



# Exposure Draft and Basis for Conclusions

## **PURCHASED INTANGIBLES: NARROW-SCOPE AMENDMENTS**

**NOVEMBER 2019**

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**COMMENTS TO PSAB MUST BE RECEIVED BY  
January 31, 2020**

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We value your input and look forward to your feedback on this Exposure Draft. Comment on this document by uploading your response letter via this [online form](#). Please address your response to:

Michael Puskaric, CPA, CMA  
Director, Public Sector Accounting  
Public Sector Accounting Board  
277 Wellington Street West  
Toronto ON M5V 3H2

This Exposure Draft reflects proposals made by the Public Sector Accounting Board (PSAB).

Individuals, governments and organizations are invited to send written comments on the Exposure Draft proposals. Comments are requested from those who agree with the Exposure Draft as well as from those who do not.

Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft should clearly explain the problem and include a suggested alternative, supported by specific reasoning. All comments PSAB receives will be available on the website shortly after the comment deadline, unless confidentiality is requested. The request for confidentiality must be stated explicitly within the response.

## HIGHLIGHTS

The Public Sector Accounting Board (PSAB) proposes, subject to comments received following exposure, to amend FINANCIAL STATEMENT CONCEPTS, Section PS 1000, and FINANCIAL STATEMENT PRESENTATION, Section PS 1201, in the CPA Canada Public Sector Accounting (PSA) Handbook to allow for the recognition of purchased intangibles in public sector financial statements.

The Basis for Conclusions, which accompanies this Exposure Draft, sets out the Board's position with its reasons.

### Main features of the Exposure Draft

Narrow-scope amendments are being proposed to:

- remove the recognition prohibition on purchased intangibles from Section PS 1000;
- remove the disclosure requirements from Section PS 1201 relating to purchased intangibles not recognized; and thus,
- allow for the recognition of purchased intangibles in public sector financial statements.

### Comments requested

PSAB welcomes comments from individuals, governments and organizations on all aspects of the Exposure Draft.

When comments have been prepared as a result of a consultative process within an organization, it is helpful to identify generically the source of the comment in the response. This promotes understanding of how the proposals affect various aspects of an organization.

Comments are most helpful if they relate to a specific principle, paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft should clearly explain the problem and include a suggested alternative, supported by specific reasoning.

Please respond to the following question:

Do you agree that the PSA Handbook should allow recognition in public sector financial statements of intangibles purchased through an exchange transaction, as proposed in the specific narrow-scope amendments for Sections PS 1000 and PS 1201 in this Exposure Draft? Why or why not?

An [online response form](#), linked to this document, has been provided to assist you in submitting your comments to PSAB. Alternatively, you may send comments via email (in Word format), to: [info@psabcanada.ca](mailto:info@psabcanada.ca).

## FINANCIAL STATEMENT CONCEPTS, Section PS 1000

### Proposal

FINANCIAL STATEMENT CONCEPTS, Section PS 1000, would be amended as indicated below. Additional text is denoted by underlining and deleted text by strikethrough.

### RECOGNITION

...

- .57 Purchased natural resources, intangibles<sup>1</sup> and Crown lands are recognized in government financial statements when they meet the asset definition and the recognition criteria. However, when natural resources, intangibles and Crown lands have been inherited by the government in right of the Crown and have not been purchased, they are not given accounting recognition as assets in government financial statements. Similarly, developed intangibles, as well as art and historical treasures are also not recognized as assets. ~~These items are not recognized as assets because the costs, benefits and economic value of such items cannot be reasonably and verifiably quantified using existing methods. Similarly, art and historic treasures are also not recognized as assets.~~
- .58 ~~In the absence of appropriate public sector recognition and measurement criteria for intangibles, all intangibles, including those that have been purchased, developed, constructed or inherited in right of the Crown, are not recognized as assets in government financial statements. The intangible often called “human capital” that embodies the talent or intellectual capital of government employees is not recognized as an asset under existing accounting principles.~~

## FINANCIAL STATEMENT PRESENTATION, Section PS 1201

### Proposal

FINANCIAL STATEMENT PRESENTATION, Section PS 1201, would be amended as indicated below. Additional text is denoted by underlining and deleted text by strikethrough.

- .068 *Financial statements should disclose that all developed or inherited intangibles, works of art and historical treasures, and items inherited by right of the Crown, such as Crown lands, ~~forests, water, and mineral~~ and natural resources; are not recognized in government financial statements. [MONTH 2020]*
- .069 FINANCIAL STATEMENT CONCEPTS, paragraphs PS 1000.57–~~58~~, specifies that all developed or inherited intangibles, works of art and historical treasures, and items inherited by right of the Crown, ~~and art and historic treasures~~ are not recognized as assets in government financial statements.

## CONSEQUENTIAL AMENDMENTS

### FINANCIAL STATEMENT OBJECTIVES, Section PS 1100:

- .25 Certain non-financial resources are, however, not given accounting recognition as assets in government financial statements. For example, ~~all government~~ intangibles, ~~and all~~ natural resources and Crown lands that have not been purchased by the government, are not given accounting recognition in government financial statements. A government’s non-financial assets, as defined in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, comprise the recognized non-financial resources of a government.

1 Applying the requirement to recognize in financial statements purchased intangibles that meet the definition of an asset and the recognition criteria is effective for fiscal years beginning on or after April 1, 2021. Earlier adoption is encouraged. Application may be retroactive or prospective in accordance with ACCOUNTING CHANGES, paragraph PS 2120.13.

## BASIS FOR CONCLUSIONS

### Introduction

1. This Basis for Conclusions is a supporting document to PSAB's Exposure Draft, "Purchased Intangibles: Narrow-Scope Amendments."
2. The Basis for Conclusions is not issued under PSAB's authority. Prior to approving the final narrow-scope amendments to the standards, the Board will review and deliberate responses to the Exposure Draft.

### Background

3. Recognition prohibitions currently exist in the PSA Handbook. They disallow certain items from recognition as assets in financial statements for pragmatic reasons.
4. The PSA Handbook currently excludes all intangibles, all works of art and historical treasures, inherited Crown lands and inherited natural resources from recognition as assets in public sector financial statements. Purchased natural resources and Crown lands can be recognized as assets in financial statements if they meet the definition of an asset set out in FINANCIAL STATEMENT CONCEPTS, paragraph PS 1000.35, and elaborated on in ASSETS, Section PS 3210, as well as the general recognition criteria in paragraphs PS 1000.55-.56.

### Proposal

5. Similar to purchased natural resources and Crown lands, PSAB proposes to allow recognition of purchased intangibles. Purchased intangibles are those acquired through an arm's length exchange transaction between knowledgeable, willing parties that are under no compulsion to act. Recognition would be appropriate if the purchased intangible meets the definition of an asset and the general recognition criteria.
6. Intangibles that are developed or inherited in right of the Crown would continue to be excluded from recognition as assets in financial statements.

### Rationale

7. The status of the recognition prohibitions is under reconsideration in PSAB's Concepts Underlying Financial Performance project (i.e., its conceptual framework and reporting model review). However, in response to stakeholders, the Board proposes to allow recognition of purchased intangibles now, rather than waiting for final pronouncements in that project.
8. Indigenous governments have asked PSAB to reconsider the prohibition on recognizing purchased intangibles. Writing off such acquisitions is a material issue for some Indigenous governments. It affects the representation of their financial results and their financial position, especially if such acquisitions are financed with debt. Some government organizations have also had to write off the cost of intangibles acquired in exchange transactions and would prefer asset recognition of purchased intangibles.
9. Purchased intangibles are acquired through an exchange transaction in which a negotiated price is paid. So, initial measurement of these intangibles is possible and their recognition appropriate if they meet the definition of an asset and the general recognition criteria.

## Implications

10. Public sector entities will need to consider if purchased intangibles meet the definition of an asset and the recognition criteria. Those that do will be required to be recognized in financial statements effective for fiscal years beginning on or after April 1, 2021, although earlier adoption is encouraged.

Entities may adopt this new requirement retroactively or prospectively in accordance with ACCOUNTING CHANGES, paragraph PS 2120.13.

11. At this time, PSAB is not proposing to include any additional guidance in the PSA Handbook as a consequence of allowing recognition of purchased intangibles in financial statements.
12. The PSA Handbook does not currently include any accounting requirements for intangibles, with two exceptions:
- (a) Software: TANGIBLE CAPITAL ASSETS, paragraph PS 3150.05(a), footnote 2, defines tangible capital assets to include computer software. Software is generally classified as an intangible asset by other standard setters (e.g., in International Accounting Standard (IAS) 38, *Intangible Assets*, and International Public Sector Accounting Standard 31, *Intangible Assets*, which is based on IAS 38).
  - (b) The purchase premium paid on acquisition of a government business enterprise: All or part of that premium may be a purchased intangible (i.e., “goodwill”). INVESTMENTS IN GOVERNMENT BUSINESS ENTERPRISES, paragraph PS 3070.17, requires the deferral and amortization of a purchase premium arising on acquisition of a government business enterprise over the lesser of the useful life of the purchase premium or 20 years (straight line or another systematic amortization method). The government business enterprise must have a realistic and specific business plan.<sup>2</sup> The plan must demonstrate that the government business enterprise’s projected results of operations would be sufficient to recover the purchase premium over its amortization period. The absence of such evidence would indicate that the purchase premium should be charged to expenses at acquisition, not deferred.  
  
In contrast, a purchase premium on acquisition of any entity other than a government business enterprise is written off at acquisition (ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510).
13. Similar to other items not currently addressed in the PSA Handbook, it is expected stakeholders will consider the following to determine when and how to account for any purchased intangibles in their financial statements:
- (a) the GAAP hierarchy in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150;
  - (b) the definition of an asset in Section PS 1000;
  - (c) the guidance in Section PS 3210; and
  - (d) the general recognition criteria in Section PS 1000.

<sup>2</sup> GOVERNMENT REPORTING ENTITY, paragraph PS 1300.31, states that one of the factors in assessing if a government business enterprise meets the financial sustainability criterion inherent in the definition of a government business enterprise is whether the organization has in place “realistic and specific plans that show how it expects to be able to maintain its operations and meet its liabilities in the future.”

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