STAFF PAPER

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IASB Meeting

Project	**Conceptual Framework**
Paper topic	Definitions of income and expenses

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Purpose of paper

1. Chapter 4 of the Exposure Draft *Conceptual Framework for Financial Reporting* ('the Exposure Draft'):
   - (a) identified 'income' and 'expenses' as the elements of the statement(s) of financial performance,
   - (b) proposed definitions for those elements; and
   - (c) discussed aspects of the definitions—but without carrying forward some of the discussion of types of income and expenses from the existing *Conceptual Framework.*
2. This paper considers whether the Board should make any changes to these proposals in the light of responses to the Exposure Draft.

Summary of staff recommendations

3. The staff recommend that:

   (a) the *Conceptual Framework* definitions of income and expenses should be those proposed in the Exposure Draft (see paragraphs 4-14); and

   (b) the chapter of the revised *Conceptual Framework* that defines the elements of financial statements:

      (i) should discuss some of the typical types of transactions and other events that may give rise to income and expenses; but

      (ii) should not discuss the presentation of items of income and expenses (see paragraphs 15–40).

Definitions of income and expenses

Exposure Draft proposals

Proposed definitions (paragraphs 4.4, 4.8, 4.9, BC4.2-4.3 and BC4.104)

4. The existing *Conceptual Framework* identifies income and expenses as the elements of financial performance, and defines those elements in terms of changes in assets and liabilities.

5. The Exposure Draft proposed no major changes to this approach. It proposed minor changes to the definitions to simplify them and align the terminology with that proposed for the definitions of an asset and a liability.

	Existing definitions	Proposed definitions
Income	Increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.	Increases in assets or decreases in liabilities that result in increases in equity, other than those relating to contributions from holders of equity claims.
Expenses	Decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.	Decreases in assets or increases in liabilities that result in decreases in equity, other than those relating to distributions to holders of equity claims.

Additional concepts to support the definitions (paragraphs 4.50-4.52 and 5.8)

6. In response to concerns that the (existing and proposed) definitions of income and expenses give undue primacy to the statement of financial position, the Exposure Draft emphasised that:

   (a) information about income and expenses is as important as information about assets and liabilities; and

   (b) important decisions on, for example, recognition and measurement are driven by considering the resulting information in both the statement of financial position and the statement(s) of financial performance.[1]

7. The Exposure Draft also carried forward from the existing *Conceptual Framework* a discussion of the role of ‘matching’ in recognition of income and expenses. Paragraph 5.8 of the Exposure Draft proposed that, although the recognition of assets or liabilities sometimes results in the simultaneous recognition of both income and related expenses (sometimes referred to as the matching of costs with income), the proposed concepts do not allow the recognition of items that do not meet the definitions of assets or liabilities.

[1] Exposure Draft, paragraphs 4.52, 5.9, 6.53 and BC4.3.

Feedback from respondents

8. Most respondents either made no comment on the proposed definitions and accompanying guidance, or said that they agreed with the Exposure Draft proposals not to make major changes to the existing definitions. A few of those who agreed with the proposed definitions said that they:

    (a) welcomed the simpler definitions; or

    (b) agreed that income and expenses should be defined by reference to changes in assets and liabilities, rather than by attempting to match income and related costs. In support of this position, a few respondents said that such matching approaches could be difficult to develop and have unwelcome consequences. Perfect matching of income and expenses is achievable only under conditions of complete certainty and matching approaches can result in deferral balances that do not meet the definitions of assets or liabilities.

9. Some respondents disagreed with the proposal to make no major changes to the existing definitions:

    (a) most of those respondents, predominantly Europeans and including some users of financial statements, expressed concerns that, in their view, the (existing and proposed) definitions:

        (i) imply a primacy of the statement of financial position over the statement(s) of financial performance;

        (ii) give insufficient weight to the importance of income and expenses; or

        (iii) raise questions of whether changes in fair value are income.

    (b) some of this group said they would prefer the overriding concept for recognising and measuring performance to be based on matching of income and related costs, or for income and expenses to be defined more directly by reference to transactions in the period. One respondent further observed that not all changes in assets and liabilities give rise to income or expenses—some give rise to equal but opposite changes in other assets and liabilities.

(c) a few academics and individuals suggested completely different definitions of income and expenses. Suggestions included:

(i) defining income as value-generating activities, and expenses as value-sacrificing activities;

(ii) focusing on wealth generation in the operating cycle;

(iii) defining income in terms of additional amounts available for spending, and expenses as the costs matched with that income; and

(iv) defining income and expenses by reference to realised and realisable gains and losses, or gains and losses from normal operations.

10 A few European respondents explicitly welcomed the statement in the Exposure Draft that information about income and expenses is just as important as information about assets and liabilities (some adding that many preparers and users of financial statements regard information about income, expenses and cash flows as *more* important). A European standard-setting body suggested that, in cases where application of the definitions would not result in matching of income and expenses, the Board should carefully consider whether the resulting information is relevant.

11 Some respondents suggested refinements to the proposed definitions. Suggestions for refinement are listed in Appendix A.

Staff analysis

12 The staff do not think that the Board should explore further any of the suggestions for major changes to the definitions of income and expenses:

(a) the Board considered the views expressed in paragraphs 9(a) and 9(b) during the development of the Exposure Draft. In the Basis for Conclusions accompanying the Exposure Draft it acknowledged those views (BC4.2), before setting out its reasons for retaining the existing approach that defines income and expenses in terms of assets and liabilities (BC4.3). Most respondents either explicitly agreed with the Board's views or implicitly accepted them by raising no concerns.

(b) the *Conceptual Framework* will emphasise that the proposed definitions do not imply a primacy of the statement of financial position over the statement(s) of financial performance.

(c) the Board expressed a view in the Basis for Conclusions accompanying the Exposure Draft that no major problems have been identified with the existing definitions (BC4.104). Respondents to the Exposure Draft did not identify any practical problems of which the Board was previously unaware. Therefore, the staff do not think the Board needs to consider the completely different definitions suggested in paragraph 9(c).

13 Furthermore, the staff do not think that the Board should refine the proposed definitions in response to any of the suggestions listed in Appendix A. Each of those refinements was suggested by only a few (often only one) respondent. And in each case, the staff think that the possible disadvantages would outweigh any advantages—see the individual explanations in Appendix A.

Staff recommendation

14 For the reasons in paragraphs 12 and 13, the staff recommend that the *Conceptual Framework* definitions of income and expenses should be those proposed in the Exposure Draft (see paragraph 5).

Question for the Board

Question 1—Definitions of income and expenses
Do you agree with the staff recommendation?

Further discussion of income and expenses

Exposure Draft proposals (paragraphs BC4.105)

15 The Exposure Draft proposed *not* to carry forward from the *Conceptual Framework* some existing discussion of specific types of income and expenses—namely gains, losses and revenue. The relevant section from the existing *Conceptual Framework* is reproduced in Appendix C to this paper. It includes a definition of revenue that is also used in IFRS 15 *Revenue from Contracts with Customers*.

16 The Basis for Conclusions accompanying the Exposure Draft explained that:

> BC4.105 Much of the discussion of income and expenses in the existing *Conceptual Framework* relates to their presentation and disclosure. Presentation and disclosure are discussed in Chapter 7 of the Exposure Draft. … The IASB thinks that [the rest of the discussion] was originally included to emphasise that income includes revenue and gains, and expenses include losses. The IASB thinks that emphasis is now unnecessary and the implication that the *Conceptual Framework* defines subclasses of income and expenses is unhelpful. The IASB does not expect the removal of that material to cause any changes in practice. …

Feedback from respondents

17 Some respondents, including several users of financial statements, disagreed with the proposal to remove from the *Conceptual Framework* the existing discussion of types of income and expenses or, more specifically, the definition of revenue. They argued that:

(a) the existing discussion is helpful and should be kept for completeness because it assists with establishing concepts of financial performance and profit or loss and makes the *Conceptual Framework* more robust.

(b) removing the discussion could indicate that the statement(s) of financial performance are less important than indicated by the existing *Conceptual Framework*.

(c) the distinction between revenue and gains is important in jurisdictions where revenue (or income) can be used as a determinant for regulatory reporting thresholds.

(d) revenue is a key performance indicator and not adequately described by the definition of income.

(e) the *Conceptual Framework* should continue to discuss the notion of 'ordinary activities', which has broad application, particularly in relation to alternative performance measures and to distinguishing revenue from other income.

(f) the discussion should be retained but would be more logically placed in the chapter on presentation and disclosure.

18 An organisation representing users of financial statements suggested that:

(a) it was important to note that different types of income have different levels of usefulness to users; and

(b) it would be useful to clarify that income and expenses include both inflows/outflows and enhancements/depletions of assets and liabilities.

19 A standard-setting body noted that IFRS 15 defines both 'revenue' and 'customer' by reference to an entity's ordinary activities. However, the Board had rejected requests for IFRS 15 to clarify the meaning of 'ordinary activities' because the notion of ordinary activities was derived from the definition of revenue in the *Conceptual Framework*. The standard-setting body suggested that, if the Board removes the term 'ordinary activities' from the *Conceptual Framework*, it should consider explaining the term better at a Standards level.

20 A few respondents commented on the income and expenses that arise when an entity receives services in exchange for share-based payments:

(a) some suggested that the ‘expenses’ required to be recognised as a result of equity-settled share-based payments do not meet the proposed definitions of expenses because there is no change in liabilities or in equity;

(b) others suggested that to address possible misunderstandings, the *Conceptual Framework* should clarify why income and expenses can arise when there is no net change in equity. The reason is that there are two equal but opposite changes to equity, one of which arises from the consumption of an asset and hence meets the definition of an expense.

21 Respondents suggested other more minor additions and changes to the guidance accompanying the definitions of income and expenses. Their suggestions are listed in Appendix B.

Staff analysis

22. This analysis is structured as follows:

(a) Concepts discussing different types of income and expenses (paragraphs 23–36)

(b) Concepts for presentation of income and expenses (paragraph 37)

(c) Other suggestions from respondents (paragraph 38)

Concepts discussing different types of income and expenses

23. The existing *Conceptual Framework* discussion of performance, and of income and expenses, not only discusses presentation; it also has some discussion of the underlying economic phenomena.

24. For example, apart from presentation, the existing *Conceptual Framework* (see Appendix C) discusses income and expenses arising from:

(a) sales, fees, interest, dividends, royalties and rent;

(b) disposal of non-current assets;

(c) changes in value of marketable securities and long-term assets;

(d) cost of sales, wages and depreciation;

(e) disasters such as fire and flood; and

(f) the effects of increases in the rate of exchange for a foreign currency.

25. The reaction of respondents suggested that the proposed removal of all of the existing discussion was perhaps a step too far.

26. Furthermore, while the Exposure Draft proposed detailed discussion to support the definitions of assets and liabilities, it proposed less discussion to support the definitions of income and expenses. The discussion supporting the definitions of assets and liabilities included concepts explaining the rights, obligations and economic benefits that constitute assets and liabilities (for example paragraphs 4.28 and 4.8 of the Exposure Draft). Some of that discussion was adapted from the existing *Conceptual Framework*. In contrast, to support the definitions of income and expenses, paragraph 4.51 simply stated that income and expenses include amounts generated by transactions and other events, including changes in the carrying amounts of assets and liabilities. The Exposure Draft did not provide a more detailed discussion of the transactions and other events that give rise to such changes.

27. Some discussion of income and expenses was included in the Exposure Draft, but was dispersed throughout subsequent chapters on recognition, measurement and presentation. For example, Table 6.1 in the proposed Exposure Draft chapter on measurement included a number of references to various types of income and expenses.

28. Other chapters of the Exposure Draft contained references to income and expenses arising from the following:

(a) sales of goods and provision of services;

(b) consumption of goods and services;

(c) enhancement of economic resources;

(d) impairment of economic resources;

(e) interest, rent and royalties paid and received;

(f) fulfilment of obligations;

(g) changes arising from the passage of time, such as the time value of money;

(h) changes in the price of an asset, or changes in the present value of future cash flows estimated to arise from the economic resources;

(i) changes in the price of a liability, or changes in the present value of future cash flows estimated to be incurred in fulfilling the liability; and

(j) changes in own credit risk.

29. In addition to the discussions above, there are, in existing IFRS Standards, references to additional economic phenomena that give rise to income and expenses. For example, IFRS 13 *Fair Value Measurement*, paragraph B9 notes that changes in the fair value of an asset not only encompass physical deterioration, they also encompass functional (technological) obsolescence and economic (external) obsolescence.

30. The staff think that it might be useful to discuss, with the definitions of income and expenses, some of the transactions and other events that give rise to income and expenses. Doing so might:

(a) provide a more balanced discussion between the financial position elements (assets and liabilities) and the financial performance elements. Providing some discussion of the underlying economic phenomena would help reinforce the views that information about financial performance is equally as important as information about financial position.

(b) help demonstrate that the elements depict real world economic phenomena, and are not just abstract accounting concepts. The proposed (and existing) definitions of income and expenses are derived from the definitions of assets and liabilities. The structure of the definitions may give the impression that income and expenses are simply mechanical consequences of assets and liabilities.

(c) help explain how income and expenses arise simultaneously with a contribution from, or distribution to, holders of equity claims (such as the immediate consumption of services paid for by issuing equity instruments). Such explanation could help explain why income and expenses arise from share-based payments for employee services.

31. Having a discussion of the underlying economic phenomena accompanying the definitions of income and expenses would also lay the foundations for further discussion in subsequent chapters on recognition, measurement and presentation. As noted in a response from a user representative group (paragraph 18), it is the underlying economic phenomena that are of interest to users of financial statements. Recognition, measurement and presentation are the processes of capturing, quantifying and presenting useful information about those economic phenomena. Paragraph 2.21 of the Exposure Draft notes that the first step in applying the qualitative characteristics is to identify an economic phenomenon that is capable of being useful to users of the reporting entity's financial information.

32. The discussion in the elements chapter of the economic phenomena (transactions and other events) that give rise to income and expense would not extend to a discussion of matters that are more appropriately discussed in later chapters (for example, recognition, measurement or presentation). This would allow the later chapters to focus on the application of the qualitative characteristics to determine what information about the phenomena should be provided in financial statements. That is, subsequent chapters could discuss which of those phenomena should be recognised and how they should be measured, and if they are recognised and measured, how they might be best presented.

33. The discussion that accompanies the definitions of income and expenses could simply include a non-exhaustive list of typical transactions and other events that result in income or expenses. This could be similar to the discussion of the typical rights and obligations that the Exposure Draft included for assets and liabilities. It could also highlight the *variety* of transactions and other events that give rise to income and expenses. The different characteristics of these economic phenomena are one of the factors to be considered for recognition, measurement and presentation.

34. The list should not be exhaustive or too definitive, allowing the Board to address specific issues for particular types of income and expense when developing Standards. Thus, we do not think that this list should refer to revenue, gains and losses and should not define items by reference to the entity's ordinary activities. The existing *Conceptual Framework* does not explain what 'ordinary activities' means, and simply having that term in the *Conceptual Framework* does not help interpret what it means. Therefore, the removal of this material should not cause any changes in practice.

35. If the discussion of income and expenses is limited to aspects that are already part of the existing *Conceptual Framework*, or were included in other chapters of the Exposure Draft, then the staff does not think that the suggested changes would require re-exposure.

36. If a discussion of transactions and events that give rise to income and expenses is included in the revised *Conceptual Framework*, it might be important to emphasise that the discussion does not imply that all such transactions and events will be captured in the accounting process (ie through recognition and measurement). Likewise, the application of the recognition criteria and the selection of measurement bases may result in different recognition and measurement requirements for income and expenses that arise from different economic phenomena. A similar statement is made for assets and liabilities in paragraph 3.6 of the Exposure Draft.

Concepts for presentation of income and expenses

37. In the staff's view, the Board should confirm its proposal to not discuss the presentation of items of income and expenses as part of the chapter defining the elements of financial statements. Thus, for example, there would be no discussion of whether to present some items gross or net. The existing *Conceptual Framework* does not have a presentation and disclosure chapter. However the revised *Conceptual Framework* will have a presentation and disclosure chapter and the staff think that any discussion of the presentation of income and expenses should be in that chapter. A more detailed discussion of the specific presentation of particular items of income and expenses would be a matter for the Board to consider when developing Standards.

Other suggestions

38 The staff have considered the more minor additions and changes to the guidance suggested by respondents and listed in Appendix B. In each case, and as explained in Appendix B, we think that we could address the suggestion at the drafting stage, or that no further action is needed. We will not raise any of these suggestions for discussion in the Board meeting unless requested to do so by a Board member.

Staff recommendation

39. On the basis of the above discussion, the staff recommend that the chapter of the revised *Conceptual Framework* that defines the elements of financial statements:

(a) should discuss some of the typical types of transactions and other events that may give rise to income and expenses; but

(b) should not discuss the presentation of items of income and expenses.

40. For the latter recommendation, we suggest including examples such as those listed below. We would consider the exact wording in more detail when drafting, to ensure, among other things, consistency with references to income and expenses in other chapters of the revised *Conceptual Framework*

4.X Income and expenses may arise from, for example:

(i) selling goods, and providing services;

(ii) exchanging assets or liabilities;

(iii) fulfilling liabilities;

(iv) producing goods, or other assets;

(v) consuming goods, services, or other assets;

(vi) enhancements of assets including physical, functional (technological) or economic (external) enhancements;

(vii) impairment of other assets through physical deterioration, or functional (technological) or economic (external) obsolescence; or

(viii) changes in the current value of an asset or a liability;

4.XA Goods and services that are received and immediately consumed (for example, employee services) sometimes arise simultaneously with contributions from holders of equity claims (for example, share-based employee payment schemes). Even though there is no net change in equity, the consumption of the economic resource received is an economic phenomenon that meets the definition of an expense, whereas the contribution of that economic resource by issuing equity claims does not.

Question for the Board

Question 2—additional discussion of types of income and expenses
Do you agree with the staff recommendation in paragraph 39?

APPENDIX A—Other comments on the definitions of income and expenses

	Respondent comment or suggestion	Reasons for taking no further action
A1	Suggest changing the terminology. The terms ‘income’ and ‘expenses’ are generally understood as referring to inflows and outflows of resources, and not encompassing re-measurements. Use the terms ‘gains’ and ‘losses’ instead. This might allow the terms income and expenses to be used for more specific purposes, for example to refer to those gains and losses that are reported in the statement of profit or loss.	Such a fundamental change in terminology could cause confusion and would have wider consequences (for example a need to reconsider any other terms, such as ‘other comprehensive income’). We do not think that improvements in terminology would be gained by reserving the terms income and expenses for items recognised in the statement of profit or loss.
A2	Suggest definitions should exclude not only contributions from, and distributions to, holders of equity claims but also transactions with parties that exercise control of the entity in other ways.	Adopting this suggestion would add complicity for no obvious benefit.
A3	Suggest omitting the phrase ‘that result in increases/decreases in equity’, either because it is unnecessary or because it seems to preclude identifying income and expenses for transactions that result in no net increase or decrease in equity (such as sales of inventory at cost).	We think it would be better to add clarification (in the supporting guidance) that income and expenses can arise when there is no net change in equity, as per the staff recommendation.
A4	Suggest reversing the definitions, so that income and expenses are defined as increases / decreases in equity, rather than increases/decreases in assets or liabilities.	We are not aware of any problems in practice that this change would help to solve. Any such change carries a risk of unintended consequences.
A5	The proposed definitions do not explain how to distinguish between those changes in assets and liabilities that are presented on a gross basis (such as sales of inventory at their carrying amount, which are accounted for as giving rise to income and expenses of equal amount), and changes in assets and liabilities that are presented on a net basis (such as repayments of debt).	This is also a feature of the existing definitions, and is addressed on a transaction by transaction basis at Standards-level.

	Respondent comment or suggestion	Reasons for taking no further action
A6	Suggest keeping the phrase 'during the accounting period', to comply with the accruals concept and avoid the risk of misinterpretation	Financial statements report the assets and liabilities that are recognised at the end of a reporting period, and the income and expenses that are recognised during that period. Accruals accounting is an outcome of applying the definitions of assets and liabilities.
A7	The proposed definitions are such that reversals of previously recognised income (or expenses) would have to be recognised as expenses (or income), which is inconsistent with current practice.	The staff do not think that any of the changes proposed to the definitions affect the way in which reversals would be presented. .

APPENDIX B—Other suggestions for guidance accompanying the definitions of income and expenses

	Respondent suggestion or comment	Staff recommendation	Reason for staff recommendation
B1	State in the *Conceptual Framework* that sometimes it is more appropriate to measure income and expenses directly, and to measure the resulting assets and liabilities indirectly by reference to the amount of income or expense. Respondents suggested that one IFRS Standard requiring such a direct measurement of income is IFRS 15.	No changes.	We disagree that there are transactions for which it would be necessary to measure income and expenses directly. Applying IFRS 15, the entity is, in effect, measuring the performance obligations, and revenue arises from the reduction in those obligations as delivery occurs.
B2	Clarify the effect of the change from ‘equity participants’ to ‘holders of equity claims’. Explain how the change would affect entities, such as companies limited by guarantee, that have equity participants who do not hold equity claims.	No changes.	‘Equity participants’ was not defined in the existing *Conceptual Framework*. The change simply aligns the definitions with the discussion under ‘equity’. The Board is further considering equity claims as part of the Financial Instruments with Characteristics of Equity research project
B3	Clarify that some changes in assets or liabilities do not give rise to income or expenses but instead to equal but opposite changes in other assets and liabilities.	Add clarification in drafting.	
B4	Clarify that changes in assets and liabilities are not income and expenses if they do not reflect a change in an attribute of an asset or a liability, for example, if the changes arise from a change in an accounting policy or the correction of an error.	No changes.	This point is already well-understood.

	Respondent suggestion or comment	Staff recommendation	Reason for staff recommendation
B5	Redraft paragraph 4.50. That paragraph should say that assessing whether a holder of an equity claim is acting in that capacity is relevant to determining whether a transaction is a contribution or distribution (rather than income or an expense). It is wrong to assert that it 'follows from the definitions of income and expenses' that transactions with holders of equity claims *acting in that capacity* do not give rise to income or expenses	Consider refinements in drafting.	It is possible that the current drafting could be read in a way that was not intended.
B7	Reconsider the statement in paragraph 4.52 of the Exposure Draft that 'income and expenses are the elements of the entity's financial performance'. This paragraph is inconsistent with paragraph 7.21 of the Exposure Draft, which describes income and expenses included in the statement of profit or loss as the 'primary' (but not only) source of information about an entity's financial performance. In place of paragraph 4.52, retain the statement in the existing *Conceptual Framework* that 'profit is frequently used as a measure of performance'. This statement implicitly acknowledges that profit is only one measure of performance, and thus that information in other statements (such as the statement of cash flows) and in the notes can help assess financial performance.	No changes.	Paragraph 7.21is explaining *which* of the statements of financial performance give the primary source of information about performance. Paragraph 7.21 is not suggesting that statements other than the statements of performance (eg the cash flow statement) give information on performance.

	Respondent suggestion or comment	Staff recommendation	Reason for staff recommendation
B8	Enhance the discussion of the role of matching in the provision of useful information. The concept of matching is important in measuring income and expenses, is necessary to provide a conceptual basis for cash flow hedge accounting, and may assist in determining when unrealised gains and losses should be recognised and where they should be presented.	No changes	The *Conceptual Framework* will identify matching as an *outcome* of applying the definitions, not as a concept in its own right. The suggested discussion would be appropriate only if the Board were to change the approach to apply matching as a concept.
B9	Make more explicit the message that matching is not proposed as a concept, and cannot justify the recognition of items that do not meet the definition of an asset or a liability.	No changes	This message is already clearly stated (paragraph 5.8 in the Exposure Draft).

APPENDIX C—Extract from existing *Conceptual Framework*

Performance

4.24 Profit is frequently used as a measure of performance or as the basis for other measures, such as return on investment or earnings per share. The elements directly related to the measurement of profit are income and expenses. The recognition and measurement of income and expenses, and hence profit, depends in part on the concepts of capital and capital maintenance used by the entity in preparing its financial statements. These concepts are discussed in paragraphs 4.57–4.65.

4.25 The elements of income and expenses are defined as follows:

(a) Income is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.

(b) Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

4.26 The definitions of income and expenses identify their essential features but do not attempt to specify the criteria that would need to be met before they are recognised in the income statement. Criteria for the recognition of income and expenses are discussed in paragraphs 4.37–4.53.

4.27 Income and expenses may be presented in the income statement in different ways so as to provide information that is relevant for economic decision-making. For example, it is common practice to distinguish between those items of income and expenses that arise in the course of the ordinary activities of the entity and those that do not. This distinction is made on the basis that the source of an item is relevant in evaluating the ability of the entity to generate cash and cash equivalents in the future; for example, incidental activities such as the disposal of a long-term investment are unlikely to recur on a regular basis. When distinguishing between items in this way consideration needs to be given to the nature of the entity and its operations. Items that arise from the ordinary activities of one entity may be unusual in respect of another.

4.28 Distinguishing between items of income and expense and combining them in different ways also permits several measures of entity performance to be displayed. These have differing degrees of inclusiveness. For example, the income statement could display gross margin, profit or loss from ordinary activities before taxation, profit or loss from ordinary activities after taxation, and profit or loss.

Income

4.29 The definition of income encompasses both revenue and gains. Revenue arises in the course of the ordinary activities of an entity and is referred to by a variety of different names including sales, fees, interest, dividends, royalties and rent.

4.30 Gains represent other items that meet the definition of income and may, or may not, arise in the course of the ordinary activities of an entity. Gains represent increases in economic benefits and as such are no different in nature from revenue. Hence, they are not regarded as constituting a separate element in this *Conceptual Framework*.

4.31 Gains include, for example, those arising on the disposal of non-current assets. The definition of income also includes unrealised gains; for example, those arising on the revaluation of marketable securities and those resulting from increases in the carrying amount of long-term assets. When gains are recognised in the income statement, they are usually displayed separately because knowledge of them is useful for the purpose of making economic decisions. Gains are often reported net of related expenses.

4.32 Various kinds of assets may be received or enhanced by income; examples include cash, receivables and goods and services received in exchange for goods and services supplied. Income may also result from the settlement of liabilities. For example, an entity may provide goods and services to a lender in settlement of an obligation to repay an outstanding loan.

Expenses

4.33 The definition of expenses encompasses losses as well as those expenses that arise in the course of the ordinary activities of the entity. Expenses that arise in the course of the ordinary activities of the entity include, for example, cost of sales, wages and depreciation. They usually take the form of an outflow or depletion of assets such as cash and cash equivalents, inventory, property, plant and equipment.

4.34 Losses represent other items that meet the definition of expenses and may, or may not, arise in the course of the ordinary activities of the entity. Losses represent decreases in economic benefits and as such they are no different in nature from other expenses. Hence, they are not regarded as a separate element in this *Conceptual Framework*.

4.35 Losses include, for example, those resulting from disasters such as fire and flood, as well as those arising on the disposal of non-current assets. The definition of expenses also includes unrealised losses, for example, those arising from the effects of increases in the rate of exchange for a foreign currency in respect of the borrowings of an entity in that currency. When losses are recognised in the income statement, they are usually displayed separately because knowledge of them is useful for the purpose of making economic decisions. Losses are often reported net of related income.