



Federal Accounting Standards Advisory Board

February 26, 2007

TO: Members of FASAB
FROM: Penny Wardlow, Consultant
THROUGH: Wendy Comes, Executive Director
SUBJECT: **Conceptual Framework: Elements—Draft Final Statement—TAB A**

NOTE: FASAB staff prepares memos and other materials to facilitate discussion of issues at Board meetings. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

This memo provides comments on the principal changes proposed to the Elements ED in the attached copies of a draft final Statement. Attachment 1 is a marked-up copy of the draft and Attachment 2 is a clean copy. Attachment 3 is a draft Basis for Conclusions (BFC), which includes comments from this memo as well as other material that may be useful to readers of the Statement. The Alternative View in the ED is not included in the draft final Statement on the assumption that, if there will be an Alternative View (Dissent), it will be rewritten.

The objective of the meeting is to approve the draft (Statement and BFC), subject to any modifications the Board makes. The next step is for the Board to consider a preballot draft.

Executive Summary

The proposed changes are to conform the Summary to changes in the text of the Statement, which are discussed in the remainder of this memo. The Board may wish to defer consideration of the revised Summary until after deciding on possible changes to the Statement.

Modifications to the Sections on “Recognition” and “Effects of Uncertainty”

The additions the Board made at the January meeting to par. 5 in the “Recognition” section and par. 60 in the “Effects of Uncertainty” section are incorporated into the attached draft. (Former par. 60 is now par. 59.) In considering those sections with the Board’s changes as well as members’ comments during the meeting, I concluded that additional modifications to both sections would make them clearer and help close the gap between the ED (majority) members’

views and the AV members' views. As a result, I have included revised wording in pars. 5 through 8 and 57 through (new) 60. Mr. Dacey reviewed the revised wording and offered some additional changes, which I have incorporated. I believe the revisions enhance both sections and make clearer the relationship between them.

Some members have indicated that the ED does not state clearly enough that the recognition criteria established in par. 5 are necessary but not sufficient conditions for recognition to occur and that the Board intends to address additional recognition issues, primarily measurement issues, including probability, in a future FASAB pronouncement. As you will see in the draft, I am proposing to refer to the recognition criteria as "*basic* recognition criteria" and add a broader discussion of "additional components of recognition decisions." The added discussion indicates that those components will be addressed in a future pronouncement and that the current Statement would not alter relevant existing standards in that regard. This change would replace FN 2 of the ED on that issue and bring its substance into the text. The additional components are identified as comprising primarily measurement issues, which would include assessments of the probability of future inflows and outflows of resources as well as the selection of measurement attributes and methods. Consistent with these proposed changes, I have changed "recognition criteria" to "basic recognition criteria" and added references to "additional components of recognition decisions" in various places in the text. The Glossary now defines "basic recognition criteria" and I have expanded the definition of "measurable" as agreed in January and added a definition of "measurement."

In the section on "Effects of Uncertainty" I have clarified the distinction between measurability and measurement, which some members found confusing in the ED text. Par. 59 includes the Board's changes at the January meeting, with some editing. I also removed some redundancy from the ED version. The revisions also are intended to link the section better to comments on uncertainty in the "Recognition" section and in various places in the "Definition" section. As a result, I believe the section's purpose is clearer and that it rounds off the document better.

<p>Does the Board agree with the modifications to the sections on "Recognition" and "Effects of Uncertainty"?</p>
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Continued Applicability of Qualitative Characteristics and Existing SFFAC

In November, the Board agreed that the qualitative characteristics of information in financial reports should not be repeated in the Statement. This would continue past practice of not repeating concepts or standards from previous pronouncements in new pronouncements when there is no change to the earlier provisions. In this way, constituents can operate on the assumption that previous FASAB statements continue in effect until specifically amended, withdrawn, or superseded. The Board decided, however, that the qualitative characteristics from SFFAC 1 should be listed in the Glossary of the Elements Statement, with a cross-reference to the relevant paragraph of SFFAC 1. This has been done in the attached draft.

It was also suggested that the continued applicability of the qualitative characteristics and prior concepts statements be made clearer in the text of the "Statement of Federal Financial Accounting Concepts" (page just before the Table of Contents). The purpose of that "Statement"

is to describe the role of the Board's conceptual framework and the SFFACs. I have strengthened that page by including "qualitative" before "characteristics" in the third paragraph, by listing the existing concepts statements, including the one on Elements (No. 5) at the end of the page, and by revising the last sentence, about the continuity of SFFACs and other FASAB pronouncements. I have also amplified the reference to continuity of concepts in the "Introduction," at the end of par. 1.

<p>Does the Board agree with the modifications to clarify the continued applicability of the qualitative characteristics and existing SFFACs?</p>
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Modifications to the Introduction

The proposed modifications to par. 1 are referred to above.

In par. 2, I propose removing "revenues" and "expenses" from the "such as" example. A respondent to the ED points out that it is inconsistent and confusing to mention "net position" in par. 3 but not in par. 2. I do not think it is confusing because par. 2 is talking about the meaning of the term "elements" and giving some examples, whereas par. 3 is stating specifically which elements are defined in the Statement. The respondent suggests adding "net position" to par. 2. However, I think it is even more confusing to state that one is citing *examples* of elements ("such as") and then include *all* of them, as restated in paragraph 3. I recommend limiting the examples in par. 2 to "assets" and "liabilities" and then listing in par. 3 all the elements defined in the Statement, as currently.

A glitch in the formatting has placed all the footnotes for the entire document on the first page of the Statement. The footnote numbers are, however, in the appropriate paragraphs throughout the text. The placement of the footnotes will be corrected.

Modifications to the Section on "Entity Concept"

The proposed changes are to conform to the modifications to the "Recognition" section discussed earlier.

Modifications to the Section on "Assets"

Asset definition: I propose changing "can control" to "is able to control." The latter wording was originally in the definition but some members preferred "could" which subsequently was changed to "can," mainly because "could" is a conditional and leaves one wondering what the condition is. Two respondents to the ED indicate that they would prefer to eliminate "can" and simply say "that the federal government controls." Both respondents say that "can" might be interpreted as applying only to the future, i.e., "might control in the future," whereas the definition is referring to the present (the balance sheet date), regardless of what might happen in the future. In my view, to say "that the federal government controls" generally would be interpreted that the government has to be actively controlling the economic benefits or services (or access to them) at the balance sheet date. I believe that is not an essential characteristic of an

asset. As long as the government *is able to* control the benefits/services, it has an asset, even if at the balance sheet date the government chooses not to actively exercise that control. For example, the government might be willing currently to allow other entities free access at will to the economic benefits or services embodied in its asset, without relinquishing its right to regulate or deny that access and obtain the benefits for itself at a future date. In that case, the government *is able to* control access but does not *control* access at the present time.

The proposed changes in par. 18 are to conform to the modifications to the “Recognition” section discussed earlier. (Similar conforming changes are proposed in par. 39, under “Definition of a Liability” and par. 54, under “Definitions of Revenue and Expense.”)

In par. 19, one respondent requests a definition of “essential characteristics” and another thinks the phrase “fundamental or essential” in the ED is ambiguous. I propose to delete “fundamental” and to include a definition of “essential characteristics” in par. 19 and in the Glossary. The Glossary definition refers to both assets and liabilities. (Par. 40 on “Essential Characteristics of Liabilities” includes an abbreviated version of the definition in the Glossary.)

The changes in the subsection that expands on the “Essential Characteristics of Assets” are proposed mainly to conform to the modifications to the “Recognition” section and the change from “can control” to “is able to control” in the definition of assets, as discussed earlier. I also propose expanding the discussion of “ability to control” in par. 28.

<p>In the “Assets” section, does the Board agree with the proposed modifications to the definition and the subsequent discussion of the essential characteristics of an asset?</p>

Modifications to the Section on Liabilities

The modifications proposed to pars. 39 and 40 are equivalent to those discussed earlier for assets.

Liability definition: Five respondents (2 federal auditors, 1 non-federal auditor, and 2 non-federal “other”) to the ED Question for Respondents on the essential characteristics of a liability say that the “settlement” characteristic is not essential. (One of the committee responses also indicates that some of their members take that view, whereas others agree with the ED position.) The settlement characteristic is “that the government and the other entity involved have an agreement or understanding concerning settlement” (par. 45). Two of the respondents who disagree with the “settlement” characteristics give the following reasons:

It is possible for two parties to agree that an amount is owed by one party to the other, but disagree on, or be in the process of negotiations about, the timing of the settlement. Under such circumstances, there would clearly be a liability. We note that the IPSAS definition of liabilities does not require an agreement between the two parties. [031—Non-federal Other]

Whether or not the government is free to decide when to settle the obligation should not affect whether a liability exists. Uncertainty as to the timing of settlement would impact the

measurement of the liability. The existence of a liability should be based solely on whether a present obligation exists which arose as a result of a past transaction or other event and has not yet been settled. [038—Non-federal auditor]

The Board discussed the “settlement” characteristic before issuing the ED and agreed that if the government *alone* can determine whether and when to settle an obligation then it does not qualify as a liability. A liability always is between two separate entities. There must be some agreement or “meeting of the minds” as to whether an obligation exists and what circumstances would trigger settlement. The two respondents cited above imply that the FASAB is saying that the timing of settlement must be agreed between the two parties. However, the Board is not saying that. As stated in par. 45 of the ED:

. . . The timing of settlement often is expressed in contracts and other agreements as a specific or determinable date. However, in some cases the parties agree that settlement will be triggered by a specific event or by the demand of the recipient of the assets or services, the timing of which may be uncertain. If the government and the other entity do not have an agreement or understanding concerning settlement *and the government is free to decide whether and when to settle the obligation*, the government’s obligation does not meet the definition of a liability. (emphasis added)

Par. 46 indicates that both the timing and the amount of the settlement may be uncertain, but that “Uncertainty regarding the amount or timing of settlement is addressed through measurement of the liability.” There is no indication that there is uncertainty about whether the government has a liability “to provide assets or services to another entity” (definition, par. 38) simply because the precise settlement date is unknown.

The Board may wish to consider that one of the essential characteristics of a liability that is identified in FASB Concepts Statement 6, par. 36) is that a liability:

. . . embodies a present duty or responsibility to one or more other entities that entails settlement by probable future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand. . .

Also, eighteen respondents to the question in the ED support both of the essential characteristics proposed in the ED. One of those respondents (024—Non-federal Other) indicates at first that “the words ‘at a determinable date, when a specified event occurs, or on demand’ in the definition . . . do not seem to add anything.” However, the respondent states that he agrees with the statement in par. 45 of the ED that “if the government can determine *whether* and when the liability can be settled it is not a liability.” He adds that “the word *whether* is very important here. If you can decide whether you will pay, you do not have a present obligation.” (emphasis in the original) Another respondent (040—Non-federal Other) seems to be thinking along similar lines with the comment that the “settlement” characteristic is not really a separate characteristic but is part of the “present obligation” characteristic.

After considering the various responses, I recommend that the Board retain the “settlement” characteristic as a separate essential characteristic of liabilities. Although there is merit in concluding that it is part of the “present obligation” characteristic, I believe it is significant

enough to be presented as a separate characteristic and, therefore, included in the definition of a liability.

An additional respondent recommends that the Board add a third essential characteristic, taken from par. 44 of the ED—namely, that:

To meet the definition of a liability, the federal government’s contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. . . (emphasis in the original)

The respondent believes that the concept in par. 44 results in the idea of a present obligation and should be elevated to an essential characteristic. I recommend against that step. The notion of “existing conditions” in par. 44 is not a separate or unique notion developed specifically for this concepts statement. Rather, it is consistent with the long-standing, general accounting principle that financial statements report transactions or other events that already have occurred. The Board discussed par. 44 at the November 2006 meeting and a majority voted to reaffirm the substance of par. 44.

Except for the few respondents who advocate changes in the essential characteristics of liabilities, respondents generally do not propose changes in the liability definition. Exceptions are those (few) respondents who say the Board should adopt the definition of a liability in FASB Concepts Statement 6 and/or should adopt the probability notions in SFAS 5 or SFFAS 5. The Board has discussed these issues and has concluded that the FASAB should *not* adopt the FASB Concepts Statement 6 definition. One reason is that the FASB definition indicates that the liability is the future sacrifice of assets, whereas the FASAB has concluded that the liability is the present obligation to provide assets or services in the future. Information available to date on the IASB/FASB joint conceptual framework project indicates that the two boards also have (tentatively) concluded that the liability is the present obligation and not the probable future sacrifice of assets, and that the asset is the entity’s present resource, not the probable future economic benefits from the resource.

In the “Liabilities” section, does the Board agree with the proposed modifications to pars. 39 and 40? (These modification are equivalent to the proposed modifications in the “Recognition” and “Assets” sections.)

Does the Board agree that the definition of a liability and the identification and discussion of the two essential characteristics of liabilities should remain unchanged?

Modifications to the Section on Net Position, Revenues, and Expenses

Net Position

A few respondents to the ED say that the definition of “Net Position” should be subdivided into two components: “unexpended appropriations” and “cumulative results of operations,” consistent with current standards. In September 2006 the Board reaffirmed its decision prior to the ED that what may be considered useful subdivisions of “Net Position” depends on the financial reporting model adopted and, therefore, the issue is one for statements of standards, rather than concepts statements. This position does not negate the potential usefulness of the current subdivision of net position in the current reporting model.

Revenue and Expense

A large majority of the respondents (25 to 6) support deriving the definitions of revenues and expenses (and net position) from the definitions of assets and liabilities. Examples of the reasons given are:

. . . The inflows and outflows of an entity are a direct result of the management of the assets and liabilities as they relate to the production of goods or services of the entity. [028—Federal Preparer]

The definitions of net position, revenues and expenses should derive from the definitions of assets and liabilities as these income statement or statement of activities accounts are used to record the inflow and outflow of assets and the accumulation or relief of liabilities. By deriving these definitions from the balance sheet accounts, it reinforces the relationships between the accounts and financial reporting statements. [030—Federal Auditor]

The three respondents who disagree prefer to base the revenue and expense definitions on the essential characteristics of those elements, but they do not indicate what they believe those essential characteristics are.

The ED definitions of revenue and expense are:

52. A revenue is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity (excluding borrowing) performed during the reporting period.
53. An expense is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or any other activity (excluding repayments of borrowing) performed during the reporting period.

A few respondents propose changes to the ED definitions. The main suggestions (most are from only one respondent) are:

- Consider referring to changes in net position rather than to increases or decreases in assets and liabilities.

- Clarify or avoid the reference to “borrowings.”
- Refer to “use of” rather than “providing” goods or services in the expense definition to avoid potential confusion with the same phrase in the revenue definition.
- Clarify the phrase “any other activity.”

For example:

The IPSASB definition of revenue is “the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.” Definitions from other countries are similar. I was wondering whether you could refer to an increase in net position rather than increases or decreases in assets and liabilities and then having to exclude borrowings. [024—Non-federal Other]

We are concerned with the definitions of revenues and expenses in that both exclude borrowing (receipts and repayments) in the respective definitions. The ED does not discuss why borrowing is excluded or how borrowing is to be treated. We assume that borrowing is excluded from the definitions of revenues and expenses since borrowing represents only changes in assets and liabilities. However, many other transactions represent changes in just assets and liabilities but those transactions are not excluded for the definition of revenues and expenses (for example, sale of an asset, paying invoices from a vendor (unless that is “borrowing”). More discussion of why borrowing is excluded may be appropriate. [039—Non-federal Other]

The definition of expense includes changes in accounts “from providing . . . goods or services, or any other activity . . .” The same phrase, “from providing goods or services . . . or any other activity” is used in the definition of revenue as well. Consider changing “from providing” in the expense definition to another phrase such as “from the use of.” [006—Federal Auditor]

Expense Definition: Some members believe that the definition of expense is very unclear, and respectfully recommend the following rewording: “An expense is a decrease in assets, an increase in liabilities, the consuming or adjusting of assets, or a combination of the above from the receipt of goods or services or any other activities during the reporting period.” [037—Federal Preparer]

One respondent (016—Federal Auditor) proposes adding “relating to the entity’s ongoing programs and missions” after “activity” in both definitions, because the current wording of “any other activity . . . performed during the reporting period” is too broad and vague.

Staff Comments on the Proposed Changes

The Board may ask whether it wishes to consider modifications to the ED definitions, given the paucity of suggestions from respondents. However, the Board looks for the merit of a proposed change rather than the number of respondents who propose it, and there are some drawbacks to the current definitions that the Board may wish to rectify.

Considering the respondents’ suggestions, the Board may agree that clarifying or avoiding the reference to “any other activity” would be an improvement, because currently the

definitions are all-encompassing. However, to clarify the reference would mean adding more examples of activities that result in revenues or expenses. The result would be a “laundry list” of activities, rather than conceptual definitions, and the list could not reasonably include all possible activities. On the other hand, omitting the reference to other activities could lead to a conclusion that only those activities specifically mentioned in the definitions could qualify as revenues or expenses. The definitions might be clearer and less likely to be misapplied if they did *not* include examples of items that typically result in revenues or expenses. Examples could be added to the discussion of revenues and expenses.

The Board may agree that it is desirable to remove the references to borrowings. Including a reference to “changes in net position,” as one respondent suggests, would achieve that result. However, I found a greater variety in the definitions of other countries than the respondent indicates. Australia, New Zealand, and Sweden refer to *both* increases and decreases in assets and liabilities *and* changes in equity or net assets. Canada refers only to increases and decreases in assets and liabilities, and the United Kingdom refers only to increases and decreases in residual interest. Possible reasons for these differences are discussed in the next section.

Given the context of the two definitions in the ED, the Board may conclude that having the phrase “providing goods or services” in both definitions is unlikely to confuse many readers. Moreover, substituting the phrase “from the use of” in the expense definition, as one respondent suggests, would not be sufficient; some expenses result from providing assets to other entities.

The Board may question whether a respondent’s proposed definition of expense quoted above would be better than the ED definition. It is not clear why the proposed addition of the phrase “the consuming or adjusting of assets” would improve the definition, because those activities result in a “decrease in assets,” a phrase that already is included in the definition. Also, the receipt of many goods would result in an asset, not an expense.

A respondent’s suggestion to add “relating to the entity’s ongoing programs and missions” after “activity” in both definitions might clarify “activity” for some readers. However, it may not be an appropriate clarification, because it would add a constraint that might inappropriately prevent certain items from meeting the definitions. Some might believe that in certain instances items that generally would be considered revenues or expenses do not have a relationship to a government program or mission and therefore do not meet the definition of an element. For example, a loss of assets caused by a natural disaster might not be considered to meet the definition of an expense because the activity has impaired the mission rather than promoting it.

Considerations for the Board

Other standard setters’ definitions of revenue and expense

Before deciding whether to reaffirm the ED definitions or adopt certain modifications, it may be helpful for the Board to review the definitions of other standard setters. Except for the

IPSASB definition, the Board discussed these definitions in December 2005, when the ED definitions were developed. The ED definitions and current FASAB definitions are presented first for comparison.

FASAB ED definitions

A **revenue** is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity (excluding borrowing) performed during the reporting period.

An **expense** is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or any other activity performed during the reporting period.

FASAB, current definitions

Revenue is an inflow of resources that the Government demands, earns, or receives by donation. (SFFAS No. 7, 1996, par. 30)

Expense: Outflows or other using up of assets or incurrences of liabilities (or a combination of both) during a period from providing goods, rendering services, or carrying out other activities related to an entity's programs and missions, the benefits from which do not extend beyond the present operating period. (Consolidated Glossary)

FASB Concepts Statement No. 6, *Elements of Financial Statements* (December 1985, pars. 78, 80, 82, and 83)¹

Revenues are inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

Expenses are outflows or other using up of assets or incurrences of liabilities (or a combination of both) from delivering or producing goods, rendering services, or carrying out other activities that constitute the entity's ongoing major or central operations.

¹ The FASB and IASB intend to review their respective definitions of revenue and expense in their joint conceptual framework project, but deliberations on those definitions have not yet begun.

Australia—Statement of Accounting Concepts No. 4, *Definition and Recognition of the Elements of Financial Statements* (1995, pars. 111 and 117)

New Zealand—*Statement of Concepts for General Purpose Financial Reporting* (1993, revised 2001, pars. 7.19 and 7.22)

Revenues are inflows or other enhancements, or savings in outflows, of future economic benefits in the form of increases in assets or reductions in liabilities of the entity, other than those relating to contributions by owners, that result in an increase in equity during the reporting period.

Expenses are consumptions or losses of future economic benefits in the form of reductions in assets or increases in liabilities of the entity, other than those relating to distributions to owners, that result in a decrease in equity during the reporting period.

Canada—CICA, *Public Sector Accounting* (Jan. 2003, Sec. 1000.45—1000.49)

Staff note to Board: My edition of the CICA Handbook (Jan. 2003) does not contain their definition of revenues. It only contains the subsequent elaboration on the sources of revenues, which is the paragraph I have reproduced below. In contrast, the Expense definition is included in the Handbook, as well as the elaboration on the sources of expenses. Assuming that the two definitions are parallel, one can probably surmise fairly accurately the definition of revenues by examining the components of the definition of expenses.

Revenues, other than gains, can arise from: taxation; the sale of goods; the rendering of services; the use by others of government economic resources yielding rent, interest, royalties or dividends; or receiving contributions such as grants, donations and bequests. Revenues do not include borrowings, such as proceeds from debt issues or transfers from other governmental units in the government reporting entity.

Expenses, including losses, are decreases in economic resources, either by way of outflows or reductions of assets or incurrences of liabilities, resulting from the operations, transactions and events of the accounting period. Expenses include transfer payments due where no value is received directly in return.

United Kingdom—*Statement of Principles for Financial Reporting—Proposed Interpretation for Public Benefit Entities* (2003, Chapter 4)

Staff note to Board: Par. 4.49 of the UK document states that “The terms ‘gains’ and ‘losses’ . . . include items that are often referred to as ‘revenue’ and ‘expenses’.”

Gains are increases in residual interest not resulting from contributions from controlling parties in their capacity as controlling parties.

Losses are decreases in residual interest not resulting from distributions to controlling parties in their capacity as controlling parties.

Sweden—*Conceptual Framework for the Preparation of Financial Statements in the Central Government of Sweden* (Jan. 2003, par. 69)

Revenue is an increase in economic benefits or service potential during an accounting period in the form of payments received, an increase in the value of assets or a reduction in the value of liabilities with a consequent increase in net assets. However, increases in net assets that arise from contributions of capital do not constitute revenue.

Expenses are decreases of economic benefits or service potential during an accounting period in the form of payments, a reduction in the value of assets or an increase in liabilities with a consequent reduction of net assets. However, reductions of net assets that consist of a reversal of additional capital do not constitute an expense.

GASB—*Exposure Draft, Elements of Financial Statements* (issued August 2006)

Staff note to Board: GASB uses the term “inflow of resources” for revenue and “outflow of resources” for expense (accrual basis) and “expenditure” (modified accrual basis).

An **inflow of resources** is an acquisition of net resources* by an entity that is applicable to the reporting period.

An **outflow of resources** is a consumption of net resources* of or by the entity that is applicable to the reporting period.

*Net resources are assets netted with liabilities.

IPSASB, *Glossary of Defined Terms*, (Issued June 2001)

Revenue: The gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.

Expenses: Decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or incurrences of liabilities that result in decreases in net assets/equity, other than those relating to distributions to owners.

Staff comments on variations in the definitions

Several observations about the differences among the above definitions may be helpful for deciding whether and if so how the FASAB’s definitions should be changed.

1. As noted earlier, the definitions of Australia, New Zealand, and Sweden refer to *both* increases and decreases in assets and liabilities *and* changes in equity or net assets.

IPSASB also refers to both types of changes for expenses but not for revenues. FASB and Canada-CICA refer only to increases and decreases in assets and liabilities. The United Kingdom, GASB, and IPSASB (for revenues) refer only to increases and decreases in residual interest, net resources, or net assets/equity.

2. In contrast to the ED definitions, the other definitions do not give examples of revenues or expenses, except for the FASB definitions, the existing FASAB (Glossary) definition of expense, and a minor example in the Swedish definitions.

These differences among standard setters' definitions may be a function of whether the standard-setting body defines gains and losses (which generally are reported net) as separate elements from revenues and expenses (which generally are reported gross). That is, standard setters that distinguish *conceptually* (not just in display standards) between revenues/-expenses and gains/losses may have concluded that they need to include examples of revenues/expenses and gains/losses in their respective definitions. Standard setters who do not make a conceptual distinction may conclude that it is unnecessary to give examples in each set of definitions. Those standard setters also may have concluded that, rather than referring to changes in assets and liabilities in their definitions of revenues and expenses, in line with reporting revenues and expenses at gross, they can refer more simply to changes in net position (or net assets, equity, or whatever term they use) and address in statements of standards any desirable reporting (display) distinctions between revenues/expenses and gains/losses, and whether items should be reported gross or net.

In support of this interpretation, FASB defines gains and losses as separate elements from revenues and expenses, includes examples of revenues and expenses in its revenue and expense definitions, and refers to changes in assets and liabilities. In contrast, Australia, New Zealand, Canada-CICA, UK, Sweden, GASB, and, I believe, IPSASB² do not distinguish conceptually between revenues/expenses and gains/losses. In their definitions of revenues and expenses they do not include examples (other than a minor one for Sweden), and they refer to changes in net position instead of or in addition to changes in assets and liabilities.

This analysis suggests that the FASAB does not need to give examples of revenues and expenses in the definitions themselves (they could be given in the subsequent discussion), if the only purpose of doing so is to distinguish between revenues/expenses and gains/losses. As the Board reaffirmed at the September 2006 meeting, the FASAB views gains and losses *conceptually* as subsets of revenues and expenses and not as separate elements, even though standards may require separate labeling and display of certain items as gains and losses. Conceptually, revenues and expenses are any inflows or outflows of assets during an accounting period that change an entity's net assets. Thus, the Board may wish to consider for the concepts statement a definition that refers to changes in net position, rather than changes in assets and liabilities. This approach would simplify the definitions of revenues and expenses without precluding separate display of gains and losses, either net or gross, in accordance with applicable standards.

² I was unable to find chapter and verse on the IPSASB treatment.

Possible Alternatives to the ED Definitions of Revenues and Expenses

Based on the foregoing discussion, the following are some alternatives to the ED definitions of revenues and expenses. To facilitate comparison of the alternatives to the ED definitions, those definitions are presented first.

ED definitions:

A **revenue** is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity (excluding borrowing) performed during the reporting period.

An **expense** is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or any other activity performed during the reporting period.

Alternatives:

1. *Refer to changes in net position instead of changes in assets and liabilities; remove references to borrowings; remove examples of revenues and expenses.*

A **revenue** is an increase in the government's net position during the reporting period.

An **expense** is a decrease in the government's net position during the reporting period.

2. *Refer to changes in net position instead of changes in assets and liabilities; remove references to borrowings; retain examples of revenues and expenses.*

A **revenue** is an increase in the government's net position that results from providing goods or services, levying taxes or other impositions, receiving donations, or other activities during the reporting period.

An **expense** is a decrease in the government's net position that results from providing cash or cash equivalents, goods or services, or other activities during the reporting period.

3. *Refer to changes in net position as well as changes in assets and liabilities; remove references to borrowings; remove examples of revenues and expenses.*

A **revenue** is an increase in assets, a decrease in liabilities, or a combination of both that results in an increase in the government's net position during the reporting period.

An **expense** is a decrease in assets, an increase in liabilities, or a combination of both that results in a decrease in the government’s net position during the reporting period.

4. Refer to changes in net position as well as changes in assets and liabilities; remove references to borrowings; retain examples of revenues and expenses

A **revenue** is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or other activities that result in an increase in the government’s net position during the reporting period.

An **expense** is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or other activities that result in a decrease in the government’s net position during the reporting period.

Staff comments and recommendations

All four alternatives to the ED definitions refer to changes in net position. This enables the deletion of the ED references to borrowings, which I believe is a definite improvement.

Alternatives 1 and 2 refer *only* to changes in net position—not changes in assets and liabilities. The difference between them is that Alternative 2 includes examples of revenues and expenses, whereas Alternative 1 does not. If the definitions do not include examples, there is no need for the phrase “any other activity” or “other activities.” Examples of revenues and expenses could be included in a paragraph following the definitions.

Alternatives 3 and 4 refer to *both* increases/decreases in assets and liabilities *and* increases/decreases in net position. Alternative 4 includes examples of revenues and expenses, whereas Alternative 3 does not.

My recommendation is Alternative 1. It is the simplest. I do not believe it is necessary to include examples of revenues and expenses in the definitions, as in Alternatives 2 and 4; a few examples could be included in the discussion after the definitions, if the Board believes that would be useful. Alternatives 3 and 4 are cumbersome. I do not believe it is necessary to refer to *both* changes in assets and liabilities *and* changes in net position.

Does the Board agree that the definitions of Revenues and Expenses in the ED should be modified?

If so, which of the four alternatives does the Board prefer? Or does the Board prefer a different alternative?

Executive Summary

Having considered the proposed changes in the body of the Statement, does the Board wish to make any changes in the Executive Summary *other than* those that will be necessary to conform it to the revised Statement?