Accounting for Intangible Assets

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Intangible Assets

Examples:

- Goodwill- internally generated and acquired
- Trade mark and brand names- internally generated and acquired
- Patents
- Copyright
- Franchise
- Licenses
- Customer loyalty

Intangible Assets

Identifiable

Un-identifiable

LKAS 38

Other LKAS/SLFRS

(e.g. SLFRS 10)

The Nature of Intangible Assets

- Intangible Assets are identifiable non-monetary assets without physical substance. *(LKAS 38)*

- Key Characteristics of Intangible Assets:
  - Identifiability
  - Control over resource
  - Existence of future economic benefits

Identifiability

- Requires to be identifiable to distinguish from goodwill.

- An asset is identifiable if it *either*:
  - **Separable** – i.e. capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so *or*
  - **Arises from contractual or other legal rights**, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

Recognition

- Recognition of an item as an intangible asset requires an entity to demonstrate that the items meets:
  - The definition of an intangible asset
  - The recognition criteria

Recognition Criteria

- An intangible asset shall be recognized if and only if:
  - It is probable that the future economic benefits that are attributable to the asset will flow to the entity; and
  - The cost of the asset can be measured reliably.

Initial Measurement of an Intangible Asset

- At cost
  - Separate acquisition
  - Acquisition as part of business combination
  - Internally generated intangible assets

Separate Acquisition

- Cost comprises of :
  - Purchase price including import duties and non-refundable purchase taxes after deducting trade discounts and rebates.
  - Any directly attributable cost of preparing the asset for its intended use.

Acquisition as part of a Business Combination

- Cost of the intangible asset is its fair value at the date of acquisition.

- An acquirer recognizes an intangible asset that meets the recognition criteria even if that had not been recognized in the F/S of the acquiree.

Measuring the fair value of an intangible asset acquired in a business combination

- If separable or arises from contractual or other legal rights, sufficient information exists to measure the fair value reliably.

- If separable from goodwill but only together with a tangible or intangible asset. Recognizes the group of assets as a single asset if fair values of individual assets in the group are not reliably measurable.

Internally Generated Intangible Assets

- Sometimes difficult to assess whether internally generated intangible assets qualifies for recognition because of the problems in:
  - identify whether and when, there is an identifiable asset that will generate expected future economic benefits; *and*
  - determine the cost of the asset reliably.

Generation of Internally Generated Intangibles

- Research Phase

Should be recognized as an expense when it is incurred.

- Development Phase

Should be recognized as an asset if certain conditions are satisfied.

Recognition of Internally Generated Intangible Assets

- If an enterprise can demonstrate all of the following:
  - Technical feasibility
  - Intention to complete and use or sell it
  - Ability to use or sell the intangible asset
  - How the intangible asset will generate probable future economic benefits
  - The availability of adequate resources
  - The ability to measure reliably expenditure attributable to the intangible asset during its development

Non-Recognition of Internally Generated Intangible Assets

Prohibits the recognition as assets - internally generated:

- goodwill,
- brands,
- mastheads,
- publishing titles,
- customer lists and
- items of similar in substance as they cannot be distinguished from the cost of developing the business as a whole.

Expenses on Intangible Assets

Expenditure on an intangible asset that was initially recognized as an expense shall not be recognized as part of the cost of an intangible asset at a latter date.

Measurement after Recognition

- Choose either cost model or revaluation model as the accounting policy.
  - **Cost Model :** Cost *less* any accumulated amortization and any accumulated impairment losses.
  - **Revaluation Model :** Fair value at the date of revaluation *less* any subsequent accumulated amortization and any subsequent accumulated impairment losses.

Revaluation of Intangible Assets

- The fair value should be determined by reference to an active market.
- Frequency of revaluation depends on the volatility of the fair values of the intangible assets being revaluated.
- If an intangible asset in a class of revalued intangible assets cannot be revalued due to absence of an active market, it should be carried out at cost less accumulated amortisation and accumulated impairment losses.

Revaluation of Intangible Assets

- If the fair value of a revalued asset can no longer be determined by reference to an active market, then its carrying value shall be its *revalued amount at the date of last revaluation by reference to the active market less any accumulated amortization and accumulated impairment losses.*

Amortization Adjustment at the date of revaluation

Either:

- Restate proportionately with the change in the gross carrying value of the asset so that carrying value after revaluation equals its revaluation amount.

- Eliminate against the gross carrying value of the asset and the net value is restated to the revalued amount of the asset.

Revaluation Increase/Decrease

- **Increase –** Recognize in other comprehensive income and accumulated in equity under the heading revaluation surplus. However, is recognized in profit or loss to the extent it reverses a revaluation decrease of the same asset previously recognized in profit or loss.

- **Decrease** – Recognize in profit or loss. However, it recognized in other comprehensive income to the extent of any credit balance in the revaluation surplus in respect of that asset.

Useful Life

Finite

- An intangible asset with an finite life is amortized.

Indefinite

An intangible with an indefinite life is not amortized and subject to impairment testing.

Amortization Period and Amortization Method

- Depreciable amount should allocate on a systematic basis over its useful life.
- Amortization should begin when asset is available for use.
- Amortization method should reflect the pattern in which the asset's economic benefits are consumed by the entity. If that pattern cannot be determined reliably, use straight line method.
- Amortization charge should be recognized in P/L unless it is included in the carrying value of another asset.

Review of Amortisation Period and Amortisation Method

- Should review at least at each financial year- end.
- If the expected useful life is different from previous estimates, amortization period should be changed.
- If there is a significant change in the expected pattern of consumption of economic benefits from the asset, amortization method should be changed.

Disclosures

(a)The useful lives or the amortization rates used;

(b) The amortization method used;

(c) The gross carrying amount and the accumulated amortization (aggregated with accumulated impairment losses) at the beginning and end of the period;

(d) The line item(s) of the income statement in which the amortization of intangible assets is included;

(e) A reconciliation of the carrying amount at the beginning and end of the period

Summary

- Definition and Recognition Criteria

- Measurement
  - At Recognition – cost
  - After Recognition – cost or revaluation

- Various issues in accounting for intangible assets in relation to their identification, recognition and measurement.