with corporate governance.

The IASB and the FASB concluded that the objective of financial reporting should be broad enough to encompass all decisions of capital providers which are made on the basis of financial reporting information. Their decisions relate both to resource allocation (i.e. making the investment) and, subsequently, protection and enhancement of the investment. The objective of financial reporting as defined in the draft framework is presented in Figure 2.

**Figure 2: The objective of financial reporting**

*Source: author’s elaboration*
There is one more interesting question to be considered. It is stated in the Basis for Conclusions, in the section dealing with definition of the primary user group, that although the entity theory has been adopted as the foundation of financial reporting, it might also be appropriate to report information that is directed towards owners. This implies that adoption of the entity theory is not in conflict with providing information that is more consistent with the proprietary theory. This view of the boards will certainly be accepted by supporters of the idea of giving priority in financial reporting to owners' needs, but it might raise objections from those in favour of granting the same status to capital providers (although this stance is not convincing, as broadening the scope of information to include that directed at owners does not entail a reduction in the amount of information for creditors and lenders; moreover, equal treatment should mean satisfaction of the information needs of each group to a similar degree, rather than provision to each group of the same amount of information). Criticism of the boards' approach to this matter might also be directed at the “mixing” of the perspectives. The opinion that if one theory is adopted the other should be rejected appears reasonable. It does not seem right to view things from the entity perspective in one place and switch to the proprietary orientation in others. The business entity should be viewed in a consistent way. But is the validity of these statements unquestionable? In the light of some contemporary concepts of organisation they might be considered to be wrong. To quote an outstanding specialist in organisation theory, G. Morgan, “organisations are many things at once”\textsuperscript{17}. Generally, they are complex, indefinite and full of paradoxes. Morgan postulates a way of critical thinking which facilitates the perception of multiple meanings of a situation. According to him, “people who view a situation from different theoretical standpoints are in a better position than people sticking to one viewpoint”. First, “they are more aware of the limitations of a particular approach”, and second, “they see how problems and situations can be shaped and transformed in different ways to find new solutions”\textsuperscript{18}. Therefore, in view of the complexity of contemporary corporations (in respect of both internal structure and external links) the adoption by the boards of the dual theoretical perspective may be regarded as an advantage rather than a weakness. Perhaps it is better sometimes to see a company from the shareholders' standpoint, and sometimes from the stakeholders' standpoint. The adoption of such an approach may reflect the boards' awareness of complexity and vagueness, as postulated by G. Morgan, rather than indecision and seeking to satisfy conflicting interests.

Finally, there remains the issue of the conceptual framework's significance for the practice of accounting, and its reception by accounting practitioners. The author's experience (as a lecturer on many training courses on IAS/IFRS for accountants and auditors) shows that conceptual frameworks are regarded by practitioners as

\textsuperscript{17} This quotation is from a fascinating book by Morgan, entitled Images of Organisation (1997), presenting different ways of viewing organisations.

\textsuperscript{18} Ibidem, p. 338.
exercises in theorising that are useless in practice. Since financial reporting standards are a manifestation of accounting as a practical discipline, then perhaps deliberating the conceptual (theoretical) basis of accounting is art for art's sake. Do the IASB and the FASB devote too much time to theory instead of dealing with the problems faced daily by accountants and auditors in companies that are using IAS/IFRS? Such reasoning does not seem right. To quote K. Levin’s words, “there is nothing more practical than good theory.” Theory supports practice by enhancing the ability to understand reality and makes action more effective by providing orientation and focus (see Morgan, 1997, pp. 398-399). This seems to be the right way to see the conceptual framework. It is developed by practitioners for practitioners on the basis of comments received from practitioners. Therefore it is not likely to be detached from reality. The conceptual framework – the theoretical foundation of accounting – like every theory, is just an ordered conceptual structure. In the case of financial reporting, such a structure defines its boundaries, objective and principal ways of fulfilling this objective. It gives direction to practical activity, i.e. the process of preparing and presenting financial statements. In this way, financial reporting is not a random set of inconsistent procedures with an indefinite objective, but something that makes profound sense. And the question asked by practising accountants “Why are we doing this?” gets a clear answer.

5. Conclusion

The joint IASB and FASB project to develop an improved common conceptual framework is an excellent starting point for discussion about the role of financial reporting (and accounting in general) in today's world, and about its theoretical foundation. This paper is a contribution to discussion on this subject. The author is of the opinion that the solutions proposed in the new (draft) framework should be examined from different perspectives and in different contexts. This will facilitate their understanding, analysis and evaluation. Both academic accountants (including students) and practitioners should become acquainted with the draft. Analysis of

19 Participants of such courses usually consider the part devoted to the conceptual framework as boring, detached from reality and useless in practical work.
20 Work on the joint IASB and FASB project to develop an improved, common conceptual framework has been going on for several years and it is nowhere near an end (dates of its finalisation are continually postponed).
22 Just as the entity theory and proprietary theory help in understanding what constitutes a business entity, which we seek to represent in accounting.
23 Under the IASB constitution, the main criteria for the board’s membership are professional competence and practical experience. In the selection of members, what is sought is a diversity of practical experience as contributed by auditors, preparers and users of financial statements.
24 An interesting contribution to the discussion of the nature of the conceptual framework for financial reporting is by W.A. Nowak (2007).
its contents might help us to answer the question about the present role and nature of our discipline.

In the author’s opinion, the objectives and users of financial reporting as defined in the conceptual framework project are logical as well as consistent with IASB’s mandatory objective.

Reference


Sobańska (2007b), Nowa orientacja systemu rachunkowości w praktyce polskiej w kontekście wdrażania MSR/MSSF, [w:] Rachunkowość, wczoraj, dziś, jutro, Stowarzyszenie Księgowych w Polsce Zarząd Główny w Warszawie COSZ, Warsaw.
