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International Public Sector Accounting Standards Board

International Federation of Accountants

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13 August 2009

Dear Stephenie,

EXPOSURE DRAFT 40: INTANGIBLE ASSETS

We enclose our response to your request for comment on Exposure Draft 40 – *Intangible Assets* issued by the International Federation of Accountants – International Public Sector Accounting Standards Board (IPSASB).

In compiling our comment, the Accounting Standards Board, the official accounting standard setter for the public sector in South Africa, consulted widely with our stakeholders (comprising professional bodies, auditors and preparers) in formulating our comment to you.

Our response is structured into specific matters, other matters and editorial amendments.

Please do not hesitate to contact me should you wish to discuss any of our comment.

Yours sincerely

Swart

Erna Swart

Chief Executive Officer

SPECIFIC MATTERS FOR COMMENT

Do you agree that the changes made to IAS 38, in particular the scope exclusions set out in paragraphs 2 and 4, and the additional public sector guidance are:

- *Necessary in the circumstances?*
- *Appropriately reflected in the revised wording?*

We support the scope exclusions in paragraphs 2 and 4, but recommend that the Basis for Conclusions should be further expanded to explain why the IPSASB has concluded that the power to grant rights and the power to tax does not meet the definition of an asset.

We also agree with the additional public sector guidance provided, and feel that it is necessary to clarify the differences between the private sector and public sector.

For further comment on the scope exclusions and on the additional guidance included in the proposed IPSAS, please refer to our comment below.

OTHER MATTERS

Introduction

1. IN5 states that intangible assets acquired in an entity combination arising from an exchange transaction are included in the scope of the Standard. As it is not clear from this description whether the proposed Standard applies to exchange transactions under common control, exchange transactions not under common control, or both, a reference to the appropriate IPSAS should rather be included (i.e. IPSAS XX (ED 41) *Entity Combinations from Exchange Transactions)*.

   This amendment should also be incorporated elsewhere in the proposed IPSAS, where appropriate (for example paragraph .44 and .45).

2. We are of the view that IN10 does not add any value to the overall understanding of the proposed IPSAS, and should only be highlighted in the comparison with IAS 38. We therefore recommend the deletion of IN10.

3. IN16 should also highlight that intangible assets that are not yet available for use are also subject to an annual impairment test under IPSAS 26. IN16 currently only highlights that an intangible asset with an indefinite useful life is subject to an annual impairment test under IPSAS 26.

4. In addition, the last sentence in IN16 should also include a reference to IPSAS 21, as the requirement to annually test an intangible asset with an indefinite useful life also applies to non-cash-generating assets subsequently measured under the cost model, as reflected in the consequential amendments to paragraph 26 in IPSAS 21 (see IPSAS 21.26 in Appendix B).

Objective

5. Paragraph .02 explains that the “power to grant rights and the power to tax” do not satisfy the criteria for recognition as an *intangible asset*. The introduction (IN2) and the Basis for Conclusions (BC3), however, explain that the criteria for recognition of an *asset* are not met. Paragraph .02 should be clarified to explain that the power to grant rights and the power to tax do not meet the definition of an asset, as opposed to an intangible asset.

6. Paragraph .02 explains that the “power to grant rights and the power to tax” are excluded from the scope of the proposed IPSAS. It is unclear whether this exclusion applies to rights and powers granted to entities in terms of legislation, for example the legislative right granted to a local authority to provide water to its citizens, or to issue fines. We recommend that the Basis for Conclusions should further explain whether the abovementioned powers and rights are by implication also excluded or included from the scope of the proposed IPSAS.

7. Furthermore, as paragraph .02 deals with a scope exclusion, we recommend that the paragraph should rather be included as an explanatory paragraph in the scope section, i.e. after paragraph .04(f), that specifically

mentions the exclusion of the power to grant rights and the power to tax. Both the introduction section of the proposed IPSAS and the Basis for Conclusions explain this scope exclusion under the heading “scope”.

Scope

8. Paragraph .05(g) as amended could be interpreted differently compared to the equivalent paragraph in IAS 38 (see IAS 38.03(g)), as “deferred acquisition costs” were deleted. The amendment to the IAS 38 paragraph should be reconsidered.

Definitions

9. The last part of the definition of “cost” should be deleted to align the definition with that in IPSAS 17:

   <u>Cost</u> is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction.

10. The concept of service potential should be included in the definition of “entity specific value”:

    <u>Entity-specific value</u> is the present value of the cash flows <u>or service potential</u> an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.

11. The definition section currently only includes the definitions relating to the impairment of cash-generating assets. As intangible assets measured under the cost method are also subject to impairment testing, the definitions for an “impairment loss of a non-cash-generating asset” should also be included.

12. The following standard paragraph as included in other IPSASs should be included after the definition section:

    Terms defined in other International Public Sector Accounting Standards are used in this Standard with the same meaning as in those other Standards, and are reproduced in the Glossary of Defined Terms published separately.

Intangible Assets

13. The example of a “franchise” in paragraph .18 is not an appropriate public sector example, and should be deleted from the list of common examples.

Intangible Assets: Identifiability

14. As the concept of a binding arrangement is unique to the public sector (paragraph .21), we recommend that explanatory guidance should be included to explain the term.

Intangible Assets: Control

15. We question the public sector relevance of paragraph .25 and propose the deletion of the paragraph.

Recognition and Measurement at Recognition

16. Paragraph .29 as amended could be interpreted differently compared to the equivalent paragraph in IAS 38 (see IAS 38.20), as “to develop” was replaced with “on behalf of”. The amendment to the IAS 38 paragraph should be reconsidered.

17. We propose that “as appropriate” in paragraph 30(b) should be deleted, and that the concepts in paragraph .33 should be addressed in two separate paragraphs, similar to that in IPSAS 17.26 and .27. In addition, the phrase “in accordance with paragraphs 34-53” only applies to intangible assets measured initially at cost. The phrase should therefore only be included as part of the first concept.

Intangible assets acquired through non-exchange transactions other than non-exchange entity combinations

18. In the public sector it might be likely that fair value can not be determined by reference to an active market, and as a result, that entity should use alternative methods to determine the fair value for the intangible asset. We therefore propose that paragraph .53 should also include the reference to paragraph .47 to .49 (and not only to paragraph .87) that allows alternative methods for determining the fair value of the intangible asset, in the absence of an active market.

Exchanges of assets in exchange transactions

19. IPSAS 23 provides guidance on the measurement of assets acquired through a non-exchange transaction that lacks commercial substance. Option (a) in paragraph .54 is therefore not appropriate, as the principles in IPSAS 23 should be applied under such circumstances. As a result, option (a) in paragraph .54 and the entire paragraph .55 should be deleted.

Recognition of an Expense

20. There seems to be a contradiction between paragraph .77(b) and the principle included in paragraph .19 of ED 41 *Entity Combinations from Exchange Transactions*. The principle in paragraph .77(b) can be interpreted as allowing and entity to recognise the “power to grant rights and the power to tax” as an asset as part of goodwill. It is recommended that the example “the power to grant rights and the power to tax” in paragraph .77(b) should be deleted.

21. The example of a “mail order catalogue” in paragraph .78(c) is not an appropriate public sector example, and should be replaced with a more appropriate one.

Measurement after Recognition

22. The revaluation model in paragraph .85 requires that intangible assets should be carried at a revalued amount less any subsequent accumulated amortisation and any subsequent accumulated *impairment losses*.

IPSAS 26 however excludes from its scope, intangible assets carried at revalued amounts that are regularly revalued to fair value. A similar scope exclusion is included in the consequential amendments to IPSAS 21 as proposed in this IPSAS (see Appendix B).

If cash-generating and non-cash-generating intangible assets are to be excluded from the scope of IPSAS 21 and IPSAS 26, the revaluation model incorrectly requires the deduction of subsequent accumulated impairment losses in paragraph .85. Similarly, paragraph .92 should exclude the reference to subsequent accumulated impairment losses.

If the revaluation model in paragraph .85 is amended, it should be explained in the Basis for Conclusions, including the reason for the departure from IAS 38. Currently the exclusion of impairment testing for cash-generating and non-cash-generating intangible assets carried at revalued amounts are only explained in the Basis for Conclusions to IPSAS 21 and IPSAS 26.

Recoverability of the carrying amount – impairment losses

23. IPSAS 26 and the proposed amendments to IPSAS 21 require an entity to test intangible assets with indefinite useful lives or intangible assets not yet available for use annually for impairment, irrespective of whether there is any indication of impairment.

Eventhough impairment testing for intangible assets carried at revalued amounts is excluded from the scope of IPSAS 21 and IPSAS 26, it is not clear whether such an exclusion also applies to intangible assets with indefinite useful lives or intangible assets not yet available for use that are carried at revalued amounts. In the absence of such an exclusion, it is assumed that intangible assets with indefinite useful lives or intangible assets not yet available for use carried at revalued amounts, are subject to an annual impairment testing.

There is thus inconsistency between the treatment of intangible assets with indefinite useful lives or intangible assets not yet available for use carried at revalued amounts, and other intangible assets carried at revalued amounts. Consideration should be given to this inconsistency and sufficient guidance should be provided to clarify the inconsistency.

Disclosure

24. The examples of “franchises” and “recipes” in paragraph .130(d) and (f) are not appropriate public sector examples, and should be deleted.

Basis for Conclusions

25. The Basis for Conclusions as currently drafted does not in all instances sufficiently explain the IPSASB’s views and reasoning behind the inclusion or exclusion of certain principles when compared to the equivalent IAS 38. For example, BC3 does not explain why the IPSASB is of the view that the definition of an asset was not met. Similarly, BC5 does not clarify why the identifiable criterion was expanded. As the Basis for Conclusions should in

all instances clearly explain the reasoning and other public sector considerations that was taken into account in drafting the proposed IPSAS, we propose that the explanations for the departure from IAS 38 should be elaborated.

26. In addition, we recommend that the amendment from “contractual or other legal rights” to “binding arrangement (including rights from contracts or other legal rights” be further explained in BC5 to further clarify the public sector amendment.

27. We propose the deletion of BC6 to BC10 as these paragraphs merely summarise the differences with IAS 38, and should only be included as part of the comparison with IAS 38.

Comparison with IAS 38

28. The comparison with IAS 38 is not included in the clean copy of the exposure draft.

29. The fifth bullet, that explains the inclusion of an intangible asset acquired as part of an entity combination, should be deleted as it is not a difference with IAS 38.

30. The following differences between the proposed IPSAS and IAS 38 should also be highlighted in the comparison:

    - IAS 38 requires intangible assets to be initially measured at cost. The IPSAS further states that where an intangible asset is acquired at no cost or for a nominal cost, its costs is its fair value as at the date it is acquired.
    - The IPSAS includes an additional scope exclusion of the power to grant rights and the power to tax. Explanatory guidance has also been included to explain this scope exclusion.

EDITORIAL AMENDMENTS

In addition to the comment above, the following editorial amendments are proposed:

Reference	Current wording	Proposed amendment
IN16 last sentence	"….under IPSAS 26, to annually test an intangible asset with an indefinite useful life"	"….under IPSAS 26, to annually test an intangible asset with an indefinite useful life for impairment"
IN20	"IPSAS XX(ED 40) also contains certain exemptions for recognition….."	"IPSAS XX(ED 40) also contains ~~certain exemptions~~ relief for recognition….."
Paragraph 11 second sentence	"…significant public person in, for example…"	"…significant public person ~~in~~ on, for example…"
Paragraph 14 first sentence	"….about recognized intangible assets…"	"….about recognized intangible heritage assets…"
Paragraph 17 Definition: impairment loss	"an impairment loss is the amount….."	"an impairment loss of a cash-generating asset is the amount…..
Paragraph 20 first sentence	"….the definition of an intangible asset require an …."	"….the definition of an intangible asset requires an ...."
Paragraph 44 first sentence	"…separable or arises from contractual or other legal rights, sufficient…"	"…separable or arises from binding arrangements (including rights from contracts ~~contractual~~ or other legal rights), sufficient…"
Paragraph 69 last sentence	"….if the asset will generate economic benefits only in …"	"….if the asset will generate economic benefits or service potential only in …"
Paragraph 75 second paragraph	"….as an element of the cost of asset that …."	"….as an element of the cost of an asset that …."

Reference	Current wording	Proposed amendment
Paragraph 77	“expenditure on an intangible item shall be …”	“expenditure on an intangible ~~item~~ <u>asset </u>shall be …”
Paragraph 87 second sentence	“….(see paragraph 74, the revaluation….”	“….(see paragraph 74<u>)</u>, the revaluation….”
Paragraph 97 first sentence	“…the increase recognised in the revaluation surplus…”	“…the ~~increase recognised in the~~ <u>accumulated</u> revaluation surplus…”
Paragraph 135(b)	“….on the distribution of the balance to shareholders or other equity holders…”	“….on the distribution of the balance to ~~shareholders or other equity holders~~ <u>owners</u>…”
Paragraph 144 second sentence	“…initially recognized an item of property, plant and equipment at cost…”	“…initially recognized an ~~item of property, plant and equipment~~ <u>intangible asset</u> at cost…”
Paragraph 150 second sentence	“…major classes of asset that have been…..”	“…major classes of <u>intangible </u>asset<u>s</u> that have been…..”
Paragraph 150 last sentence	“…details of the assets or classes of asset that were not …..”	“…details of the <u>intangible</u> assets or classes of <u>intangible </u>asset<u>s</u> that were not …..”
Comparison bullet 2	“…include contractual rights arising …”	“…include contractual rights <u>and other legal rights</u> arising …”
Comparison bullet 8	“…have been modified only as necessary to better”	“…have been modified ~~only as necessary~~ to better”