UNIT 6:
INDIAN ACCOUNTING STANDARD 38 : INTANGIBLE ASSETS

LEARNING OUTCOMES

After studying this unit, you will be able to

- Understand the Scope and Meaning of Intangible Asset
- Recognise the criteria
- Measure the intangible assets at Initial Recognition
- Examine the Mode of Acquisition
- Measure the intangible assets after Recognition
- Evaluate Amortisation and useful life of Intangible Asset
- De-Recognition and comply with the Disclosure requirements of the standard.
Objective
Prescribe the accounting treatment for Intangible Assets which are not dealt in another standard

Scope exclusion:
• Intangible assets covered by another Standards
• Financial Assets
• Exploration and evaluation assets
• Mineral rights and mineral reserves

Meaning of Intangible Asset
• Identifiable
• Non-monetary asset
• Without physical substance

Measurement of Intangible Asset:
Initial Measurement: At Cost
Subsequent Measurement: Cost or Revaluation Model

Intangible Asset may arise from:
Separate Acquisition
Part of a Business combination
Government Grant
Internally generated goodwill
Internally generated intangible assets
Exchange of assets

Amortisation of I.A. with finite useful life.
I.A. with indefinite useful lives review for annual impairment
6.1 OBJECTIVE

The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. This standard specifies the requirement of recognition, measurement and disclosures of Intangible Assets.

The Standard states that intangible assets are initially measured at cost, subsequently measured at cost or using the revaluation model, and amortised on a systematic basis over their useful lives unless the asset has an indefinite useful life, in which case it is not amortised.

6.2 SCOPE

6.2.1 Applicability

This Standard shall be applied to all intangible assets, except:

(a) intangible assets that are within the scope of another Standard, for example:

- Intangible assets held for sale in ordinary course of business (Ind AS 2)
- Deferred tax assets (Ind AS 12)
- Leases of intangibles assets (Ind AS 116)
- Assets arising from employee benefits (Ind AS 19)
- Financial assets (Ind AS 32)
- Goodwill arising in a business combination (Ind AS 103)
- Deferred acquisition costs and intangible assets arising from insurance contract (Ind AS 104)
- Non Current intangible assets classified as held for sale (Ind AS 105)
- Assets arising from contracts with customers (Ind AS 115)

(b) financial assets, as defined in Ind AS 32, Financial Instruments: Presentation;

(c) the recognition and measurement of exploration and evaluation assets (see Ind AS 106, Exploration for and Evaluation of Mineral Resources); and

(d) expenditure on the development and extraction of minerals, oil, natural gas and similar non-renewable resources.
6.2.2 Intangible assets contained in or on a physical substance

Some intangible assets may be contained in or on a physical substance such as a compact disc (in the case of computer software), legal documentation (in the case of a licence or patent) or film. In determining whether an asset that incorporates both tangible and intangible elements should be treated under Ind AS 16, Property, Plant and Equipment, or as an intangible asset under this Standard, an entity uses judgement to assess which element is more significant.

For example, computer software for a computer-controlled machine tool that cannot operate without that specific software is an integral part of the related hardware and it is treated as property, plant and equipment. The same applies to the operating system of a computer. When the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

Research and development activities are directed to the development of knowledge. Therefore, although these activities may result in an asset with physical substance (eg a prototype), the physical element of the asset is secondary to its intangible component, ie the knowledge embodied in it.

6.2.3 Intangible assets on leases

Rights under licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights are excluded from the scope of Ind AS 116, and are within the scope of this Standard.

6.2.4 Intangible assets used in the extractive and insurance industries

This Standard does not apply to expenditure on the exploration for, or development and extraction of, oil, gas and mineral deposits in extractive industries and in the case of insurance contracts. However, this Standard applies to other intangible assets used (such as computer software), and other expenditure incurred (such as start-up costs), in extractive industries or by insurers.

6.2.5 Amortisation method specified in this standard not to apply to intangible assets arising from service concession arrangements in respect of toll roads

The amortisation method specified in this Standard does not apply to an entity that opts to amortise the intangible assets arising from service concession arrangements in respect of toll roads recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS reporting period as per the optional exemption given in Ind AS 101, First time adoption of Indian Accounting Standards.
6.3 RELEVANT DEFINITIONS

The following are the key terms used in this standard:

- **Amortisation** is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

- An **asset** is a resource:
  
  (a) controlled by an entity as a result of past events; and
  
  (b) from which future economic benefits are expected to flow to the entity.

- **Carrying amount** is the amount at which an asset is recognised in the balance sheet after deducting any accumulated amortisation and accumulated impairment losses thereon.

- **Cost** is the amount of cash or cash equivalents paid or the fair value of other consideration given to acquire an asset at the time of its acquisition or construction, or, when applicable, the amount attributed to that asset when initially recognised in accordance with the specific requirements of other Indian Accounting Standards, for e.g Ind AS 102, *Share-based Payment*.

- **Depreciable amount** is the cost of an asset, or other amount substituted for cost, less its residual value.

- **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.

- **Entity-specific value** is the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.

- **Fair value** is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (See Ind AS 113, *Fair Value Measurement*. )
7.270  FINANCIAL REPORTING

- An **impairment loss** is the amount by which the carrying amount of an asset exceeds its recoverable amount.
- An **intangible asset** is an identifiable non-monetary asset without physical substance.
- **Monetary assets** are money held and assets to be received in fixed or determinable amounts of money.
- **Research** is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
- The **residual value** of an intangible asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.
- **Useful life** is:
  (a) the period over which an asset is expected to be available for use by an entity; or
  (b) the number of production or similar units expected to be obtained from the asset by an entity.

6.4  IDENTIFICATION OF INTANGIBLE ASSETS

6.4.1 Meaning of Intangible asset

An intangible asset is an identifiable non-monetary asset without physical substance. The key components of this definition are:

(i) Identifiability; and

(ii) Asset

Entities frequently expend resources, or incur liabilities, on the acquisition, development, maintenance or enhancement of intangible resources such as:

- Scientific or technical knowledge
- Design and implementation of new processes or systems

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• Licences
• Intellectual property
• Market knowledge and trademarks (including brand names and publishing titles).

Common examples of items encompassed by these broad headings are:
• Computer software
• Patents
• Copyrights
• Motion picture films
• Customer lists
• Mortgage servicing rights
• Fishing licences
• Import quotas
• Franchises
• Customer or supplier relationships
• Customer loyalty
• Market share and marketing rights.
Let's run through some examples of each broad category listed above:

- Trade Mark
- Internet Domain Names
- Non Competitive Agreements
- Customer lists
- Customer Contracts
- Non Contractual Customer Relationship
Artistic Related

- Musical Works
- Pictures and Photograph
- Plays, operas and Ballets
- Magazines, Newspapers and other literary works

Customer Based

- Franchise Agreements
- Lease Agreements
- Operating and broadcasting Rights
- Employment Contracts
Not necessarily all of the above item meet the conditions of recognizing as an Intangible Assets within purview of this standard:

- Identifiability
- Control over a Resource (Asset) and

**Note:** If an item within the scope of this Standard does not meet the definition of an intangible asset, expenditure to acquire it or generate it internally is recognised as an expense when it is incurred. However, if the item is acquired in a business combination, it forms part of the goodwill recognised at the acquisition date.

Let us understand each concept one by one.

### 6.4.2 Identifiability

The definition of an intangible asset requires an intangible asset to be identifiable to distinguish it from goodwill. Goodwill recognised in a business combination is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised. The future economic benefits may result from synergy between the identifiable assets acquired or from assets that, individually, do not qualify for recognition in the financial statements.
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.

Illustration 1: Identifiability

Sun Ltd has an expertise in consulting business. In past years, company has gained a market share for its services of 30 percent and considers recognising it as an intangible asset. Is the action by company is justified?

Solution

Market share does not meet the definition of intangible assets as is not identifiable i.e. It is neither separable and nor arised from contractual or legal rights.

6.4.3 Asset

An asset is a resource:

(a) controlled by an entity as a result of past events; and

(b) from which future economic benefits are expected to flow to the entity.

6.4.3.1 Control

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.
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.

**Example:**

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.

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 (e.g. 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.

**Illustration 2 : Control**

*Company XYZ ltd has provided training to its staff on various new topics like GST, Ind AS etc. to ensure the compliance as per the required law. Can the company recognise such cost of staff training as intangible asset?*

**Solution**

It is clear that the company will obtain the economic benefits from the work performed by the staff as it increases their efficiency. But it does not have control over them because staff could choose to resign the company at any time.

Hence the company lacks the ability to restrict the access of others to those benefits. Therefore, the staff training cost does not meet the definition of an intangible asset.

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6.4.3.2 Future economic benefits

The future economic benefits flowing from an intangible asset may include:

(a) Revenue from the sale of products or services;
(b) Cost savings; or
(c) 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.

Illustration 3: Identifiability of Intangible assets

Pluto Ltd. intends to open a new retail store in a new location in the next few weeks. Pluto Ltd has spent a substantial sum on a series of television advertisements to promote this new store. The Company has paid an amount of ₹ 800,000 for advertisements before 31\textsuperscript{st} March, 20X1. ₹ 700,000 of this sum relates to advertisements shown before 31\textsuperscript{st} March, 20X1 and ₹ 100,000 to advertisements shown in April, 20X1. Since 31\textsuperscript{st} March, 20X1. The Company has paid for further advertisements costing ₹ 400,000.

Pluto Ltd is of view that such costs can be carried forward as intangible assets. Since market research indicates that this new store is likely to be highly successful. Please explain and justify the treatment of the above costs in the financial statements for the year ended 31\textsuperscript{st} March, 20X1.

Solution

Under Ind AS 38 – Intangible Assets – intangible assets can only be recognised if they are identifiable and have a cost which can be reliably measured.

These criteria are very difficult to satisfy for internally developed intangibles.

For these reasons, Ind AS 38 specifically prohibits recognising advertising expenditure as an intangible asset. The issue of how successful the store is likely to be does not affect this prohibition. Therefore, such costs should be recognised as expenses.

However, the costs would be recognised on an accruals basis. Therefore, of the advertisements paid for before 31\textsuperscript{st} March, 20X1, ₹ 7,00,000 would be recognised as an expense and ₹ 1,00,000 as a pre-payment in the year ended 31\textsuperscript{st} March, 20X1. The ₹ 4,00,000 cost of advertisements paid for since 31\textsuperscript{st} March, 20X1 would be charged as expenses in the year ended 31\textsuperscript{st} March, 20X2.

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6.5 RECOGNITION OF INTANGIBLE ASSET

6.5.1 Recognition of Intangible assets – general principles

Provided that an item meets the definition of an intangible asset, it should be recognised in the financial statements 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.

This requirement applies to:

(a) costs incurred initially to acquire or internally generate an intangible asset; and

(b) those incurred subsequently to add to, replace part of, or service it.

An entity should assess the probability of expected future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset.

The nature of intangible assets is such that, in many cases, there are no additions to such an asset or replacements of part of it. Accordingly, most subsequent expenditures are likely to maintain the expected future economic benefits embodied in an existing intangible asset rather than meet the definition of an intangible asset and the recognition criteria in this Standard.

In addition, it is often difficult to attribute subsequent expenditure directly to a particular intangible asset rather than to the business as a whole. Therefore, only rarely will subsequent expenditure — expenditure incurred after the initial recognition of an acquired intangible asset or after completion of an internally generated intangible asset — be recognised in the carrying amount of an asset.
Subsequent expenditure on brands, mastheads, publishing titles, customer lists and items similar in substance (whether externally acquired or internally generated) is always recognised in profit or loss as incurred. This is because such expenditure cannot be distinguished from expenditure to develop the business as a whole.

Illustration 4

Mercury Ltd is preparing its accounts for the year ended 31st March, 20X2 and is unsure about how to treat the following items.

1. The company completed a grand marketing and advertising campaign costing ₹ 4.8 lakh. The finance director had authorised this campaign on the basis that it would create ₹ 8 lakh of additional profits over the next three years.

2. A new product was developed during the year. The expenditure totalled ₹ 3 lakh of which ₹ 1.5 lakh was incurred prior to 30th September, 20X1, the date on which it became clear that the product was technically viable. The new product will be launched in the next four months and its recoverable amount is estimated at ₹ 1.4 lakh.

3. Staff participated in a training programme which cost the company ₹ 5 lakh. The training organisation had made a presentation to the directors of the company outlining that incremental profits to the business over the next twelve months would be ₹ 7 lakh.

What amounts should appear as intangible assets in accordance with Ind AS 38 and Ind AS 36 in Mercury’s balance sheet as on 31st March, 20X2?

Solution

The treatment in Mercury’s financials as at 31st March, 20X2 will be as follows:

1. Marketing and advertising campaign: No intangible asset will be recognised, because it is not possible to identify future economic benefits that are attributable only due to this campaign. All of the expenditure should be expensed in the statement of profit and loss.

2. New product: Development expenditure appearing in the balance sheet will be valued at ₹ 1.5 lakh as per Ind AS 38. The expenditure prior to the date on which the product becomes technically feasible is recognised in the statement of profit and loss. However, its recoverable amount is also given in the question. Therefore, applying provisions of Ind AS 36, the revised carrying amount on 31st March, 20X2 after impairment will be ₹ 1.4 lakh.

3. Training programme: No asset will be recognised, because there is no control of the company over the staff and when staff leaves the benefits of the training, whatever they may be, also departs.

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### 6.6 MEASUREMENT OF INTANGIBLE ASSET

An intangible asset should be measured initially at cost.

Intangible assets may be acquired or can be self generated. The below diagram reflect the method and mode by which Intangible assets may arise:

![Diagram showing intangible asset acquisition methods](image)

#### 6.6.1 Separate acquisition

**6.6.1.1 Recognition criteria for intangible assets acquired separately**

Generally, the price an entity pays to acquire separately an intangible asset will reflect expectations about the probability that the expected future economic benefits associated with 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 specified above is always considered to be satisfied for separately acquired intangible assets.

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.

**6.6.1.2 Measurement of cost for intangible assets acquired separately**

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.

**Cost includes**

- Purchase price including import duties and non-refundable purchase taxes
- Directly attributable Cost of preparing the asset for its intended use.
  - (Cost of Employee Benefits, Professional and Legal Fees Cost of Testing)

**Examples of directly attributable costs are:**

- Employee benefits cost (as defined in Ind AS 19) arising directly from bringing the asset to its working condition
- Professional Fees arising directly from bringing the asset to its working condition
- Costs of testing - whether the asset is working 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 cost 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)
- Administrative and other general overhead costs
Deferred Consideration

If payment for an intangible asset is deferred beyond normal credit terms, then cost of such intangible asset 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 Ind AS 23, Borrowing Costs.

Cessation of capitalisation

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.

For example, the following costs are not included in the carrying amount of an intangible asset:

(a) costs incurred in using or redeploying an intangible asset;
(b) costs incurred while an asset capable of operating in the manner intended by management has yet to be brought into use; and
(c) initial operating losses, such as those incurred while demand for the asset’s output builds up.

Example: Separate Acquisition

Jupiter Ltd acquires new energy efficient technology that will significantly reduce its energy costs for manufacturing.

<table>
<thead>
<tr>
<th>Costs incurred include</th>
<th>Cost to be capitalised as per Ind AS 38</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of new solar technology</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Trade discount provided</td>
<td>(1,00,000)</td>
</tr>
<tr>
<td>Training course for staff in new technology</td>
<td>50,000</td>
</tr>
<tr>
<td>Initial testing of new technology</td>
<td>35,000</td>
</tr>
<tr>
<td>Losses incurred while other parts of plant shut down during testing and training</td>
<td>25,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>10,10,000</strong></td>
</tr>
</tbody>
</table>

Illustration 5: Separate Acquisition

Venus India Private Ltd acquired a software for its internal use costing ₹ 10,00,000. The amount payable for the software was ₹ 60,00,000 immediately and ₹ 40,00,000 in one year time. The other expenditure incurred were:-

Purchase tax : ₹ 1,00,000

Entry Tax : 10% (recoverable later from tax department)

Legal fees: ₹ 87,000
Consultancy fees for implementation: ₹ 1,20,000

Cost of capital of the company is 10%.

Calculate the cost of the software on initial recognition using the principles of Ind AS 38 Intangible Assets.

Solution

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash paid</td>
<td>600,000</td>
</tr>
<tr>
<td>Deferred consideration (₹ 400,000/1.1)</td>
<td>3,63,636</td>
</tr>
<tr>
<td>Purchase Tax</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Entry tax (not to be considered as it is a refundable tax)</td>
<td>-</td>
</tr>
<tr>
<td>Legal fees</td>
<td>87,000</td>
</tr>
<tr>
<td>Consultancy fees for implementation</td>
<td>1,20,000</td>
</tr>
<tr>
<td><strong>Total cost to be capitalised</strong></td>
<td><strong>12,70,636</strong></td>
</tr>
</tbody>
</table>

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6.6.2 Acquisition as part of a business combination

6.6.2.1 Recognition criteria for intangible assets acquired as part of a business combination

- In accordance with Ind AS 103, Business Combinations, if an intangible asset is acquired in a business combination, the cost of that intangible asset is its fair value at the acquisition date. The fair value of an intangible asset will reflect market participants’ expectations at the acquisition date 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 is always considered to be satisfied for intangible assets acquired in business combinations.

- An acquirer recognises at the acquisition date, separately from goodwill, an intangible asset of the acquiree, irrespective of whether the asset had been recognised by the acquiree before the business combination.

- This means that the acquirer recognises as an asset separately from goodwill an in-process research and development project of the acquiree if the project meets the definition of an intangible asset. An acquiree’s in-process research and development project meets the definition of an intangible asset when it:
  (a) meets the definition of an asset; and
  (b) is identifiable, i.e., is separable or arises from contractual or other legal rights.
Measuring fair value

- If an intangible asset acquired in a business combination is separable or arises from contractual or other legal rights, sufficient information exists to measure reliably the fair value of the asset.

- When, for the estimates used to measure an intangible asset’s fair value, there is a range of possible outcomes with different probabilities that uncertainty enters into the measurement of the asset’s fair value.

- An intangible asset acquired in a business combination might be separable, but only together with a related contract, identifiable asset or liability. In such cases, the acquirer recognises the intangible asset separately from goodwill, but together with the related item.

- The acquirer may recognise a group of complementary intangible assets as a single asset provided the individual assets have similar useful lives. For example, the terms ‘brand’ and ‘brand name’ are often used as synonym for trademarks and other marks.

**Illustration 6: Business Combination**

On 31st March, 20X1, Earth India Ltd. paid ₹ 50,00,000 for a 100% interest in Sun India Ltd. At that date Sun Ltd.’s net assets had a fair value of ₹ 30,00,000. In addition, Sun Ltd. also held the following rights:

- Trade Mark named “GRAND” – valued at ₹ 180,000 using a discounted cash flow technique.
- Sole distribution rights to an electronic product; future cash flows from which are estimated to be ₹ 150,000 per annum for the next 6 years.

10% is considered an appropriate discount rate.

The 6 year, 10% annuity factor is 4.36.

Calculate goodwill and other Intangible assets arising on acquisition.

**Solution**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase Consideration (A)</td>
<td></td>
<td>50,00,000</td>
</tr>
<tr>
<td>Net Asset acquired</td>
<td>30,00,000</td>
<td></td>
</tr>
<tr>
<td>Trade Mark</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Distribution Rights (1,50,000 x 4.36)</td>
<td>6,54,000</td>
<td></td>
</tr>
<tr>
<td>Total (B)</td>
<td>(38,34,000)</td>
<td></td>
</tr>
<tr>
<td>Goodwill on Acquisition</td>
<td>11,66,000</td>
<td></td>
</tr>
</tbody>
</table>

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6.6.3 Acquisition by way of a government grant

An intangible asset may be acquired free of charge, or for nominal consideration, by way of a government grant. This may happen when a government transfers or allocates to an entity intangible assets such as airport landing rights, licences to operate radio or television stations, import licences or quotas or rights to access other restricted resources.

In accordance with Ind AS 20, *Accounting for Government Grants and Disclosure of Government Assistance*, an entity should recognise both the intangible asset and the grant initially at fair value.

If an entity chooses not to recognise the asset initially at fair value, the entity recognises the asset initially at a nominal amount (the other treatment permitted by Ind AS 20) plus any expenditure that is directly attributable to preparing the asset for its intended use.

6.6.4 Exchange of assets

One or more intangible assets may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The cost of such an intangible asset is measured at fair value (even if an entity cannot immediately derecognise the asset given up) unless either:

(a) the exchange transaction lacks commercial substance; or

(b) the fair value of neither the asset received nor the asset given up is reliably measurable.

- If the acquired asset is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

- An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows are expected to change as a result of the transaction. An exchange transaction has commercial substance if:

  (a) the configuration (ie risk, timing and amount) of the cash flows of the asset received differs from the configuration of the cash flows of the asset transferred; or

  (b) the entity-specific value of the portion of the entity’s operations affected by the transaction changes as a result of the exchange; and

  (c) the difference in (a) or (b) is significant relative to the fair value of the assets exchanged.

- No intangible asset can be recognised unless its cost can be measured reliably. If an entity is able to measure reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost. However, if the fair value of the asset received is more clearly evident, then fair value of the asset received is taken up as cost.

- The fair value of an intangible asset is reliably measurable if:

  (a) the variability in the range of reasonable fair value measurements is not significant for that asset; or
(b) the probabilities of the various estimates within the range can be reasonably assessed and used when measuring fair value.

**Illustration 7: Exchange of Asset**

Sun Ltd acquired a software from Earth Ltd. in exchange for a telecommunication license. The telecommunication license is carried at ₹ 5,00,000 in the books of Sun Ltd. The Software is carried at ₹ 10,00,000 in the books of the Earth Ltd which is not the fair value.

Advise journal entries in the following situations in the books of Sun Ltd and Earth Ltd:-

1) Fair value of software is ₹ 5,20,000 and fair value of telecommunication license is ₹ 5,00,000.

2) Fair Value of Software is not measureable. However similar Telecommunication license is transacted by another company at ₹ 4,90,000.

3) Neither Fair Value of Software nor Telecommunication license could be reliably measured.

**Solution**

<table>
<thead>
<tr>
<th>Situation</th>
<th>Sun Ltd.</th>
<th>Earth Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Software Dr. 500</td>
<td>Telecommunication license Dr. 520</td>
</tr>
<tr>
<td></td>
<td>To Telecommunication license 500</td>
<td>To Software 10</td>
</tr>
<tr>
<td></td>
<td>To Profit on Exchange Nil</td>
<td>To Profit on Exchange 510</td>
</tr>
<tr>
<td>2</td>
<td>Software Dr. 490</td>
<td>Telecommunication license Dr. 490</td>
</tr>
<tr>
<td></td>
<td>Loss on Exchange Dr. 10</td>
<td>To Software 10</td>
</tr>
<tr>
<td></td>
<td>To Telecommunication license 500</td>
<td>To Profit on Exchange 480</td>
</tr>
<tr>
<td><strong>Note:</strong> The company may first recognise Impairment loss and then pass an entry. The effect is the same as impairment loss will also be charged to Income Statement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Software Dr. 500</td>
<td>Telecommunication license Dr. 10</td>
</tr>
<tr>
<td></td>
<td>To Telecommunication license 500</td>
<td>To Software 10</td>
</tr>
</tbody>
</table>

****

**6.6.5 Internally generated goodwill**

This standard prohibits the recognition of internally generated goodwill as an asset.

Internally generated goodwill is not recognised as an asset because it is not an identifiable resource (i.e. it is not separable nor does it arise from contractual or other legal rights) controlled by the entity that can be measured reliably at cost.

In some cases, expenditure is incurred to generate future economic benefits, but it does not result in the creation of an intangible asset that meets the recognition criteria in this Standard. Such expenditure is often described as contributing to internally generated goodwill.

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Differences between the fair value of an entity and the carrying amount of its identifiable net assets at any time may capture a range of factors that affect the fair value of the entity. However, such differences do not represent the cost of intangible assets controlled by the entity.

6.6.6 Internally generated intangible assets

- 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.

Therefore, in addition to complying with the general requirements for the recognition and initial measurement of an intangible asset, this standard includes additional recognition criteria for internally generated intangible assets which expand on the general recognition criteria.

- 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) a development phase.

- 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.

Items that should not be recognised as internally generated intangible assets

This standard prohibits the recognition of internally generated goodwill as an asset. Some other internally generated items that are prohibited to be recognised as an intangible assets are brands, mastheads, publishing titles, customer lists and items similar in substance shall not be recognised as intangible assets.

Research phase

- **Research** is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

- No intangible asset arising from research (or from the research phase of an internal project) should be recognised. Expenditure on research (or on the research phase of an internal project) should be recognised as an expense when it is incurred.

- In the research phase of an internal project, an entity cannot demonstrate that an intangible asset exists that will generate probable future economic benefits. Therefore, this expenditure is recognised as an expense when it is incurred.

- Examples of research activities are:
  (a) activities aimed at obtaining new knowledge;
  (b) the search for, evaluation and final selection of, applications of research findings or other knowledge;
(c) the search for alternatives for materials, devices, products, processes, systems or services; and

(d) the formulation, design, evaluation and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.

**Development Phase**

**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.

- **Examples of development activities are:**
  
  - Design, construction and testing of pre-production or pre-use prototypes and models;
  - Design of tools, jigs, moulds and dies involving new technology;
  - Design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production;
  - Design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

An intangible asset arising from development (or from the development phase of an internal project) should be recognised if, and only if, an entity can demonstrate all of the following:

- Technical feasibility of completion of Intangible asset to make it available for use or sale
- 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. Among other things, the entity can demonstrate the 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.
- Adequate resources (like technical, financial or others) to complete the development.
- Ability to measure reliably the expenditure attributable to the intangible asset during its development.
In the development phase of an internal project, an entity can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits. This is because the development phase of a project is further advanced than the research phase.

To demonstrate how an intangible asset will generate probable future economic benefits, an entity assesses the future economic benefits to be received from the asset using the principles in Ind AS 36, *Impairment of Assets*. If the asset will generate economic benefits only in combination with other assets, the entity applies the concept of cash-generating units in Ind AS 36.

Availability of resources to complete, use and obtain the benefits from an intangible asset can be demonstrated by, for example, a business plan showing the technical, financial and other resources needed and the entity’s ability to secure those resources. In some cases, an entity demonstrates the availability of external finance by obtaining a lender’s indication of its willingness to fund the plan.

An entity’s costing systems can often measure reliably the cost of generating an intangible asset internally, such as salary and other expenditure incurred in securing copyrights or licences or developing computer software.

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**Research is mainly acquisition of Knowledge**

**Development is application of Knowledge**

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**Cost of an internally generated asset**

The cost of an internally generated intangible asset for the purpose of initial measurement at recognition is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria including the additional criteria specified above.

**Cost -Inclusions**

The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce, and prepare the asset to be capable of operating in the manner intended by management.
Examples of directly attributable costs are:

- Costs of materials and services used or consumed in generating the intangible asset
- Costs of employee benefits (as defined in Ind AS 19) arising from the generation of the intangible asset
- Fees to register a legal right
- Amortisation of patents and licences that are used to generate the intangible asset

The specific guidance is given for borrowing costs to be capitalized as part of the cost of a self-generated intangible asset.

This standard prohibits reinstatement of expenditure previously recognised as an expense.

**Cost - Exclusions**

The following are not components of the cost of an internally generated intangible asset:

(a) selling, administrative and other general overhead expenditure unless this expenditure can be directly attributed to preparing the asset for use;

(b) identified inefficiencies and initial operating losses incurred before the asset achieves planned performance; and

(c) expenditure on training staff to operate the asset.

**Illustration 8**

Venus Ltd. is preparing its accounts for the year ended 31st March, 20X2 and is unsure how to treat the following items.

1. Company has completed a big marketing and advertising campaign costing ₹2,40,000. The finance director had authorised this campaign on the basis that it would create ₹5,00,000 of additional profits over the next three years.

2. A new product was developed during the year. The expenditure totalled ₹1,50,000 of which ₹1,00,000 was incurred prior to 30th September, 20X1, the date on which it became clear that the product was technically viable. The new product will be launched in the next four months and its recoverable amount is estimated at ₹70,000.

3. Staff participated in a training programme which cost the company ₹300,000. The training organisation had made a presentation to the directors of Baxter outlining that incremental profits to the business over the next twelve months would be ₹500,000.

What amounts should appear as assets in Venus Ltd. Balance sheet as at 31st March, 20X2?
Solution

The treatment in Venus Ltd’s balance sheet as at 31st March, 20X2 will be as follows:

1. Marketing and advertising campaign: no asset will be recognised, because it is not possible to identify future economic benefits that are attributable only to this campaign. All of the expenditure should be expensed in the statement of profit and loss account.

2. New product: development expenditure appearing in the statement of financial position will be valued at ₹ 50,000. The expenditure prior to the date on which the product becomes technically feasible is recognised in the statement of profit and loss account.

3. Training programme: no intangible asset will be recognised, because staff are not under the control of Venus Ltd. and when staff leave the benefits of the training, whatever they may be, also leave.

Illustration 9: Development Phase

Expenditure on a new production process in 20X1-20X2:

<table>
<thead>
<tr>
<th>Period</th>
<th>Expenditure (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st April to 31st December</td>
<td>2,700</td>
</tr>
<tr>
<td>1st January to 31st March</td>
<td>900</td>
</tr>
<tr>
<td></td>
<td>3,600</td>
</tr>
</tbody>
</table>

The production process met the intangible asset recognition criteria for development on 1st January, 20X2. The amount estimated to be recoverable from the process is ₹ 1,000.

Expenditure incurred for development of the process in FY 20X2-20X3 is ₹ 6,000. Asset was brought into use on 31st March, 20X3 and is expected to be useful for 6 years.

What is the carrying amount of the intangible asset at 31st March, 20X2 and 31st March, 20X3? Also determine the charge to profit or loss for 20X1-20X2?

At 31st March, 20X4, the amount estimated to be recoverable from the process is ₹ 5,000.

What is the carrying amount of the intangible asset at 31st March, 20X4 and the charge to profit or loss for 20X3-20X4?

Solution

1) Expenditure to be transferred to profit or loss in 20X1-20X2

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Expenditure</td>
<td>3,600</td>
</tr>
<tr>
<td>Less: Expenditure during development phase</td>
<td>(900)</td>
</tr>
<tr>
<td>Expenditure to be transferred to profit or loss</td>
<td>2,700</td>
</tr>
</tbody>
</table>
2) **Carrying amount of intangible asset on 31st March, 20X2**
   Expenditure during Development Phase will be capitalised ₹ 900
   (Recoverable amount is higher being ₹ 1,000, hence no impairment)

3) **Carrying amount of intangible asset on 31st March, 20X3**
   Carrying amount of intangible asset on 31st March, 20X2 ₹ 900
   Add: Further expenditure during development phase 6,000
   Total capital expenditure on development phase 6,900

4) **Expenditure to be charged to profit or loss in 20X3-20X4**
   Opening balance of Intangible Asset 6,900
   Add: Amortisation for the year (6,900 / 6) (1,150)
   Carrying amount of intangible asset 5,750
   Less: Recoverable Amount (5,000)
   Amount charged to profit or loss (Impairment Loss) 750

5) **Carrying Amount of Intangible Asset on 31st March, 20X4**
   Value of Intangible Asset will be recoverable amount i.e. ₹ 5,000
   *****

6.7. **RECOGNITION OF AN EXPENSE**

- Expenditure on an intangible item should be recognised as an expense when it is incurred unless:
  (a) it forms part of the cost of an intangible asset that meets the recognition criteria; or
  (b) the item is acquired in a business combination and cannot be recognised as an intangible asset. In such case, it forms part of the amount recognised as goodwill at the acquisition date.

- This standard states that the following types of expenditure should always be recognised as an expense:
  (a) expenditure on research (except when it is acquired as part of a business combination);
  (b) expenditure on start-up activities (ie start-up costs), unless this expenditure is included in the cost of an item of property, plant and equipment in accordance with Ind AS 16. Start-up costs may consist of:
      (i) establishment costs such as legal and secretarial costs incurred in establishing a legal entity;
      (ii) expenditure to open a new facility or business (ie pre-opening costs);
      (iii) expenditures for starting new operations or launching new products or processes (ie
pre-operating costs);
(c) expenditure on training activities;
(d) expenditure on advertising and promotional activities (including mail order catalogues); and
(e) expenditure on relocating or reorganising part or all of an entity.

More generally, if expenditure does not give rise to an intangible asset:

(a) for the supply of goods, an expense is recognised when the entity has a right to access those goods. An entity has a right to access goods when it owns them. Similarly, it has a right to access goods when they have been constructed by a supplier in accordance with the terms of a supply contract and the entity could demand delivery of them in return for payment.

(b) for a supply of services, the entity recognises the expenditure as an expense when it receives the services. Services are received when they are performed by a supplier in accordance with a contract to deliver them to the entity and not when the entity uses them to deliver another service, for example, to deliver an advertisement to customers.

This does not preclude an entity from recognising a prepayment as an asset when payment for goods has been made in advance of the entity obtaining a right to access those goods or in advance of the entity receiving those services.

Expenditure on an intangible item that was initially recognised as an expense should not be recognised as part of the cost of an intangible asset at a later date.

6.8 MEASUREMENT AFTER RECOGNITION

An entity should choose either the cost model or the revaluation model as its accounting policy.

| Cost Model | Revaluation Model |

6.8.1 Cost model

After initial recognition, an intangible asset is carried at its cost less any accumulated amortisation and any accumulated impairment losses.
6.8.2 Revaluation model

After initial recognition, an intangible asset is carried at a revalued amount, being its fair value at
the date of the revaluation less any subsequent accumulated amortisation and any subsequent
accumulated impairment losses.

- For the purpose of revaluations under this Standard, fair value is measured by reference to an
active market.

- The revaluation model does not allow:
  
  (a) the revaluation of intangible assets that have not previously been recognised as assets; or
  
  (b) the initial recognition of intangible assets at amounts other than cost.

- The revaluation model is applied after an asset has been initially recognised at cost. However,
if only part of the cost of an intangible asset is recognised as an asset because the asset did
not meet the criteria for recognition until part of the way through the process, the revaluation
model may be applied to the whole of that asset.

- Also, the revaluation model may be applied to an intangible asset that was received by way of
a Government grant and recognised at a nominal amount.

Frequency of revaluations

- Revaluations should be made with such regularity that at the end of the reporting period the
carrying amount of the asset does not differ materially from its fair value.

- The frequency of revaluations depends on the volatility of the fair values of the intangible assets
being revalued. If the fair value of a revalued asset differs materially from its carrying amount,
a further revaluation is necessary.

- Some intangible assets may experience significant and volatile movements in fair value, thus
necessitating annual revaluation. Such frequent revaluations are unnecessary for intangible
assets with only insignificant movements in fair value.

Scope of revaluations

- If an intangible asset is accounted for using the revaluation model, all the other assets in its
class should also be accounted for using the same model, unless there is no active market for
those assets.

- If an intangible asset in a class of revalued intangible assets cannot be revalued because there
is no active market for this asset, the asset is carried at its cost less any accumulated
amortisation and impairment losses.
A class of intangible assets is a grouping of assets of a similar nature and use in an entity’s operations.

If the fair value of a revalued intangible asset can no longer be measured by reference to an active market, the carrying amount of the asset is its revalued amount at the date of the last revaluation by reference to the active market less any subsequent accumulated amortisation and any subsequent accumulated impairment losses.

The fact that an active market no longer exists for a revalued intangible asset may indicate that the asset may be impaired and that it needs to be tested in accordance with Ind AS 36. If the fair value of the asset can be measured by reference to an active market at a subsequent measurement date, the revaluation model is applied from that date.

Accumulated amortisation at the date of revaluation

When an intangible asset is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, the asset is treated in one of the following ways:

(a) the gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. For example, the gross carrying amount may be restated by reference to observable market data or it may be restated proportionately to the change in the carrying amount. The accumulated amortisation at the date of the revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account accumulated impairment losses; or

(b) the accumulated amortisation is eliminated against the gross carrying amount of the asset.

Treatment of surplus or deficit arising on revaluation

If an intangible asset’s carrying amount is increased as a result of a revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus.

However, the 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.

If an intangible asset’s carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in profit or loss.

However, the decrease shall be recognised in other comprehensive income to the extent of any credit balance in the revaluation surplus in respect of that asset. The decrease recognised in other comprehensive income reduces the amount accumulated in equity under the heading of revaluation surplus.

The cumulative revaluation surplus included in equity may be transferred directly to retained earnings when the surplus is realised. The whole surplus may be realised on the retirement or disposal of the asset. Some realisation of the revaluation surplus may occur, however, through the use of the intangible asset.
The amount of the surplus realised is the difference between amortisation based on the revalued carrying amount of the asset and amortisation that would have been recognised based on the asset’s historical cost. The transfer from revaluation surplus to retained earnings is not made through profit or loss.

**Treatment of Revaluation Gain or Loss**

**First time revaluation**
- Increase in the carrying amount (CA) of the revalued asset
  - Recognise the revaluation gain in OCI

**Subsequent revaluation**
- Decrease in the carrying amount (CA) of the revalued asset
  - Recognise the revaluation loss in P & L

**Was there a previous increase in CA of the revalued asset?**
- Yes
  - Recognise the revaluation gain in P & L to the extent that it reverses a revaluation decrease of the same asset previously recognised in P & L
  - Remaining increase to be recognised in OCI

- No
  - Recognise the revaluation loss in OCI to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
  - Remaining decrease to be recognised in P & L

**Was there a previous decrease in CA of the revalued asset?**
- Yes
  - Recognise the revaluation loss in P & L

- No
  - Recognise the revaluation gain in OCI

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Illustration 10 : Revaluation Model

1. Saturn Ltd. acquired an intangible asset on 31st March, 20X1 for ₹ 1,00,000. The asset was revalued at ₹ 1,20,000 on 31st March, 20X2 and ₹ 85,000 on 31st March, 20X3.

2. Jupiter Ltd. acquired an intangible asset on 31st March, 20X1 for ₹ 1,00,000. The asset was revalued at ₹ 85,000 on 31st March, 20X2 and at ₹ 1,05,000 on 31st March, 20X3.

Assuming that the year-end for both companies is 31st March, and that they both use the revaluation model, show how each of these transactions should be dealt with in the financial statements. Explain the treatment for revaluation of intangible asset. Ignore computation of amortization on them for ease of understanding.

Solution

Saturn Ltd.

₹ 20,000 revaluation increase on 31st March, 20X2 should be credited to the revaluation reserve and recognised in other comprehensive income. ₹ 20,000 of the revaluation decrease on 31st March, 20X3 should be debited to revaluation reserve and remaining ₹ 15,000 should be recognised as an expense.

Jupiter Ltd.

₹ 15,000 revaluation decrease on 31st March, 20X2 should be recognised as an expense in the Statement of Profit and loss. ₹ 15,000 out of the ₹ 20,000 increase on 31st March, 20X3 should be recognised as income. The remaining ₹ 5,000 should be credited to revaluation reserve and recognised in other comprehensive income.

Note: The above amount will be different if amortization of intangible asset is taken into consideration.

*****

6.9 USEFUL LIFE

- The accounting for an intangible asset is based on its useful life. An intangible asset with a finite useful life is amortised, and an intangible asset with an indefinite useful life is not amortised and tested for impairment.

Finite or indefinite useful life

- Entities are required to assess whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that useful life.

- An intangible asset should be regarded by the entity as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.
Factors for consideration in determining useful life

- Many factors are considered in determining the useful life of an intangible asset, including:
  - Expected usage of the asset by the entity
  - Product life cycles for the asset and public information on estimates of useful life of similar asset used in a similar way
  - Technical, technological, commercial or other type of obsolescence
  - Industrial Stability in which the asset operate and changes in market demand for the products or services from the output
  - Expected actions by competitors or potential competitors
  - Period of control over the asset and legal or similar limits on the use of assets, like expiry dates of related leases
  - Whether the useful life is dependent on the useful lives of other assets of the entity

- The useful life of an intangible asset reflects only that level of future maintenance expenditure required to maintain the asset at its standard of performance assessed at the time of estimating the asset’s useful life, and the entity’s ability and intention to reach such a level.

- A conclusion that the useful life of an intangible asset is indefinite should not depend on planned future expenditure in excess of that required to maintain the asset at that standard of performance.

- This standard notes that, given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it will often be the case that their useful life is short. Expected future reductions in the selling price of an item that was produced using an intangible asset could indicate the expectation of technological or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in the asset.

- The useful life of an intangible asset may be very long or even indefinite. Uncertainty justifies estimating the useful life of an intangible asset on a prudent basis, but it does not justify choosing a life that is unrealistically short.
Intangible asset arising from contractual or other legal rights

- The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset.

- If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

- Existence of the following factors, among others, indicates that an entity would be able to renew the contractual or other legal rights without significant cost:
  
  (a) there is evidence, possibly based on experience, that the contractual or other legal rights will be renewed. If renewal is contingent upon the consent of a third party, this includes evidence that the third party will give its consent;
  
  (b) there is evidence that any conditions necessary to obtain renewal will be satisfied; and
  
  (c) the cost to the entity of renewal is not significant when compared with the future economic benefits expected to flow to the entity from renewal.

- If the cost of renewal is significant when compared with the future economic benefits expected to flow to the entity from renewal, the ‘renewal’ cost represents, in substance, the cost to acquire a new intangible asset at the renewal date.

- The useful life of a reacquired right recognised as an intangible asset in a business combination is the remaining contractual period of the contract in which the right was granted and shall not include renewal periods.
6.10 INTANGIBLE ASSETS WITH FINITE USEFUL LIVES

6.10.1 Depreciable amount to be amortised over the asset’s useful life

- The depreciable amount of an intangible asset with a finite useful life is allocated on a systematic basis over its useful life. The depreciable amount of an asset is defined as the cost of an asset, or other amount substituted for cost, less its residual value.

- Amortisation is usually recognised in profit or loss. However, sometimes the future economic benefits embodied in an asset are absorbed in producing other assets. In this case, the amortisation charge constitutes part of the cost of the other asset and is included in its carrying amount. For example, the amortisation of intangible assets used in a production process is included in the carrying amount of inventories (see Ind AS 2, Inventories).

6.10.2 Residual Value

- The residual value of an intangible asset with a finite useful life should be assumed to be zero unless:

  (a) there is a commitment by a third party to purchase the asset at the end of its useful life; or
  
  (b) there is an active market (as defined in Ind AS 113) for the asset and:

    (i) residual value can be determined by reference to that market; and
    
    (ii) it is probable that such a market will exist at the end of the asset’s useful life.

The residual value is reviewed at least at each financial year-end. An estimate of an asset’s residual value is based on the amount recoverable from disposal using prices prevailing at the date of the estimate for the sale of a similar asset that has reached the end of its useful life and has operated under conditions similar to those in which the asset will be used.

- A change in the asset’s residual value is accounted for as a change in an accounting estimate in accordance with Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors.
The residual value of an intangible asset may increase to an amount equal to or greater than the asset’s carrying amount. If it does, the asset’s amortisation charge is zero unless and until its residual value subsequently decreases to an amount below the asset’s carrying amount.

6.10.3 Amortisation period

Commencement of amortisation
Amortisation commence from the date when the asset is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

Cessation of amortisation
Amortisation ceases at the earlier of:

(a) the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with Ind AS 105; and

(b) the date that the asset is derecognised.

Amortisation of an intangible asset with a finite useful life does not cease when the intangible asset is no longer used, unless the asset has been fully depreciated or is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with Ind AS 105.

Review of amortisation period
The amortisation period for an intangible asset with a finite useful life should be reviewed at least at each financial year-end. If the expected useful life of the asset is different from previous estimates,
the amortisation period should be changed accordingly. Such change is accounted for as a change in accounting estimates in accordance with Ind AS 8.

6.10.4 Amortisation method

The amortisation method used should reflect the pattern in which the asset’s future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method should be used.

A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method.

In choosing an appropriate amortisation method, an entity could determine the predominant limiting factor that is inherent in the intangible asset. For example, the contract that sets out the entity’s rights over its use of an intangible asset might specify the entity’s use of the intangible asset as a predetermined number of years (i.e. time), as a number of units produced or as a fixed total amount of revenue to be generated.

Identification of such a predominant limiting factor could serve as the starting point for the identification of the appropriate basis of amortisation, but another basis may be applied if it more closely reflects the expected pattern of consumption of economic benefits.

The amortisation method for an intangible asset with a finite useful life should be reviewed at least at each financial year-end. If there has been a change in the expected pattern of consumption of the future economic benefits embodied in the asset, the amortisation method should be changed to reflect the changed pattern. Such change is accounted for as a change in accounting estimates in accordance with Ind AS 8.

Amortisation method based on revenue

There is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate.

The revenue generated by an activity that includes the use of an intangible asset typically reflects factors that are not directly linked to the consumption of the economic benefits embodied in the intangible asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

This presumption can be overcome only in the limited circumstances:

(a) in which the intangible asset is expressed as a measure of revenue, as described in paragraph 98C; or

(b) when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.
In the circumstance in which the predominant limiting factor that is inherent in an intangible asset is the achievement of a revenue threshold, the revenue to be generated can be an appropriate basis for amortisation. For example, an entity could acquire a concession to explore and extract gold from a gold mine. The expiry of the contract might be based on a fixed amount of total revenue to be generated from the extraction (for example, a contract may allow the extraction of gold from the mine until total cumulative revenue from the sale of gold reaches ₹ 2 billion) and not be based on time or on the amount of gold extracted.

In another example, the right to operate a toll road could be based on a fixed total amount of revenue to be generated from cumulative tolls charged (for example, a contract could allow operation of the toll road until the cumulative amount of tolls generated from operating the road reaches ₹ 100 lakh). In the case in which revenue has been established as the predominant limiting factor in the contract for the use of the intangible asset, the revenue that is to be generated might be an appropriate basis for amortising the intangible asset, provided that the contract specifies a fixed total amount of revenue to be generated on which amortisation is to be determined.

**Example : An acquired customer list**

A direct-mail marketing company acquires a customer list and expects that it will be able to derive benefit from the information on the list for at least one year, but no more than three years.

The customer list would be amortised over management’s best estimate of its useful life, say 18 months. Although the direct-mail marketing company may intend to add customer names and other information to the list in the future, the expected benefits of the acquired customer list relate only to the customers on that list at the date it was acquired. The customer list also would be reviewed for impairment in accordance with Ind AS 36, *Impairment of Assets*, by assessing at the end of each reporting period whether there is any indication that the customer list may be impaired.

**Example : An acquired patent that expires in 15 years**

The product protected by the patented technology is expected to be a source of net cash inflows for at least 15 years. The entity has a commitment from a third party to purchase that patent in five years for 60 per cent of the fair value of the patent at the date it was acquired, and the entity intends to sell the patent in five years.

The patent would be amortised over its five-year useful life to the entity, with a residual value equal to the present value of 60 per cent of the patent’s fair value at the date it was acquired. It may be noted that the estimated useful life has to be considered with reference to the entity only though the total life of the patent is much higher i.e., 15 years. The patent would also be reviewed for impairment in accordance with Ind AS 36 by assessing at the end of each reporting period whether there is any indication that it may be impaired.

**Example : An acquired copyright that has a remaining legal life of 50 years**

An analysis of consumer habits and market trends provides evidence that the copyrighted material will generate net cash inflows for only 30 more years.
It needs to be noted that although the remaining legal life of the patent is 50 years, however the useful life from the entity’s perspective is only 30 years. The copyright would be amortised over its 30-years estimated useful life. The copyright also would be reviewed for impairment in accordance with Ind AS 36 by assessing at the end of each reporting period whether there is any indication that it may be impaired.

**Example A: An acquired broadcasting licence that expires in five years**

The broadcasting licence is renewable every 10 years if the entity provides at least an average level of service to its customers and complies with the relevant legislative requirements. The licence may be renewed indefinitely at little cost and has been renewed twice before the most recent acquisition. The acquiring entity intends to renew the licence indefinitely and evidence supports its ability to do so. Historically, there has been no compelling challenge to the licence renewal. The technology used in broadcasting is not expected to be replaced by another technology at any time in the foreseeable future. Therefore, the licence is expected to contribute to the entity’s net cash inflows indefinitely.

The broadcasting licence would be treated as having an indefinite useful life because it is expected to contribute to the entity’s net cash inflows indefinitely. Therefore, the licence would not be amortised until its useful life is determined to be finite. The licence would be tested for impairment in accordance with Ind AS 36 annually and whenever there is an indication that it may be impaired.

**Example : The broadcasting licence in Example A**

The licensing authority subsequently decides that it will no longer renew broadcasting licences, but rather will auction the licences. At the time the licensing authority’s decision is made, the entity’s broadcasting licence has three years until it expires. The entity expects that the licence will continue to contribute to net cash inflows until the licence expires.

Because the broadcasting licence can no longer be renewed, its useful life is no longer indefinite. Thus, the acquired licence would be amortised over its remaining three-year useful life and immediately tested for impairment in accordance with Ind AS 36.

**Example : An acquired airline route authority between two European cities that expires in three years**

The route authority may be renewed every five years, and the acquiring entity intends to comply with the applicable rules and regulations surrounding renewal. Route authority renewals are routinely granted at a minimal cost and historically have been renewed when the airline has complied with the applicable rules and regulations. The acquiring entity expects to provide service indefinitely between the two cities from its hub airports and expects that the related supporting infrastructure (airport gates, slots, and terminal facility leases) will remain in place at those airports for as long as it has the route authority. An analysis of demand and cash flows supports those assumptions.

Since the facts and circumstances support the acquiring entity’s ability to continue providing air service indefinitely between the two cities, the intangible asset related to the route authority is treated
as having an indefinite useful life. Therefore, the route authority would not be amortised until its useful life is determined to be finite. It would be tested for impairment in accordance with Ind AS 36 annually and whenever there is an indication that it may be impaired.

**Example: An acquired trademark used to identify and distinguish a leading consumer product that has been a market-share leader for the past eight years**

The trademark has a remaining legal life of five years but is renewable every 10 years at little cost. The acquiring entity intends to renew the trademark continuously and evidence supports its ability to do so. An analysis of (1) product life cycle studies, (2) market, competitive and environmental trends, and (3) brand extension opportunities provides evidence that the trademarked product will generate net cash inflows for the acquiring entity for an indefinite period.

The trademark would be treated as having an indefinite useful life because it is expected to contribute to net cash inflows indefinitely. Though the remaining legal life is five years, the possibility that it can be renewed every ten years and the entity’s intention to renew the same leads to the conclusion that the trademark has an indefinite useful life. Therefore, the trademark would not be amortised until its useful life is determined to be finite. It would be tested for impairment in accordance with Ind AS 36 annually and whenever there is an indication that it may be impaired.

**Example: A trademark acquired 10 years ago that distinguishes a leading consumer product**

The trademark was regarded as having an indefinite useful life when it was acquired because the trademarked product was expected to generate net cash inflows indefinitely. However, unexpected competition has recently entered the market and will reduce future sales of the product. Management estimates that net cash inflows generated by the product will be 20 per cent less for the foreseeable future. However, management expects that the product will continue to generate net cash inflows indefinitely at those reduced amounts.

As a result of the projected decrease in future net cash inflows, the entity determines that the estimated recoverable amount of the trademark is less than its carrying amount, and an impairment loss is recognised. Since it is still regarded as having an indefinite useful life, the trademark would continue not to be amortised but would be tested for impairment in accordance with Ind AS 36 annually and whenever there is an indication that it may be impaired.

**Example: Trademark for a line of products that was acquired several years ago in a business combination**

At the time of the business combination the acquiree had been producing the line of products for 35 years with many new models developed under the trademark. At the acquisition date the acquirer expected to continue producing the line, and an analysis of various economic factors indicated there was no limit to the period the trademark would contribute to net cash inflows. Consequently, the trademark was not amortised by the acquirer. However, management has recently decided that production of the product line will be discontinued over the next four years.
Since the useful life of the acquired trademark is no longer regarded as indefinite, the carrying amount of the trademark would be tested for impairment in accordance with Ind AS 36 and amortised over its remaining four-year useful life.

6.11 INTANGIBLE ASSETS WITH INDEFINITE USEFUL LIVES

- An intangible asset with an indefinite useful life should not be amortised.
- In accordance with Ind AS 36, 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
  
  (a) annually; and
  
  (b) whenever there is an indication that the intangible asset may be impaired.
- The useful life of an intangible asset that is not being amortised should be reviewed each period to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate in accordance with Ind AS 8.
- In accordance with Ind AS 36, reassessing the useful life of an intangible asset as finite rather than indefinite is an indicator that the asset may be impaired. As a result, the entity tests the asset for impairment by comparing its recoverable amount, determined in accordance with Ind AS 36, with its carrying amount, and recognising any excess of the carrying amount over the recoverable amount as an impairment loss.

6.12 IMPAIRMENT

- To determine whether an intangible asset is impaired, an entity applies Ind AS 36. That Standard explains when and how an entity reviews the carrying amount of its assets, how it determines the recoverable amount of an asset and when it recognises or reverses an impairment loss.
- For an intangible asset with indefinite useful lives, an impairment review is required at least annually.

6.13 RETIREMENTS AND DISPOSALS

- An intangible asset should be derecognised:
  
  (a) on disposal; or
  
  (b) when no future economic benefits are expected from its use or disposal.
The disposal of an intangible asset may occur in a variety of ways (e.g. by sale, by entering into a finance lease, or by donation).

- The gain or loss arising from the derecognition of an intangible asset should be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It is to be recognised in profit or loss when the asset is derecognised (unless Ind AS 116 requires otherwise on a sale and leaseback). Gains should not be classified as revenue.

- If in accordance with the recognition principle an entity recognises in the carrying amount of an asset the cost of a replacement for part of an intangible asset, then it derecognises the carrying amount of the replaced part. If it is not practicable for an entity to determine the carrying amount of the replaced part, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or internally generated.

- The date of disposal of an intangible asset is the date that the recipient obtains control of that asset in accordance with the requirements for determining when a performance obligation is satisfied as per Ind AS 115. **Ind AS 116 applies to disposal by a sale and leaseback.**

- In the case of a reacquired right in a business combination, if the right is subsequently reissued (sold) to a third party, the related carrying amount, if any, should be used in determining the gain or loss on reissue.

- The amount of consideration to be included in the gain or loss arising from the derecognition of an intangible asset is determined in accordance with the requirements for determining the transaction price (as per Ind AS 115). Subsequent changes to the estimated amount of the consideration included in the gain or loss shall be accounted for in accordance with the requirements for changes in the transaction price in Ind AS 115.

### 6.14 DISCLOSURE

#### 1) Disclosure – general

An entity should disclose the following for each class of intangible assets, distinguishing between internally generated intangible assets and other intangible assets:

- whether the useful lives are indefinite or finite and, if finite, the useful lives or the amortisation rates used;
b) the amortisation methods used for intangible assets with finite useful lives;

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

d) the line item(s) of the statement of profit and loss in which any amortisation of intangible assets is included; and

e) a reconciliation of the carrying amount at the beginning and end of the period showing:

(i) additions, indicating separately those from internal development, those acquired separately, and those acquired through business combinations;

(ii) assets classified as held for sale or included in a disposal group classified as held for sale in accordance with Ind AS 105 and other disposals;

(iii) increases or decreases during the period resulting from revaluations and from impairment losses recognised or reversed in other comprehensive income;

(iv) impairment losses recognised in profit or loss during the period;

(v) impairment losses reversed in profit or loss during the period;

(vi) any amortisation recognised during the period;

(vii) net exchange differences arising on the translation of the financial statements into the presentation currency, and on the translation of a foreign operation into the presentation currency of the entity; and

(viii) other changes in the carrying amount during the period.

2) **Intangible assets having an indefinite useful life**

For an intangible asset assessed as having an indefinite useful life, financial statement should disclose the carrying amount of that asset and the reasons supporting the assessment of an indefinite useful life. In giving these reasons, the entity shall describe the factor(s) that played a significant role in determining that the asset has an indefinite useful life.

3) **Intangible assets that are individually material**

Financial statement should disclose a description, the carrying amount and remaining amortisation period of any individual intangible asset that is material to the entity’s financial statements.

4) **Intangible assets acquired by way of government grant**

For intangible assets acquired by way of a government grant and initially recognised at fair value, the financial statement should disclose:

a) the fair value initially recognised for these assets;

b) their carrying amount; and
c) whether they are measured after recognition under the cost model or the revaluation model.

5) **Title restrictions and capital commitments**

The financial statement should also disclose:

the existence and carrying amounts of intangible assets whose title is restricted and the carrying amounts of intangible assets pledged as security for liabilities and the amount of contractual commitments for the acquisition of intangible assets.

6) **Intangible assets carried at revalued amounts**

If intangible assets are accounted for at revalued amounts, an entity should disclose the following:

a) by class of intangible assets:
   (i) the effective date of the revaluation;
   (ii) the carrying amount of revalued intangible assets; and
   (iii) the carrying amount that would have been recognised had the revalued class of intangible assets been measured after recognition using the cost model; and

b) the amount of the revaluation surplus that relates to intangible assets at the beginning and end of the period, indicating the changes during the period and any restrictions on the distribution of the balance to shareholders.

If necessary, it is acceptable to aggregate the classes of revalued assets into larger classes for disclosure purposes. However, classes are not aggregated if this would result in the combination of a class of intangible assets that includes amounts measured under both the cost and revaluation models.

7) **Research and development expenditure**

An entity should disclose the aggregate amount of research and development expenditure recognised as an expense during the period.

8) **Other information**

An entity is encouraged, but not required, to disclose the following information:

a) a description of any fully amortised intangible asset that is still in use; and

b) a brief description of significant intangible assets controlled by the entity but not recognised as assets because they did not meet the recognition criteria in this Standard or because they were acquired or generated before this standard was effective.
**Illustration 11**

X Limited engaged in the business of manufacturing fertilisers entered into a technical collaboration agreement with a foreign company Y Limited. As a result, Y Limited would provide the technical know-how enabling X Limited to manufacture fertiliser in a more efficient way. X Limited paid ₹10,00,00,000 for the use of know-how for a period of 5 years. X Limited estimates the production of fertiliser as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>(In metric tons)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>50,000</td>
</tr>
<tr>
<td>2</td>
<td>70,000</td>
</tr>
<tr>
<td>3</td>
<td>1,00,000</td>
</tr>
<tr>
<td>4</td>
<td>1,20,000</td>
</tr>
<tr>
<td>5</td>
<td>1,10,000</td>
</tr>
</tbody>
</table>

At the end of the 1st year, it achieved its targeted production. At the end of 2nd year, 65,000 metric tons of fertiliser was being manufactured, and X Limited considered to revise the estimates for the next 3 years. The revised figures are 85,000, 1,05,000 and 1,15,000 metric tons for year 3, 4 & 5 respectively.

*How will X Limited amortise the technical know-how fees as per Ind AS 38?*

**Solution**

Based on the above data, it may be suitable for X Ltd. to use unit of production method for amortisation of technical know-how.

The total estimated unit to be produced 4,50,00 MT. The technical know-how will be amortised on the basis of the ratio of yearly production to total production.

The first year charge should be a proportion of 50,000/4,50,00 on ₹ 10,00,00,000 = ₹ 1,11,11,111.

At the end of 2nd year, as per revised estimate the total number of units to be produced in future are 3,70,00 MT (ie 65,000 + 85,000 + 1,05,000 + 1,15,000).

The amortisation for second year will be 65,000 / 3,70,000 on (10,00,00,000 – 1,11,11,111) i.e 1,56,15,615 and so on for remaining years unless the estimates are again revised.

*****

**Illustration 12**

X Ltd. purchased a patent right on 1st April, 20X1, for ₹3,00,000; which has a legal life of 15 years. However, due to the competitive nature of the product, the management estimates a useful life of only 5 years. Straight-line amortisation is determined by the management to be the best method. As at 1st April, 20X2, management is uncertain that the process can actually be made economically...
feasible, and decides to write down the patent to an estimated market value of ₹ 1,50,000 and decides to amortise over 2 years. As at 1st April, 20X3, having perfected the related production process, the asset is now appraised at a value of ₹ 3,00,000. Furthermore, the estimated useful life is now believed to be 4 more years. Determine the value of intangible asset at the end of each financial year?

Solution

Value as on 31st March, 20X2

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Original cost</td>
<td>₹ 3,00,000</td>
</tr>
<tr>
<td>Less: amortisation</td>
<td>(₹ 60,000)</td>
</tr>
<tr>
<td>Net Value</td>
<td>₹ 2,40,000</td>
</tr>
</tbody>
</table>

Value as on 31st March, 20X3

On 1st April, 20X2, the impairment is recorded by writing down the asset to the estimated value of ₹ 1,50,000, which necessitates a ₹ 90,000 charge to profit & loss (carrying value, ₹ 2,40,000 less fair value ₹ 1,50,000).

Amortisation provided for the financial year 20X2-20X3 is ₹ 75,000 (₹ 1,50,000/2)

Net value is = ₹ 1,50,000 – ₹ 75,000 = ₹ 75,000.

Value as on 31st March, 20X4

As of 1st April, 20X3, the carrying value of the patent is ₹ 75,000.

Revalued amount of patent is ₹ 3,00,000.

Out of total revaluation gain of ₹ 2,25,000, ₹ 90,000 will be charged to profit & loss and balance amount of ₹ 1,35,000 (₹ 2,25,000 – ₹ 90,000) will be credited to revaluation reserve.

Illustration 13

X Pharmaceutical Ltd. seeks your opinion in respect of following accounting transactions:

1. Acquired a 4 year license to manufacture a specialised drug at a cost of ₹ 1,00,00,000 at the start of the year. Production commenced immediately.

2. Also purchased another company at the start of year. As part of that acquisition, X Pharmaceutical Ltd. acquired a brand with a fair value of ₹ 3,00,00,000 based on sales revenue. The life of the brand is estimated at 15 years.

3. Spent ₹ 1,00,00,000 on an advertising campaign during the first six months. Subsequent sales have shown a significant improvement and it is expected this will continue for 3 years.
4. It has commenced developing a new drug ‘Drug-A’. The project cost would be ₹10,00,00,000. Clinical trial proved successful and such drug is expected to generate revenue over the next 5 years.

Cost incurred (accumulated) till 31st March, 20X1 is ₹5,00,00,000.

Balance cost incurred during the financial year 20X1-20X2 is ₹5,00,00,000.

5. It has also commenced developing another drug ‘Drug B’. It has incurred ₹50,00,000 towards research expenses till 31st March, 20X2. The technological feasibility has not yet been established.

How the above transactions will be accounted for in the books of account of X Pharmaceutical Ltd?

Solution

X Pharmaceutical Ltd. is advised as under:

1. It should recognise the drug license as an intangible asset, because it is a separate external purchase, separately identifiable asset and considered successful in respect of feasibility and probable future cash inflows.

   The drug license should be recorded at ₹1,00,00,000.

2. It should recognise the brand as an intangible asset because it is purchased as part of acquisition and it is separately identifiable. The brand should be amortised over a period of 15 years.

   The brand will be recorded at ₹3,00,00,000.

3. The advertisement expenses of ₹1,00,00,000 should be expensed off.

4. The development cost incurred during the financial year 20X1-20X2 should be capitalised.

   Cost of intangible asset (Drug A) as on 31st March, 20X2
   
<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cost</td>
<td>₹5,00,00,000</td>
</tr>
<tr>
<td>Development cost</td>
<td>₹5,00,00,000</td>
</tr>
<tr>
<td>Total cost</td>
<td>₹10,00,00,000</td>
</tr>
</tbody>
</table>

5. Research expenses of ₹50,00,000 incurred for developing ‘Drug B’ should be expensed off since technological feasibility has not yet been established.

*****
### 6.15 Significant Differences in Ind AS 38 vis-à-vis AS 26

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Particular</th>
<th>Ind AS 38</th>
<th>AS 26</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Exclusions:</td>
<td>Ind AS 38 does not include any such exclusion specifically as these are</td>
<td>Paragraph 5 of AS 26, does not apply to accounting issues of specialised nature that arise in respect of accounting for discount or premium relating to borrowings and ancillary costs incurred in connection with the arrangement of borrowings, share issue expenses and discount allowed on the issue of shares.</td>
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<td></td>
<td></td>
<td>covered by other accounting standards.</td>
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<td></td>
<td></td>
<td>Ind AS 38 contains a scope exclusion with regard to the amortisation</td>
<td></td>
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<td></td>
<td></td>
<td>method for intangible assets arising from service concession</td>
<td></td>
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<td></td>
<td></td>
<td>arrangements in respect of toll roads recognised in the financial</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>statements before the beginning of the first Ind AS financial reporting</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>period as per the previous GAAP, i.e., Schedule II to the Companies Act,</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>2013</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Definition of Intangible Assets:</td>
<td>Ind AS 38, the requirement for the asset to be held for use in the</td>
<td>AS 26 standard defines an intangible asset as an identifiable non-monetary asset without physical substance held for use in the production or supply of goods or services, for rental to others, or for administrative purposes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>production or supply of goods or services, for rental to others, or for</td>
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<tr>
<td></td>
<td></td>
<td>administrative purposes has been removed from the definition of an</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>intangible asset.</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Identifiability</td>
<td>Ind AS 38 provides detailed guidance in respect of identifiability.</td>
<td>AS 26 does not define 'identifiability', but states that an intangible asset could be distinguished clearly from goodwill if the asset was separable, but that separability was not a necessary condition for identifiability.</td>
</tr>
<tr>
<td>4.</td>
<td>Separately Acquired</td>
<td>As per Ind AS 38, in the case of separately acquired intangibles, the</td>
<td>There is no such provision in AS 26.</td>
</tr>
<tr>
<td>Intangible Assets</td>
<td>always considered satisfied, even if there is uncertainty about the timing or the amount of the inflow.</td>
<td></td>
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<td>-------------------</td>
<td>-------------------------------------------------------------------------------------------------</td>
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<tr>
<td>5. Revenue Based Amortisation Method</td>
<td>In Ind AS 38 there is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. Ind AS 38 allows use of revenue based method of amortisation of intangible asset, in a limited way.</td>
<td>AS 26 does not specifically deal with revenue based amortisation method.</td>
<td></td>
</tr>
<tr>
<td>6. Payment Deferred beyond Normal Credit Terms</td>
<td>Under Ind AS 38, if payment for an intangible asset is deferred beyond normal credit terms, the difference between this amount and the total payments is recognised as interest expense over the period of credit unless it is capitalised as per Ind AS 23.</td>
<td>There is no such provision in AS 26.</td>
<td></td>
</tr>
<tr>
<td>7. Intangible Assets acquired in Business Combination</td>
<td>Ind AS 38 deals in detail in respect of intangible assets acquired in a business combination.</td>
<td>AS 26 refers only to intangible assets acquired in an amalgamation in the nature of purchase and does not refer to business combinations as a whole.</td>
<td></td>
</tr>
<tr>
<td>8. Subsequent Expenditure on in Process Research and Development Project</td>
<td>Ind AS 38 gives guidance for the treatment of such expenditure</td>
<td>AS 26 is silent regarding the treatment of subsequent expenditure on an in-process research and development project acquired in a business combination.</td>
<td></td>
</tr>
<tr>
<td>9. Intangible Assets Acquired in Exchange</td>
<td>Ind AS 38 requires that if an intangible asset is acquired in exchange of a non-monetary asset, it should be recognised at the fair value of the asset given up unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable.</td>
<td>AS 26 requires the principles of AS 10 to be followed which require that when an asset is acquired in exchange for another asset, its cost is usually determined by reference to the fair market value of the consideration given. It may be appropriate to consider also the fair market value of the asset</td>
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<td>7.315</td>
<td>acquired if this is more clearly evident. An alternative accounting treatment to record the asset acquired at the net book value of the asset given up; in each case an adjustment is made for any balancing receipt or payment of cash or other consideration also.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
| 10. | Intangible Assets acquired Free of Charge or for a Nominal Consideration by way of Government Grant | As per Ind AS 38, when intangible assets are acquired free of charge or for nominal consideration by way of government grant, an entity should, in accordance with Ind AS 20, record both the grant and the intangible asset at fair value. An alternative course that is sometimes followed is to record both asset and grant at a nominal amount.  
As per AS 26, intangible assets acquired free of charge or for nominal consideration by way of government grant is recognised at nominal value or at acquisition cost, as appropriate plus any expenditure that is attributable to making the asset ready for intended use. |   |
| 11. | Useful Life of an Intangible Asset | That rebuttable presumption is not there in Ind AS 38. Ind AS 38 recognizes that the useful life of an intangible asset can even be indefinite subject to fulfillment of certain conditions, in which case it should not be amortised but should be tested for impairment.  
AS 26 is based on the assumption that the useful life of an intangible asset is always finite, and includes a rebuttable presumption that the useful life cannot exceed ten years from the date the asset is available for use |   |
| 12. | Guidance on Certain Issues | In Ind AS 38, guidance is available on cessation of capitalisation of expenditure, de-recognition of a part of an intangible asset and useful life of a reacquired right in a business combination.  
There is no such guidance in AS 26 on these aspects. |   |
| 13. | Valuation Model as Accounting Policy | Ind AS 38 permits an entity to choose either the cost model or the revaluation model as its accounting policy  
In AS 26, revaluation model is not permitted. |   |
| 14. | Intangible Assets recognised as an Expense | Ind AS 38 provides more guidance on recognition of intangible items recognised as expense. Ind AS 38 clarifies that in respect of prepaid Further, unlike AS 26 mail order catalogues have been specifically identified as a form of advertising and |   |
| 15. Contractual or Legal Rights may be Shorter than Legal Life | Ind AS 38 acknowledges that the useful life of an intangible asset arising from contractual or legal rights maybe shorter than the legal life. | AS 26 does not include such a provision |
| 16. Amortisation Lower than under SLM | Ind AS 38 does not contain any such provision. | As per AS 26, there will rarely, if ever, be persuasive evidence to support an amortisation method for intangible assets that results in a lower amount of accumulated amortisation than under straight-line method. |
| 17. Subsequent Increase of Residual Value for Changes in Prices or Value | Under Ind AS 38, the residual value is reviewed at least at each financial year-end. If it increases to an amount equal to or greater than the asset’s carrying amount, amortisation charge is zero unless the residual value subsequently decreases to an amount below the asset’s carrying amount. | However, AS 26 specifically requires that the residual value is not subsequently increased for changes in prices or value. |
| 18. Change in Method of Amortization | This is a change in accounting estimate. | The change in the method of amortisation is a change in accounting policy |
| 19. Annual Impairment Testing | There is no such requirement in Ind AS 38. | AS 26 also requires annual impairment testing of an intangible asset not yet available for use. |
| 20. Intangible Assets Retired from Use and Held for Sale: | Ind AS 38 does not include such intangible assets since they would be covered by Ind AS 105. | Intangible assets retired from use and held for sale are covered by AS 26. |
TEST YOUR KNOWLEDGE

Questions

1. X Ltd. is engaged in the business of publishing Journals. They acquired 50% stake in Y Ltd., a company in the same industry. X Ltd. paid purchase consideration of ₹ 10,00,00,000 and fair value of net asset acquired is ₹ 8,50,00,000. The above purchase consideration includes:
   
(a) ₹ 30,00,000 for obtaining the skilled staff of Y Ltd.
   
(b) ₹ 50,00,000 by way of payment towards ‘Non-compete Fee’ so as to restrict Y Ltd. to compete in the same line of business for next 5 years.

How should the above transactions be accounted for by X Ltd?

2. X Ltd. purchased a franchise from a restaurant chain at a cost of ₹ 1,00,00,000 and the franchise has 10 years life. In addition, the franchise agreement mentions that the franchisee would also pay the franchisor royalty as a percentage of sales made. Can the franchise rights be treated as an intangible asset under Ind AS 38?

3. An entity regularly places advertisements in newspapers advertising its products and includes a reply slip that informs individuals replying to the advertisement that the entity may pass on the individual’s details to other sellers of similar products, unless the individual ticks a box in the advertisement.

   Over a period of time the entity has assembled a list of customers’ names and addresses. The list is provided to other entities for a fee. The entity would like to recognise an asset in respect of the expected future economic benefits to be derived from the list. Can the customer list be treated as an intangible asset under Ind AS 38?

4. A software company X Ltd. is developing new software for the telecom industry. It employs 100 engineers trained in that particular discipline who are engaged in the development of the software. X Ltd. feels that it has an excellent HR policy and does not expect any of its employees to leave in the near future. It wants to recognise these set of engineers as a human resources asset in the form of an intangible asset. What would be your advice to X Ltd?

5. X Ltd. has acquired a telecom license from Government to operate mobile telephony in two states of India. Can the cost of acquisition be capitalised as an intangible asset under Ind AS 38?

6. X Ltd. purchased a standardised finance software at a list price of ₹ 30,00,000 and paid ₹ 50,000 towards purchase tax which is non-refundable. In addition to this, the entity was granted a trade discount of 5% on the initial list price. X Ltd. incurred cost of ₹ 7,00,000 towards customisation of the software for its intended use. X Ltd. purchased a 5-year maintenance contract with the vendor company of ₹ 2,00,000. At what cost the intangible asset will be recognised?
7. X Limited in a business combination, purchased the net assets of Y Limited for ₹ 4,00,000 on 31st March, 20X1. The assets and liabilities position of Y Limited just before the acquisition is as follows:

<table>
<thead>
<tr>
<th>Assets</th>
<th>Cost (in ₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, Plant &amp; Equipment</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Intangible asset 1</td>
<td>20,000</td>
</tr>
<tr>
<td>Intangible asset 2</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash &amp; Bank</td>
<td>1,30,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Liabilities</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade payable</td>
<td>50,000</td>
</tr>
</tbody>
</table>

The fair market value of the PPE, intangible asset 1 and intangible asset 2 is available and they are ₹ 1,50,000, ₹ 30,000 and ₹ 70,000 respectively.

How would X Limited account for the net assets acquired from Y Limited?

8. X Ltd. acquired Y Ltd. on 30th April, 20X1. The purchase consideration is ₹ 50,00,000. The fair value of the tangible assets is ₹ 45,00,000. The company estimates the fair value of “in-process research projects” at ₹ 10,00,000. No other Intangible asset is acquired by X Ltd. in the transaction. Further, cost incurred by X Ltd. in relation to that research project is as follows:

(a) ₹ 5,00,000 – as research expenses
(b) ₹ 2,00,000 – to establish technological feasibility
(c) ₹ 7,00,000 – for further development cost after technological feasibility is established.

At what amount the intangible asset should be measured under Ind AS 38?

9. X Ltd. acquired a patent right of manufacturing drug from Y Ltd. In exchange X Ltd. gives its intellectual property right to Y Ltd. Current market value of the patent and intellectual property rights are ₹ 20,00,000 and ₹ 18,00,000 respectively. At what value patent right should be initially recognised in the books of X Ltd. in following two situations?

(a) X Ltd. did not pay any cash to Y Ltd.
(b) X Ltd. pays ₹ 2,00,000 to Y Ltd.

10. X Garments Ltd. spent ₹ 1,00,00,000 towards promotions for a fashion show by way of various on-road shows, contests etc.

After that event, it realised that the brand name of the entity got popular and resultantly, subsequent sales have shown a significant improvement. It is further expected that this hike will have an effect over the next 2-3 years.

How the entity should account for the above cost incurred on promoting such show?
11. An entity is developing a new production process. During 20X1-20X2, expenditure incurred was ₹ 1,000, of which ₹ 900 was incurred before 1st March, 20X2 and ₹ 100 was incurred between 1st March, 20X2 and 31st March, 20X2. The entity is able to demonstrate that at 1st March, 20X2, the production process met the criteria for recognition as an intangible asset. The recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be ₹ 500.

During 20X2-20X3, expenditure incurred is ₹ 2,000. At the end of 20X3, the recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be ₹ 1,900.

12. X Ltd. is engaged in developing computer software. The expenditures incurred by X Ltd. in pursuance of its development of software is given below:

(a) Paid ₹ 2,00,000 towards salaries of the program designers.
(b) Incurred ₹ 5,00,000 towards other cost of completion of program design.
(c) Incurred ₹ 2,00,000 towards cost of coding and establishing technical feasibility.
(d) Paid ₹ 7,00,000 for other direct cost after establishment of technical feasibility.
(e) Incurred ₹ 2,00,000 towards other testing costs.
(f) A focus group of other software developers was invited to a conference for the introduction of this new software. Cost of the conference aggregated to ₹ 70,000.
(g) On 15th March, 20X1, the development phase was completed and a cash flow budget was prepared.

Net profit for the year was estimated to be equal ₹ 40,00,000. How X Ltd. should account for the above mentioned cost?

13. X Ltd. has started developing a new production process in financial year 20X1-20X2. Total expenditure incurred till 30th September, 20X1, was ₹ 1,00,00,000. The expenditure on the development of the production process meets the recognition criteria on 1st July, 20X1. The records of X Ltd. show that, out of total ₹ 1,00,00,000, ₹ 70,00,000 were incurred during July to September, 20X1. X Ltd. publishes its financial results quarterly. How X Ltd. should account for the development expenditure?

14. X Ltd. decides to revalue its intangible assets on 1st April, 20X1. On the date of revaluation, the intangible assets stand at a cost of ₹ 1,00,00,000 and accumulated amortisation is ₹ 40,00,000. The intangible assets are revalued at ₹ 1,50,00,000. How should X Ltd. account for the revalued intangible assets in its books of account?
Answers

1. X Ltd. should recognise an intangible asset in respect of the consideration paid towards ‘Non-Compete Fee’.

However, amount paid for obtaining skilled staff amounting to ₹ 30,00,000 does not meet the definition of intangible asset since X Ltd. has not established any right over the resource and should be expensed. The entity has insufficient control over the expected future economic benefits arising from a team of skilled staff.

Therefore, ₹ 50,00,000 will be separately recognised as an intangible asset, whereas amount paid for obtaining skilled staff does not meet the recognition criteria. However, since it is acquired in a business combination, it forms part of the goodwill recognised at the acquisition date.

The value of goodwill is ₹ 1,00,00,000 (₹ 1,50,00,000 – ₹ 50,00,000).

2. The franchise rights meets the identification criterion in the definition of an intangible asset since it arises from the contractual rights. It is acquired separately and its cost can be measured reliably. In addition, X Ltd. will have future economic benefits and control over them from the franchise rights.

X Ltd. should recognise the franchise right as intangible asset and amortise it over 10 years. Royalty as a percentage of sales paid to the franchisor would be a charge to the profit and loss in the books of the X Ltd.

3. In this situation, the entity has no legal rights to the customer relationship, but exchange transactions have taken place that evidence separability of the asset and the control that the entity is able to exercise over the asset. Therefore, the list is an intangible asset. However, the entity may not recognise the asset because the cost of generating the customer list internally cannot be distinguished from the cost of developing the business as a whole.

4. Although, without doubt the skill sets of the employees make them extremely valuable to the company, however it does not have control over them. Merely having good HR policies would not make them eligible to be recognised as an intangible asset.

5. Cost of acquisition of the telecom license can be capitalised as an intangible asset under the head Licenses, as it will lead to future economic benefits for X Ltd.

6. In accordance with Ind AS 38, the cost of a separately acquired intangible asset is its purchases price and non-refundable purchase taxes, after deducting trade discounts and rebates and any directly attributable cost of preparing the asset for its intended use.

Therefore, the initial cost of the asset should be:

<table>
<thead>
<tr>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>List price</td>
</tr>
</tbody>
</table>
Less: Trade discount (5%) \( (1,50,000) \)
Non-refundable purchase tax \( 28,50,000 \)
Customisation cost \( 7,00,000 \)
Total cost \( 36,00,000 \)

The maintenance contract of `2,00,000 is an expense and therefore should be taken as a prepaid expense and charged to profit and loss over a period of 5 years.

7. X Limited will account for the assets acquired from Y Limited in following manner:

<table>
<thead>
<tr>
<th>Assets</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, plant and equipment</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Goodwill</td>
<td>70,000</td>
</tr>
<tr>
<td>Intangible asset 1</td>
<td>30,000</td>
</tr>
<tr>
<td>Intangible asset 2</td>
<td>70,000</td>
</tr>
<tr>
<td>Cash &amp; Bank</td>
<td>1,30,000</td>
</tr>
</tbody>
</table>

Liabilities

| Trade payable         | 50,000     |

Note 1- Goodwill is the difference between fair value of net assets acquired and purchase consideration paid when is calculated as follow:

Goodwill = `4,00,000 - (1,50,000 + 70,000 + 30,000 + 1,30,000 - 50,000) = `70,000.

8. X Ltd. should initially recognise the acquired “in house research project” at its fair value i.e., ₹10,00,000. Research cost of ₹5,00,000 and cost of ₹2,00,000 for establishing technical feasibility should be charged to profit & loss. Costs incurred from the point of technological feasibility/asset recognition criteria until the time when development costs are incurred are capitalised.

So the intangible asset should be recognised at ₹17,00,000 (₹10,00,000 + ₹7,00,000).

9. If an entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

The transaction at the fair value of the asset received adjusted for any cash received or paid. Therefore, in case (a) patent is measured at ₹18,00,000, in case (b) it is measured at ₹20,00,000 (18,00,000 + 2,00,000).

10. Expenditure of ₹1,00,000 though increased future economic benefits, but it does not result in creation of an intangible asset.

Such promotional cost should be expensed off.
11. At the end of the financial year 20X2, the production process is recognised as an intangible asset at a cost of ₹ 100 (expenditure incurred since the date when the recognition criteria were met, i.e., 1st March, 20X2). ₹ 900 expenditure incurred before 1st March, 20X2 is recognised as an expense because the recognition criteria were not met until 1st March, 20X2. This expenditure does not form part of the cost of the production process recognised in the balance sheet.

At the end of 20X3, the cost of the production process is ₹ 2,100 (₹ 100 expenditure recognised at the end of 20X2 plus ₹ 2,000 expenditure recognised in 20X3). The entity recognises an impairment loss of ₹ 200 to adjust the carrying amount of the process before impairment loss (₹ 2,100) to its recoverable amount (₹ 1,900). This impairment loss will be reversed in a subsequent period if the requirements for the reversal of an impairment loss in Ind AS 36 are met.

12. Costs incurred in creating computer software, should be charged to research & development expenses when incurred until technical feasibility/asset recognition criteria have been established for the product. Here, technical feasibility is established after completion of detailed program design.

In this case, ₹ 9,00,000 (salary cost of ₹ 2,00,000, program design cost of ₹ 5,00,000 and coding and technical feasibility cost of ₹ 2,00,000) would be recorded as expense in Profit and Loss since it belongs to research phase.

Cost incurred from the point of technical feasibility are capitalised as software costs. But the conference cost of ₹ 70,000 would be expensed off.

In this situation, direct cost after establishment of technical feasibility of ₹ 7,00,000 and testing cost of ₹ 2,00,000 will be capitalised.

The cost of software capitalised is = ₹ (7,00,000 + 2,00,000) = ₹ 9,00,000.

13. X Ltd. should recognise the intangible asset at ₹ 70,00,000 and ₹ 30,00,000 which was already recognised as an expenses in first quarter should not be capitalised.

14. The intangible assets are revalued to ₹ 1,50,00,000 on an amortised replacement cost basis, which is a 150% increase from its original cost. Thereby applying the existing ratio of accumulated depreciation to the cost the revalued gross amount would be ₹ 2,50,00,000 gross and ₹ 1,00,00,000 on amortisation.