

## STAFF PAPER

10 – 11 September 2013

## IFRS Interpretations Committee Meeting

IFRS IC Jul 2013, Mar 2012 and Nov 2011  
| IASB Apr 2012 and Oct 2012

Project	Narrow-scope amendment
Paper topic	IAS 16 <i>Property, Plant and Equipment</i> and IAS 38 <i>Intangible Assets</i> —Clarification of methods of depreciation and amortisation
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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in IFRIC *Update*. The approval of a final Interpretation by the Board is reported in IASB *Update*.

## Introduction

1. In December 2012 the IASB published the Exposure Draft (ED) *Clarification of Acceptable Methods of Depreciation and Amortisation (ED/2012/5)*, which contained a proposal to amend IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*.
2. At the July 2013 meeting, the Interpretations Committee was presented with a summary and an analysis of the 98 comment letters received on the ED. The members of the Interpretations Committee discussed the comments received and directed the staff to develop the proposed amendment further, in order to clarify the principle in paragraph 60 of IAS 16 for depreciating assets and the principle in paragraph 97 of IAS 38 for amortising intangible assets.

## Purpose of this paper

3. This paper presents our proposal to finalise the propose amendment to IAS 16 and IAS 38.

## Summary of the Interpretations Committee discussion at the July 2013 meeting

### ***The focus of the proposed amendments is to emphasise the principle for depreciation and/or amortisation***

4. Some respondents to the ED had pointed out that the explanations in the proposed Basis for Conclusions (BC) introduced limited circumstances in which revenue data would be correlated with production data, which they interpreted as allowing the use of revenue as an approximation of the pattern of consumption of an asset. These respondents thought that these limited circumstances should be included within the body of the Standard (in both IAS 16 and IAS 38) because they believed that a revenue-based method could be used as a reliable proxy. They thought that this would avoid inconsistencies between the core guidance in the Standard and the explanations in the BC.
5. At the July 2013 meeting, there was general agreement among the Interpretation Committee members to eliminate any ambiguity between the explanations in the BC and in the body of the Standard. However, some noted that to achieve this, the proposed amendments should not be focused on prohibiting the use of a revenue-based approach in all circumstances or on creating rules for limited circumstances in which revenue data might be correlated with production data, but instead on reaffirming the principle for depreciating and/or amortising assets.
6. There was general agreement among the Interpretation Committee members that the focus of the proposed amendments should be to:
  - (a) emphasise the main principle for depreciating assets and for amortising intangible assets; and
  - (b) avoid creating rules for the limited circumstances in which revenue data would be correlated with production data.

### *Our view*

7. We agree that any ambiguity between the body of the Standard and the basis for conclusions should be eliminated.

8. We think that the Interpretations Committee could recommend to the IASB to state that paragraph 60 of IAS 16 and paragraph 97 of IAS 38 establish the consumption of the benefits inherent in the asset as the principle for depreciation/amortisation.
9. The proposed amendment should also state that the resulting depreciation and/or amortisation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset.

***Revenue is not a valid ‘proxy’ for consumption***

10. At the July 2013 meeting, some Interpretations Committee members thought that prohibiting the use of a revenue-based method in all circumstances appeared to be too restrictive, mainly because respondents to the ED had highlighted some rare circumstances in which certain industries (such as the media and entertainment industry) might use revenue as a proxy for consumption.
11. Yet, a majority of the Interpretations Committee members reaffirmed their position that revenue cannot be used as a proxy for consumption. They also emphasised that the proposed amendment should avoid introducing examples where it could be interpreted that revenue could be used as a ‘proxy’ for consumption.
12. Some added that the only circumstance in which revenue would be appropriate to reflect the basis of the expected pattern of consumption of an asset would be in the rare circumstances in which there is a perfect correlation between consumption and revenue; however this circumstance should not be interpreted as a confirmation that revenue could in some circumstances be used as a ‘proxy’ for consumption.
13. Some noted that a rare circumstance in which there is a perfect correlation between consumption and revenue is in cases in which the right implicit in an intangible asset is based on the amount of revenue generated. The following case

extracted from one of the comment letters received on the ED<sup>1</sup> illustrates this view (emphasis added):

Example 2 - Mining Rights

Company A acquired a concession to explore and extract gold from a gold mine. **The grantor wanted to keep the gold price risk, so, instead of fixing a contract in a time basis or in amount of gold-extracted basis, the duration of the contract is based on the amount of gross revenue obtained from the extraction. Suppose the agreed upon fixed amount is US\$ 2 billion.**

Company A is given rights to explore the mine until it extracts US\$ 2 billion of gold. The risk of the price variation of gold is with the grantor. That is, if gold is valued at US\$ 1,000 per ounce, Company A would be able to extract 2 million ounces. If the price rises to US\$ 2,000 per ounce, Company A would be able to extract 1 million ounces.

**Company A is required to amortize the concession, which was recognized as an intangible asset, according to the consumption of the contractual rights which would be based on the expected pattern of revenue earned.**

14. Some Interpretations Committee members considered that the objective should be to keep the proposed guidance at a principle level and they thought that the proposed amendments should be ‘silent’ on the rare circumstances in which there is a perfect correlation between revenue and consumption. Some others however, were of the opinion that this circumstance should be highlighted in the body of the Standard.

*Our view*

15. We think that the Interpretations Committee could recommend to the IASB that it should explicitly state in the proposed amendment to IAS 38 that only in those

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<sup>1</sup> Extracted from the comment letter sent by IOSCO.

cases in which the right implicit in an intangible asset is limited by the amount of revenue generated, the amortisation of an intangible asset could be based on the expected pattern of revenue generated.

16. We think that the Interpretations Committee could recommend to the IASB the insertion of guidance in IAS 38 on choosing an amortisation method. We think that this guidance could direct the entity to determine the limiting factor that is inherent in the intangible asset; for example, the contract that sets out the entity's rights over its use of an intangible asset might limit the entity's use of the intangible asset to a pre-determined number of years (ie time) or to a number of units produced or, as we have discussed above, to an amount of revenue earned.

### ***The use of an intangible asset in multiple activities***

17. At the July 2013 meeting some Interpretations Committee members referred to the case raised by some respondents to the ED of intellectual property that is used to generate multiple different cash flow streams in various different markets. These respondents had pointed out that in such cases the best way to amortise the intangible asset (eg a film right) is to use a revenue-based method. This is because they think that revenue reflects the pattern of consumption of all the multiple activities in which an intangible asset could be used. The example below, which is extracted from one of the comment letters received<sup>2</sup>, illustrates this view:

The straight line method does not reflect the pattern of consumption of the assets, as explained in the BC, which is generally initially high during the first weeks following the release of a movie in theatres and then decline until the movie is out on DVDs, then on VOD (video-on-demand) and then broadcasted on TV, etc. The useful life of a movie is often unpredictable, and depends notably on the success of the release in theatres at first and then on the other distribution platforms. It can thus be shorter or longer than initially expected. In some cases, some movies which

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<sup>2</sup> Extracted from the comment letter sent by Vivendi.

were a fiasco in theatres can be successful when sold in DVDs. **As such, it is difficult to determine a reliable useful life on which we could eventually base a straight-line amortization method, which, above all, would not reflect the pattern of consumption of the asset.**

**The application of a unit of production method is not practicable as units of production in film production and distribution are various and not homogeneous: number of tickets sold in theatres, number of DVDs sold, number of viewings on VOD, number of subscribers watching the film shown on a pay-TV channel, etc. Also, the advertising fees the movie will contribute to generate on free-to-air TV channels is difficult to translate into units of production.**

**We therefore believe revenue generated is reflective of these various units of production in combination with a market price for each nature of units.** Our managing of our movies production and distribution activities are based on the estimated revenue generated and are in our opinion reflective of the consumption of the future economic benefits embodied in the asset.

18. During the discussion some Interpretations Committee members acknowledged that finding a single amortisation basis that would take into account all of the different activities in which an intangible asset will be used could be very difficult.
19. However, they observed that a possible solution would be to split the cost of the intangible asset into different components (ie multiple intangible assets), each of which would reflect the right to use the asset in a particular activity (or group of activities).
20. The allocation to each activity could be done on the basis of their relative fair values at the date of purchase.

21. Each separate component would then be amortised, not on the basis of the revenue generated for each portion, but based on amortisation methods that would reflect the expected pattern consumption of each component of the intangible asset's future economic benefits.

*Our view*

22. We observe that the notion of separating a single asset or transaction into its separate identifiable components to reflect the way the asset is consumed or the substance of the transaction is not a new notion neither in business (as it is routinely done) nor in IFRSs.
23. For instance, paragraph 13 of IAS 18 *Revenue* states that in certain circumstances it is necessary to apply the recognition criteria to the separate identifiable components of a transaction. In this respect it states that (emphasis added):

The recognition criteria in this Standard are usually applied separately to each transaction. **However, in certain circumstances, it is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction. For example, when the selling price of a product includes an identifiable amount for subsequent servicing, that amount is deferred and recognised as revenue over the period during which the service is performed.** Conversely, the recognition criteria are applied to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole. For example, an entity may sell goods and, at the same time, enter into a separate agreement to repurchase the goods at a later date, thus negating the substantive effect of the transaction; in such a case, the two transactions are dealt with together.

24. A requirement to allocate the cost of a group of assets based on the relative fair value amounts of the separate identifiable components can be found in paragraph

2(b) of IFRS 3 *Business Combinations*, which states the following (emphasis added):

**2(b) the acquisition of an asset or a group of assets that does not constitute a business. In such cases the acquirer shall identify and recognise the individual identifiable assets acquired** (including those assets that meet the definition of, and recognition criteria for, intangible assets in IAS 38 Intangible Assets) and liabilities assumed. **The cost of the group shall be allocated to the individual identifiable assets and liabilities on the basis of their relative fair values at the date of purchase.** Such a transaction or event does not give rise to goodwill.

25. On the basis of the above, we think that the Interpretations Committee could recommend to the IASB that it should include the guidance in IAS 38 for circumstances in which an intangible asset is used in multiple activities. In this respect we think that in the proposed amendment to IAS 38 we could propose an entity to:
- (a) segment the asset into separate identifiable components based on the way the asset is used or is expected to be used in the business (this could be done, for example, by allocating the cost of the intangible asset based on the relative fair value of the identifiable components); and
  - (b) amortise the separately different components of the intangible asset that are used in different activities using amortisation methods and useful economic lives appropriate to each component.
26. We think that the need to identify separate components for a single transaction in order to apply an appropriate amortisation method should remain the primary consideration of this guidance. How this segmentation is done and how an entity determines an appropriate method of amortisation for each portion identified would require the use of judgement.
27. We think that leaving this guidance at a ‘principle level’ would be in line with previous decisions made by the Interpretations Committee. For instance we



observe that in 2006 the IFRIC (as it was called then) rejected a request for guidance on accounting by mobile telecommunications operators for telephone handsets given to subscribers free or at heavily discounted prices. The IFRIC was asked at the time whether:

- (a) the contracts should be treated as comprising two separately identifiable components (ie the sale of a telephone and the rendering of telecommunication services) and revenue would be attributed to each component; or
- (b) the telephones should be treated as the cost of acquiring the new customer with no revenue attributed to them.

28. The IFRIC noted the following (extracted from the [IFRIC Update of March 2006](#), emphasis has been added):

The IFRIC acknowledged that the question is of widespread relevance, both across the telecommunications industry and, more generally, in other sectors. IAS 18 does not give guidance on what it means by ‘separately identifiable components’ and practices diverge.

**However, the IFRIC noted that the terms of subscriber contracts vary widely. Any guidance on accounting for discounted handsets would need to be principles-based to accommodate the diverse range of contract terms that arise in practice. The IASB is at present developing principles for identifying separable components within revenue contracts.** In these circumstances, the IFRIC does not believe it could reach a consensus on a timely basis. The IFRIC, therefore, decided not to take the topic onto its agenda.<sup>3</sup>

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<sup>3</sup> Subsequent to the IFRIC’s discussion, the Exposure Draft [Revenue from Contracts with Customers](#) (issued in June 2010) and the revised Exposure draft [Revenue from Contracts with Customers](#) (issued in November 2011) provided guidance on the identification of separate performance obligations (see paragraphs 23 –30 of the revised ED). Paragraph 23 of the revised ED states that: “An entity shall evaluate the goods or services promised in a contract and shall identify which goods or services (or which bundles of

## Other issues that were raised in our comment letter analysis

### ***Remove the proposed guidance in regard to the diminishing balance method because it is confusing and include a clarification to paragraph 56(c) of IAS 16***

29. At the July 2013 meeting we noted that some respondents to the ED had questioned the addition of paragraph 62B of IAS 16 and paragraph 98B of IAS 38 to clarify the application of the diminishing balance method, because they find the wording in these paragraphs confusing and cannot see the point of their inclusion. They also questioned why the guidance is specific to the application of the diminishing balance method.
30. We understand that the IASB's objective was to clarify that reductions in the selling price could signal the existence of obsolescence, which in turn reflects a reduction in the economic benefits consumed from the asset.
31. We reaffirm our view that the best way to clarify the IASB's intention is to amend paragraph 56(c) of IAS 16, because the guidance in paragraph 56(c) already takes into consideration technical or commercial obsolescence as a factor to determine the useful life of an asset and further explains how obsolescence could arise in some cases.
32. We observe that paragraph 90(c) of IAS 38, refers to factors considered in determining the useful life of an intangible asset, and among them considers: "technical, technological, commercial or other types of obsolescence".
33. We think that further guidance could be added to paragraph 92 of IAS 38 to explain that future reductions in the selling price could indicate the existence of commercial obsolescence, which in turn reflects a reduction in the economic benefits consumed from the asset.
34. Consequently we think that the Interpretations Committee could recommend to the IASB to:

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goods or services) are distinct and, hence, that the entity shall account for as a separate performance obligation". The article *Revenue recognition and your mobile*, published on the IASB website as an Investor Perspectives article, refers to the application of the guidance in the first ED (refer to: <http://www.ifrs.org/Investor-resources/2010-perspectives/June-2010-perspectives/Pages/Revenue-recognition-and-your-mobile-phone.aspx>).

- (a) amend paragraph 56(c) of IAS 16 to state that technical or commercial obsolescence could also be indicated by or arise from a change in the market demand as indicated by a future expected reduction in the unit selling price for the product or service output of the asset; and
- (b) amend paragraph 92 of IAS 38 to explain that a future expected reduction on the selling price of an intangible asset could indicate the existence of commercial obsolescence.

***Delete the statement “when it was acquired” in proposed paragraph 62A of IAS 16 and in proposed paragraph 98A of IAS 38***

35. At the meeting we also noted that some respondents to the ED had proposed to the IASB that it should delete the phrase “when it was acquired” in proposed paragraph 62A (of IAS 16) and in proposed paragraph 98A (of IAS 38) because this statement contradicts other guidance in IAS 16 and IAS 38. For instance (emphasis added):

- (a) Proposed paragraph 62A in the ED states that: “Paragraph 60 establishes consumption of the benefits that were inherent in the asset when it was acquired as the principle for depreciation”.
- (b) Proposed paragraph 98A in the ED states that: “Paragraph 97 establishes consumption of the benefits that were inherent in the asset when it was acquired as the principle for amortisation”.

36. We think that in this respect the Interpretations Committee could recommend to the IASB that it should not mention the phrase “when it was acquired” in the final drafting of the proposed amendment (ie in proposed paragraph 60A of IAS 16 and in proposed paragraph 97A of IAS 38).

***The proposed amendment to IAS 16 should be applied prospectively***

37. We reaffirm our position of supporting the prospective application of the proposed amendments to IAS 16 and IAS 38, because applying the proposed amendment on a prospective basis, rather than on a retrospective basis, is in line with existing requirements for changes in accounting estimates in paragraphs 32–38 of IAS 8

*Accounting Policies, Changes in Accounting Estimates and Errors*. This would also be consistent with the requirements for revisions of estimates in paragraph 61 of IAS 16 and in paragraph 102 of IAS 38.

38. We think that the Interpretations Committee could recommend to the IASB that it should reaffirm the application of the proposed amendments to IAS 16 and IAS 38 to be prospective because this would be consistent with the requirements in IAS 8 for revisions of estimates.

### **Summary of staff recommendations**

39. We think that the Interpretations Committee should recommend to the IASB that it should:
- (a) state in the proposed amendment to IAS 16 and in IAS 38 (paragraphs 60A and 97A, respectively) that paragraph 60 and paragraph 97 (respectively) establish the consumption of the benefits inherent in the asset as the principle for depreciation and amortisation and that the resulting depreciation and/or amortisation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset;
  - (b) state in the proposed amendment to IAS 38 that in cases in which the right implicit in an intangible asset is expressed as a measure of the amount of revenue generated, the amortisation of an intangible asset should be based on the expected pattern of revenue generated;
  - (c) state in the proposed amendment to IAS 38 that in choosing an amortisation method an entity could determine what the limiting factor is for the intangible asset; for example a contract could be limited by a number of years (ie time) or a number of units produced or an amount of revenue earned;
  - (d) include guidance in IAS 38 on circumstances in which an intangible asset is used in multiple activities, such as a proposal to:

- (i) segment the asset into separate identifiable components based on the way the asset is used or is expected to be used in the business (this could be done, for example, by allocating the cost of the intangible asset based on the relative fair value of the identifiable components); and
  - (ii) amortise the separately different components of the intangible asset that are used in different activities using amortisation methods and useful economic lives appropriate to each component;
- (e) remove the proposed guidance with regard to the diminishing balance method that we had in paragraph 62B of IAS 16 and paragraph 98B of IAS 38 in the ED and instead:
- (i) amend paragraph 56(c) of IAS 16 to state that technical or commercial obsolescence could also arise from a change in the market demand as indicated by a future expected reduction in the unit selling price for the product or service output of the asset;
  - (ii) amend paragraph 92 of IAS 38 to explain that a future expected reduction on the selling price of an intangible asset could indicate the existence of commercial obsolescence.
- (f) apply the proposed amendments to IAS 16 and IAS 38 prospectively.

40. Our recommended changes to the draft wording are included as appendices:

- (a) **Appendix A** shows the proposed amendment, including our recommendations in this paper, highlighting differences from the currently effective Standard; and
- (b) **Appendix B** shows revisions to the wording in the previously published Exposure Draft, following our recommendations in this paper.

## Questions for the Interpretations Committee

### Questions for the Interpretations Committee

1. Does the Interpretations Committee agree with our conclusions in this paper?
2. Does the Interpretations Committee agree with our proposed amendments to:
  - (a) state in the proposed amendment to IAS 16 and in IAS 38 (paragraphs 60A and 97A, respectively) that paragraph 60 and paragraph 97 (respectively) establish the consumption of the benefits inherent in the asset as the principle for depreciation and amortisation and that the resulting depreciation and/or amortisation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset;
  - (b) state in the proposed amendment to IAS 38 that in cases in which the right implicit in an intangible asset is expressed as a measure of the amount of revenue generated, the amortisation of an intangible asset should be based on the expected pattern of revenue generated;
  - (c) the guidance in IAS 38 could direct the entity to determine the limiting factor that is inherent in the intangible asset; for example, the contract that sets out the entity's rights over its use of an intangible asset might limit the entity's use of the intangible asset to a pre-determined number of years (ie time) or to a number of units produced or, as we have discussed above, to an amount of revenue earned;
  - (d) include guidance in IAS 38 on circumstances in which an intangible asset is used in multiple activities, such as a proposal to:
    - (i) segment the asset into separate identifiable components based on the way the asset is used or is expected to be used in the business (this could be done, for example, by allocating the cost of the intangible asset based on the relative fair value of the identifiable components); and
    - (ii) amortise the separately different components of the intangible asset that are used in different activities using amortisation methods and useful economic lives appropriate to each component;
  - (e) remove the proposed guidance with regard to the diminishing balance method that we had in paragraph 62B of IAS 16 and paragraph 98B of IAS 38 in the ED and instead:
    - (i) amend paragraph 56(c) of IAS 16 to state that technical or commercial obsolescence could also arise from a change in the market demand which could be indicated by a future expected reduction in the unit selling price for the product or service output of the asset;
    - (ii) amend paragraph 92 of IAS 38 to explain that a future expected reduction on the selling price of an intangible asset could indicate the existence of commercial obsolescence.
  - (f) apply the proposed amendments to IAS 16 and IAS 38 prospectively?

## Appendix A—Draft wording of the proposed amendment, showing differences from the currently effective standard

### [Draft] Amendments to IAS 16 *Property, Plant and Equipment*

Paragraph 56 (c) is amended. Paragraphs 60A, 62A and 81G are added. Paragraphs 60 and 62 are not proposed for amendment but are included here for ease of reference. New text is underlined.

#### Depreciable amount and depreciation period

56 The future economic benefits embodied in an asset are consumed by an entity principally through its use. However, other factors, such as technical or commercial obsolescence and wear and tear while an asset remains idle, often result in the diminution of the economic benefits that might have been obtained from the asset. Consequently, all the following factors are considered in determining the useful life of an asset:

- (a) ...
- (c) technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand or as indicated by a future expected reduction in the unit selling price for the product or service output of the asset.

#### Depreciation method

- 60 The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.
- 60A Paragraph 60 establishes consumption of the future economic benefits that are inherent in the asset as the principle for depreciation. The resulting depreciation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset.
- 62 A variety of depreciation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. The straight-line method results in a constant charge over the useful life if the asset's residual value does not change. The diminishing balance method results in a decreasing charge over the useful life. The units of production method results in a charge based on the expected use or output. The entity selects the method that most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. That method is applied consistently from period to period unless there is a change in the expected pattern of consumption of those future economic benefits.

62A A revenue-based depreciation method is one that is derived from an interaction between units (ie quantity) and price, and that takes into account the expected future changes in price in determining the pattern of allocation of the cost of the asset for depreciation purposes. Such revenue-based method is not an appropriate depreciation method because it reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset. A revenue-based depreciation method is, consequently, inconsistent with the depreciation principle in paragraph 60.

### Effective date and transition

81G Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38), issued in [date], added paragraphs 60A and 62A. An entity shall apply these amendments for annual periods beginning on or after 1 January 2016 prospectively. Earlier application is permitted.

### Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, the proposed amendments.*

#### Depreciation method

- BC33A The IASB discussed whether it would be appropriate for plant and equipment to be depreciated using a revenue-based depreciation. Paragraph 60 of IAS 16 states that the depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.
- BC33B In response to the comments received on the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38)*, the IASB decided to clarify that a revenue-based depreciation method should not be applied because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset. The IASB also observed that the price component of revenue is sometimes affected by inflation and noted that inflation has no bearing upon the way in which the asset is worn out or used up. Consequently, the IASB observed that the use of a revenue-based method is not consistent with the main principle for depreciation in paragraph 60.
- BC33C The future economic benefits embodied in an asset are consumed by an entity principally through its use as described in paragraph 56 of IAS 16. The use of an asset can be assessed by reference to the asset's expected capacity or physical output as described in paragraph 56(a) of IAS 16. Other factors are mentioned in paragraph 56(b)–(d) of IAS 16 to assist in the determination of a pattern of consumption of an asset.
- BC33D The IASB also decided to clarify that reductions in the selling price could signal the existence of obsolescence which in turn reflects a reduction in the economic benefits consumed from the asset. Consequently, the IASB decided to amend paragraph 56(c) of IAS 16. The IASB noted that the guidance in paragraph 56(c) already considers technical or commercial obsolescence as a factor to determine the useful life of an asset and indicates how obsolescence can arise in some cases.



## Appendix A— Draft wording of the proposed amendment, showing differences from the currently effective standard (continued)

### [Draft] Amendments to IAS 38 *Intangible Assets*

Paragraphs 97A, 98A–98D and 130G are added. Paragraphs 92 and 98 are amended. Paragraph 97 is not proposed for amendment but is included here for ease of reference. New text is underlined.

#### Amortisation period and amortisation method

- 92 Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it is likely that their useful life is short. Future reductions in the selling price of an intangible asset could indicate the existence of commercial obsolescence, which in turn reflects a reduction in the economic benefits consumed from the intangible asset.
- 97 The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. Amortisation shall begin when the asset is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortisation shall cease at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 and the date that the asset is derecognised. The amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used. The amortisation charge for each period shall be recognised in profit or loss unless this or another Standard permits or requires it to be included in the carrying amount of another asset.
- 97A Paragraph 97 establishes consumption of the future economic benefits that are inherent in the asset as the principle for amortisation. The resulting amortisation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset.
- 98 A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits.
- 98A A revenue-based amortisation method is one that is derived from an interaction between units (ie quantity) and price, and that takes into account the expected future changes in price in determining the pattern of allocation of the cost of the asset for amortisation purposes. Such revenue-based method is not an appropriate amortisation method because it reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset. A revenue-based amortisation method is, consequently, inconsistent with the amortisation principle in paragraph 97

- 98B On choosing an appropriate amortisation method in accordance with paragraph 98, an entity could determine the limiting factor that is inherent in the intangible asset; for example, the contract that sets out the entity's rights over its use of an intangible asset might limit the entity's use of the intangible asset to a pre-determined number of years (ie time) or to a number of units produced or to an amount of revenue earned.
- 98C In the rare circumstance in which the right to use an intangible asset is expressed as a function of the revenue generated, then the revenue generated is a measure of consumption of the future economic benefits embodied in the asset. For example, an entity could acquire a concession to explore and extract gold from a gold mine. The duration of the contract is not based on time or in the amount of gold-extracted, but instead, it is based on the amount of gross revenue obtained from the extraction (eg a contract agreed upon an amount CU 2 billion currency units).
- 98D In some instances, the pattern of consumption of the economic benefits embodied in an intangible asset may be different because of the multiple activities in which the intangible asset is used. In such circumstances an entity could identify the different components inherent in the intangible asset that have different patterns of consumption of the economic benefits embodied in the intangible asset. The allocation of the cost of the intangible asset shall be done on a reasonable basis, for example, on the basis of the relative fair values of each component identified at the date of purchase. Once the cost of the intangible asset is allocated to the different components identified, each component shall be amortised over its respective useful economic life using an amortisation method that reflects the pattern of consumption of the economic benefits embodied in that components.

### **Effective date and transition**

- 130G Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38), issued in [date], added paragraphs 97A and 98A–98C and amended paragraph 98. An entity shall apply these amendments for annual periods beginning on or after [date] prospectively. Earlier application is permitted.

### **[Draft] Amendments to the Basis for Conclusions on IAS 38 *Intangible Assets***

Paragraph BC72A is amended. New text is underlined.

- BC72A The last sentence of paragraph 98 previously stated, 'There is rarely, if ever, persuasive evidence to support an amortisation method for intangible assets with finite useful lives that results in a lower amount of accumulated amortisation than under the straight-line method.' In practice, this wording was perceived as preventing an entity from using the units of production method to amortise assets if it resulted in a lower amount of accumulated amortisation than the straight-line method. However, using the straight-line method could be inconsistent with the general requirement of paragraph 38 that the amortisation method should reflect the expected pattern of consumption of the expected future economic benefits embodied in an intangible asset. Consequently, the Board decided to delete the last sentence of paragraph 98.

## Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, the proposed amendments.*

### Amortisation method

- BC75A The IASB discussed whether it would be appropriate for an intangible asset to be amortised using a revenue-based amortisation method. Paragraph 97 of IAS 38 states that the amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.
- BC75B In response to the comments received on the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38)*, the IASB decided to provide guidance on how an entity could choose an amortisation method. The IASB determined that in choosing an amortisation method an entity could determine what the limiting factor is for the use of the intangible asset; for example, a contract could be limited by a number of years (ie time) or a number of units produced or an amount of revenue earned.
- BC75C During its deliberations, the IASB considered the question of whether there could be limited circumstances in which revenue could be used to reflect the pattern in which the future economic benefits of the asset are expected to be consumed. The IASB noted that the limited circumstance when revenue could be used is when the right embodied by an intangible asset is contractually expressed as a function of revenue, such that the generation of revenue is the measure used to determine when the right expires. The IASB noted that in this case the pattern of consumption of the asset is defined by reference to the revenue earned.
- BC75D The IASB also decided to clarify that a revenue-based amortisation method should not be applied because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset. The IASB also observed that the price component of revenue is sometimes affected by inflation and noted that inflation has no bearing upon the way in which the asset is worn out or used up. Consequently, the IASB observed that the use of a revenue-based method is not consistent with the main principle for amortisation in paragraph 97. The one exception to this observation that the IASB noted was when revenue was the basis that limited the entity's use of the asset.
- BC75E In response to the Exposure Draft of this amendment, the IASB received comment letters indicating that revenue-based methods are sometimes used in situations in which an intangible asset is used in multiple activities and generates multiple cash flow streams on various different markets. For example, the producer of a motion picture often intends to use the intellectual property embodied in the film to generate cash flows through exhibiting the film in theatres, licensing the rights to characters to manufacturers of toys and other goods, selling DVDs or digital copies of the film, and licensing broadcast rights to television broadcasters.
- BC75F These respondents had pointed out that in such cases neither the straight-line amortisation method nor the application of a unit of production method would appropriately reflect the pattern of consumption of the intangible asset (eg. a film right). These respondents thought that a revenue-based method would be the most appropriate method to amortise the intangible asset because they thought that revenue would reflect the pattern of consumption of all the multiple activities in which an intangible asset could be used.

- BC75G The IASB acknowledged that determining an appropriate amortisation method for situations in which an intangible asset is used in multiple activities and generates multiple cash flow streams in various different markets requires significant judgement, particularly because different factors might appear to be appropriate measures of amortisation for each one of the different activities in which the intellectual property will be used.
- BC75H Nevertheless, the IASB noted that an amortisation method based on revenue is inconsistent with the principle stated in paragraph 97 of IAS 38, because this method reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset.
- BC75I The IASB believes that an appropriate measure of amortisation for such assets can be arrived at in a number of ways, including the allocation of the cost of the intangible asset into separate components, with each component reflecting the right to use the intellectual property in a particular activity (or group of activities). In doing so, an entity could identify the individual components (ie multiple intangible assets) and allocate the cost of the single intangible to the individual components identified on a reasonable basis, for example, on the basis of the relative fair values of each component identified at the date of purchase. An entity would then be able to apply an amortisation method to each portion of the asset, consistent with the principle in paragraph 97. The IASB determined that the need to identify separate components for a single transaction in order to apply an appropriate amortisation method should remain the primary consideration of this guidance. How this segmentation is done and how an entity determines an appropriate method of amortisation for each portion identified would require the use of judgement.
- BC75J The IASB noted that separating an asset into different components is not a new practice in business and consequently, it considered that this concept could be added as part of this amendment. The IASB also observed that the allocation of the cost of a single asset (or group of assets) based on the relative fair value amounts of the separate identifiable components, is not a new requirement in IFRSs.
- BC75K The IASB observed that paragraph 90(c) of IAS 38, refers to factors considered in determining the useful life of an intangible asset, and among them considers: “technical, technological, commercial or other types of obsolescence”. The IASB determined that further guidance could be added to paragraph 92 of IAS 38 to explain that future reductions in the selling price could indicate the existence of commercial obsolescence, which in turn reflects a reduction in the economic benefits consumed from the intangible asset.

### **Consistency in the use of the phrase “units of production”**

- BC75L The IASB decided to make consistent the phrase ‘units of production method’ and has therefore amended those instances of phrases ‘unit of production method’.

### **[Draft] Amendments to the Basis for Conclusions on IFRIC 12 Service Concession Arrangements**

Paragraph BC64 is amended. New text is underlined.
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- BC64 The IFRIC considered whether it would be appropriate for intangible assets under paragraph 26 to be amortised using an 'interest' method of amortisation, ie one that takes account of the time value of money in addition to the consumption of the intangible asset, treating the asset more like a monetary than a non-monetary asset. However, the IFRIC concluded that there was nothing unique about these intangible assets that would

justify use of a method of depreciation different from that used for other intangible assets. The IFRIC noted that paragraph 98 of IAS 38 provides for a number of amortisation methods for intangible assets with finite useful lives. These methods include the straight-line method, the diminishing balance method and the units of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits.

## Appendix B— Draft wording showing changes from the Exposure Draft

This Appendix shows revisions to the wording in the previously published exposure draft (December 2012), following our recommendations in this paper. New text is underlined and deleted text is ~~struck through~~

### [Draft] Amendments to IAS 16 *Property, Plant and Equipment*

Paragraph 56 (c) is amended. Paragraphs 60A, 62A and 81G are added. Paragraphs 60 and 62 are not proposed for amendment but are included here for ease of reference. ~~Paragraphs 62A–62B and 81G are added.~~ New text is underlined.

#### Depreciable amount and depreciation period

56 The future economic benefits embodied in an asset are consumed by an entity principally through its use. However, other factors, such as technical or commercial obsolescence and wear and tear while an asset remains idle, often result in the diminution of the economic benefits that might have been obtained from the asset. Consequently, all the following factors are considered in determining the useful life of an asset:

- (a) ...
- (c) technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand or as indicated by a future expected reduction in the unit selling price for the product or service output of the asset.

#### Depreciation method

60 The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

60A Paragraph 60 establishes consumption of the future economic benefits that are inherent in the asset as the principle for depreciation. The resulting depreciation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset.

62 A variety of depreciation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. The straight-line method results in a constant charge over the useful life if the asset's residual value does not change. The diminishing balance method results in a decreasing charge over the useful life. The units of production method results in a charge based on the expected use or output. The entity selects the method that most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. That method is applied consistently from period to period unless there is a change in the expected pattern of consumption of those future economic benefits.

~~62A A revenue-based depreciation method is one that is derived from an interaction between units (ie quantity) and price, and that takes into account the expected future changes in price in determining the pattern of allocation of the cost of the asset for depreciation purposes. Such revenue-based method is not an appropriate depreciation method because it reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset. A revenue-based depreciation method is, consequently, inconsistent with the depreciation principle in paragraph 60.~~

~~62A A method that uses revenue generated from an activity that includes the use of an asset is not an appropriate depreciation method for that asset, because it reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset. Paragraph 60 establishes consumption of the benefits that were inherent in the asset when it was acquired as the principle for depreciation.~~

~~62B When applying the diminishing balance method, information about technical or commercial obsolescence of the product or service output is relevant for estimating both the pattern of consumption of future economic benefits and the useful life of the asset. An expected future reduction in unit selling price of the product or service output of the asset could be an indication of the diminution of the future economic benefits of the asset as a result of technical or commercial obsolescence.~~

## Effective date and transition

~~81G Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38), issued in [date], added paragraphs 60A and 62A and 62B. An entity shall apply these amendments for annual periods beginning on or after [date] retrospectively prospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Earlier application is permitted.~~

## Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, the proposed amendments.*

### Depreciation method

~~BC33A The IASB discussed whether it would be appropriate for plant and equipment to be depreciated using a revenue-based depreciation. Paragraph 60 of IAS 16 states that the~~

depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

BC33B In response to the comments received on the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38)*, the IASB decided to clarify that a revenue-based depreciation method should not be applied because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset. The IASB also observed that the price component of revenue is sometimes affected by inflation and noted that inflation has no bearing upon the way in which the asset is worn out or used up. Consequently, the IASB observed that the use of a revenue-based method is not consistent with the main principle for depreciation in paragraph 60.

BC33C The future economic benefits embodied in an asset are consumed by an entity principally through its use as described in paragraph 56 of IAS 16. The use of an asset can be assessed by reference to the asset's expected capacity or physical output as described in paragraph 56(a) of IAS 16. Other factors are mentioned in paragraph 56(b)–(d) of IAS 16 to assist in the determination of a pattern of consumption of an asset.

BC33D The IASB also decided to clarify that reductions in the selling price could signal the existence of obsolescence which in turn reflects a reduction in the economic benefits consumed from the asset. Consequently, the IASB decided to amend paragraph 56(c) of IAS 16. The IASB noted that the guidance in paragraph 56(c) already considers technical or commercial obsolescence as a factor to determine the useful life of an asset and indicates how obsolescence can arise in some cases.



## Appendix B— Draft wording showing changes from the Exposure Draft (*continued*)

### [Draft] Amendments to IAS 38 *Intangible Assets*

Paragraphs 97A, 98A–98D and 130G are added. Paragraphs 92 and 98 are amended. Paragraph 97 is not proposed for amendment but is included here for ease of reference. ~~Paragraphs 98A–98B and 130G are added.~~ New text is underlined.

#### Amortisation period and amortisation method

- 92 Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it is likely that their useful life is short. Future reductions in the selling price of an intangible asset could indicate the existence of commercial obsolescence, which in turn reflects a reduction in the economic benefits consumed from the intangible asset.
- 97 The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. Amortisation shall begin when the asset is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortisation shall cease at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 and the date that the asset is derecognised. The amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used. The amortisation charge for each period shall be recognised in profit or loss unless this or another Standard permits or requires it to be included in the carrying amount of another asset.
- 97A Paragraph 97 establishes consumption of the future economic benefits that are inherent in the asset as the principle for amortisation. The resulting amortisation charge results from an estimation process and represents a measure of the consumption of the economic benefits inherent in the asset.
- 98 A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits.
- ~~98A A method that uses revenue generated from an activity that includes the use of an intangible asset is not an appropriate amortisation method for that intangible asset, because it reflects a pattern of economic benefits being generated from the intangible asset, rather than a pattern of consumption of the future economic benefits embodied in the intangible asset. Paragraph 97 establishes consumption of the benefits that were inherent in the asset when it was acquired as the principle for amortisation.~~

- 98A A revenue-based amortisation method is one that is derived from an interaction between units (ie quantity) and price, and that takes into account the expected future changes in price in determining the pattern of allocation of the cost of the asset for amortisation purposes. Such revenue-based method is not an appropriate amortisation method because it reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset. A revenue-based amortisation method is, consequently, inconsistent with the amortisation principle in paragraph 97
- 98B On choosing an appropriate amortisation method in accordance with paragraph 98, an entity could determine the limiting factor that is inherent in the intangible asset; for example, the contract that sets out the entity's rights over its use of an intangible asset might limit the entity's use of the intangible asset to a pre-determined number of years (ie time) or to a number of units produced or to an amount of revenue earned.
- 98C In the rare circumstance in which the right to use an intangible asset is expressed as a function of the revenue generated, then the revenue generated is a measure of consumption of the future economic benefits embodied in the asset. For example, an entity could acquire a concession to explore and extract gold from a gold mine. The duration of the contract is not based on time or in the amount of gold-extracted, but instead, it is based on the amount of gross revenue obtained from the extraction (eg a contract agreed upon an amount CU 2 billion currency units).
- ~~98B When applying the diminishing balance method, information about technical or commercial obsolescence of the product or service output is relevant for estimating the pattern of consumption of future economic benefits of the asset and the useful life of the asset. A future expected reduction in unit selling price of the product or service output of the asset could be an indication of the diminution of the future economic benefits of the intangible asset as a result of technical or commercial obsolescence.~~
- 98D In some instances, the pattern of consumption of the economic benefits embodied in an intangible asset may be different because of the multiple activities in which the intangible asset is used. In such circumstances an entity could identify the different components inherent in the intangible asset that have different patterns of consumption of the economic benefits embodied in the intangible asset. The allocation of the cost of the intangible asset shall be done on a reasonable basis, for example, on the basis of the relative fair values of each component identified at the date of purchase. Once the cost of the intangible asset is allocated to the different components identified, each component shall be amortised over its respective useful economic life using an amortisation method that reflects the pattern of consumption of the economic benefits embodied in that components.

### **Effective date and transition**

- 130G *Clarification of Acceptable Methods of Depreciation and Amortisation* (Amendments to IAS 16 and IAS 38), issued in [date], added paragraphs 97A and 98A–98C and amended paragraph 98 and added paragraphs 98A–98B. An entity shall apply these amendments for annual periods beginning on or after [date] ~~retrospectively~~ prospectively. Earlier application is permitted.

## [Draft] Amendments to the Basis for Conclusions on IAS 38 *Intangible Assets*

Paragraph BC72A is amended. New text is underlined.

BC72A The last sentence of paragraph 98 previously stated, 'There is rarely, if ever, persuasive evidence to support an amortisation method for intangible assets with finite useful lives that results in a lower amount of accumulated amortisation than under the straight-line method.' In practice, this wording was perceived as preventing an entity from using the units of production method to amortise assets if it resulted in a lower amount of accumulated amortisation than the straight-line method. However, using the straight-line method could be inconsistent with the general requirement of paragraph 38 that the amortisation method should reflect the expected pattern of consumption of the expected future economic benefits embodied in an intangible asset. Consequently, the Board decided to delete the last sentence of paragraph 98.

### Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, the proposed amendments.*

#### Amortisation method

BC75A The IASB discussed whether it would be appropriate for an intangible asset to be amortised using a revenue-based amortisation method. Paragraph 97 of IAS 38 states that the amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

BC75B In response to the comments received on the Exposure Draft *Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38)*, the IASB decided to provide guidance on how an entity could choose an amortisation method. The IASB determined that in choosing an amortisation method an entity could determine what the limiting factor is for the use of the intangible asset; for example, a contract could be limited by a number of years (ie time) or a number of units produced or an amount of revenue earned.

BC75C During its deliberations, the IASB considered the question of whether there could be limited circumstances in which revenue could be used to reflect the pattern in which the future economic benefits of the asset are expected to be consumed. The IASB noted that the limited circumstance when revenue could be used is when the right embodied by an intangible asset is contractually expressed as a function of revenue, such that the generation of revenue is the measure used to determine when the right expires. The IASB noted that in this case the pattern of consumption of the asset is defined by reference to the revenue earned.

BC75D The IASB also decided to clarify that a revenue-based amortisation method should not be applied because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset. The IASB also observed that the price component of revenue is sometimes affected by inflation and noted that inflation has no bearing upon the way in which the asset is worn out or used up. Consequently, the IASB observed that the use of a revenue-based method is not consistent with the main principle for

amortisation in paragraph 97. The one exception to this observation that the IASB noted was when revenue was the basis that limited the entity's use of the asset.

BC75E In response to the Exposure Draft of this amendment, the IASB received comment letters indicating that revenue-based methods are sometimes used in situations in which an intangible asset is used in multiple activities and generates multiple cash flow streams on various different markets. For example, the producer of a motion picture often intends to use the intellectual property embodied in the film to generate cash flows through exhibiting the film in theatres, licensing the rights to characters to manufacturers of toys and other goods, selling DVDs or digital copies of the film, and licensing broadcast rights to television broadcasters.

BC75F These respondents had pointed out that in such cases neither the straight-line amortisation method nor the application of a unit of production method would appropriately reflect the pattern of consumption of the intangible asset (eg. a film right). These respondents thought that a revenue-based method would be the most appropriate method to amortise the intangible asset because they thought that revenue would reflect the pattern of consumption of all the multiple activities in which an intangible asset could be used.

BC75G The IASB acknowledged that determining an appropriate amortisation method for situations in which an intangible asset is used in multiple activities and generates multiple cash flow streams in various different markets requires significant judgement, particularly because different factors might appear to be appropriate measures of amortisation for each one of the different activities in which the intellectual property will be used.

BC75H Nevertheless, the IASB noted that an amortisation method based on revenue is inconsistent with the principle stated in paragraph 97 of IAS 38, because this method reflects a pattern of the future economic benefits being generated from the asset, rather than a pattern of consumption of the future economic benefits embodied in the asset.

BC75I The IASB believes that an appropriate measure of amortisation for such assets can be arrived at in a number of ways, including the allocation of the cost of the intangible asset into separate components, with each component reflecting the right to use the intellectual property in a particular activity (or group of activities). In doing so, an entity could identify the individual components (ie multiple intangible assets) and allocate the cost of the single intangible to the individual components identified on a reasonable basis, for example, on the basis of the relative fair values of each component identified at the date of purchase. An entity would then be able to apply an amortisation method to each portion of the asset, consistent with the principle in paragraph 97. The IASB determined that the need to identify separate components for a single transaction in order to apply an appropriate amortisation method should remain the primary consideration of this guidance. How this segmentation is done and how an entity determines an appropriate method of amortisation for each portion identified would require the use of judgement.

BC75J The IASB noted that separating an asset into different components is not a new practice in business and consequently, it considered that this concept could be added as part of this amendment. The IASB also observed that the allocation of the cost of a single asset (or group of assets) based on the relative fair value amounts of the separate identifiable components, is not a new requirement in IFRSs.

BC75K The IASB observed that paragraph 90(c) of IAS 38, refers to factors considered in determining the useful life of an intangible asset, and among them considers: "technical, technological, commercial or other types of obsolescence". The IASB determined that further guidance could be added to paragraph 92 of IAS 38 to explain that future reductions in the selling price could indicate the existence of commercial obsolescence, which in turn reflects a reduction in the economic benefits consumed from the intangible asset.

## **Consistency in the use of the phrase “units of production”**

BC75L The IASB decided to make consistent the phrase ‘units of production method’ and has therefore amended those instances of phrases ‘unit of production method’.

### **Basis for Conclusions**

*This Basis for Conclusions accompanies, but is not part of, the proposed amendments.*

#### **Depreciation and amortisation method**

- ~~BC1—The IASB discussed whether it would be appropriate for plant and equipment to be depreciated and for intangible assets to be amortised using a revenue-based depreciation or amortisation method. A revenue-based depreciation or amortisation method is one that is derived from an interaction between units (ie quantity) and price, and that takes into account the expected future changes in price as the depreciation basis to allocate the amount of an asset that is to be depreciated or amortised. Paragraph 60 of IAS 16 and paragraph 97 of IAS 38 states that the depreciation or amortisation method used shall reflect the pattern in which the asset’s future economic benefits are expected to be consumed by the entity.~~
- ~~BC2—The IASB proposes that a revenue-based depreciation or amortisation method should not be applied because it reflects a pattern of economic benefits being generated from operating the business (of which the asset is part) rather than the economic benefits being consumed through the use of the asset. The future economic benefits embodied in an asset are consumed by an entity principally through its use as described in paragraph 56 of IAS 16. The use of an asset can be assessed by reference to the asset’s expected capacity or physical output as described in paragraph 56(a) of IAS 16. Other factors are mentioned in paragraph 56(b)–(d) of IAS 16 to assist in the determination of a pattern of consumption of an asset.~~
- ~~BC3—During its deliberations, the IASB considered the question of whether there could be limited circumstances in which revenue could be used to reflect the pattern in which the future economic benefits of the asset are expected to be consumed. The IASB noted that the limited circumstance when revenue could be used is when the use of a revenue-based method gives the same result as the use of a units of production method.~~
- ~~BC4—For example, some types of intellectual property assets (for example, acquired rights to broadcast a film) will initially incur a significant decline in value followed by a diminishing rate of decline (for example, when a film is initially shown and with each subsequent showing the value of the rights typically decrease quickly at first and then at a slower rate). The IASB noted that the use of a time-based straight line amortisation method may not be appropriate in those cases because these rights have an inherent and fast initial pattern of decline in value.~~
- ~~BC5—The IASB observed that in those cases a measure such as the number of viewers attracted could be used as a reasonable basis for the pattern in which the benefits for those rights are expected to be consumed. In rare cases such as this, advertising revenue could serve as an equivalent for viewer numbers to the extent that advertising revenue has a linear relationship with viewer numbers.~~
- ~~BC6—The IASB also proposes to clarify that expected future reductions in the unit selling price of the product or service output of the asset could be an indicator of the diminution of the future economic benefits of the asset as a result of technical or commercial obsolescence (which is described as a factor for determining the useful life of an asset in paragraph~~

~~56(c) of IAS 16 and in paragraph 90(c) of IAS 38), and thereby relevant when applying the diminishing balance method.~~

~~BC7— The IASB decided to make consistent the phrase ‘units of production method’ and has therefore amended those instances of phrases ‘unit of production method’.~~

## **[Draft] Amendments to the Basis for Conclusions on IFRIC 12 *Service Concession Arrangements***

Paragraph BC64 is amended. New text is underlined.

BC64 The IFRIC considered whether it would be appropriate for intangible assets under paragraph 26 to be amortised using an 'interest' method of amortisation, ie one that takes account of the time value of money in addition to the consumption of the intangible asset, treating the asset more like a monetary than a non-monetary asset. However, the IFRIC concluded that there was nothing unique about these intangible assets that would justify use of a method of depreciation different from that used for other intangible assets. The IFRIC noted that paragraph 98 of IAS 38 provides for a number of amortisation methods for intangible assets with finite useful lives. These methods include the straight-line method, the diminishing balance method and the units of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits.