Accounting for Assets – Intangible Assets

Intangible asset: identifiable non-monetary asset without physical substance (**AASB 138.8**).

- E.g. patents (granted by Cth government and give the owner exclusive rights to a product or process for 16 years), copyrights, research and development, trademarks (used to differentiate products and brands in the eyes of consumers), brand names, television and radio licenses, franchises, computer software and website costs, etc.
- If an intangible asset is purchased in an arm's length transaction, its cost should be recorded as an asset in the same way as plant and equipment.
- If an internally developed intangible is expected to yield future economic benefits, it should also be recorded as an asset at its cost of development.

Goodwill: future economic benefits from assets that are not capable of being individually identified and separately recognised.

Three factors necessary for the existence of an intangible asset

- **Identifiability (AASB 138.12)**
- **Control (AASB 138.13-16)**
- **Existence of future economic benefits (AASB 138.17)**

AASB 138.12: *An asset is identifiable if it either: (a) is separable, ie is 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 (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.*

AASB 138.13: *An entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way.*

AASB 138.14: *Market and technical knowledge may give rise to future economic benefits. An entity controls those benefits if, for example, the knowledge is protected by legal rights such as copyrights, a restraint of trade agreement (where permitted) or by a legal duty on employees to maintain confidentiality.*

AASB 138.15: *An entity may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits from training. The entity may also expect that the staff will continue to make their skills available to the entity. However, an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.*

AASB 138.16: *An entity may have a portfolio of customers or a market share and expect that, because of its efforts in building customer relationships and loyalty, the customers will continue to trade with the entity. However, in the absence of legal rights to protect, or other ways to control, the relationships with customers or the loyalty of the customers to the entity, the entity usually has insufficient control over the expected economic benefits from customer relationships and loyalty for such items (eg portfolio of customers, market shares, customer relationships and customer loyalty) to meet the definition of intangible assets. In the absence of legal rights to protect customer relationships, exchange transactions for the same or similar non-contractual customer relationships (other than as part of a business combination) provide evidence that the entity is nonetheless able to control the expected future economic benefits flowing from the customer*

relationships. Because such exchange transactions also provide evidence that the customer relationships are separable, those customer relationships meet the definition of an intangible asset.

AASB138.17: *The future economic benefits flowing from an intangible asset 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. For example, the use of intellectual property in a production process may reduce future production costs rather than increase future revenues.*

Recognition of an Intangible

If future economic benefits are acquired, an asset should be recognised.

Expense internally developed intangibles unless they meet AASB 138.57.

Immediate expensing is justified:

- if it is consistent with the treatment of cost for income tax purposes;
- if the cost fails to meet the asset-recognition criteria;
- if the cost of intangibles is frequently immaterial.

AASB 138.21: *An intangible asset shall be recognised if, and only if:*
(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.

- For purchased intangible assets, recognition is required in similar circumstances to other assets.

AASB 138.25: *Normally, the price an entity pays to acquire separately an intangible asset will reflect expectations about the probability that the expected future economic benefits embodied in the asset will flow to the entity. In other words, the entity expects there to be an inflow of economic benefits, even if there is uncertainty about the timing or the amount of the inflow. Therefore, the probability recognition criterion in paragraph 21(a) is always considered to be satisfied for separately acquired intangible assets.*

AASB 138.26: *In addition, the cost of a separately acquired intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.*

AASB 138.27: *The cost of a separately acquired intangible asset comprises:*
(a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
(b) any directly attributable cost of preparing the asset for its intended use.

AASB 138.28: *Examples of directly attributable costs are:*
(a) costs of employee benefits (as defined in AASB 119) arising directly from bringing the asset to its working condition;
(b) professional fees arising directly from bringing the asset to its working condition; and
(c) costs of testing whether the asset is functioning properly.

AASB 138.29: *Examples of expenditures that are not part of the cost of an intangible asset are:*
(a) costs of introducing a new product or service (including costs of advertising and promotional activities);
(b) costs of conducting business in a new location or with a new class of customer (including costs of staff training); and
(c) administration and other general overhead costs.

AASB 138.30: *Recognition of costs in the carrying amount of an intangible asset ceases when the asset is in the condition necessary for it to be capable of operating in the manner intended by management. Therefore, costs incurred in using or*

redeploying an intangible asset are not included in the carrying amount of that asset. For example, the following costs are not included in the carrying amount of an intangible asset:
(a) costs incurred while an asset capable of operating in the manner intended by management has yet to be brought into use; and
(b) initial operating losses, such as those incurred while demand for the asset's output builds up.

AASB 138.31: *Some operations occur in connection with the development of an intangible asset, but are not necessary to bring the asset to the condition necessary for it to be capable of operating in the manner intended by management. These incidental operations may occur before or during the development activities. Because incidental operations are not necessary to bring an asset to the condition necessary for it to be capable of operating in the manner intended by management, the income and related expenses of incidental operations are recognised immediately in profit or loss, and included in their respective classifications of income and expense.*

AASB 138.32: *If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. The difference between this amount and the total payments is recognised as interest expense over the period of credit unless it is capitalised in accordance with AASB 123 Borrowing Costs.*

- For internally generated intangible assets, an entity must **distinguish between a research phase and a development phase** and recognition is limited.
  - *Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding (**AASB 138.8**).*
  - *Development is 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 (**AASB 138.8**).*

AASB 138.51: *It is sometimes difficult to assess whether an internally generated intangible asset qualifies for recognition because of problems in:*
(a) identifying whether and when there is an identifiable asset that will generate expected future economic benefits; and
(b) determining the cost of the asset reliably. In some cases, the cost of generating an intangible asset internally cannot be distinguished from the cost of maintaining or enhancing the entity's internally generated goodwill or of running day-to-day operations. Therefore, in addition to complying with the general requirements for the recognition and initial measurement of an intangible asset, an entity applies the requirements and guidance in paragraphs 52–67 to all internally generated intangible assets.

AASB 138.52: *To assess whether an internally generated intangible asset meets the criteria for recognition, an entity classifies the generation of the asset into:*
(a) a research phase; and
(b) (b) a development phase. Although the terms 'research' and 'development' are defined, the terms 'research phase' and 'development phase' have a broader meaning for the purpose of this Standard.

AASB 138.53: *If an entity cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the entity treats the expenditure on that project as if it were incurred in the research phase only.*

Accounting Methods for R&D:

1. Expense method: costs recognised as expenses in the period in which they are incurred.

2. Expense and reinstate method: costs recognised as expenses in the period in which they are incurred and reinstated if the costs are subsequently expected to generate future economic benefits.

3. Selective capitalisation method: some of the costs are recognised as intangible assets while others are recognised as expenses. AASB 138 adopts this approach:
   - all research costs must be expensed
   - development costs meeting stringent conditions may be capitalised (**AASB 138.57**)
   - development costs not meeting the conditions shall be expenses.
   - intangible assets arising are initially measured at cost (**AASB 138.66-67**).
   - Cost is the sum of all expenditure incurred from the date when the intangible asset first meets all the recognition requirements (**AASB 138.65**).
   - Because development assets do not have an active market, only the cost model can be used (**AASB 138.81**).