Workshop on IND AS – Intangible assets

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Contents

BACKGROUND & SCOPE

Background

- Applicable for intangible assets acquired in business combinations for which agreement date is on or after March 31, 2004.
- Other intangible assets for years beginning on or after March 31, 2004
- Replaced the earlier standard issued in 1998
- Revised the IAS as part of its business combinations project “accounting for goodwill and intangible assets acquired in a business combination”
- Changes made from earlier IAS only related to
  - Clarifying the notion of “identifiability”
  - Useful life and amortization and
  - Accounting for in process R&D projects in business combinations
- Previous definition included the asset to be “held for use in the prodn or supply of goods/services, for rental or for admin purposes”

Background

- Identifiability not defined earlier. Separability was only criterion
- Identifiability criterion met when
  - Asset is separable, ie capable of being separated from the entity and sold, transferred, licensed, rented or exchanged either individually or together with a related contract, asset or liability
  - Arises from contractual or legal right
- Previously could be recognised only when flow of expected future economic benefits attributable to the asset to the entity was probable
- Now probability criterion is considered to be met when the intangible asset is acquired separately or in a business combination
- Introduced concept of “indefinite useful live life” intangible assets

DEFINITIONS

Definition

- **Cost** [in addition to cash or fair value (in an exchange transaction)] is defined to include the amount attributed to the asset when initially recognised in accordance with other IFRSs.
- Also present in other assets standards but relevant here due to impact on business combinations
- **Intangible asset** is an identifiable non-monetary asset without physical substance
- Standard also clarifies that expenditure on items which do not meet the definition of an intangible asset are charged to p&l, except in case of a business combination – included in goodwill
- As a corollary, identifiable intangible assets in a business combination are recognised on the financial statements. IAS 38 read with IFRS 3

RECOGNITION & MEASUREMENT

Recognition

- Standard has separate criteria for recognition of
  - Separately acquired intangible assets
  - Intangible assets acquired in a business combination
  - Initial measurement of intangible assets acquired by way of a Govt grant
  - Exchanges of intangible assets
  - Internally generated goodwill
  - Internally generated intangible assets
- Intangible assets to be recognised only if probable that future economic benefits attributable to the asset will flow to the entity and its costs can be measured reliably
- Above criterion always deemed to be satisfied in a separate acquisition

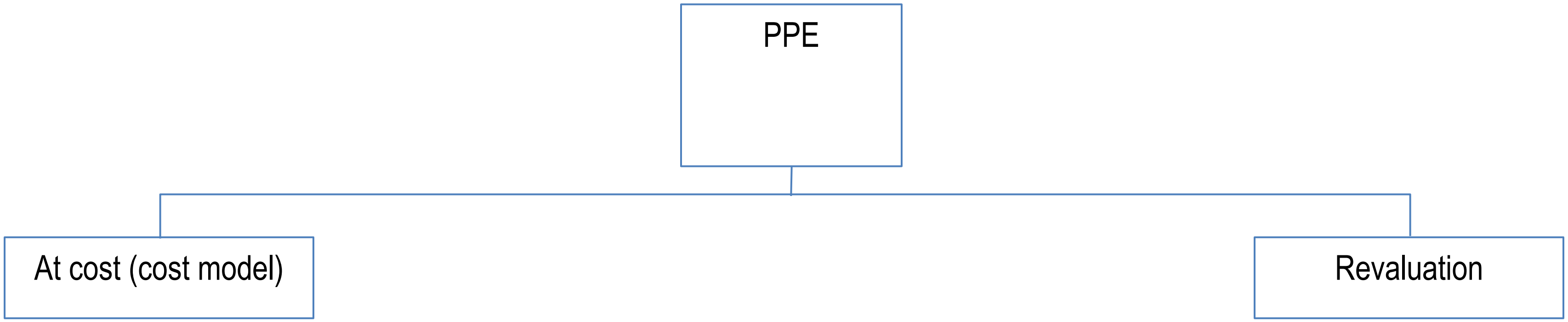
Recognition – in a business combination

- Intangible asset acquired in a business combination deemed to meet the flow of probable economic resources criterion and reliable measurement criterion in a business combination
- Does this mean all intangibles in a business combination would be automatically recognised?
- Ensuring satisfying the requirements of the definition important. Especially identifiability [separability (capable of being separated, divided from the entity via sale, rent, exchange, etc) and arising from contractual or legal rights]
- Why is identifiability/separability not as important in a separate acquisition of an intangible asset?
- Recognised separately from goodwill irrespective of whether these were recognised in the books of the acquiree (eg customer lists – illustrative examples to the IAS)
- Employee base in a company?

Recognition – Government Grants, exchanges and internally generated goodwill

- Recognised as a separate asset
- Either at fair value or at nominal amount
- IND AS permits recognition only at fair value
- This seems to be the only difference between IND AS and the IFRS (as per Appendix 1 on to the Standard)
- Internally generated goodwill – not recognised as an intangible asset

Measurement after recognition



- When revaluation model used, to be applied to entire class of assets
- Revaluation to be frequent enough to keep carrying values close to fair value. No period specified as in case of PPE
- Similar to the model followed for PPE
- Revaluation surplus transferred directly to retained earnings when the PPE is derecognised
- Can also be transferred as the asset is used by the entity
- Measured as the difference between depreciation on original cost and revaluated amount
- However, difference will not be routed through p&l

AMORTIZATION

Amortization and indefinite life intangible assets

- Indefinite useful life intangible assets
- Are those assets intangible assets when based on analysis of relevant factors there is no forseeable limit to the period over which the asset is expected to generate net cash flows
- Assets with indefinite useful lives not amortized
- Tested for impairment annually and when there is an indicated that it may be impaired
- Examples given in the illustrative examples to the standard
  - Broadcast rights renewable at a low renewal cost with a recent history of renewal; change assessment of indefinite life on amendment of renewal conditions
  - Airline route
  - Trademarks with renewal at low cost and expected to generate benefits for an indefinite period
  - If indefinite useful life assumption unchanged; no amortization even if impairment recorded

DISCLOSURES

Disclosure requirements

- For each class of intangible assets disclosure required of
  - Assets internally generated and others
  - Whether indefinite useful lives or definite useful lives (including period of amortization(
  - Amortization methods and line items of where amortization is included
  - Movement during the year – gross amount and accumulated depreciation
- For indefinite life intangible assets the carrying amount of the same and reasons why useful life assessed as indefinite. Also required to give factors that played a role in determining indefinite life
- Description, carrying amount and remaining amortization period of any individual material intangible asset
- Disclose the aggregate R&D expenditure charged to the income statement during the period

DIFFERENCES WITH EXISTING ACCOUNTING STANDARD

Differences with IND AS

- Existing definition the asset to be “held for use in the prodn or supply of goods/services, for rental or for admin purposes” dropped in IND AS
- Identifiability not specifically mentioned in existing standards.
- Probable inflow always considered satisfied in IND AS
- Indefinite useful life
- Discounting to be done if payment for acquired intangible assets
- Detailed guidance for recognising intangibles in a business combination v/s amalgamation in the nature of a purchase in the existing standard
- Detailed guidance of accounting for assets acquired in exchange v/s current standard
- Assets acquired by Government Grant – to be recognised at fair value v/s nominal value at present
- Revaluation model permitted

SPECIALISED INTANGIBLE ASSETS (SIC 32 AND IFRIC 12)

SIC 32 – Website development costs

- Entities develop websites for internal or external access
  - External (for promoting & advertising its products & services, providing electronic services and for selling services)
  - Internal (to store company policies, etc.)
- Interpretation deals with whether
  - Website is an internally generated intangible asset as per IAS 38; and
  - Accounting for the same

SIC 32 – Website development costs

- Concludes that that a website is an internally generated asset covered by IAS 38
- Can be recognised as an intangible if the conditions of IAS 38 paras 21 & 57 are met. Para 57 specifically deals with internally generated intangible assets and requires the entity to demonstrate
  - Technical feasibility so that the asset is available for use or sale, its intention to complete it and its ability to use/sell it
  - How the (website) will generate future probable future economic benefits
  - The availability of adequate technical, financial and other resources & to reliably measure expenditure incurred to develop the asset
- SIC 12 states this may be demonstrable if the website is capable of generating revenues from enabling orders to be placed.
- Also states entity cannot demonstrate this if it is developed “solely or primarily for promoting or advertising its own products and services.” Amt incurred would be expensed.

SIC 32 – Website development costs

- Indicates that there are the following stages in the development of a website
  - Planning stage – deemed similar to research phase; costs expensed
  - Application and Infrastructure Development
  - Graphical Design
  - Content Development
  - Operating stage – costs expensed
- Phases 2-4 above Capitalized if criteria of para 8 of SIC (corresponding to paras 21 and 57 of IAS 38 are met); if however, these are for promoting and advertising products and services
- Illustrative examples in Part B to the SIC outline the specific types of costs which may be covered in each of the above stages

IFRIC 12 – Service Concession Arrangements (Intangible Asset Model)

This Interpretation gives guidance on the accounting by operators for public-to-private service concession arrangements.

This Interpretation applies to public-to-private service concession arrangements if:

- the grantor controls or regulates what services the operator must provide with the infrastructure, to whom it must provide them, and at what price; and
- the grantor controls—through ownership, beneficial entitlement or otherwise—any significant residual interest in the infrastructure at the end of the term of the arrangement.

- The operator shall recognise and measure revenue in accordance with IASs 11 and 18 for the services it performs.
- The nature of the consideration determines its subsequent accounting treatment – whether it is a financial asset or an intangible asset
- Treated as an intangible asset if realization of cost is via collection of tolls

IFRIC 12 – Service Concession Arrangements (Intangible Asset Model)

Assumptions

- Company has obtained a service concession arrangement for 12 yrs (2 yrs construction + 10 yrs operation)
- Total toll revenues expected are Rs 1,000 over 10 yrs
- Total cost is expected to be Rs 800 (Rs 600 for construction and Rs 200 in the operations phase)
- The total concession period profit of Rs 200 would need to be split into that attributable to construction and that attributable to maintenance <u>(assume that construction profit out of this is Rs 150 and operation profit is Rs 50)</u>

Accounting for a toll project – Indian GAAP & IFRS (Year 1)

Indian GAAP P&L	Rs	IFRS P&L	Rs
Income	-	Construction income (50% of Rs 750; construction cost Rs 600 & profit Rs 150)	375
Expense	-	Expense	300
	-	Profit	75
Balance Sheet		**Balance Sheet**	
Capital WIP	300	Intangible Asset	375
Creditors	(300)	Creditors	(300)
		Accumulated Profit	(75)
	-		-

Accounting for a toll project – Indian GAAP & IFRS (Year 2)

Indian GAAP	Rs	IFRS	Rs
Income	-	Construction income	375
Expense	-	Expense	300
	-	Profit	75
Balance Sheet		**Balance Sheet**	
Capital WIP	600	Intangible Asset	750
Creditors	(600)	Creditors	(600)
		Accumulated profit	
		Opening balance	(75)
		Profit for the year	(75)
	-		-

Accounting for a toll project – Indian GAAP & IFRS (Year 3)

Indian GAAP	Rs	IFRS	Rs
Income	97	Toll revenue	97
Expense (Dep – Rs 60; maintenance cost Rs 20)	80	Expense (Dep – Rs 75; maintenance cost Rs 20)	95
Profit	17	Profit	2
Balance Sheet		**Balance Sheet**	
Asset (Rs 600 – dep of Rs 60)	540	Intangible Asset (Rs 750 – dep)	675
Cash	97	Cash	97
Creditors (op bal + exp)	(620)	Creditors	(620)
Profit	(17)	*Accumulated profit*	
		Opening balance	(150)
		Profit for the year	(2)
	-		-

Thank you