STAFF PAPER

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REG IASB Meeting

Project	Conceptual Framework		
Paper topic	Elements: economic resources and economic benefits		
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Purpose of this paper

1. The draft definition of an asset refers to economic resources. The draft definition of an economic resource refers, in turn, to future economic benefits. This paper considers what guidance the *Conceptual Framework* should provide on economic resources and economic benefits.

2. This paper does not discuss:

   (a) executory contracts (Agenda paper 10D);

   (b) unit of account (Agenda paper 10E);

   (c) supporting guidance on the following issues, which will be the subject of future papers:

      (i) whether to retain the notion of control, in either the definition of an asset or in recognition criteria, and how to define control. Also, implications of control for agents and principals; and

      (ii) reporting the substance of contractual rights and obligations;

(d) the IASB's tentative decisions in May 2014:

   (i) to view assets as rights, or bundles of rights, rather than as underlying physical or other objects.

   (ii) to specify that an economic resource must be capable of generating economic benefits.

Summary of staff recommendations

3. The staff recommend that:

   (a) the *Conceptual Framework* should provide examples of economic resources, along the lines of paragraph 3.5 of the Discussion Paper *A Review of the Conceptual Framework for Financial Reporting*. (paragraphs 4-14);

   (b) the *Conceptual Framework* should include guidance on economic benefits, broadly consistent with the guidance in paragraph 3.6 of the Discussion Paper, and paragraph 35 of IFRS 15 *Revenue from Contracts with Customers* (paragraphs 15-18); and

   (c) the purpose of depreciation and amortisation is to depict consumption of the bundle of rights that constitutes an asset (paragraphs 19-37).

Economic resource

Background

4. The Discussion Paper suggested the following definitions:

   (a) An asset of an entity is a present economic resource controlled by the entity as a result of past events.

   (b) An economic resource is a right, or other source of value, that is capable of producing economic benefits.

5. The Discussion Paper also:

(a) suggested the *Conceptual Framework* should provide guidance on the meaning of ‘economic resource’, covering matters set out in paragraphs 3.5-3.15 of the Discussion Paper, see Appendix A to this paper.

(b) indicated, in paragraph 3.5(c), that examples of ‘other sources of value’ are know-how, customer lists, customer and supplier relationships, an existing work force and goodwill.

(c) suggested, in paragraph 3.29, that an entity does not control an economic resource if it does not have the present ability to direct the use of the economic resource. The Discussion Paper indicated that, in consequence, the following are not assets of an entity:[1]

  (i) rights of access to public goods, such as open roads, if similar rights are available to any party at no cost.

  (ii) fish in water to which access is not restricted. Although a potential source of economic benefits, this is not an economic resource of any one entity because those benefits are available to any party. (An exclusive right to catch fish would be an asset of an entity that has that right. Similarly, if fishing quotas are introduced, the quota of each party would become an asset of that party, though the rights associated with possession of the fish would still not become an economic resource until the fish are caught.)

  (iii) knowledge that is in the public domain and freely available to anyone without significant effort or cost. No party controls such knowledge.

(d) suggested, in paragraph 4.26, that the *Conceptual Framework* could list the following as indicators that recognition might not provide relevant information:

  (i) if the range of possible outcomes is extremely wide and the likelihood of each outcome is exceptionally difficult to estimate.

[1] In a future paper, the staff will review feedback received on the discussion of control in paragraphs 3.26-3.34 of the Discussion Paper.

(ii) if an asset (or a liability) exists, but there is only a low probability that an inflow (or outflow) of economic benefits will result.

(iii) if identifying the resource or obligation is unusually difficult.

(iv) if measuring a resource or obligation requires unusually difficult or exceptionally subjective allocations of cash flows that do not relate solely to the item being measured.

(v) if recognising an asset (particularly, internally generated goodwill) is not necessary to meet the objective of financial reporting.

6. In May 2014, the IASB tentatively decided:

(a) to use the definition of an asset, as proposed in the Discussion Paper.

(b) to delete the phrase ‘or other source of value’ from the definition of an economic resource. Thus an economic resource would be ‘a right that is capable of producing economic benefits’. The supporting guidance should confirm that the notion of a ‘right’ is broad enough to capture any know-how that is controlled by keeping it secret.

(c) that the *Conceptual Framework* should describe factors to consider in deciding whether to recognise an asset or liability. Those factors would include whether the resulting information would be relevant and provide a faithful representation, and the costs of providing information relative to the benefits. Information might not be relevant if, for example, it is uncertain whether the asset or liability exists, if it is unlikely that future flows of economic benefits will occur or if there is very significant measurement uncertainty associated with the item.

Feedback received

7. Some respondents welcomed the definitions in the Discussion Paper and suggested that they:

(a) are better suited than the existing definition of an asset to make room for considering intellectual property and other intangibles as assets.

(b) would make it clearer that 'regulatory assets' and 'regulatory liabilities' arising from rate regulation qualify as assets and liabilities. Some respondents thought this conclusion might depend on whether the unit of account was a contract with an individual subscriber or a defined subscriber base.

8. Several other respondents expressed concerns that the new definitions would widen considerably the range of items that will be identified as assets, leading to:

(a) recognition of assets whose existence is uncertain, or that are hard to measure.

(b) significant operational burdens to identify every possible asset, for little benefit if ultimately the asset is not recognised, or is measured at nil.

(c) pressure for disclosure about unrecognised assets for which inflows of economic benefits are possible but unlikely.

9. As noted above, the Discussion Paper's suggested definition of an economic resource included not only 'rights', but also 'other sources of value' that are capable of producing economic benefits. Paragraph 3.5(c) of the Discussion Paper indicated that examples of such 'other sources of value' are know-how, customer lists, customer and supplier relationships, an existing work force and goodwill.

10. Several respondents expressed concerns about some of the items listed in paragraph 3.5(c) of the Discussion Paper. They thought that:

(a) Know-how and customer lists may be assets. They enable the entity to do something advantageous (eg manufacture a product or carry out a targeted marketing exercise). However, the remaining items seem more doubtful. For example, a customer relationship does not give rise to a right to future business, only to the hope of future business and it would be difficult to be sure that any such business will occur on more advantageous terms because of the relationship.

(b) A company's workforce, fundamental research and the ability to raise prices or to reduce a liability in the future, all appear to meet the proposed definition of assets but should continue not to be recognised or, if recognised, should be measured at nil. Some suggested that the definition of an asset should include notions such as identifiability or separability, as in the treatment of intangible assets in IAS 38 *Intangible Assets*.

(d) Although the IASB concluded in IFRS 3 that goodwill is an asset, the rationale is not convincing. Goodwill by itself is incapable of producing economic benefits and relies on the cash generating abilities of other assets. Moreover, the amount attributed to goodwill includes amounts relating to other unrecognised assets and liabilities, and amounts arising from measurement anomalies relating to recognised assets and liabilities.

Staff analysis

11. Some of the concerns expressed by respondents about the breadth of the new definitions may have arisen from the vagueness of the phrase 'other source of value'. The IASB tentatively decided in May 2014 to delete this phrase. In addition, the IASB noted in May 2014 that its aim in revising the definitions of an asset and of a liability and the recognition criteria was to provide more clarity, not to broaden or narrow the range of recognised assets and recognised liabilities.

12. In relation to the concerns raised by respondents about particular items:

(a) A patent is a right that meets the definition of an asset (if the patent is capable of producing economic benefits). However, even if not protected by a patent, know-how clearly meets the proposed definition of an asset. An entity can control it (by legal rights or by keeping it secret) and it is capable of producing economic benefits. Indeed, the IASB decided tentatively in May 2014 that the supporting guidance in the *Conceptual Framework* should confirm that the notion of a 'right' is broad enough to capture any know-how that is controlled by keeping it secret. This is consistent with existing requirements, which result in their recognition in a business combination or in a separate acquisition. In many circumstances, it is not recognised if internally generated, but that is a matter of recognition criteria, not of definition. Similar comments apply to customer lists.

(b) In relation to an assembled workforce:

(i) Paragraph 15 of IAS 38 *Intangible Assets* states that 'an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset'. Moreover, paragraph B37 of IFRS 3 states that an assembled workforce is not an identifiable asset to be recognised separately from goodwill. On the other hand, paragraph IE 7 of the Illustrative Examples on IFRS 3 refers to employment contracts that are beneficial to the employer because their pricing is favourable relative to market terms. Paragraph IE 7 states that these contracts are one type of contract-based intangible asset.

(ii) The staff believes that employment contracts create rights and obligations that can meet the definition of an asset or a liability. Whether an entity should recognise such an asset or liability will depend on the recognition criteria. Moreover, in some instances, employment contracts may be executory. Agenda paper 10D discusses executory contracts.

(c) Some respondents expressed concerns about whether an entity's ability to raise prices, or to reduce a liability in the future, constitutes an asset or liability. These concerns may arise mainly from recent discussions about 'regulatory assets' and 'regulatory liabilities' in the context of rate regulation. In the staff's view, there is a difference between the right to raise prices in such a context and the general ability of an entity to set prices in other contexts:

(i) In the particular context of rate regulation, an entity might have a bundle of explicit legal rights to operate in a specified market, with one component of that bundle being an explicit, legally enforceable right to raise future prices. The IASB is considering in its project on rate-regulated activities whether such rights meet the definition of an asset, and whether they should be recognised.

(ii) In other contexts, entities generally have the right to operate their business. As discussed below, that right is one component of what is currently labelled 'goodwill'. The right to operate the business generally implies an ability to set pricing policy, although within the constraints imposed by many factors, including law, regulation, market forces, the needs and preferences of customers, suppliers and employees. However, an ability to set prices within those constraints does not constitute a separate 'right' and so would not meet the draft definition of an asset.

(d) Applying IAS 38, research does not qualify for recognition as an asset. IAS 38 explains that in the research phase of an internal project, an entity cannot demonstrate the existence of an intangible asset that will generate probable future economic benefits.[2] Applying the definitions suggested in the Discussion Paper and tentatively confirmed by the IASB in May 2014, if know-how generated by research is capable of producing economic benefits, that know-how meets the definition of an asset. The guidance on recognition would determine whether that asset is recognised.

(e) The definition of an intangible asset in IAS 38 requires an intangible asset to be identifiable, so as to distinguish it from goodwill. IAS 38 states that an asset is identifiable if it either is separable from the entity, or arises from contractual or other legal rights.[3] In the staff's view, if an asset is separable, or arises from contractual or other legal rights, it is

[2] IAS 38, paragraph 55

[3] IAS 38, paragraphs 11-12

likely to be easier to identify, measure and describe the asset. However, the staff believes it is unnecessary to include in the definition of an asset a requirement for the asset to be identifiable (as defined in IAS 38).

(f) As explained in paragraphs BC313-BC323 of the Basis for Conclusions on IFRS 3, the IASB has previously concluded that goodwill meets the definition of an asset. IFRS 3 defines goodwill recognised in a business combination as an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised. The Basis for Conclusions on IFRS 3 indicates that the future economic benefits may result from synergy between the identifiable assets acquired and from assets that, individually, do not qualify for recognition in the financial statements.[4] In the staff's view:

(i) a business produces economic benefits that, typically, exceed the benefits generated by the recognised assets less liabilities employed in the business. Thus, typically, the party controlling the business has a resource in addition to the resources recognised as separate assets.

(ii) goodwill is the name given to that additional resource. It might be viewed as the right to operate the business and retain the economic benefits derived from operating it.

(iii) because goodwill is, if recognised at all, measured as a residual, the measurement is necessarily imperfect and includes various factors that would not appear in an ideal depiction of the additional resource (if such a thing were possible). Nevertheless, although goodwill is difficult to measure, that fact does not disqualify goodwill from meeting the definition of an asset.

(iv) as noted in paragraph 4.9(c) of the Discussion Paper, recognising internally generated goodwill is not necessary to meet the objectives of financial reporting.

[4] Basis for Conclusions on IFRS 3, paragraphs BC313-BC318

13. In the staff's view it would be helpful for the *Conceptual Framework* to provide examples of economic resources, along the lines of paragraph 3.5 of the Discussion Paper (see Appendix A). Some changes will be needed to those examples:

(a) the wording of item (c) would need updating to reflect the IASB's tentative decision in May 2014 to delete the reference to 'other sources of value'.

(b) the reference to an existing workforce should be reworded to focus on the entity's rights under employment contracts.

(c) the reference to goodwill in paragraph 3.5(c) should be deleted. The conclusion that goodwill includes at least some items that meet the definition of an asset already appears in the Basis for Conclusions on IFRS 3. There is nothing to be gained by repeating it in the *Conceptual Framework*.

14. Appendix B summarises some other comments received, and the staff's reaction, The staff does not plan to discuss the items in appendix B with the IASB, unless IASB members request it.

Question 1 Economic resources
Does the IASB agree that the *Conceptual Framework* should provide examples of economic resources, along the lines of paragraph 3.5 of the Discussion Paper (modified as described in paragraph 13)?

Economic benefits

Background

15. Paragraph 3.6 of the Discussion Paper suggested that the economic benefits derived from an asset are the potential cash flows that can be obtained directly or indirectly in many ways, for example, by:

(a) using the asset to produce goods or provide services;

(b) using the asset to enhance the value of other assets;

(c) using the asset to fulfil liabilities;

(d) using the asset to reduce expenses;

(e) leasing the asset to another party;

(f) selling or exchanging the asset;

(g) receiving services from the asset;

(h) pledging the asset to secure a loan; and

(i) holding the asset.

Feedback

16. A number of respondents asked for more detailed guidance on the notion of economic benefits.

Staff analysis

17. The list in paragraph 3.6 of the Discussion Paper is largely consistent with paragraph 33 of IFRS 15 *Revenue from Contracts with Customers*, and was derived from a draft of that wording. The final wording in IFRS 15 is as follows.

> 33 Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services). Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset. The benefits of an asset are the potential cash flows (inflows or savings in outflows) that can be obtained directly or indirectly in many ways, such as by:
>
> (a) using the asset to produce goods or provide services (including public services);
>
> (b) using the asset to enhance the value of other assets;

(c) using the asset to settle liabilities or reduce expenses;

(d) selling or exchanging the asset;

(e) pledging the asset to secure a loan; and

(f) holding the asset.

18. In the staff's view, a list along those lines is helpful and should be included in the *Conceptual Framework*. The staff will consider the exact wording in drafting.

Question 2 Economic benefits
Does the IASB agree that the *Conceptual Framework* should include guidance on economic benefits, broadly consistent with the guidance in paragraph 3.6 of the Discussion Paper, and paragraph 33 of IFRS 15?

Depreciation

Background

19. Some respondents to the Discussion Paper stated that the IASB should clarify the term 'economic benefits' because respondents to the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation* had provided various interpretations.

20. IAS 16 *Property, Plant and Equipment*:

(a) defines depreciation as 'the systematic allocation of the depreciable amount of an asset over its useful life'.[5]

(b) states that the depreciation method used 'shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity'.[6]

21. IAS 38 *Intangible Assets* contains broadly similar requirements for the amortisation of those intangible assets that have a finite useful life.

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[5] IAS 16, paragraph 6. This also defines depreciable amount as 'the cost of an asset, or other amount substituted for cost, less its residual value'.

[6] IAS 16, paragraph 60

22. In May 2014, the IASB amended IAS 16 and IAS 38 by issuing *Clarification of Acceptable Methods of Depreciation and Amortisation*. Appendix C contains extracts from this amendment, which states that:

    (a) it is not appropriate to use a depreciation method based on revenue that is generated by an activity that includes the use of an asset. This is because such revenue generally reflects factors other than the consumption of the economic benefits of the asset. Those factors include other inputs and processes, selling activities, changes in sales volumes and prices and inflation.[7]

    (b) for an intangible asset, a revenue-based deprecation method might be appropriate in the following limited circumstances:

        (i) when the intangible asset is expressed as a measure of revenue; or

        (ii) when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.[8]

23. The existing guidance on depreciation in IAS 16 and IAS 38 was developed in the context of the following definition of an asset in the existing *Conceptual Framework*: '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'.

24. In May 2014, the IASB tentatively decided that:

    (a) an asset of an entity is 'a present economic resource controlled by the entity as a result of past events'.

    (b) an economic resource is 'a right that is capable of producing economic benefits'.

[7] IAS 16, paragraph 62A

[8] IAS 38, paragraph 98A

Staff analysis

25. The existing requirements in IAS 16 and IAS 38 rest on the notion that depreciation and amortisation reflect the consumption of future economic benefits embodied in the asset.

26. The main aims of the IASB's tentative decisions to change the definition of an asset are to confirm that:

    (a) an asset is a resource, rather than the ultimate inflow of economic benefits that the resource may generate.

    (b) an economic resource (an asset) is a bundle of rights.

27. This line of thinking is inconsistent with the notions that an asset embodies economic benefits, and that depreciation or amortisation are consumption of those economic benefits. Instead, the item being consumed is the economic resource (the right).

28. The following example might clarify the concepts involved. Suppose that an entity owns a machine with a useful life of five years. In most cases, the entity would account for that bundle of rights as a single asset and would describe it using a simple and understandable label, such as 'machine'. However, conceptually, the entity's asset is a bundle of rights over that machine. Those rights include:

    (a) the right to use the machine for the first year;

    (b) the right to use the machine in the second year;

    (c) similar rights for each subsequent year; and

    (d) the right to obtain and retain the proceeds (if any) from disposal of the machine at the end of its useful life.

29. At the end of the first year, the entity still has the right to use the machine in the second year, similar rights for each subsequent year, and the right to any disposal proceeds. However, it has consumed the right to use the machine during the first year. Depreciation for the first year depicts the consumption of that right.

(Another way to describe this would be to say that depreciation, in effect, depicts the derecognition of that part of the bundle of rights that no longer exists.)

30. Thus, to be fully consistent with the concepts embodied in the new definitions, the purpose of depreciation and amortisation would need to be described as being to depict the consumption of the economic resource (ie the consumption of part of the bundle of rights), rather than the consumption of the economic benefits.

31. In the staff's view, this revised description could have made it easier to reach and explain the conclusions the IASB reached in the recent amendment to IAS 16 and IAS 38. In most cases, the pattern of revenue reflects not only the pattern of consumption of rights, but other factors. (Nevertheless, in limited circumstances, such as those identified in paragraph 98A of IAS 38, the pattern of consumption of rights will be driven by, or correlated with, the pattern of revenue).

32. In the staff's view, this line of thinking is also a straightforward extension of the line of thinking embodied in what is often called the 'components approach' in IAS 16. This approach allocates the cost of a depreciable asset to its significant parts (the airframe and engines of an aircraft) and depreciates each part separately.[9] The bundle of rights approach extends this thinking to components such as the right of use for the first year, the right of use for the second year and so on.[10]

33. The staff believes that an entity would not generally need to account separately for each individual right within a bundle of rights. For example, for a machine with an estimated useful life of five years and an even pattern of consumption, the simplest and most understandable accounting would be to label the bundle of rights as a single 'machine', depreciated over five years on a straight-line basis. However, the conceptual foundation for that accounting is that the asset is actually a bundle of rights over the machine, and that the 'depreciation' depicts the consumption of parts of that bundle of rights.[11] An entity selects the depreciation

[9] IAS 16, paragraph 44

[10] If an entity concluded that the units of production method would best depict the consumption of the bundle of rights, the components identified would refer to units of production, rather than to time periods.

[11] The wording in this paper reflects a depreciation model that uses original cost. Similar thinking would apply in a model that uses current cost.

method and pattern (such as straight-line, diminishing balance or units of production) that most faithfully depicts that consumption.

34. For practical purposes, the depreciation for a period might be described as depicting either partial consumption of the entire bundle of rights, or the entire consumption of some of those rights. In many cases, those descriptions will be equivalent. The first description may often be simpler. The second description may be more helpful when the rights consumed differ significantly in nature or extent in different periods.

35. The staff also believe that this line of thinking can help explain two other issues:

    (a) The distinction between inventory and property, plant and equipment. Inventory is a bundle of rights that an entity consumes at a single date, when it transfers control of the physical inventory. Cost of sales depicts the consumption of that item at that single date. In contrast, for property, plant and equipment, an entity disposes of different parts of the bundle of rights at different times.

    (b) Impairment and depreciation are linked. Impairment of an item of property, plant and equipment might arise for either or both of the following reasons:

        (i) part of the bundle of rights no longer exists (for example, if a machine had an expected useful life of five years, but obsolescence means that it will no longer generate any economic benefits in the last two of those years).

        (ii) the entire bundle of rights still exists, but its value has declined.

36. In summary, the staff believe that the purpose of depreciation and amortisation is to depict consumption of the bundle of rights that constitutes an asset.

37. In the staff's view, this clarification could help with future standard setting decisions, but there is no urgent need to amend IAS 16 and IAS 38.

Question 3 Depreciation
Does the IASB agree that the purpose of depreciation and amortisation is to depict consumption of the bundle of rights that constitutes an asset?

Appendix A

Extract from Discussion Paper

Economic resource

3.5 Economic resources may take various forms:

(a) enforceable rights established by contract, law or similar means, such as:

(i) enforceable rights arising from a financial instrument, such as an investment in a debt security or an equity investment.

(ii) enforceable rights over physical objects, such as property, plant and equipment or inventories. Such rights might include ownership of a physical object, the right to use a physical object or the right to the residual value of a leased object.

(iii) enforceable rights to receive another economic resource if the holder of the right chooses to exercise that right (an option to acquire the underlying economic resource) or is required to exercise that right (a forward contract to buy the underlying economic resource). Examples include options to receive other assets, net rights under forward contracts to buy or sell other assets and rights to receive services for which the entity has already paid.

(iv) enforceable rights to benefit from the stand-ready obligations of another party (see paragraphs 3.70–3.71).

(v) enforceable intellectual property rights (for example, registered patents).

(b) rights arising from a constructive obligation of another party (see paragraphs 3.39–3.62).

(c) other sources of value if they are capable of generating economic benefits. Examples of such economic resources include:

(i) know-how;

(ii) customer lists;

(iii) customer and supplier relationships;

(iv) an existing work force; and

(v) goodwill. The IASB concluded in paragraphs BC313–BC323 of the Basis for Conclusions on IFRS 3 Business Combinations that goodwill does meet the definition of an asset. However, paragraph 4.9(c) of this Discussion Paper explains that recognising internally generated goodwill does not provide relevant information.

(d) some assets, particularly many services, that are consumed immediately on receipt.

3.6 The guidance would clarify that economic benefits derived from an asset are the potential cash flows that can be obtained directly or indirectly in many ways, for example, by:

(a) using the asset to produce goods or provide services;

(b) using the asset to enhance the value of other assets;

(c) using the asset to fulfil liabilities;

(d) using the asset to reduce expenses;

(e) leasing the asset to another party;

(f) selling or exchanging the asset;

(g) receiving services from the asset;

(h) pledging the asset to secure a loan; and

(i) holding the asset.

3.7 The guidance would further clarify that, for a physical object, such as an item of property, plant and equipment, the economic resource is not the underlying object but a right (or set of rights) to obtain the economic benefits generated by the physical object. Accordingly, although there is a difference in degree between full, unencumbered legal ownership of, for example, a machine and a right to use such a machine for a fixed period under a lease, there is no difference in principle. Both full ownership and the lease give rise to assets, and both provide rights to use the underlying machine, albeit for a period that may be less than the useful life in the case of the leased asset:

(a) in the case of the right to use under a lease, the lessee's right is to obtain some of the benefits generated by the machine—those benefits generated during the period for which the lessee has the right of use; and

(b) in the case of full, unencumbered legal ownership, the owner's right is to obtain all of the benefits generated by the machine throughout its useful life.

3.8 In many cases, economic resources will comprise various different rights. For example, if an entity has legal ownership of a physical object, the economic resource will comprise rights such as:

(a) the right to use the object;

(b) the right to sell the object;

(c) the right to pledge the object; and

(d) legal title to the object (ie any rights conferred by legal title that are not mentioned separately in (a)–(c)).

3.9 In many cases, one party holds all these rights. Sometimes, as in a lease, different parties each hold some of the rights. In those cases, the IASB would need to decide how each party accounts for the rights.

3.10 In many cases, an entity treats all of the rights it holds as a single asset. Nevertheless, an entity would treat some of the rights as one or more separate assets if such a separation produces information that is relevant to users of financial statements and provides a faithful representation of the entity's resources, at a cost that does not exceed the benefits of doing so. Whether rights should be accounted for separately or combined into a single asset is discussed further in Section 9.

3.11 An entity should describe an economic resource in a manner that is clear, concise and understandable. For example, if an entity has legal ownership of a machine and all rights associated with that machine, strictly speaking the entity's asset is the bundle of all rights associated with that machine. However, it would generally be perfectly clear, concise and understandable to describe the entity's asset as a machine, rather than as rights to a machine. More detailed and sophisticated descriptions of the asset would be needed only in less common circumstances in which a summarised or non-technical description would not convey the nature of the asset. Furthermore, it would typically be acceptable, and indeed preferable, to use a concise label on the face of the statement of financial position, providing any necessary details in the notes.

3.12 Sometimes, a single resource contains obligations as well as rights. For example, contracts create a series of rights and obligations for each party. The unit of account (see Section 9) will determine whether the entity accounts for that package as a single asset or a single liability or as one or more separate assets and one or more separate liabilities. Generally, when a package of rights and obligations arises from the same source, an entity will account for them at the highest level of aggregation that enables it to depict the rights and obligations, and the changes in those rights and obligations, in the most relevant, faithful and understandable manner.

3.13 The unit of account will determine whether a contract is viewed as giving rise to a single net right or net obligation, or to one or more separate rights and obligations. Offsetting is not the same as having a single (net) right or a single (net) obligation. When a single (net) right or a single (net) obligation exists in a particular case, the entity has only a single asset or a single liability. For example, suppose that an entity holds an option to buy an asset if it pays CU100 and that the asset has an expected value of CU140.[12] The entity does not have an asset of CU140 and a liability to pay the strike price of CU100. Instead, the entity has an asset of CU40. In contrast, offsetting arises when an entity has both an asset and a liability and recognises and measures them separately, but presents them as a single (net) amount (possibly with disclosure of the separate asset and liability).

3.14 Paragraph 3.5(a) refers to enforceable rights. A right is enforceable if the holder of the right can ensure that it is the party that will receive, and can retain, any economic benefits generated by the right. Enforceability does not mean that the entity can ensure that those economic benefits will arise. For example, shares normally give the holder an enforceable right to receive its share of any dividends that the issuer chooses to pay, even if the holder cannot compel the issuer to declare a dividend.

3.15 The following are examples of items that do not meet the definition of an economic resource and hence do not meet the definition of an asset:

[12] In this Discussion Paper, currency amounts are denominated in 'currency units' (CU).

(a) debt or equity instruments issued by the entity and repurchased and held by it (for example, treasury shares). Similarly, in consolidated financial statements, debt or equity instruments issued by one member of the consolidated group and held by another member of that group are not economic resources of the group. Those instruments are not capable of providing economic benefits to the reporting entity because the reporting entity cannot have a claim on itself. (However, if another party held those equity instruments, they would be an asset for that party because they are capable of providing economic benefits, such as dividends.)

(b) a call option on the entity's own equity instruments. This is not an asset for the issuer of the equity instruments because the underlying equity instruments that would be received on exercise are not an asset for the entity. (However, if another party held that call option, the call option would be an asset for that party, because the equity instruments would be an asset for that party.)

Appendix B

Other comments received

Comment	*Staff reaction*
B1 Provide a natural definition of 'right', such as an 'entitlement to have or do something' (Oxford English Dictionary). This encompasses rights arising under contract, statute or other similar enforceable arrangements that provide rights to resources.	Not clear that this would add clarity.
B2 Provide a definition of contractual rights, as in IAS 32.13 ('an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law')	Will consider in drafting.
B3 Clarify that 'rights' are not limited to contractual rights, but also include, for example, rights arising under statute.	Paragraph 3.5(a) already makes this point.
B4 Can an entity control know-how, customer relationships and existing work force? If so, when? These have been the difficult cases in the past.	Paragraph 3.14 clarifies that a right is enforceable if the holder can ensure that it is the party that will receive, and can retain, any economic benefits generated by the right. Enforceability does not mean that the entity can ensure that those economic benefits will arise.
B5 The distinction between an asset and economic rights to an asset may not be clear in some cases. For example, if an entity has an interest in a building through a joint operating agreement, should the entity characterize the asset as a direct interest in the building that it does not control or as the right to the economic benefits of the asset which it controls (rights to cash flows)? There should be some discussion at the concepts level of this distinction, which is also important for derecognition.	Will consider in drafting
B6 Paragraph 3.5(d) states that some assets, particularly many services, are consumed immediately on receipt. This is circular. The right to these services might be an economic resource, not the service, because the	IFRS 15, paragraph 33 states that goods and services are assets, even if only momentarily, when

Comment	*Staff reaction*
services are consumed and thus of no future value. Moreover, in reality, transactions are not accounted for like this.	they are received and used (as in the case of many services). In the staff's view, this reasoning is still valid.
B7 Definitions of economic resource and 'economic benefits' should exclude economic benefits produced exclusively by the reporting entity (eg own shares, or shares of a parent whose only investment is in the reporting entity).	Paragraph 3.15 clarifies this.
B8 Inherent in treasury shares are a number of rights which can be controlled and monetised by the entity and which would therefore appear to satisfy the proposed definition of an asset. Therefore to exclude treasury shares from recognition as an asset is a standard-level decision not a conceptual principle.	Paragraph 3.15 clarifies that an entity cannot have a claim on itself.

Appendix C
Extracts from the amendments to IAS 16 and IAS 38

Extract from IAS 16

62A A depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate. The revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits of the asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

Extract from IAS 38

98A There is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. The revenue generated by an activity that includes the use of an intangible asset typically reflects factors that are not directly linked to the consumption of the economic benefits embodied in the intangible asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed. This presumption can be overcome only in the limited circumstances:

(a) in which the intangible asset is expressed as a measure of revenue, as described in paragraph 98C; or

(b) when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.

98B In choosing an appropriate amortisation method in accordance with paragraph 98, an entity could determine the predominant limiting factor that is inherent in the intangible asset. For example, the contract that sets out the entity's rights over its use of an intangible asset might specify the entity's use of the intangible asset as a predetermined number of years (ie time), as a number of units produced or as a fixed total amount of revenue to be generated. Identification of such a predominant limiting factor could serve as the starting point for the identification of the appropriate basis of amortisation, but another basis may be applied if it more closely reflects the expected pattern of consumption of economic benefits.

98C In the circumstance in which the predominant limiting factor that is inherent in an intangible asset is the achievement of a revenue threshold, the revenue to be generated can be an appropriate basis for amortisation. For example, an entity could acquire a concession to explore and extract gold from a gold mine. The expiry of the contract might be based on a fixed amount of total revenue to be generated from the extraction (for example, a contract may allow the extraction of gold from the mine until total cumulative revenue from the sale of gold reaches CU2 billion) and not be based on time or on the amount of gold extracted. In another example, the right to operate a toll road could be based on a fixed total amount of revenue to be generated from cumulative tolls charged (for example, a contract could allow operation of the toll road until the cumulative amount of tolls generated from operating the road reaches CU100 million). In the case in which revenue has been established as the predominant limiting factor in the contract for the use of the intangible asset, the revenue that is to be generated might be an appropriate basis for amortising the intangible asset, provided that the contract specifies a fixed total amount of revenue to be generated on which amortisation is to be determined.

Extract from Basis for Conclusions on IAS 16

BC33A The IASB decided to amend IAS 16 to address the concerns regarding the use of a revenue-based method for depreciating an asset. The IASB's decision was in response to a request to clarify the meaning of the term 'consumption of the expected future economic benefits embodied in the asset' when determining the appropriate amortisation method for intangible assets of service concession arrangements (SCA) that are within the scope of IFRIC 12 *Service Concession Arrangements*. The issue raised is related to the application of paragraphs 97–98 of IAS 38 *Intangible Assets* although the IASB decided to address the issue broadly, rather than limit it only to intangible assets arising in an SCA.

BC33B The IASB observed that a revenue-based depreciation method is one that allocates an asset's depreciable amount based on revenues generated in an accounting period as a proportion of the total revenues expected to be generated over the asset's useful economic life. The total revenue amount is affected by the interaction between units (ie quantity) and price and takes into account any expected changes in price.

BC33C The IASB observed that paragraph 60 of IAS 16 states that the depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. The IASB noted that even though revenue could sometimes be considered to be a measurement of the output generated by the asset, revenue does not, as a matter of principle, reflect the way in which an item of property, plant and equipment is used or consumed. The IASB observed that the price component of revenue may be affected by inflation and noted that inflation has no bearing upon the way in which an asset is consumed.

BC33D On the basis of the guidance in IAS 16, the IASB proposed to clarify in the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation* (Proposed amendments to IAS 16 and IAS 38) (the 'ED') that a method of depreciation that is based on revenue generated from an activity that includes the use of an asset is not appropriate, because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset.

BC33E During its redeliberations of the ED the IASB decided to reaffirm its conclusion that the use of a revenue-based method is not appropriate, because the principle in paragraph 60 of IAS 16 is that the "depreciation method shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity". A method that is based on revenue generated from an activity that includes the use of an asset would be, in contrast, a method based on the generation of future economic benefits from the use of the asset. As a result of the feedback received on the ED, the IASB also decided not to retain the comments that it had included in the Basis for Conclusions on the ED on the limited circumstances in which a revenue-based method gives the same result as a units of production method. Many respondents to the ED found these comments contradictory to the guidance proposed in the Standard.

BC33F In the ED the IASB proposed to provide guidance to clarify the role of obsolescence in the application of the diminishing balance method. In response to the comments received about the proposed guidance the IASB decided to change the focus of this guidance. The IASB decided to explain that expected future reductions in the selling price of an item could indicate the expectation of technical or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in the asset. The IASB noted that the expectation of technical or commercial obsolescence is relevant for estimating both the pattern of consumption of future economic benefits and the useful life of an asset. The IASB noted that the diminishing balance method is an accepted depreciation methodology in paragraph 62 of IAS 16, which is capable of reflecting an accelerated consumption of the future economic benefits embodied in the asset.

BC33G Some respondents to the ED suggested that the IASB should define the notion of 'consumption of economic benefits' and provide guidance in this respect. During its redeliberations the IASB decided against doing so, noting that explaining the notion of consumption of economic benefits would require a broader project.

Extracts from Basis for conclusions on IAS 38

Paragraphs BC72B-BC72E and BC72K-BC72L are not included below, because they are almost identical to paragraphs BC33A-BC33D and BC33F-BC33G of the Basis for Conclusions on IAS 16. Paragraphs BC72F-72J address cases where revenue could reflect the pattern in which the future economic benefits of the intangible asset are expected to be consumed

BC72F During its redeliberations of the ED the IASB decided to include a rebuttable presumption that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in the intangible asset. The IASB also considered the question of whether there could be circumstances in which revenue could be used to reflect the pattern in which the future economic benefits of the intangible asset are expected to be consumed.

BC72G In finalising the proposed amendments to IAS 38, the IASB decided to make clear in the Standard that the presumption precluding the use of revenue as a basis for amortisation could be overcome in two circumstances. One of those circumstances is when it can be demonstrated that revenue is highly correlated with the consumption of the economic benefits embodied in an intangible asset. The IASB also noted that another circumstance in which revenue could be used is when the right embodied by an intangible asset is expressed as a total amount of revenue to be generated (rather than time, for example), in such a way that the generation of revenue is the measurement used to determine when the right expires. The IASB noted that, in this case, the pattern of consumption of future economic benefits that is embodied in the intangible asset is defined by reference to the total revenue earned as a proportion of the contractual maximum and, consequently, the amount of revenue generated contractually reflects the consumption of the benefits that are embodied in the asset.

BC72H The IASB also analysed situations in which an intangible asset is used in multiple activities to provide multiple revenue streams. Some respondents commented that the application of a units of production method did not seem practicable, because the units of production were not homogeneous. For example, the producer of a motion picture will typically use the intellectual property embodied in the film to generate cash flows through exhibiting the film in theatres, licensing the rights to characters to manufacturers of toys and other goods, selling DVDs or digital copies of the film and licensing broadcast rights to television broadcasters. Some respondents thought that the best way to amortise the cost of the intellectual property embodied in the film was to use a revenue-based method, because revenue was considered a common denominator to reflect a suitable proxy of the pattern of consumption of all the benefits received from the multiple activities in which the intellectual property could be used.

BC72I The IASB acknowledged that determining an appropriate amortisation method for situations in which an intangible asset is used in multiple activities, and generates multiple cash flow streams in different markets, requires judgement. The IASB considered suggestions that an intangible asset should be componentised for amortisation purposes in circumstances in which the asset is used to generate multiple cash flow streams. It observed that separating an asset into different components is not a new practice in business or in IFRS—it is routinely done for property, plant and equipment and IAS 16 provides guidance in this respect—but refrained from developing guidance in this respect for intangible assets.

BC72J The IASB also decided to provide guidance on how an entity could identify an amortisation method in response to some respondents who observed that further guidance was required in the application of paragraph 98 of IAS 38, which is limited to providing a description of the amortisation methods most commonly used. During its deliberations the IASB determined that, when choosing an amortisation method, an entity could determine the predominant limiting factor for the use of the intangible asset. For example, a contract could be limited by a number of years (ie time), a number of units produced or an amount of revenue to be generated. The IASB clarified that identifying such a predominant limiting factor is only a starting point for the identification of the amortisation method and an entity may apply another basis if the entity determines that it more closely reflects the expected pattern of consumption of economic benefits.