

Intangible Assets

Ind AS 38

Agenda

Objective and Scope

Definitions

Recognition

Initial Measurement

Subsequent Measurement

Retirement and Disposals

Disclosures

Key Differences

Objective and scope

- ▶ **Ind AS 38 prescribes the** accounting treatment for intangible assets, except:
 - ▶ That are within the scope of other standards
 - ▶ Intangible assets held for sale in the ordinary course of business (Ind AS 2)
 - ▶ Deferred tax assets (Ind AS 12)
 - ▶ Leases within scope of Ind AS 17
 - ▶ Assets arising from employee benefits (Ind AS 19)
 - ▶ Goodwill acquired in a business combination (Ind AS 103)
 - ▶ Non-current intangible assets classified as held for sale (Ind AS 105)
 - ▶ Financial assets (Ind AS 32)
 - ▶ Expenditure on development and extraction of minerals, oil, natural gas and similar non-regenerative resources
 - ▶ Exploration and evaluation assets (Ind AS 106)

Definitions

▶ Intangible Assets

- ▶ An **identifiable** non-monetary asset without physical substance
- ▶ Examples include Patents, Copyrights, Licenses, Intellectual Property, Trademarks etc.
- ▶ An intangible asset is identifiable when it is separable and arises from contractual or other legal rights.

▶ Asset

- ▶ An **asset** is a resource:
 - ▶ Controlled by an entity as a result of past events
 - ▶ From which future economic benefits are expected to flow to the entity
- ▶ **Control** means the the power to obtain the future economic benefits from the underlying resource; and the ability to restrict the access of others to those benefits.
- ▶ **Future Economic Benefits** may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity.

Definitions

- ▶ Identifiability criterion is met when an intangible item:
 - ▶ Arises from contractual or other legal rights, or
 - ▶ Is capable of being separated or divided from the entity and sold, transferred, licensed, rented, or exchanged
- ▶ Control criterion is met on existence of (illustrative list):
 - ▶ Legal rights that are enforceable in a court of law, or
 - ▶ Exchange transactions for the same or similar item

Case study 1 – customer portfolio

- ▶ Entity X acquires a customer portfolio in a business acquisition.
- ▶ There are no legal contracts with customers to protect Entity X's interests.
- ▶ Would Entity X be able to recognise an intangible asset?

No X cannot recognise an intangible asset since there is insufficient control over the expected economic benefits from customer portfolio

Example

- ▶ Classify each of the following assets as either tangible or intangible:
 1. The operating system of a personal computer
 2. An off-the-shelf integrated publishing software package
 3. Specialized software embedded in computer controlled machine tools
 4. A “firewall” controlling access to restricted sections of an Internet website

Example

1. Tangible: the operating system (e.g. DOS or Windows) of a personal computer is an integral part of the related hardware and should be accounted for under Ind AS 16
2. Intangible: such computer software is not an integral part of the hardware on which it is used.
3. Tangible: specialised software integrated into production line “robots” is similar in nature to (1)
4. Intangible: companies developing “firewall” software to protect their own websites may also sell the technology to other companies

Recognition of intangible assets

- ▶ An intangible asset should be recognised only when:

It is probable that expected future economic benefits that are attributable to the asset will flow to the entity.

and

The cost of the asset can be measured reliably.

- ▶ An intangible asset should be measured initially at cost.

Initial measurement



Initial measurement



Separate acquisition

- ▶ Includes
 - ▶ Purchase price + import duties + non-refundable purchase taxes - trade discounts - rebates
 - ▶ Directly attributable cost of preparing the asset
- ▶ Excludes*
 - ▶ Cost of introducing a new product or service
 - ▶ Costs of conducting business in a new location or with new class of customers (including costs of staff training)
 - ▶ Administration and other general overhead
 - ▶ Initial operating losses

* *illustrative*

Case study

- ▶ Theo is an incorporated entity. On 31 December it acquired the exclusive rights to a patent that had been developed by another entity. The amount payable for the rights was \$900,000 immediately and \$500,000 in one year's time. Theo has incurred legal fees of \$117,000 in respect of the bid.
- ▶ Theo operates in a jurisdiction where the government charges a flat rate fee (a “stamp duty”) of \$5,000 for the registration of patent rights
- ▶ Theo's cost of capital is 10%

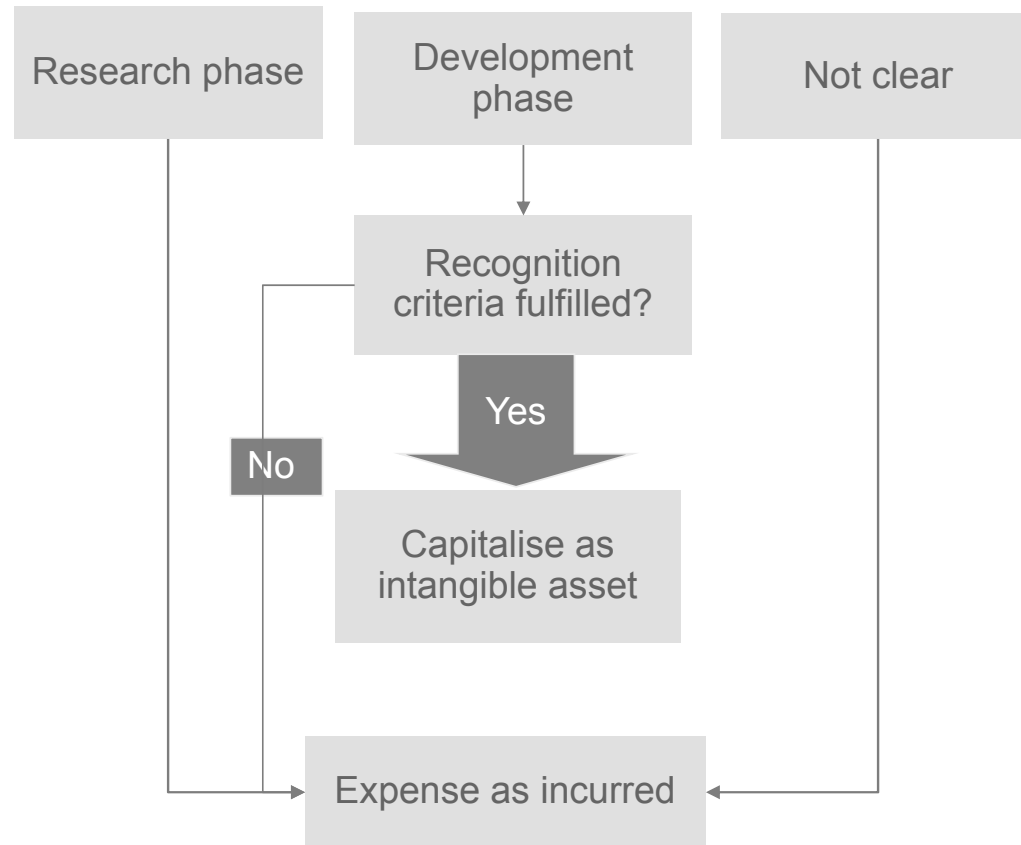
Calculate the cost of the patent rights on initial recognition

Solution

- ▶ Cost of patent rights on initial recognition:

| Particulars | Amount |
|---|-----------|
| Cash Paid | 900,000 |
| Deferred consideration (500,000 X 1/1.1) | 454,545 |
| Legal Fees | 117,000 |
| Stamp Duty | 5,000 |
| Total | 1,476,545 |

Internally generated intangibles



Internally generated intangibles (cont.)

Criteria for recognizing development expense:

- ▶ Expense is capitalized only if ALL below mentioned criteria are met:
 - ▶ Technical feasibility of completing the intangible asset
 - ▶ Intention to complete the intangible asset and use or sell it
 - ▶ Ability to use or sell the intangible asset
 - ▶ How the intangible asset will generate probable future economic benefits
 - ▶ Availability of adequate technical, financial and other resources to complete the development and to use and sell the intangible asset
 - ▶ Ability to reliably measure the expenditure attributable to intangible asset during its development

Internally generated intangibles (cont.)

Cost includes:

- ▶ Costs of materials and services
- ▶ Costs of employee benefits
- ▶ Fees to register a legal right
- ▶ Amortisation of patents and licences
- ▶ Overheads to the extent necessary to generate the asset and can be allocated on a reasonable and consistent basis
- ▶ Borrowing costs in certain cases (i.e., Ind AS 23)

Recognise from the day recognition criteria are fulfilled

Costs already expensed are never recognised, i.e., past expenses not to be recognised as an asset

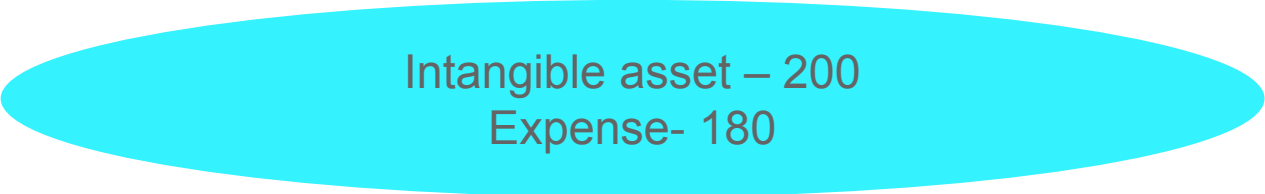
Internally generated intangibles (cont.)

Costs not to capitalise –

- ▶ Selling, administrative and other general overhead expenditure unless it can be directly attributed to preparing the asset for use
- ▶ Inefficiencies and initial operating losses
- ▶ Expenditure on training staff to operate the asset

Case study 2 – R&D expenditure

- ▶ An undertaking is developing a new process. During 2014, expenditure incurred was 2,000, of which 1,800 were incurred before 1 Nov 2014 and 200 were incurred between 1 Nov 2014 and 31 Dec 2014.
- ▶ At 1 Nov 2014, the process met the criteria for recognition as an intangible asset. The fair value of the know-how in the process is 1,000.
- ▶ Explain the treatment of the expenditure incurred.

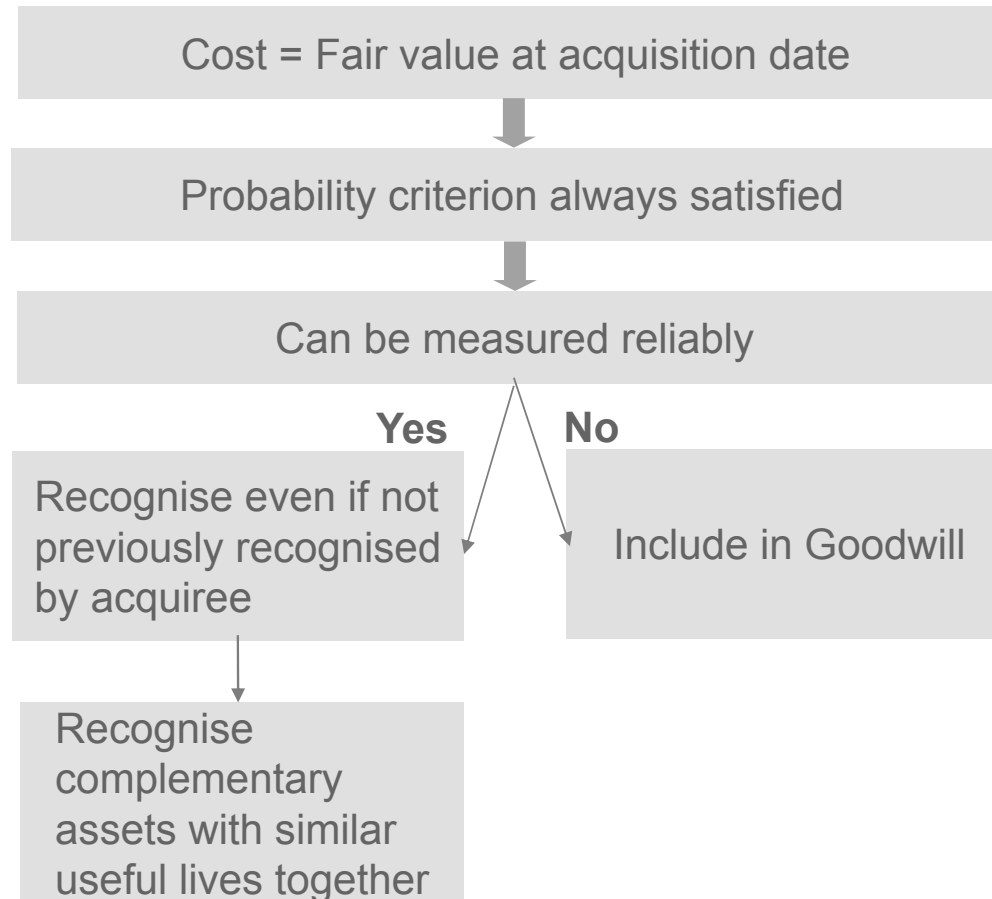


Intangible asset – 200
Expense- 180

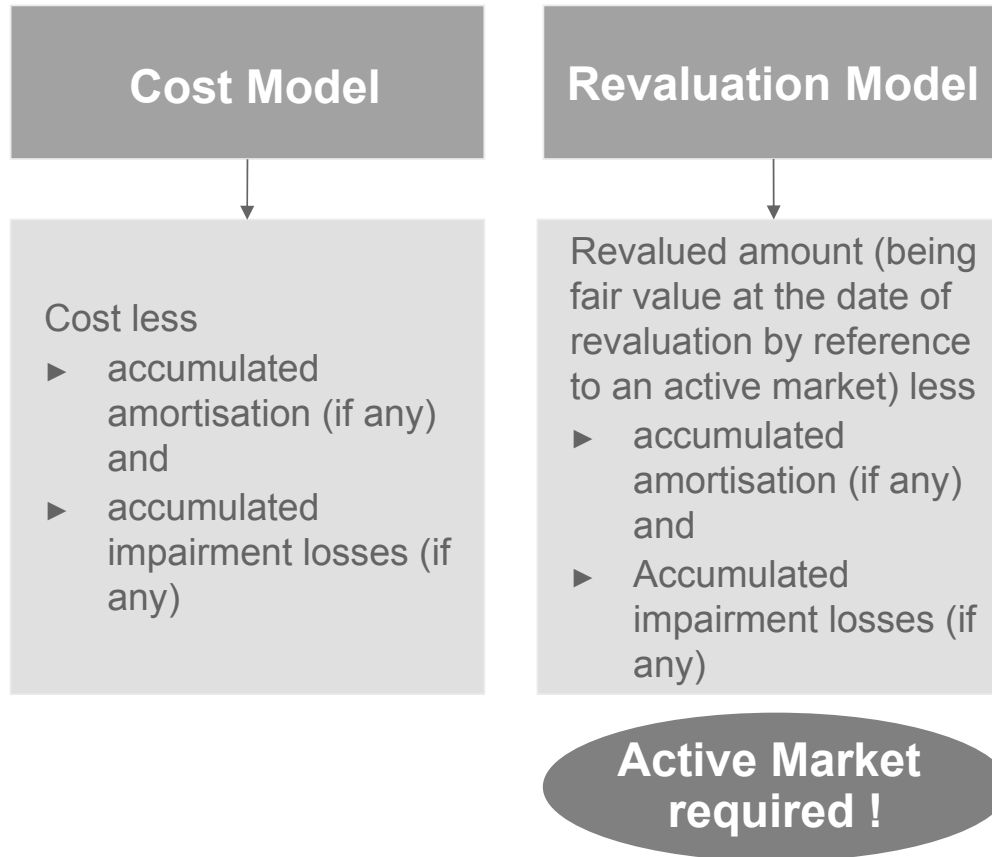
Measurement of intangible asset through government grants

- ▶ Intangible asset acquired by way of government grant includes airport landing rights, licences to operate radio or television stations
- ▶ Initially intangible assets and the grant can be recognized in accordance with Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance at fair value.

Measurement of intangible asset through business combination



Subsequent measurement



Revaluation model

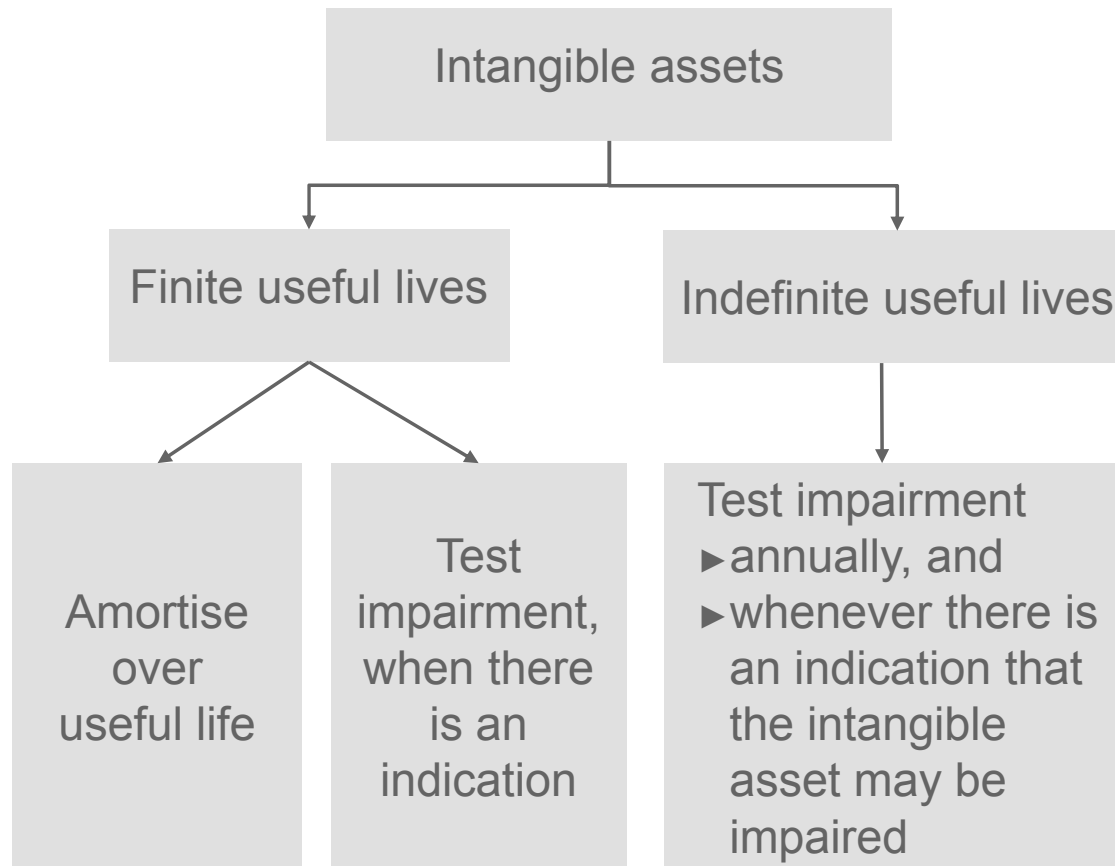
Intangible asset's carrying value increased as a result of revaluation

- ▶ increase recognised in Other Comprehensive Income and accumulated in equity under revaluation surplus
- ▶ increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss.

Intangible asset's carrying value decreased as a result of revaluation

- ▶ decrease shall be recognised in profit or loss.
- ▶ decrease shall be recognised in Other Comprehensive Income to the extent of any credit balance in the revaluation surplus in respect of that asset.

Amortization and impairment



Useful life

- ▶ Factors to consider in determining useful life include –
 - ▶ typical product life cycles for the asset and public information on estimates of useful lives of similar assets used in a similar way
 - ▶ technical, technological, commercial or other types of obsolescence
 - ▶ changes in the market demand for the products or services output from the asset
 - ▶ expected actions by competitors or potential competitors
 - ▶ the level of maintenance expenditure required
 - ▶ period of control over the asset

Retirement and disposals

- ▶ An asset is derecognised:
 - ▶ On disposal (e.g., sale or finance lease); or
 - ▶ When no future economic benefits are expected from its use or disposal
- ▶ Recognise gain or loss on derecognition (i.e., difference between net disposable proceeds and the carrying amount of the asset) in profit or loss when the asset is derecognised
 - ▶ Gains should not be classified as revenue

Disclosures

Disclose* for each class of intangible assets, distinguishing between internally generated and other intangible assets:

- ▶ Whether useful lives are indefinite or finite
- ▶ Useful lives or amortisation rates and method used
- ▶ Gross carrying amount and accumulated amortisation and impairment loss at beginning and end of the period
- ▶ Line item of the statement of comprehensive income in which any amortisation of intangibles asset is included
- ▶ Reconciliation of the carrying amounts at the beginning and end of reporting period

* *illustrative list*

Disclosures

More detailed disclosures* are required for:

- ▶ Intangible assets with indefinite useful life
- ▶ Intangible assets measured after recognition using the revaluation model
- ▶ Research and development expenditure

* *illustrative list*

Key differences with Ind AS and Indian GAAP

| Difference | Ind AS 38 | Indian GAAP |
|--------------------|--|--|
| Measurement | IAS 38 allows measurement either at cost or revalued amounts | AS 26 requires measurement at cost |
| Useful life | Useful life may be finite or indefinite | No concept of indefinite life. Presumption that life cannot exceed 10 years. |

Key differences with Ind AS and Indian GAAP

| Difference | Ind AS 38 | Indian GAAP |
|-------------------------------|---|--|
| Deferred payment | If payment for an intangible asset is deferred beyond the normal credit terms, the difference between this amount and total payments is recognised as interest expense over the period of credit unless it is capitalized as per Ind AS 23. | No such provision in AS 26. |
| Subsequent expenditure | Subsequent expenditure on an in-process research and development project acquired in a business combination is dealt with Para 42 and 43 of Ind AS 38. | No guidance regarding the accounting treatment in AS 26. |

Key differences with Ind AS and Indian GAAP

| Difference | Ind AS 38 | Indian GAAP |
|---|--|---|
| Residual value | Residual value is reviewed at least at each financial year end. | AS 26 specifically requires that the residual value is not subsequently increased for changes in prices or value. |
| Change in method of amortization | considered as change in estimate | considered as change in accounting policy |
| Asset not yet available for use | No requirement for impairment testing of assets not yet available for use. | Requires annual impairment testing of assets not yet available for use. |

Thank You