

INTANGIBLE ASSETS: IAS 38

Definition

- An **intangible asset** is an **identifiable** non-monetary asset **without physical substance** that the entity has **control** over
- **identifiable**
 - The definition of an intangible asset requires an intangible asset to be identifiable to **distinguish it from goodwill**.
 - An asset is identifiable if it either:
 - a) is **separable**, is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged; or
 - b) 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.
- **Control**= entity has the power to obtain the future economic benefits flowing from the asset

Recognition and measurement

- An item is recognized as an intangible asset, if it meets the following :
 - It meets the **definition of an intangible asset (identifiable/control); and**
 - It meets the recognition criteria:
 - (a) it is **probable that the expected future economic benefits** that are attributable to the asset will flow to the entity; and
 - (b) the cost of the asset can be **measured** reliably.
- An intangible asset is measured at cost

Separate acquisition

- The cost of a separately acquired intangible asset comprises:
 - its **purchase price**, including **import duties** and **non-refundable purchase taxes**, after deducting **trade discounts and rebates**; and
 - any **directly attributable cost** of preparing the asset for its intended use
- Examples of directly attributable costs are:
 - costs of employee benefits arising directly from bringing the asset to its working condition;
 - professional fees arising directly from bringing the asset to its working condition; and
 - costs of testing whether the asset is functioning properly.
- Examples of expenditures that are not part of the cost of an intangible asset are:
 - costs of introducing a new product or service (including costs of **advertising and promotional activities**);
 - costs of conducting business in a new location or with a new class of customer (including costs of **staff training**); and
 - administration and other general overhead costs

Incidental Operations

- the income and expenses of incidental operations are recognised immediately in profit or loss

Internally generated goodwill

- **Goodwill** is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized
- Internally generated goodwill shall not be recognized as an asset

Internally generated intangible assets

- To assess whether an internally generated intangible asset meets the criteria for recognition, an entity classifies the generation of the asset into:
 - a research phase; **and**
 - a development phase
- **Research**
 - original and planned investigation undertaken to gain new scientific or technical knowledge and understanding
 - expenditure on research is **expensed**
 - examples of research activities:
 - activities aimed at obtaining new knowledge;
 - the **search** for, **evaluation** and **final selection** of research findings/other knowledge;
 - the **search** for alternatives for materials, devices, products, processes, systems or services; and
 - the formulation, design, evaluation and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.
- **Development**
 - the **application of research findings or other** knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use
 - An intangible asset arising from development is capitalized if **all** of the following are met:
 1. the **technical feasibility** of completing the intangible asset so that it will be available for use or sale.
 2. its **intention to complete** the intangible asset and use or sell it.
 3. its **ability to use or sell** the intangible asset.
 4. how the intangible asset will generate probable future economic benefits.
 - **existence of a market** for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the **usefulness of the intangible asset**
 5. the availability of **adequate technical, financial and other resources** to complete the development and to use or sell the intangible asset.
 6. its ability to **measure reliably the expenditure** attributable to the intangible asset during its development.
 - If an entity cannot distinguish the research phase from the development phase, the entity treats the expenditure as if it were incurred in the research phase only
 - Examples of development activities are:
 - the design, construction and testing of prototypes and models;
 - the design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production; and
 - the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

- **Internally generated brands, mastheads, publishing titles, customer lists** and items similar in substance are not recognised as intangible assets (these are expensed)

What do you capitalize as development costs?

- costs of materials/services used to generate the intangible asset
- costs of employee salaries, wages and benefits to generate intangible asset
- fees to register a legal right
- amortization of patents and licenses used to generate the intangible asset
- interest costs

What not to capitalize as development costs?

- selling, administrative and other general overhead expenditure **unless** this expenditure can be directly attributed to preparing the asset for use;
- cost of training staff to operate the asset

Recognition of an Expense

- Expenditures that are incurred that provide future economic benefits but for which no intangible asset is set up are to be expensed
- Examples include:
 - Research costs
 - Start-up costs
 - Establishment costs such as legal and secretarial costs incurred in establishing a legal entity,
 - expenditure to open a new facility or business (i.e. pre-opening costs)
 - expenditures for starting new operations
 - launching new products or processes (i.e. pre-operating costs)
 - training costs
 - advertising and promotional activities
 - relocating costs
 - reorganization costs

Measurement after recognition

- **Intangible assets are measured using:**
 - i. cost model; or
 - ii. revaluation model
- 1. **Cost model**
 - cost less any accumulated amortization and any accumulated impairment losses
- 2. **Revaluation model (same as IAS 16)**
 - Carried at fair value at the date on revaluation less subsequent accumulated amortization and impairment losses
 - Revaluations should be done with sufficient regularity to ensure that the carrying amount does not differ materially from the fair value
 - There is no requirement to do a revaluation every year

- **Initial Revaluation**
 - gains – goes to other comprehensive income – revaluation surplus (OCI)
 - loss – goes to profit & loss (P&L)
- **subsequent revaluation**
 - gains – goes to P&L to the extent of reversing prev. losses; remainder goes to OCI
 - losses – goes to OCI to the extent of reversing gains in OCI; remainder goes to P&L
- If an item of intangible asset is measured using the revaluation model, all other intangible assets in that class needs to be revalued on the same date (unless if there is no active market)
 - If one patent is measured with the revaluation method; all other patents must also be revalued on the same date that the patent is revalued at

Intangible assets with finite useful lives

- Intangible assets with finite useful lives need to be **amortized**
- Amortization expense = (cost – residual value)/useful life
- Residual value
 - The residual value is assumed to be \$NIL unless at the end of the useful life, the asset is expected to have a useful life to another entity and;
 - There is a commitment from a 3rd party to purchase it @ end of useful life; or
 - Residual value can be determined by referring to transactions in an existing market, and the market is expected to exist at the end of the useful life
- The method of amortization should reflect the pattern in which the economic benefits are consumed from the intangible asset; if pattern cannot be determined use **straight line method**
- Must review amortization method and useful life at each year end

Intangible assets with indefinite useful lives

- An intangible asset with an indefinite useful life is not amortized
- an entity is required to test an intangible asset with an indefinite useful life for impairment by comparing its recoverable amount with its carrying amount:
 - annually, and
 - whenever there is an indication that the intangible asset may be impaired
- The useful life of an intangible asset that is not being amortised shall be reviewed each period (any changes are handled as a change in estimate)

Comparison to ASPE

- No revaluation model under ASPE
- Under ASPE there is a policy choice to expense or capitalize development costs
- The impairment testing is to be done whenever events indicate (doesn't have to be annually)
 - Impairment losses are not reversed under ASPE
- ASPE Section 3064 includes goodwill impairment rules; the rules for goodwill impairment is covered under IAS 36 (impairment of assets) and the calculation is different