



NZ ACCOUNTING  
STANDARDS  
BOARD

## **Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to NZ IAS 16 and NZ IAS 38)**

This Standard was issued by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013 on 3 July 2014.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on 31 July 2014.

Reporting entities that are subject to this Standard are required to apply it in accordance with the effective date, which is set out in Part C.

In finalising this Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to amend the relevant New Zealand Tier 1 and Tier 2 For-profit Accounting Standards as a result of changes to an International Financial Reporting Standard.

CLARIFICATION OF ACCEPTABLE METHODS OF DEPRECIATION AND AMORTISATION  
(AMENDMENTS TO NZ IAS 16 AND NZ IAS 38)

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## Part A

### Introduction

This Standard amends NZ IAS 16 *Property, Plant and Equipment* and NZ IAS 38 *Intangible Assets*.

NZ IAS 16 and NZ IAS 38 both establish the principle for the basis of depreciation and amortisation as being the expected pattern of consumption of the future economic benefits of an asset. This Standard clarifies that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. This Standard also clarifies that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. This presumption, however, can be rebutted in certain limited circumstances.

## Part B

### Amendments to NZ IAS 16 *Property, Plant and Equipment*

#### Scope

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This Standard applies to Tier 1 and Tier 2 for-profit entities.

Paragraph 56 is amended and paragraphs 62A and 81I are added. Paragraphs 60–62 are not amended 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 for the product or service output of the asset. Expected future reductions in the selling price of an item that was produced using an asset could indicate the expectation of technical or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in 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.
- 61 The depreciation method applied to an asset shall be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method shall be changed to reflect the changed pattern. Such a change shall be accounted for as a change in an accounting estimate in accordance with NZ IAS 8.
- 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. Straight-line depreciation 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 depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate. The revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits of the asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.
- ...

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**Effective date**

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...

81I Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to NZ IAS 16 and NZ IAS 38), issued in July 2014, amended paragraph 56 and added paragraph 62A. An entity shall apply those amendments prospectively for annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

## Amendments to NZ IAS 38 *Intangible Assets*

### Scope

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This Standard applies to Tier 1 and Tier 2 for-profit entities.

Paragraph 92 is amended. In paragraph 98, the phrase 'unit of production method' has been amended to 'units of production method'. Paragraphs 98A–98C and 132I are added. Paragraph 97 is not amended but is included here for ease of reference. Deleted text is struck through and new text is underlined.

### Useful life

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...

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~~ will often be the case that their useful life is short. Expected future reductions in the selling price of an item that was produced using an intangible asset could indicate the expectation of technological or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in the asset.

...

### Amortisation period and amortisation method

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 NZ 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.**

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 There is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. The revenue generated by an activity that includes the use of an intangible asset typically reflects factors that are not directly linked to the consumption of the economic benefits embodied in the intangible asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed. This presumption can be overcome only in the limited circumstances:

- (a) in which the intangible asset is expressed as a measure of revenue, as described in paragraph 98C;  
or
- (b) when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.

98B In choosing an appropriate amortisation method in accordance with paragraph 98, an entity could determine the predominant 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 specify the entity's use of the intangible asset as a predetermined number of years (ie time), as a number of units produced or as a fixed total amount of

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revenue to be generated. Identification of such a predominant limiting factor could serve as the starting point for the identification of the appropriate basis of amortisation, but another basis may be applied if it more closely reflects the expected pattern of consumption of economic benefits.

98C In the circumstance in which the predominant limiting factor that is inherent in an intangible asset is the achievement of a revenue threshold, the revenue to be generated can be an appropriate basis for amortisation. For example, an entity could acquire a concession to explore and extract gold from a gold mine. The expiry of the contract might be based on a fixed amount of total revenue to be generated from the extraction (for example, a contract may allow the extraction of gold from the mine until total cumulative revenue from the sale of gold reaches CU2 billion) and not be based on time or on the amount of gold extracted. In another example, the right to operate a toll road could be based on a fixed total amount of revenue to be generated from cumulative tolls charged (for example, a contract could allow operation of the toll road until the cumulative amount of tolls generated from operating the road reaches CU100 million). In the case in which revenue has been established as the predominant limiting factor in the contract for the use of the intangible asset, the revenue that is to be generated might be an appropriate basis for amortising the intangible asset, provided that the contract specifies a fixed total amount of revenue to be generated on which amortisation is to be determined.

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## **Transitional provisions and effective date**

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132I Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to NZ IAS 16 and NZ IAS 38), issued in July 2014, amended paragraphs 92 and 98 and added paragraphs 98A–98C. An entity shall apply those amendments prospectively for annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.



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**Part C**

**Effective date**

This Standard is effective for annual periods beginning on or after 1 January 2016. Earlier application is permitted.