



**International  
Accounting Standards  
Board**

**30 Cannon Street, London EC4M 6XH, United Kingdom**  
**Phone: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411**  
**Email: [iasb@iasb.org](mailto:iasb@iasb.org) Website: <http://www.iasb.org>**

*This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.*

*These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.*

## **INFORMATION FOR OBSERVERS**

**IASB Meeting:** 17 July 2007, London (Agenda Paper 2A.1)

**Project:** Conceptual Framework

**Subject:** Phase B: Elements and Recognition - Asset Consultation

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### **Introduction**

1. The definition of an asset is a fundamental starting point from which other parts of the conceptual framework derive, including the definitions of other elements and recognition and measurement. Thus, it is important that the proposed definition is as robust as possible. Accordingly, in October 2006, the Boards agreed to conduct an informal external consultation on the definition of an asset.
2. The consultation was to solicit fresh and objective feedback on the shortfalls identified with the present definitions of an asset and the Boards' proposals to address those shortfalls. Questions posed involved assessing whether the working definition:
  - a. overcomes the shortcomings of the existing definitions;
  - b. communicates more clearly; and
  - c. facilitates a more disciplined analysis than the existing definitions.

We also asked whether those consulted thought that the proposed working definition would include items that are not considered assets today or would exclude items that are considered assets today, and why.

## **Who We Consulted**

3. As part of the informal external consultation, feedback on the working definition of an asset and amplifying text was received from the Boards' advisory councils, a conference with academics, and a meeting of National Standard Setters, as well as six individuals expected to be able to provide expert advice.
4. The advisory council discussions were held with the FASB's Financial Accounting Standards Advisory Council and FASB's Small Business Advisory Council in December 2006, and the IASB's Standards Advisory Council in February 2007. At the American Accounting Association/FASB financial reporting issues conference in December 2006, academics, preparers, advisors, regulators and some Board and senior staff members from the IASB and the FASB discussed the proposals and an extensive list of examples during the one and a half-day conference. At the March 2007 liaison meeting between the IASB and national standards setters, views were provided by the chairs and senior staff of the Australian, Canadian, French, German, Indian, Japanese, New Zealand, Singapore and United Kingdom standard setters, and European Financial Reporting Advisory Group (EFRAG). [Sentences omitted from observer notes] Board Members have previously been provided with a summary of the discussions at the December 2006 AAA/FASB Conference.

## **Working Definition for Consultation**

5. For reference purposes, the consultation draft of the working definition of an asset, amplifying text and discussion of the perceived shortfalls of the existing definitions and how those shortfalls are overcome by the working definition, is attached in Appendix A to this paper.

## **What We Heard**

6. The following summary comprises the main messages we heard from the consultations.
7. *Overall, an improvement*—Compared to the present definitions, most agreed that the working definition includes improvements. However, it is evident that we have not yet sufficiently demonstrated the case for some of the improvements. Responses tended to be more favourable in forums where we had the opportunity to explain what we were doing, rather than from those who read the proposals solely. Often the discussions involved the explanation of key concepts, such as rights, privileged access, enforceability, scarcity and the different types of contractual promises. Some questioned whether some of the improvements were sufficiently significant to warrant the effort of change and thought that a better explanation of the existing definitions might be sufficient.
8. Other main messages were:
  - a. *Favourable views on removal of notions of “probable” and “likelihood”*—The most favoured improvement was the removal of the likelihood assessment from the existing definitions.
  - b. *Support for focus on what “presently” exists*—There is support for focussing the definition on what presently exists, rather than seeking out whether there has been a past transaction or other event.
  - c. *Support for focus on stocks rather than flows*—There is support for focusing the definition on the present “stock” or item, rather than the future “flows” or future economic benefits from the item.
  - d. *A desire to also deal with recognition*—While a number of those consulted appreciated the approach of addressing definitions separately from recognition, many commented that to fully evaluate and understand the implications of the proposals, unit of account, recognition and derecognition, and maybe even aspects of measurement, need to be considered.
  - e. *Rights versus economic resource*—Mixed views were provided as to whether an asset is a *right* to an economic resource or is the economic resource. On balance, more think that

an asset definition that focuses on what an *entity's rights* are will be more reflective of how business is conducted today and will be a more effective tool.

- f. *Control*—The replacement of “control” by “rights or other privileged access” received the least support, with some questioning whether it might be better to explain how the term “control” should be used, rather than to replace the term. Others struggled with whether “rights or other privileged access” is a clearer notion than “control” (see concerns, below, with “rights or other privileged access”).
- g. *Rights versus access*—Several of those consulted suggested that rather than referring to “rights or other privileged access” we should refer only to “rights,” but explain that concept in the amplifying text in terms that include the ideas of “other privileged access”. This would reduce the difficulties of understanding what “privileged access” means. An alternative, suggested by some, would be to refer to “access” as the generic term and explain that access comprises both rights and other privileged access.
- h. *Enforceability*—Several of those consulted cautioned against undue focus on legal enforceability and requested a clearer articulation of the interaction of “legal enforceability,” “enforceability by equivalent means” and “privileged access”. Some reviewers questioned the need to refer to enforceability at all. Others questioned how much enforceability is necessary.
- i. *Measurement*—Several of those consulted were concerned that application of the definition requires consideration of some aspects of measurement, such as in assessing whether there is a non-zero probability of positive cash flows. Some also noted similar concerns in assessing whether a resource is “economic” and “scarce”.
- j. *Gross versus net*—Some of those consulted questioned whether one should consider gross or net cash flows in assessing whether something has positive economic value. At least in part, this is a “unit of account” question.
- k. *Focus on cash flows*—Several of those consulted noted that the amplifying text over-emphasises cash flows. They think that economic benefits should be able to be explained without a lengthy discussion back to cash and some have concerns about the focus on

cash flows when the definitions are applied, in due course, to not-for-profit organizations and public sector entities.<sup>1</sup>

9. In most of these cases, there were also minority views held contrary to these main messages. There were also a number of useful suggestions to improve and clarify the paper, which are not included above but will be taken into account in drafting.

## **What We Are Doing**

10. The comments received from the consultation are being analysed in detail and will be evaluated by the staff and Boards when further development of the asset definition and amplifying text is undertaken.
11. As noted above, when we had the opportunity to discuss some of the issues with those consulted, greater understanding seemed to be achieved, which suggests that we need to be much clearer in how we communicate the intent of the proposals. We acknowledge that new thinking takes some time to get used to (for example, when the FASB issued Concepts Statement No. 1, the decision usefulness objective of financial reporting received only minority support). We also think that some derive comfort from the existing definitions because of the way they interpret the definitions, rather than from what the definitions are intended to say and, hence, they are concerned about more precise wording that might challenge those prior interpretations.
12. We have done some preliminary thinking about some of the matters arising. Some of those preliminary thoughts are outlined below.

### **Rights versus Economic Resource**

13. With regard to the desire of some to focus first on an entity's present rights, rather than a present economic resource (see point e in paragraph 8, above) we note that all definitions used by national standards setters, except that of the UK, focus first on the asset as being the

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<sup>1</sup> The Boards are, for the time being, considering only private sector business entities. Not-for-profit organizations will be considered in a later phase of the project. Accounting by public sector entities does not fall within the Boards' mandate. However, the International Public Sector Accounting Standards Board is presently undertaking a project to develop a conceptual framework, in which it is being guided by thinking in the IASB Framework.

economic resource, rather than on the linkage of the entity to that resource. This is illustrated in the following table, which indicates, in bold, which part of existing definitions relates to what the asset is:

<b>Definitions of an Asset</b>	
IASB	<b>An asset is a resource</b> controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity. (paragraph 49(a))
FASB	<b>Assets are probable future economic benefits</b> obtained or controlled by a particular entity as a result of past transactions or events. (paragraph 25)
Australia	<b>"Assets" are future economic benefits</b> controlled by the entity as a result of past transactions or other past events; and "control of an asset" means the capacity of the entity to benefit from the asset in the pursuit of the entity's objectives and to deny or regulate the access of others to that benefit. (paragraph 14)
Canada	<b>Assets are economic resources</b> controlled by an entity as a result of past transactions or events and from which future economic benefits may be obtained. (paragraph 29)
Germany	<b>An asset is a resource</b> controlled by an enterprise as a result of past events. (paragraph 66)
Japan	<b>Assets are economic resources or their equivalents</b> that the reporting entity controls as a result of past transactions or events. (paragraph 4)
New Zealand	<b>Assets are service potential or future economic benefits</b> controlled by the entity as a result of past transactions or other past events. (paragraph 7.7)
United Kingdom	<b>Assets are rights or other access</b> to future economic benefits controlled by an entity as a result of past transactions or events. (paragraph 4.6)
CFA Institute – Comprehensive Business Reporting Model <sup>2</sup>	An enterprise must recognize <b>an economic resource as an asset</b> in the financial statements when all of the following conditions are met: <ul style="list-style-type: none"> <li>a. The resource is a present right or other access to a future benefit that will flow to the company and will contribute directly or indirectly to future net cash inflows;</li> <li>b. The right to the future benefit is controlled by the company;</li> <li>c. There is a nonzero probability that the benefit will occur;</li> <li>d. The right to the future benefit is separable from the company; that is, it can be transferred to an external party;</li> <li>e. The right to the future benefit is the result of past events; and</li> </ul>

<sup>2</sup> *A Comprehensive Business Reporting Model: Financial Reporting for Investors*, CFA Centre for Financial Market Integrity, September 2005. Note that this definition mixes both the definition of an asset and recognition criteria.

	f. The fair value of the right to future benefits can be measured. (page 19)
FASAB <sup>3</sup>	<b>An asset is a resource</b> that embodies economic benefits or services that the federal government can control. (paragraph 17)
GASB <sup>4</sup>	<b>Assets are resources</b> with present service capacity that the government presently controls.

14. Only the UK definition states that assets are rights or other access. We note that, in the proposed working definition of an asset, *right* (or other privileged access) replaces the word *control* in the existing definitions. We think that those who argue that the asset is the *right*, would not make the same argument that the asset is *control*. [Sentence omitted from Observer Notes]

15. One way to reorder the words in the definition might be to consider wording the definition along the following lines:

“An entity has an asset when it has a present right/access to a present economic resource.”

This would avoid the connotation that the asset is the right/access, rather than the economic resource. It would indicate also that, in evaluating whether an entity has an asset, one might first consider whether the entity has a right/access to something and then consider whether that thing is an economic resource, rather than evaluating a wide range of economic resources before ascertaining whether the entity has a right/access to them.

16. However, we also note that, regardless of the order of the words in the definition both a present economic resource and a present right or other privileged access are necessary in order for the definition to be met.

### **Other Privileged Access**

17. Another aspect of the working definition that is of concern to many is the reference to “other privileged access” (see points f and g in paragraph 8, above). We had proposed that phrase to

<sup>3</sup> Federal Accounting Standards Advisory Board, July 2006 Exposure Draft, *Proposed Statement of Federal Financial Accounting Concepts: Definition and Recognition of Elements of Accrual-Basis Financial Statements*.

<sup>4</sup> Governmental Accounting Standards Board, June 2007, Concepts Statement No. 4, *Elements of Financial Statements*.

indicate that rights include more than legal rights, as well as to exclude from the definition rights that are available to all.

18. We think that we can address this concern by referring only to a *right* or *access* in the first sentence of the definition; then explaining in more detail in the amplifying text what nature of rights or access qualifies to meet the definition. This would avoid placing significant emphasis on a single word such as *privileged*—a word that, it seems, is not clearly understood and does not translate well into all languages.
19. Such an approach might help, also, to address the concern about the undue focus on legal enforceability (see point h in paragraph 8, above). The definition of rights, or access, could refer to the entity's ability to enforce that right or access, and enforceability could be explained in the amplifying text.

#### **Measurement and Gross or Net Cash Flows**

20. Concerns about the need to consider aspects of measurement (see point i in paragraph 8, above), as well as concerns about whether one should consider gross or net cash flows (see point j in paragraph 8, above), in assessing whether something has positive economic value, might be alleviated by stating that, “An *economic resource* is something that ~~has positive economic value.~~ It is scarce and capable of being used to carry out economic activities such as production and exchange.”
21. We plan to consider all of the above issues in more detail when the time is right. This paper does not seek to resolve these issues—merely it seeks to illustrate some of the possible resolutions that staff are presently considering.