Mr Kevin Stevenson
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Dear Kevin

Exposure Draft ED 231 – ED/2012/5 - Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38)

Grant Thornton Australia Limited (Grant Thornton) is pleased to provide the Australian Accounting Standards Board with its comments on ED 231 which is a re-badged copy of the International Accounting Standards Board's (the Board) Exposure Draft Clarification of Acceptable Methods of Depreciation and Amortisation (Proposed amendments to IAS 16 and IAS 38) (the ED). We have considered the ED, as well as the accompanying draft Basis for Conclusions.

Grant Thornton's response reflects our position as auditors and business advisers to the Australian business community. We work with listed and privately held companies, government, industry, and not-for-profit organisations (NFPs). This submission has benefited with input from our clients, Grant Thornton International which will be finalising a global submission to the IASB by its due date of 2 April 2013, and discussions with key constituents.

We support clarification in these areas. We also agree with the proposal to prohibit the use of depreciation or amortisation methods that are based on actual revenue generated. However, we suggest that the final amendments should acknowledge that for some assets the expected future pattern of revenue generation can serve as a valid proxy for the expected consumption of economic benefits.

Our detailed comments set out in the Appendix to this letter.

If you require any further information or comment, please contact me.

Yours sincerely
GRANT THORNTON AUSTRALIA LIMITED

Keith Reilly
National Head of Professional Standards

A. IASB Comments on specific proposals

Question 1 - the IASB proposes to amend IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets to prohibit a depreciation or amortisation method that uses revenue generated from an activity that includes the use of an asset. This is because it reflects a pattern of future economic benefits being generated from the asset, rather than reflecting the expected pattern of consumption of the future economic benefits embodied in the asset. Do you agree? Why or why not?

We agree that a depreciation or amortisation method based on actual revenue generated (presumably as a proportion of expected lifetime revenue) is inappropriate. This is because revenues are a measure of the results of using an asset (usually along with other assets, people and processes) rather than a measure of the economic benefits embodied within the asset. For example, a method based on actual revenues earned would result in zero depreciation/amortisation during periods in when an entity uses an intangible asset for defensive purposes rather than for revenue generation.

That said, we note that the concept of the economic benefits embodied within an asset is not precise or well-elaborated in IFRSs. For those assets with a reasonably objective and determinable revenue potential which is consumed through usage, estimated future reductions in that potential would seem to be a valid proxy for usage (and, therefore, for the consumption of economic benefits). Accordingly, we think that for some assets the expected <u>future</u> pattern of revenue generation can serve as a valid proxy for the expected consumption of economic benefits embodied within an asset. This seems to be acknowledged in discussion in paragraphs BC3 – BC6 of the ED.

BC3 asserts 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. This may be so, but we note that the units of production method is not defined in IFRS and is normally used only for tangible assets that have a finite capacity and produce homogeneous outputs. An intangible asset such as acquired film rights does not fit this description.

We would therefore prefer that the main body of the amendments acknowledges the use of expected revenue as a proxy, and outlines the situations in which such an approach might be appropriate.

Question 2 - do you have any other comments on the proposals?

New paragraphs 62A of IAS 16 and 98A of IAS 38 mention that paragraphs 60 of IAS 16 and 97 of IAS 38 establish the consumption of the benefits that were inherent in the asset (or intangible asset) when it was acquired as the principle for depreciation. However, paragraphs 60 of IAS 16 and 97 of IAS 38 do not make reference to "when the asset was acquired". The depreciation method should not only reflect the expected pattern of consumption of the future economic benefits on acquisition but should also constantly be re-examined. Therefore, we suggest removing the following words in paragraphs 62A of

IAS 16 and 98A of IAS 38: "...establishes consumption of the benefits inherent in the asset as the principle of depreciation".

New paragraphs 62B of IAS 16 and 98B of IAS 38 explain that an expected future reduction in the unit selling price of the product or service output of an asset could indicate technical or commercial obsolescence and could therefore be relevant to the application of the diminishing balance method. We agree with the basic statement, but suggest that its purpose and effect should be clarified.

The new text expands on paragraphs 56 of IAS 16 and 90 of IAS 38 on estimating useful life. This guidance therefore seems relevant to any method of depreciation or amortisation, and also to revising the useful life, estimating and revising residual values and to assessing impairment.

If the Board considers that an expected future reduction in unit selling price of the product or service output has a specific impact on the application of the diminishing balance method (for example in selecting the percentage rate to be used over the life of the asset or in specific periods) we suggest this should be stated more explicitly.

Lastly, new paragraph 98A of IAS 38 should include the following underlined words in order to be consistent with paragraph 62A of IAS 16:

"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 <u>the future</u> economic benefits being generated from the intangible asset, rather than a pattern of consumption of the future economic benefits embodied in the intangible asset."

B. AASB invitation to comment questions

Question 1 - Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

a not-for-profit entities; and

b public sector entities – including any implications for GAAP/GFS harmonisation.

We are not aware of any regulatory issues.

Question 2 - Whether, overall, the proposals would result in financial statements that would be useful to users.

We agree that the proposals would result in financial statements that would be useful to users.

Question 3 - Whether the proposals are in the best interests of the Australian economy.

We agree that the proposals are in the best interests of the Australian economy.

Question 4 - Unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

We have no further comment.