MAZARS

Comment Letters
IASB
30 Cannon Street
London EC4M 6XH
United Kingdom

Paris, March 28th, 2013

Exposure Draft 2012/5: Clarification of Acceptable Methods of Depreciation and Amortisation

Dear Sir or Madam,

MAZARS welcomes the opportunity to comment on the International Accounting Standards Board's Exposure Draft, *Clarification of Acceptable Methods of Depreciation and Amortisation*.

While we agree that revenue-based depreciation (or amortisation) methods are usually not appropriate, we disagree with the proposition to completely prohibit their use, since valid examples exist where such methods faithfully reflect the consumption pattern of economic benefits embodied in the asset (such as acquired rights to broadcast a film – as rightfully pointed out in the Basis for conclusions of the Exposure Draft – or more broadly, film rights or TV program rights in the media industry).

Should the Board decide to maintain these amendments, we would recommend modifying the wording so as to permit the use of revenue-based depreciation (or amortisation) methods in limited circumstances (we propose an alternative wording in the appendix to this letter) and explaining in the Basis for Conclusions that the equivalence between the revenue-based method and the units of production method can be assessed using qualitative arguments.

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Our detailed answers to the questions raised in the Exposure Draft are shown in the appendix to this letter.

We would be pleased to discuss our comments with you and remain at your disposal should you need further clarification or additional information.

Best regards,

Michel Barbet-Massin
Head of Financial Reporting Technical Support

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 disagree with the proposed amendments.

To support its view, the Exposure Draft mainly focuses on the distinction between the generation pattern of revenues and the consumption pattern of economic benefits embodied in an asset. We do not deny that this is a meaningful distinction to consider when determining the depreciation (or amortisation) method for an asset: revenue-based depreciation methods are generally not appropriate for investments in property, plant and equipment for that precise reason (since in most cases, the normal wear and tear of PPE will not be directly linked to the generation of revenue).

However, determining the appropriate depreciation (or amortisation) method for an asset is essentially a matter of judgment, as is clear from the following requirements of IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*:

- *"Depreciation (amortisation) is the systematic allocation of the depreciable amount of an asset over its useful life"* (IAS 16 Definitions; IAS 38 Definitions)

- *"The depreciation (amortisation) method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity."* (IAS 16.60; IAS 38.97)

- *"A variety of depreciation (amortisation) methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. [...]"* (IAS 16.62; IAS 38.98)

- *"[...] If that pattern cannot be determined reliably, the straight-line method shall be used. [...]"* (IAS 38.97)

In practice, selecting the appropriate depreciation (or amortisation) method requires taking into account entity specific circumstances and making assumptions: this necessarily entails accepting a reasonable degree of judgment. Therefore we do not consider it appropriate in IFRSs to prohibit a specific depreciation (or amortisation) method, unless it has been established that applying this method always leads to significantly inappropriate results.

The Exposure Draft does not demonstrate that revenue-based depreciation (or amortisation) methods always lead to significantly inappropriate results. On the contrary, paragraphs BC3-BC5 present a case (acquired rights to broadcast a film) where the use of a revenue-based amortisation method is perfectly justified.

Moreover, the fundamental principle for depreciation (or amortisation) under IAS 16 and IAS 38 is that the method used should *"reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity"*. In cases where no other feasible method appears to faithfully reflect that pattern, prohibiting revenue-based methods could potentially lead to major inconstancies with this principle. We believe that such regrettable consequence could be reached in the media industry, where revenue-based methods are commonly used for amortising rights on films and TV programs in IFRS financial statements (economic benefits embodied in these assets are neither consumed in a linear relationship with time, nor in a linear relationship with the number of viewers since the economic benefits associated with each viewing can significantly differ from one broadcasting media to another) and appear to be the methods that best represent the consumption of economic benefits embodied in such assets.

We do not perceive any added value in introducing a prohibition to use revenue-based methods in IAS 16 and IAS 38 as a mere rule of prudence either since we feel the current requirements of the standards are sufficient to ensure prudence is respected.

However, should the Board decide to maintain these amendments, we would then recommend:

- modifying the wording so as to permit the use of revenue-based depreciation (or amortisation) methods in limited circumstances (we would also recommend supressing the words *"when it was acquired"* which are inconsistent with the requirements of IAS 16 and IAS 38 to regularly review the depreciation / amortisation method of an asset); for instance:

  "A method that uses revenue generated from an activity that includes the use of an asset is <u>usually</u> not an appropriate depreciation (amortisation) 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 (amortisation)."

- expanding the discussions in BC3-BC5 to explain that the equivalence between the revenue-based method and the units of production method can be assessed using qualitative arguments.

Question 2
Do you have any other comments on the proposals?

No.