

Proposal to ban revenue-based amortisation

Consumption, not generation

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IN THE HEADLINES

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“The proposals seek to bring closure to a long-running technical debate, but it remains to be seen whether all industries agree.”

– Paul Munter
KPMG’s global IFRS business combinations and consolidation leader

Revenue-based amortisation would be banned

The IASB proposes to amend IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* to state explicitly that revenue-based methods of amortisation (and depreciation) cannot be used. Under revenue-based methods, the profile of amortisation expense reflects the profile of revenues generated through use of the asset.

Sectors most likely to be impacted

Revenue-based methods are sometimes used to amortise intangible assets in the media sector, because films and video games often generate higher revenues in the earlier years of their life; this means that revenue-based amortisation tends to accelerate expense recognition in these cases. In addition, some service concession operators believe that revenue-based amortisation is appropriate for intangible assets recognised under IFRIC 12 *Service Concession Arrangements*. However, in contrast to the media sector, service concession intangible assets often generate higher revenues in the later years of their life; therefore, revenue-based amortisation tends to defer expense recognition in these cases.

Consumption, not generation

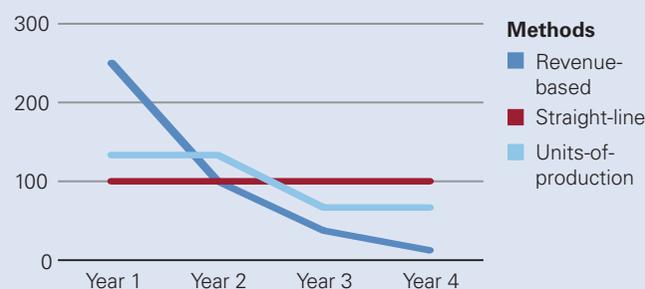
The IASB notes that revenue-based methods of amortisation reflect a pattern of generation of economic benefits rather than a pattern of consumption of the underlying asset’s benefits. The IASB believes that amortisation should reflect consumption only. Under the proposals, an entity would still be required to use judgement to determine an appropriate amortisation method – e.g. straight-line or units-of-production; however, revenue-based methods as a general concept would be off the table.

Example fact pattern

- An entity has programme rights that last for 4 years, which cost 400 to acquire.
- The programme rights are expected to generate total revenue of 800, and the programme is expected to run 6 times over 4 years. (In other cases, viewer numbers might be chosen as a proxy for units of production.)
- Actual revenue and runs are as follows.

	Revenue	Runs
Year 1	500	2
Year 2	200	2
Year 3	75	1
Year 4	25	1
TOTAL	800	6

Results



Observations

As the example demonstrates, the extent of the impact would depend on the correlation between an alternative amortisation method based on consumption and revenue generation.

In some sectors, banning revenue-based amortisation could lead to an increase in usage of the straight-line method, which is simple to apply. Entities in other sectors may be drawn more to the units-of-production method. The IASB appears to envisage this method being used in the media sector, and anticipates advertising revenue being used as a basis for amortisation in rare cases – i.e. when a linear relationship between advertising revenue and viewer numbers can be established.

However, any change in amortisation method may result in impairment charges in the later years of the asset’s life when there is a significant decline in future cash flows.

Adoption and comment deadline

The exposure draft does not propose an effective date but indicates that early adoption would be allowed. Retrospective application is proposed. Comments are due to the IASB by 2 April 2013.

Find out more

For more information on the amendments, please speak to your usual KPMG contact or go to the [IASB press release](#).

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