



Project	Agenda decision
Topic	IAS 38 <i>Intangible Assets</i> – Amortisation method

Introduction

1. In November 2009, the IFRIC published a tentative agenda decision not to add to its agenda a request asking for guidance on the meaning of 'consumption of economic benefits' when determining the appropriate amortisation method for an intangible asset with a finite useful life.
2. This issue was discussed at the November 2009 IFRIC meeting; it was set out in agenda paper reference 6 that can be found on the public website¹.

Background

3. As published in the November 2009 IFRIC Update:

The IFRIC noted that paragraph 98 of IAS 38 states that 'the method used is based on the expected pattern of consumption of the expected future economic benefits embodied in the asset...'. It also noted that the determination of the amortisation method is therefore a matter of judgement. In addition, in accordance with paragraph 122 of IAS 1 Presentation of Financial Statements, significant judgements made in determining the amortisation methods should be disclosed in the notes to the financial statements.

The IFRIC noted that any guidance it could give on making the judgements necessary to determine the amortisation method would be in the nature of application guidance rather than an interpretation. Therefore, the IFRIC [decided] not to add the issue to its agenda.

¹ <http://www.iasb.org/NR/ronlyres/0C877AEB-9E60-4BF9-BC24-5A7052DE4007/0/0911ap6obsIAS38Amortisationmethodforintangibleassets.pdf>

This paper has been prepared by the technical staff of the IASCF for discussion at a public meeting of the IFRIC. The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRIC or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRIC or the IASB can make such a determination.

Decisions made by the IFRIC are reported in IFRIC *Update*.

Interpretations are published only after the IFRIC and the Board have each completed their full due process, including appropriate public consultation and formal voting procedures. The approval of an Interpretation by the Board is reported in IASB *Update*.

Comment letters analysis

4. Of the four comment letters that were received, two agree² and two disagree³ with the IFRIC tentative decision not to take the issue onto its agenda. The main comments are analysed in the paragraphs below.

Need for an interpretation: the basis on which the unit of production method is applied

5. The IFRIC tentatively decided in November 2009 that the criteria to add the issue to its agenda were not met. However, as stated above, two constituents disagree with this tentative agenda decision.
6. These two constituents argue that the issue is a matter of interpretation and would appreciate the IFRIC reconsidering taking the issue onto its agenda.
7. One constituent⁴ believes that an interpretation should address whether a unit of production amortisation method based on estimated revenue can be a systematic basis for amortising an intangible asset. The constituent believes that such an interpretation would also assist in clarifying what methods are acceptable when applying IFRIC 12's intangible asset model. The constituent asks, for example, 'would actual revenue, rather than expected revenue be an appropriate basis for amortisation?'
8. In the staff's opinion, this is another variation on the example provided in the submission, which considered using the ratio of actual revenue to estimated future revenue as the amortisation basis. The staff also notes that paragraph 26 of IFRIC 12 requires IAS 38 to be applied to the accounting for an intangible asset recognised in accordance with IFRIC 12. Accordingly, in the staff's opinion, the concern about applying IFRIC 12 is another perspective on the concern about applying IAS 38.
9. The staff believes that the arguments raised in this comment letter are additional perspectives on the same issue that was discussed by the IFRIC in November.

² DTT CL 2, Muhammad Ali CL 4

³ EY CL 1, HKICPA CL 3

⁴ EY CL 1

The staff therefore does not see a reason to propose a change to the IFRIC's tentative decision not to take this issue onto its agenda.

10. The second constituent⁵ highlights additional arguments that it believes were not fully drawn out in the IFRIC's discussion in November. These additional arguments relate to whether the future economic benefits established in the asset represent its ability to:
 - (a) contribute to the generation of future revenues;
 - (b) contribute to the generation of future profits;
 - (c) produce units of output, or perform services, *based on the maximum productive capacity* of the asset; or
 - (d) produce units of output, or perform services, *based on the expected output* of the asset.

11. This constituent observes that two views exist in practice:
 - (a) view 1: revenues, profits and expected output are not features of the asset being amortised. They are only factors associated with the environment in which it is used, hence only the method described in (c) above is acceptable; or
 - (b) view 2: the asset is not used in isolation, hence the method of amortisation should reflect the economic benefits arising from its use in the environment in which it is expected to be used and all methods listed above are acceptable.

12. The staff observes that this argument can also be seen as highlighting a distinction between the consumption of the asset's economic benefits (the use / operation of the asset in the production of outputs/ provision of services) and the generation of economic benefits through the asset's use (generation of revenues and profits). In this regard, the staff notes that paragraph 97 of IAS 38 is clear that the amortisation method should 'reflect the pattern in which the asset's

⁵ HKICPA CL 3

future economic benefits are expected to be *consumed* by the entity' [emphasis added].

13. In the staff's opinion, a revenue or profit basis for the amortisation method is a focus on the generation of economic benefits, rather than the consumption of them.
14. However, the staff also notes that IAS 38 implies judgment is required in determining the amortisation method ('the pattern in which...*expected* to be consumed...' [emphasis added]). Therefore if, in applying judgement, an entity concludes that the pattern of expected revenue is an appropriate proxy for the pattern of expected consumption of the asset's future economic benefits, then the requirements of paragraph 97 of IAS 38 can be judged to have been met.
15. The staff acknowledges that the arguments raised in this second comment letter are different from those debated in the November IFRIC meeting, but the staff believes that the issue ultimately returns to a question of how to make the judgements necessary to determine the amortisation method. This was the basis on which the IFRIC tentatively decided not to take the issue onto its agenda. Accordingly, the staff recommends that the IFRIC confirm its decision not to take the issue onto its agenda, for the reasons set out in the tentative agenda decision.

Consideration of the subject of the licence

16. One of the issues raised in Agenda Paper 6 of the November IFRIC meeting, and discussed by the IFRIC, was whether an entity should consider the nature of the asset underlying a licence when selecting an appropriate amortisation method.
17. Two constituents⁶ note that the tentative agenda decision does not reflect the discussion of this issue. They are concerned that opinions are divergent as to whether an entity should consider the underlying item when selecting an

⁶ Muhammad Ali CL 4

appropriate amortisation method. One of these constituents requests that the wording for the tentative agenda decision reflects this discussion and elaborates on whether an entity should consider the subject of the licence when determining the appropriate amortisation method. The other constituent believes an interpretation should be developed to clarify what methods are acceptable when applying IFRIC 12 *Service Concession Arrangements* intangible asset model.

18. The staff notes that the amortisation method should reflect the ‘pattern in which the asset’s future economic benefits are expected to be consumed by the entity’. The staff is of the view that there is only one set of benefits that the entity receives and consumes as a result of a licence to use / operate an asset. The staff does not believe that the entity receives separate benefits from the licence and the underlying asset. IAS 38 requires the amortisation method to reflect the pattern of consumption of those benefits. The staff believes the focus should therefore be on that pattern. There may be some circumstances when the terms of the licence have a greater impact on the pattern of consumption and other circumstances when the characteristics of the underlying asset have a greater impact. The staff believes the amortisation method selected should take account of those circumstances.
19. Regarding the first request, the staff notes that the tentative agenda decision not to take the issue on to the IFRIC agenda reflects the assessment against the agenda criteria. The staff does not agree that the agenda decision should go further than this by describing the acceptable accounting treatment.
20. The second constituent’s request for an interpretation has been considered above in paragraphs 7 to 9 of this paper.

Staff recommendation

21. Based on the comments received, the **staff recommends that the tentative agenda decision be finalised with no change from the Tentative Agenda Decision published in the November 2009 IFRIC Update.**

Questions to the IFRIC

Question – Finalisation of IFRIC Agenda Decision

Question 1 – The staff recommends that the IFRIC finalise its Tentative Agenda Decision not to add this issue to its agenda. Does the IFRIC agree with the staff's recommendation?

Question 2 – Appendix A includes the staff's proposed wording for the final Agenda Decision. Does the IFRIC agree with the proposed final Agenda Decision wording?

Appendix A – IFRIC Final Agenda Decision DRAFTING

A1. The staff proposes the following wording for the **final** agenda decision.

(Deleted text is struck through.)

IAS 38 *Intangible Assets* - Amortisation method

The IFRIC received requests for guidance on the meaning of 'consumption of economic benefits' when determining the appropriate amortisation method for an intangible asset with a finite useful life. The methods considered in the submissions are the straight-line method and the unit of production method (including a revenue-based unit of production method).

The IFRIC noted that paragraph 98 of IAS 38 states that 'the method used is based on the expected pattern of consumption of the expected future economic benefits embodied in the asset...' It also noted that the determination of the amortisation method is therefore a matter of judgement. In addition, in accordance with paragraph 122 of IAS 1 *Presentation of Financial Statements*, significant judgements made in determining the amortisation methods should be disclosed in the notes to the financial statements.

The IFRIC noted that any guidance it could give on making the judgements necessary to determine the amortisation method would be in the nature of application guidance rather than an interpretation. Therefore, the IFRIC [decided] not to add the issue to its agenda.