IASB/FASB Joint Board Meeting
September 2010

IASB Agenda reference	**10A**
FASB Agenda reference	**6A**

Staff Paper

Project	**Emissions Trading Schemes**
Topic	**Recognition of assets in a cap and trade scheme**

Purpose

1. The purpose of this paper is to address the recognition of assets in a voluntary and statutory cap and trade scheme. This paper is separated into two parts:
   - **Part A** provides analysis of the recognition of purchased allowances as assets.
   - **Part B** provides analysis of the recognition of allocated allowances as assets.

2. The staff recommend that purchased (paragraph 14) and allocated (paragraph 18) allowances in a cap and trade scheme are recognised as assets.

3. This paper does not discuss the existence and recognition of liabilities for the allocation of allowances. These issues are discussed in AP 10B/6B.

4. This paper does not discuss the following issues that will be addressed at a future board meeting:
   - i. the measurement of the allowances;
   - ii. the interaction of the entity's emissions with the liability for the allocation;
   - iii. the presentation issue of netting (ie offsetting);
   - iv. whether, and when, a right to future allocations constitutes an asset; and
   - v. presentation and disclosure issues (other than netting).

AP 10C/6C provides a basic description of these issues and some of the alternatives under consideration.

Board decisions

5. At the March 2009 meeting, the IASB tentatively decided that an entity should recognise allocated allowances (in a cap and trade scheme) as assets[1] . The FASB discussed these issues at its April 2009 meeting, but made no decisions.

Part A - Should purchased allowances be recognised as assets?

6. Allowances are certificates, similar to a currency, that can be used to settle scheme liabilities. Allowances can be purchased from the scheme administrator (through an auction), or in the market, and are freely tradable. These features related to the allowances are the same in both voluntary and statutory schemes.

Staff analysis

Does a purchased allowance meet the definition of an asset?

7. The definition of an asset in the IASB's *Framework* is as follows:

> An asset is a resource 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]

8. The definition of an asset in FASB's Concepts Statement No. 6 *Elements of Financial Statements* defines an asset as follows:

> Assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events. [paragraph 25]

9. Although the definitions appear slightly different, both broadly include the concepts of a past transaction or event that results in a controlled resource that will yield future economic benefits[2]. Purchased allowances easily meet all of these concepts. The purchase of allowances is a past event and benefits are evidenced by the entity's ability to sell the allowances for cash in markets, or to

[1] The IASB also tentatively decided that these assets should be initially measured at fair value.
[2] FASB *Concepts Statement 6* indicates that an asset is a *probable* future economic benefit, as opposed to a resource, however the staff think that this distinction is not critical to the analysis for the allowances.

use the allowances to settle scheme liabilities. Control over allowances results from the entity's ability to obtain economic benefits from the allowances – either to hold or to trade – and to restrict the access of others to the allowances, including restricting the access of the scheme administrator.

10. The staff conclude that purchased allowances meet the definition of an asset in both boards' frameworks.

Do the purchased allowances meet the recognition criteria?

11. The recognition criteria of the boards' frameworks are not congruent with each other. The staff believe that this is due to the different structure of the frameworks and not due to fundamental differences. The recognition criteria for both frameworks are similar in that an item must meet the element definition in the respective framework and that the item must be reliably measurable. In accordance with the staff's conclusion in paragraph 10 above, purchased allowances meet the definition of an asset in both frameworks. In addition, the allowances are freely tradable in markets[3], where the value of the allowances can be determined with reference to quoted market prices. The value of the allowances can therefore be measured reliably.

12. Two areas in which the two frameworks differ in their recognition criteria are the 'probable future economic benefits flowing to the entity for items that meet the asset definition' criteria in the IASB *Framework* and the 'relevance' criteria in the FASB's Concepts Statement No. 5 *Recognition and Measurement in Financial Statements of Business Enterprises*. These differences do not present difficulties in analysing whether the criteria of recognition for the purchased allowances are met. Specifically, the concept of 'probable future economic benefit' is also included in the definition of an asset in FASB *Concepts Statement 6* and (as noted above) is met for allowances because the entity can sell allowances for cash or use them to settle scheme liabilities. In addition,

[3] The markets in the EU for allowances in the EU ETS is established and active. Markets in other jurisdictions where a statutory scheme has only recently been implemented, or is yet to be implemented may be less active, however generally a market still exists.

because these economic benefits will affect an entity's future cash flows, the staff believe that information about an entity's allowances also meet the criteria of relevance, because information related to the allowances is capable of making a difference in user decisions.

13. The staff therefore conclude that purchased allowances meet the criteria for recognition.

Staff recommendation

14. The staff recommend that purchased allowances are recognised as assets.

Part B – Are allocated allowances[4] also assets?

15. In addition to being purchased, allowances can also be received from the scheme administrator as an allocation[5]. Entities provide no monetary consideration for the allocated allowances. The issue is how the lack of monetary consideration affects the analysis of whether the allocated allowances are assets. Alternatively, whether there is another element resulting from the allocation that should be recognised.

Staff analysis

Do allocated allowances meet the definition of an asset?

16. The allocated allowances are also certificates that have the same features as purchased allowances. In fact, after an allowance is allocated to an entity, it is impossible to distinguish a purchased allowance from an allocated allowance. Thus it appears that an allocated allowance will also meet the definition of an asset in the boards' frameworks: results from a past transaction (the allocation) and is a resource that will result in economic benefits (trade for cash or settlement of liabilities). However, because the allowances are allocated from

[4] This paper does not discuss whether a right to future allocations constitutes an asset. This issue is described in AP 10C/6C and will be discussed at a future board meeting.

[5] The volume of these allocations is expected to decrease over time.

the scheme administrator some may question if the entity fully ‘controls’ the allowance. Furthermore, because the allowances are allocated for no monetary consideration, it is not clear whether they must return them or do something to be able to keep them. At the time the allowances are allocated, does the entity have an unfettered right to keep the allocated allowances?[6]

17. Even though an entity may be required to return the allocated allowances, the entity can choose to either trade or hold the allocated allowance until settlement of scheme liabilities is required. Further, the entity can choose to use any allowance, purchased or allocated, to settle the scheme liabilities. This illustrates that the entity can restrict access to the allocated allowances. Thus the entity is able to control the allocated allowances and hence the allocated allowances meet the definition of an asset in the boards’ frameworks. Since allocated allowances are indistinguishable from purchased allowances, allocated allowances will also meet the recognition criteria in the boards’ frameworks. Allocated allowances should therefore be recognised as assets.

Staff recommendation

18. The staff recommend that allocated allowances are recognised as assets.[7]

Question for the boards:
Do the boards agree with the staff recommendation that purchased and allocated allowances should be recognised as assets? If not, why not?

[6] The same analysis was not completed for purchased allowances. When allowances are purchased, all rights (and obligations) to the seller are specified at the time of exchange.
[7] AP 10C/6C includes a description of the presentation issue of offsetting (ie netting). This issue will be discussed at a future board meeting.