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IFRS Foundation: Training Material for the *IFRS® for SMEs*

Module 18 – Intangible Assets other than Goodwill

IFRS™

IFRS Foundation: Training Material for the *IFRS® for SMEs*

including the full text of
Section 18 *Intangible Assets other than Goodwill*
of the International Financial Reporting Standard (IFRS)
for Small and Medium-sized Entities (SMEs)
issued by the International Accounting Standards Board on 9 July 2009

with extensive explanations, self-assessment questions and case studies

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This training material has been prepared by IFRS Foundation education staff. It has not been approved by the International Accounting Standards Board (IASB). The training material is designed to assist those training others to implement and consistently apply the *IFRS for SMEs*. For more information about the IFRS education initiative visit http://www.ifrs.org/Use+around+the+world/Education/Education.htm.

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Module 18 – Intangible Assets other than Goodwill

This training material has been prepared by IFRS Foundation education staff and has not been approved by the International Accounting Standards Board (IASB).
The accounting requirements applicable to small and medium-sized entities (SMEs) are set out in the *International Financial Reporting Standard (IFRS) for SMEs*, which was issued by the IASB in July 2009.

INTRODUCTION

This module focuses on the accounting and reporting of intangible assets other than goodwill in accordance with Section 18 *Intangible Assets other than Goodwill* of the *IFRS for SMEs*.
It introduces the learner to the subject, guides the learner through the official text, develops the learner's understanding of the requirements through the use of examples and indicates significant judgements that are required in accounting for intangible assets. Furthermore, the module includes questions designed to test the learner's knowledge of the requirements and case studies to develop the learner's ability to account for intangible assets in accordance with the *IFRS for SMEs*.

Learning objectives

Upon successful completion of this module you should know the financial reporting requirements for intangible assets other than goodwill in accordance with the *IFRS for SMEs*. Furthermore, through the completion of case studies that simulate aspects of the real-world application of that knowledge, you should have enhanced your competence to account for intangible assets in accordance with the *IFRS for SMEs*. In particular you should, in the context of the *IFRS for SMEs*, be able to:

- distinguish intangible assets from other assets of an entity
- determine when an intangible asset qualifies for recognition in financial statements
- measure intangible assets on initial recognition and subsequently
- present and disclose intangible assets in financial statements
- identify when an intangible asset is to be derecognised and account for that derecognition
- demonstrate an understanding of significant estimates and other judgements that are required in accounting for intangible assets.

Module 18 – Intangible Assets other than Goodwill

IFRS for SMEs

The *IFRS for SMEs* is intended to apply to the general purpose financial statements of entities that do not have public accountability (see Section 1, *Small and Medium-sized Entities*).

The *IFRS for SMEs* includes mandatory requirements and other material (non-mandatory) that is published with it.

The material that is not mandatory includes:

- a preface, which provides a general introduction to the *IFRS for SMEs* and explains its purpose, structure and authority.
- implementation guidance, which includes illustrative financial statements and a disclosure checklist.
- the Basis for Conclusions, which summarises the IASB's main considerations in reaching its conclusions in the *IFRS for SMEs*.
- the dissenting opinion of an IASB member who did not agree with the publication of the *IFRS for SMEs*.

In the *IFRS for SMEs* the Glossary is part of the mandatory requirements.

In the *IFRS for SMEs* there are appendices in Section 21 *Provisions and Contingencies*, Section 22 *Liabilities and Equity* and Section 23 *Revenue.* Those appendices are non-mandatory guidance.

Introduction to the requirements

The objective of general purpose financial statements of a small or medium-sized entity is to provide information about the entity's financial position, performance and cash flows that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs. The objective of Section 18 to is prescribe the accounting and reporting requirements for intangible assets that are not addressed elsewhere in the *IFRS for SMEs* (eg Section 19 *Business Combinations and Goodwill* specifies requirements for goodwill that arises in a business combination, and the requirements for intangible assets held by an entity for sale in the ordinary course of business are specified in Sections 13 *Inventories* and 23 *Revenue*).

Section 18 of the *IFRS for SMEs* requires an entity to recognise an intangible asset (ie an identifiable non-monetary asset without physical substance) 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 or value of the asset can be measured reliably.

On initial recognition an entity measures an intangible asset at cost. Section 18 provides mandatory application guidance on the measurement of the cost of an intangible asset for a variety of circumstances. On subsequent recognition, all intangible assets are measured at cost less any accumulated amortisation and accumulated impairment losses.

All costs incurred in research and development activities are recognised as an expense when incurred.

Every intangible asset is considered to have a finite useful life and is amortised over that useful life. Except in specified circumstances, the residual value of an intangible asset is assumed to be nil. Factors may indicate that the residual value or useful life of an intangible asset has changed since the most recent annual reporting date. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, amortisation method or useful life.

At each reporting date, an entity shall assess whether there is any indication that any intangible asset may be impaired. If any such indication exists, that intangible asset is tested for impairment in accordance with Section 27 *Impairment of Assets*.

When an intangible asset is disposed of, the gain or loss on disposal is included in profit or loss.

Module 18 – Intangible Assets other than Goodwill

REQUIREMENTS AND EXAMPLES

The contents of Section 18 *Intangible Assets other than Goodwill* of the *IFRS for SMEs* are set out below and shaded grey. Terms defined in the Glossary of the *IFRS for SMEs* are also part of the requirements. They are in **bold type** the first time they appear in the text of Section 18. The notes and examples inserted by the IFRS Foundation education staff are not shaded. Other annotations inserted by the IFRS Foundation staff are presented within square brackets in ***bold italics***. The insertions made by the staff do not form part of the *IFRS for SMEs* and have not been approved by the IASB.

Scope of this section

18.1 This section applies to accounting for all **intangible assets** other than goodwill (see Section 19 *Business Combinations and Goodwill*) and intangible assets held by an entity for sale in the ordinary course of business (see Section 13 *Inventories* and Section 23 *Revenue*).

18.2 An intangible asset is an identifiable non-monetary asset without physical substance. Such an asset is identifiable when:

(a) it is separable, ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or liability, or

(b) it 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.

Notes

An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.

An intangible asset is an identifiable non-monetary resource without physical substance that is controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity. An asset is identifiable when it is separable or it arises from contractual or other legal rights.

A non-monetary asset is an asset that is not currency held or an asset to be received in a fixed or determinable amount of money. Other assets are non-monetary.

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, 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.

Note that the intangible resources listed in the paragraph directly above might not all satisfy the definition of an intangible asset for financial reporting purposes (ie some of them might not be identifiable, an entity might not have control over the resource and some of them might not result in future economic benefits). In addition, Section 18 prohibits an entity from recognising its internally generated intangible assets, even when the entity's internally generated items meet the definition of an intangible asset (see paragraphs 18.4(c) and 18.14).

Identifiability

The identifiability criterion distinguishes goodwill from other intangible assets. Goodwill is the future economic benefits arising from assets that are not capable of being individually identified and separately recognised. Goodwill arising in a business combination is accounted for according to Section 19 *Business Combinations and Goodwill*. Internally generated goodwill is not recognised.

In some cases, expenditure incurred by an entity to generate future economic benefits does not result in the creation of an intangible asset that meets the recognition criteria in Section 18. Such expenditure is often described as contributing to internally generated goodwill. Internally generated goodwill does not meet the definition of an intangible asset because it is not an identifiable resource (ie it is not separable and nor does it arise from contractual or other legal rights) controlled by the entity and its cost cannot be measured reliably.

Control

An entity controls an asset if it has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. Usually, such control would come from legal rights that are enforceable in a court of law, for example through licences, patents or trademarks. 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, for example through keeping the resource a secret from others.

In the absence of legal rights, exchange transactions (eg the sale of the intangible asset) provide evidence of control.

Future economic benefits

The future economic benefits flowing from an intangible asset may include revenue from the sale of products or services, cost savings or other benefits resulting from the use of the asset by the entity. For example, the use of intellectual property in a production process may reduce future production costs rather than increase future revenues. Intellectual property is an intangible item that arises from human creativity or intellect (ie it consists of human knowledge and ideas) and has commercial value (eg copyright artistic works, patented business methods and patented industrial processes).

Intangible assets do not have physical substance. Assets with physical substance are sometimes referred to as tangible assets. Tangible assets are accounted for in accordance with other sections of the *IFRS for SMEs*. For example, depending on the purpose for which an entity holds land and buildings, they are accounted for in accordance with Section 13 *Inventories*, Section 16 *Investment Property* or Section 17 *Property, Plant and Equipment*.

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 a DVD (containing a film). In determining whether an asset that incorporates both intangible and tangible elements should be accounted for as property, plant and equipment (in accordance with Section 17) or as an intangible asset (in accordance with Section 18), 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. However, when the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

Examples – intangible assets

Ex 1 **An entity owns a brand name that it purchased from a competitor. The brand name is legally protected through registration with the local government of a trademark[(1)].**

The brand name (a trademark) is an intangible asset of the entity. It is an asset of the entity—control is evidenced by the legal right and the entity would have purchased the brand name with the expectation that it would increase future revenues either by selling products or by preventing its competitors from selling products (future economic benefits). The asset (brand name) is an intangible asset—it is non-monetary (ie it is neither currency held nor an asset receivable in a fixed or determinable amount of money), without physical substance (because it is a legal right), identifiable (because it is evidenced by legal protection through registration) and can be sold (ie it is separable).

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its brand name intangible asset.

Ex 2 **An entity holds an exclusive licence to operate a particular fast-food outlet in a specified jurisdiction under a franchise agreement.**

The exclusive right to operate in a particular jurisdiction is an intangible asset. It is an asset because the entity has control through the contractual right and because it expects to generate future economic benefits by operating the fast-food outlet. The asset (licence) is an intangible asset—it is non-monetary (ie it is neither currency held nor an asset receivable in a fixed or determinable amount of money), it does not have physical substance (because it is a right) and is identifiable (because it arises from a contractual right).

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its licence intangible asset.

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(1) Trademarks are words, names, symbols or other devices used in trade to indicate the source of a product and to distinguish it from the products of others.

Ex 3 **An entity owns and operates an interactive Internet site on which anyone can post material related to a particular subject. The entity generates revenue by selling advertising space on the site. The domain name is protected legally through registration with the appropriate parties.**

The Internet site is an intangible asset of the entity. It is an asset of the entity because the entity has control through ownership of the website and expects to generate future economic benefits by selling advertising space on the Internet site. The asset (Internet site) is an intangible asset—it is non-monetary (ie it is neither currency held nor an asset receivable in a fixed or determinable amount of money), does not have physical substance (because it is an electronic website) and it is identifiable (the entity has a contractual-legal right of ownership).

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its Internet site intangible asset.

Ex 4 **An entity owns 20 software licences. The software licences are used by the entity's production and administrative staff.**

The software licences are intangible assets of the entity. They are assets of the entity because the entity has the legal right to use the software under the licences to generate future economic benefits. The assets (software licences) are intangible assets—they are non-monetary (ie they are neither currency held nor assets receivable in a fixed or determinable amount of money), without physical substance (because they are electronic software) and identifiable (because they arise from contractual rights).

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its software licence intangible asset.

Ex 5 **An entity operates 20 taxis under licence in city A. The taxi licences are transferable to other qualified taxi operators.**

The taxi licences are intangible asset of the entity. The licences are assets of the entity because the entity has control through the legal right to operate 20 taxis in the city to generate future economic benefits from taxi fares. The assets (taxi licences) are non-monetary (ie they are neither currency held nor assets receivable in a fixed or determinable amount of money), without physical substance (because they are legal rights), identifiable (because they arise from purchased contractual rights) and can be sold (they are separable).

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its taxi licence intangible asset.

Ex 6 **An entity owns digital audiovisual material—films and audio recordings that it licenses to its customers.**

The digital audiovisual material is an intangible asset. It is an asset because control of the digital audiovisual material is evidenced by the entity's ability to license it to others in return for future economic benefits (ie licence payments). The asset (films and audio recordings) is an intangible asset (ie an identifiable non-monetary asset without physical substance) because the asset:

- is identifiable—as evidenced by the licensing arrangements (ie it is separable);

- is non-monetary—because it is neither currency held nor an asset receivable in a fixed or determinable amount of money; and
- it does not have physical substance—the value of the physical asset on which the digital, audiovisual material is stored (eg CD, DVD, Blu-Ray) is ignored if it is immaterial.

The entity applies the recognition criteria in paragraph 18.4 for determining whether to recognise its digital audiovisual material intangible asset.

Examples – items that do not satisfy the definition of an intangible asset

Ex 7 **Because of its efforts in building customer relationships and loyalty (eg through advertising), an entity expects that its customers will continue to trade with the entity (eg a fast-food outlet). There are no contracts with those customers.**

In the absence of legal rights to protect the entity's relationships with its customers or to control the customers' loyalty to the entity, an entity usually has insufficient control over the expected economic benefits from its customer relationships and loyalty for such items (eg a portfolio of customers, market-share, customer relationships and customer loyalty) to meet the definition of an intangible asset.

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. However, exchange transactions for non-contractual customer relationships are uncommon.

Note: when an entity establishes relationships with its customers through fixed-term contracts, and those contracts contain legally enforceable contractual rights to future revenue (over which the entity has control), the definition of an intangible asset will be met. However, in accordance with Section 18, internally generated intangible assets are not recognised (see paragraphs 18.4(c), 18.14 and 18.15). Accordingly, internally generated customer lists may not be recognised, but separately acquired (purchased) customer lists may qualify for recognition (see paragraphs 18.4, 18.7 and 18.10).

Ex 8 **A bakery manufactures rye bread that is very popular with its customers using a recipe that it found in a famous cookbook that is in the public domain. Although the cookbook's publication is protected by copyright, there is no limitation on the use of the recipe. Many of the bakery's competitors produce rye bread.**

The recipe does not meet the definition of an asset of the bakery because the bakery does not have control over the recipe. The bakery is unable to restrict the access of others to the benefits from using the recipe because the recipe is available to the public.

Ex 9 **An entity has a team of skilled employees and it can identify the incremental staff skills leading to future economic benefits that will flow from training that it has provided to its employees. The entity does not expect that any of its employees will**

leave the entity, and as a result their skills are expected to remain available to the entity for the foreseeable future.

In the absence of evidence to the contrary, the entity is unlikely to have sufficient control over the expected future economic benefits arising from its team of skilled staff and from training provided to its employees in order for these items to meet the definition of an intangible asset of the entity.

Similarly, specific technical talent held by particular employees is unlikely to meet the definition of an intangible asset, unless legal rights protect the entity's right to use that talent and also protect the future economic benefits expected from it (and the technical talent also meets the other requirements to be regarded as meeting the definition of an intangible asset of the entity).

18.3 Intangible assets do not include:

(a) **financial assets**, or

(b) mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources.

Notes

Other intangible assets that are outside the scope of Section 18 because they are within the scope of another section of the *IFRS for SMEs* include intangible assets that are held for sale in the ordinary course of business (which are accounted for in accordance with Section 13 *Inventories*) and goodwill (which is accounted for in accordance with Section 19 *Business Combinations and Goodwill*).

Examples – intangible assets outside the scope of Section 18

Ex 10 **An entity that trades in transferable fishing licences acquires 1,000 licences, each of which entitles the holder to catch one tonne of fish in a specified jurisdiction's waters. The entity does not own a boat and does not intend to catch any fish. It has advertised the licences for sale at a price that is set to achieve a 40 per cent gross profit margin.**

Although each licence satisfies the definition of an intangible asset, the licences are not classified as intangible assets of the entity (see paragraph 18.1). The licences are inventories of the entity because they are assets held for sale in the ordinary course of business (see paragraph 13.1).

Ex 11 **When accounting for the acquisition of the net assets and operations of one of its competitors, an entity recognised future economic benefits arising from assets that are not individually identified as assets (goodwill).**

Because the assets that represent goodwill could not be individually identified they are not recognised as individual intangible assets when accounting for the business combination. Instead, they are collectively recognised as goodwill. Goodwill is accounted for in accordance with Section 19 *Business Combinations and Goodwill* (see paragraph 18.1).

Recognition

Notes

Paragraph 18.4 sets out the general principle for the recognition of intangible assets developed from the concepts set out in paragraph 2.27 of Section 2 *Concepts and Pervasive Principles*. Paragraphs 2.27 and 2.28 set out the overall principles for recognising elements in the financial statements.

Paragraphs 18.5 to 18.8 provide guidance on how to apply the recognition principle in a variety of circumstances. In accordance with these requirements, internally generated intangible assets are not recognised (eg internally generated brands) because it is often difficult to attribute expenditure directly to a particular intangible asset rather than expenditure to develop the business as a whole.

General principle for recognising intangible assets

18.4 An entity shall apply the recognition criteria in paragraph 2.27 in determining whether to recognise an intangible asset. Therefore, the entity shall recognise an intangible asset as an asset 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;

(b) the cost or value of the asset can be measured reliably; and

(c) the asset does not result from expenditure incurred internally on an intangible item.

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

Note

An asset's useful life is the period over which the asset is expected to be available for use by the entity.

18.6 An entity uses judgement to assess the degree of certainty attached to the flow of future economic benefits that are attributable to the use of the asset on the basis of the evidence available at the time of initial recognition, giving greater weight to external evidence.

18.7 The probability recognition criterion in paragraph 18.4(a) is always considered satisfied for intangible assets that are separately acquired.

Examples – general recognition criteria

Ex 12 **An entity developed a formula that it uses to manufacture a unique glue. The glue is the leading adhesive product in the market because of its distinctive mix of chemicals. The special formula is known only by the entity's two owner-managers and hence no competitors have been able to discover and replicate the formula. The formula is not protected by a patent, or by other means. Many competitors have approached the entity to try to purchase the formula.**

The formula meets the definition of an intangible asset of the entity. It is identifiable because it is capable of being separated from the entity and sold (ie it is separable). It is non-monetary because it is neither currency held nor an asset receivable in a fixed or determinable amount of money. It meets the definition of an asset of the entity because, although the formula is not protected by legal rights, the entity has control over the formula by keeping the formula a secret from its competitors.

However, in accordance with Section 18, internally generated intangible assets are not recognised as assets (see paragraphs 18.4(c), 18.14 and 18.15).

Ex 13 **An entity developed a successful brand that allows the entity to charge a premium for its products. The entity continues to spend large amounts on maintaining the brand and on developing the brand further (eg sponsoring local sports events, sponsoring select cultural events and advertising the brand).**

The costs incurred in developing the brand do not satisfy the recognition criteria in paragraph 18.4. The expenditures incurred for sponsorships and advertising are not recognised as an intangible asset. They cannot be distinguished from costs incurred in respect of developing the business as a whole. The costs are recognised as an expense as they are incurred (see paragraphs 18.4(c), 18.14 and 18.15).

Ex 14 **An entity acquires a competitor's brand in a separate acquisition for CU100,000[(2)]. The entity uses the brand to charge a premium for the products that it manufactures.**

The entity recognises the brand acquired from its competitor as an intangible asset. The CU100,000 incurred to acquire the brand satisfies the recognition criteria in paragraph 18.4. (Note: the probability recognition criterion in paragraph 18.4(a) is always considered as being satisfied for intangible assets that are separately acquired—see paragraph 18.7).

Note: amounts incurred by the entity for maintaining and improving the brand will be recognised as an expense as incurred (ie expenditures incurred for sponsorships and advertising cannot be separated from costs incurred in respect of the business as a whole—see paragraphs 18.4(c), 18.14 and 18.15).

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(2) In this example, and in all other examples in this module, monetary amounts are denominated in 'currency units (CU)'.

Acquisition as part of a business combination

18.8 An intangible asset acquired in a **business combination** is normally recognised as an asset because its **fair value** can be measured with sufficient reliability. However, an intangible asset acquired in a business combination is not recognised when it arises from legal or other contractual rights and its fair value cannot be measured reliably because the asset either

(a) is not separable from **goodwill**, or

(b) is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would be dependent on immeasurable variables.

Examples – application of recognition principle – recognise separate asset

Ex 15 **An entity acquired a number of marketing-related assets (trademarks, service marks(3), collective marks(4) and certification marks(5)) in a business combination.**

When it is protected legally (eg through registration with governmental agencies, continuous use in commerce, or other means) a marketing-related asset (trademark, service mark, collective mark and certification mark) is an intangible asset—it is an identifiable (see paragraph 18.2(b)) non-monetary asset without physical substance (ie a legal right).

Contractual-legal intangible assets (trademarks, service marks, collective marks and certification marks) are recognised separately from goodwill in the accounting for the business combination, unless their fair values cannot be measured reliably because either they are not separable from goodwill, or they are separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables (see paragraph 18.8).

Ex 16 **An entity acquired a registered Internet domain name (a unique alphanumeric name that is used to identify a particular numeric Internet address used primarily in the marketing or promotion of products and services) in a business combination. Its registration is renewable.**

Registration of the domain name creates an association between that name and a designated computer on the Internet for the period of the registration. The registered Internet domain name meets the contractual-legal criterion for identification as an intangible asset (see paragraph 18.2(b)). Consequently, it is recognised separately from goodwill in the accounting for the business combination, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables (see paragraph 18.8).

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(3) A service mark identifies and distinguishes the source of a service rather than a product.

(4) Collective marks are used to identify the goods or services of members of a group.

(5) Certification marks are used to certify the geographical origin or other characteristics of a good or service.

Ex 17 **An entity acquired a valuable customer list (a database that includes information about customers, such as their names, contact information, order histories and demographic information) in a business combination. The customer list does not arise from contractual or other legal rights.**

Customer lists are often leased or exchanged. Such customer lists acquired in a business combination normally meet the separability criterion (see paragraph 18.2(a)). Consequently, the customer list acquired in the business combination would be recognised separately from goodwill in accordance with paragraph 18.8.

Ex 18 **An entity acquired a collection of patented artistic-related intangible assets (plays, books, song lyrics, paintings and films) in a business combination.**

When it is protected legally (eg through patent) an artistic-related intangible asset acquired in a business combination is an intangible asset that meets the contractual-legal criterion.

Contractual-legal intangible assets are recognised separately from goodwill in the accounting for the business combination, unless their fair values cannot be measured reliably because either they are not separable from goodwill or they are separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Ex 19 **An entity acquired two databases (a collection of information stored in electronic form) in a business combination. Database A includes original works of authorship and is copyright-protected. Database B contains information created as a consequence of an entity's research (scientific data that is not copyright-protected).**

Database A meets the contractual-legal criterion for identification as an intangible asset—it is protected by copyright. This database is recognised separately from goodwill in the accounting for the business combination, unless its fair value cannot be measured reliably because either it is not separable from goodwill or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Database B does not meet the contractual-legal criterion for identification as an intangible asset—it is not protected by copyright. Even though the future economic benefits from the database do not arise from legal rights, it is identified as a separate intangible asset—it meets the separability criterion in paragraph 18.2(a) because such databases can be, and often are, exchanged, licensed or leased to others in their entirety or in part. Consequently, in accordance with paragraph 18.8, Database B would be accounted for as a separate intangible asset acquired in the business combination.

Ex 20 **An entity acquired computer software in a business combination. Some of the software is patented. However, some of the software is internally developed and is not patented.**

The patented software meets the contractual-legal criterion for identification as an intangible asset (because it is protected by patent). It is recognised separately from goodwill in the accounting for the business combination, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Unpatented software does not meet the contractual-legal criterion for identification as an intangible asset—it is not patent-protected. Even though the future economic benefits from the unpatented software does not arise from legal rights, it is identified as a separate intangible asset—it meets the separability criterion in paragraph 18.2(a) because such software can be, and often is, exchanged, licensed or leased to others in its entirety or in part. In such cases, in accordance with paragraph 18.8, the unpatented software would be accounted for as a separate intangible asset acquired in the business combination.

Ex 21 **An entity acquired two trade secrets (secret recipes) in a business combination. Recipe A is patented. Recipe B is not legally protected.**

Recipe A meets the contractual-legal criterion for identification as an intangible asset (because it is protected by patent). This recipe is recognised separately from goodwill in the accounting for the business combination, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Because it is not patented protected, Recipe B does not meet the contractual-legal criterion for identification as an intangible asset. Even though the future economic benefits from the unpatented recipe do not arise from legal rights, it is identified as a separate intangible asset because it meets the separability criterion in paragraph 18.2(a)—such software can be, and often is, exchanged, licensed or leased to others in its entirety or in part. In such cases, in accordance with paragraph 18.8, the unpatented recipe would be accounted for as a separate intangible asset acquired in the business combination.

Ex 22 **An entity acquired an order (or production) backlog in a business combination.**

An order (or production) backlog acquired in a business combination meets the contractual-legal criterion (it arises from contracts such as orders from customers) for identification as an intangible asset. This is the case even if the purchase or sales orders are cancellable. It is separately recognised in the accounting for the business combination, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Ex 23 **An entity acquired customer contracts and the related customer relationships in a business combination.**

Because the relationships with the customers are established through contracts, those customer relationships arise from contractual rights. Consequently, customer contracts and the related customer relationships acquired in the business combination meet the contractual-legal criterion for identification as intangible assets. This will be the case even if confidentiality or other contractual terms prohibit the sale or transfer of a contract separately from the acquired entity or business.

Customer relationships also meet the contractual-legal criterion for identification as intangible assets when an entity has a practice of establishing contracts with its customers, regardless of whether a contract exists at the acquisition date.

The customer contracts and the related customer relationships are recognised separately from goodwill in the accounting for the business combination unless the fair value cannot be measured reliably because either they are not separable from goodwill, or they are separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.

Ex 24 **An entity acquired several non-contractual customer relationships in a business combination.**

If a customer relationship acquired in a business combination does not arise from a contract, the relationship is an intangible asset if it meets the separability criterion. Exchange transactions for the same asset, or for a similar asset, provide evidence of separability of a non-contractual customer relationship and may also provide information about exchange prices to consider when measuring fair value.

The non-contractual customer relationships are recognised separately from goodwill in the accounting for the business combination, provided that they are separable.

Ex 25 **Acquirer Company (AC) acquires Target Company (TC) in a business combination on 31 December 20X5. TC manufactures goods in two distinct lines of business: sporting goods and electronics. Customer A purchases both sporting goods and electronics from TC. TC has a contract with Customer A to be its exclusive provider of sporting goods but has no contract for the supply of electronics to Customer A. Both TC and AC believe that only one overall customer relationship exists between TC and Customer A.**

The contract to be Customer A's exclusive supplier of sporting goods, whether cancellable or not, meets the contractual-legal criterion for identification as an intangible asset, and is therefore recognised separately from goodwill, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables. Additionally, because TC establishes its relationship with Customer A through a contract, the customer relationship with Customer A meets the contractual-legal criterion for identification as an intangible asset. Consequently, the customer relationship intangible asset is also recognised separately from goodwill, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables. Because TC has only one customer relationship with Customer A, the fair value of that relationship incorporates assumptions about TC's relationship with Customer A related to both sporting goods and electronics. However, if AC determines that the customer relationships with Customer A for sporting goods and for electronics are separate from each other, AC would assess whether the customer relationship for electronics meets the separability criterion for identification as an intangible asset.

Ex 26 **AC acquires TC in a business combination on 31 December 20X5. TC does business with its customers solely through purchase and sales orders. At 31 December 20X5 TC has a backlog of customer purchase orders from 60 per cent of its customers, all of whom are recurring customers. The other 40 per cent of TC's customers are also recurring customers. However, as of 31 December 20X5 TC has no open purchase orders or other contracts with those customers.**

Regardless of whether they are cancellable or not, the purchase orders from 60 per cent of TC's customers meet the contractual-legal criterion for identification as intangible assets, and are therefore recognised separately from goodwill, unless its fair value cannot be measured reliably because either it is not separable from goodwill, or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables. Additionally, because TC has established its relationship with 60 per cent of its customers through contracts, not only the purchase orders but also TC's customer relationships meet the contractual-legal criterion for identification as an intangible asset. Consequently, the customer relationship intangible asset is also recognised separately from goodwill unless its fair value cannot be measured reliably because either it is not separable from goodwill or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would be dependent on immeasurable variables

Because TC has a practice of establishing contracts with the remaining 40 per cent of its customers, its relationship with those customers also arises through contractual rights and therefore meets the contractual-legal criterion for identification as an intangible asset. Even though TC does not have contracts with those customers at 31 December 20X5, it recognises this customer relationship separately from goodwill, unless its fair value cannot be measured reliably because either it is not separable from goodwill or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would be dependent on immeasurable variables.

Example – application of recognition principle – cannot recognise separately

Ex 27 **A group acquired water acquisition rights as part of a business combination. The rights are extremely valuable to many manufacturers operating in the same jurisdiction becuase manufacturers cannot acquire water and, in many cases, cannot operate their plants without them. Local authorities grant the rights at little or no cost, but in limited numbers, for fixed periods (normally 10 years), and renewal is certain at little or no cost. The rights cannot be sold other than as part of the sale of a business as a whole, so there exists no secondary market in the rights. If a manufacturer hands the rights back to the local authority, it is prohibited from reapplying.**

In this case because the legal rights cannot be measured separately from the business as a whole (and therefore from goodwill) the businesses would cease to exist without the rights. Therefore, the legal rights would not be accounted for as a separate intangible asset acquired in the business combination because the fair value cannot be measured reliably because the legal rights cannot be separated from goodwill.

Initial measurement

18.9 An entity shall measure an intangible asset initially at cost.

Note

Paragraphs 18.10–18.16 provide application guidance for the determination of the cost of an intangible asset in a variety of circumstances.

Separate acquisition

18.10 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.

Notes

Examples of directly attributable costs of preparing the asset for its intended use are:

- costs of employee benefits (as defined in Section 28 *Employee Benefits*) arising directly from bringing the asset to its working condition;
- professional fees arising directly from bringing the asset to its working condition; and
- costs of testing whether the asset is functioning properly.

Examples of expenditures that are not part of the cost of an intangible asset are:

- costs of introducing a new product or service (including costs of advertising and promotional activities);
- costs of conducting business in a new location or with a new class of customer (including costs of staff training); and
- administration and other general overhead costs.

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. Consequently, costs incurred in using or redeploying an intangible asset are not included in the carrying amount of that asset.

Example – measurement of intangible assets acquired separately

Ex 28 On 1 January 20X1 an entity purchased a new software package to operate its production equipment for CU600,000, including CU50,000 refundable purchase taxes. The purchase price was funded by incurring a loan of CU605,000 (including CU5,000 loan origination fees). The loan is secured against the software licences.

In January 20X1 the entity incurred the following costs in customising the software so that it is more suited to the systems used by the entity:

• Labour – CU120,000

• Depreciation of plant and equipment used to perform the modifications – CU15,000.

In January 20X1 the entity's production staff were trained in how to operate the new software. Training costs included:

• Cost of an expert external instructor – CU7,000

• Labour – CU3,000.

In February 20X1 the entity's production team tested the software and the information technology team made further modifications necessary to get the new software to function as intended by management. The following costs were incurred in the testing phase:

• Material, net of CU3,000 recovered from the sale of the scrapped output – CU21,000

• Labour – CU11,000

• Depreciation of plant and equipment while it was used to perform the modifications – CU5,000.

The new software was ready for use on 1 March 20X1. However, because of low initial order levels, the entity incurred a loss of CU23,000 on operating the software during March.

What is the cost of the software at initial recognition?

Description	*Calculation or reason*	*CU*	*Reference to* IFRS for SMEs
Purchase price	CU600,000 purchase price less CU50,000 refundable purchase taxes	550,000	18.10(a)
Loan raising fee	Included in the measurement of the liability	–	11.18
Preparation costs	CU120,000 labour + CU15,000 depreciation	135,000	18.10(b)
Training costs	Recognised as expenses in profit or loss. The software is capable of operating in the manner intended by management without incurring the training costs.	–	5.4 & 18.15(c)
Cost of testing	CU21,000 material (ie net of the CU3,000 recovered from the sale of the scrapped output) + CU11,000 labour + CU5,000 depreciation	37,000	18.10(b)
Operating loss	Recognised as expenses in profit or loss	–	5.4 & 18.15(b)
Borrowing costs	Recognised as expenses in profit or loss	–	25.2
Cost of software		**722,000**	

Acquisition as part of a business combination

18.11 If an intangible asset is acquired in a business combination, the cost of that intangible asset is its fair value at the acquisition date.

Notes

A quoted price for an identical asset in an active market provides the most reliable estimate of the fair value of an intangible asset. The appropriate market price is usually the current bid price. If current bid prices are unavailable, the price of the most recent similar transaction may provide a basis from which to measure fair value, provided that there has not been a significant change in economic circumstances between the transaction date and the date at which the asset's fair value is measured.

It is uncommon for an active market to exist for an intangible asset, although this may happen. For example, in some jurisdictions, an active market may exist for freely transferable taxi licences, fishing licences or production quotas. However, an active market cannot exist for brands, newspaper mastheads, music and film publishing rights, patents or trademarks, because each such asset is unique.

If no active market exists for an intangible asset, its fair value is the amount that the entity would have paid for the asset, at the acquisition date, in an arm's length transaction between knowledgeable and willing parties, on the basis of the best information available. In estimating this amount, an entity considers the outcome of recent transactions for similar assets.

In addition, although intangible assets are occasionally bought and sold, contracts are normally negotiated between individual buyers and sellers, and so such transactions are relatively infrequent. As a result, it is difficult to find transactions in identical and similar intangible assets. Also, many intangible assets are unique, so the price paid for one asset may not provide sufficient evidence of the fair value of another, even if the assets have some similarities (eg similar intended uses, similar cash flows etc). Moreover, prices are often not available to the public since many transactions are carried out privately.

In addition, making adjustments to observable prices so that they can be used to assess the value of the subject asset can be highly subjective.

Accordingly, it is expected that in the majority of cases, the fair value of an intangible asset will need to be measured using valuation techniques. Valuation techniques may be used to measure the fair value of an intangible asset acquired in a business combination if the valuation technique reflects current transactions and practices in the industry to which the asset belongs and current market conditions. These techniques include, for example:

(a) discounting estimated future net cash flows from the asset; or

(b) estimating the costs that the entity avoids by owning intangible assets and not needing (i) to license it from another party in an arm's length transaction (as ‘relief from royalty’ approach, using discounted net cash flows); or

(ii) to recreate or replace it (as in the cost approach).

When measuring fair value is complex, entities may need to use external valuation specialists.

Example – measurement of intangible assets acquired in a business combination

Ex 29 **On 1 January 20X1 an entity (the acquirer) acquired all of the issued shares of a competitor (the acquiree) when the acquiree’s intangible assets were:**

	Carrying amounts	*Fair values*
	CU	*CU*
Customer list	–	50,000
In-process research and development project	–	80,000
Licence to operate	100,000	150,000
Brand, including trademark and brand name	–	300,000

In 20X1 the acquirer incurred CU200,000 in additional expenditure to complete the acquired in-process research and development project and subsequently decides to develop the related product commercially.

On 1 January 20X1 the consolidated entity—the acquirer and the acquiree viewed as a single entity—will include intangible assets as follows:

	CU
Customer list	50,000
In-process research and development project	80,000
Licence to operate	150,000
Brand, including trademark and brand name	300,000
Cost of intangibles assets	580,000

Although the acquired in-process research and development is recognised as an intangible asset because it was acquired in a business combination, the subsequent expenditure of CU200,000 is treated in the same way as expenditure to create an internally generated intangible asset (ie it is recognised as an expense when incurred—see paragraph 18.14).

Acquisition by way of a government grant

18.12 If an intangible asset is acquired by way of a **government grant**, the cost of that intangible asset is its fair value at the date the grant is received or receivable in accordance with Section 24 *Government Grants*.

Example – measurement of intangible assets acquired by way of a government grant

Ex 30 **On 1 January 20X1 a local government issued three identical licences to broadcast in a particular city for a ten-year period. Two licences were sold by public auction to independent third parties from outside the local community. In an attempt to develop local ownership, the third licence was given to a local entity free of charge. The fair value of each broadcasting licence is CU100,000. The grant does not impose specified future performance conditions.**

In accordance with Section 24 *Government Grants*, the local entity that received the third broadcasting licence shall measure the licence (the intangible asset acquired by way of government grant) at CU100,000 (its fair value) on initial recognition and recognise the grant of CU100,000 in income (see paragraphs 24.4(a) and 24.5).

Exchanges of assets

18.13 An intangible asset may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. An entity shall measure the cost of such an intangible asset at fair value 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. In that case, the asset's cost is measured at the **carrying amount** of the asset given up.

Examples – measurement of intangible assets acquired in an exchange of assets

Ex 31 **On 1 January 20X1 an entity received landing rights at a local airport in exchange for 100 ounces of gold, when gold was trading at CU1,000 per ounce.**

The landing rights received (the intangible asset acquired in the exchange transaction) must be measured at CU100,000 (their fair value) on initial recognition. Because there is an active market for gold, the fair value of the landing rights received is most easily determined by reference to the fair value of the gold given up in the exchange transaction (ie 100 ounces × CU1,000 per ounce).

Ex 32 **On 1 January 20X1 an entity received landing rights at a local airport in exchange for 90,000 litres of aviation fuel and CU10,000 cash. Aviation fuel costs CU1 per litre.**

The landing rights received (the intangible asset acquired in the exchange transaction) must be measured at CU100,000 (their fair value) on initial recognition. The fair value of the landing rights is determined by reference to the fair values of the aviation fuel CU90,000 (ie 90,000 litres × CU1 per litre) plus CU10,000 cash given up in the exchange transaction.

Ex 33 **Entities A and B manufacture chemicals in jurisdictions A and B, respectively. On 1 January 20X1 entities A and B extended their respective product ranges by granting each other the right to manufacture each other's patented products in**

their respective home jurisdictions. Assume that the fair value of neither the asset received nor the asset given up can be measured reliably. The carrying amount of the patented rights given up by entities A and B in the exchange transaction was CU100 and CU200 respectively.

The trademark received (the intangible asset acquired in the exchange transaction) must be measured on initial recognition at CU100 and CU200 by entities A and B, respectively (ie it is measured at the carrying amount of the asset given up in the exchange transaction).

Internally generated intangible assets

18.14 An entity shall recognise expenditure incurred internally on an intangible item, including all expenditure for both **research** and **development** activities, as an expense when it is incurred unless it forms part of the cost of another asset that meets the recognition criteria in this IFRS.

Notes

The research phase includes the original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding. Examples of research activities are:

- activities aimed at obtaining new knowledge;
- the search for, evaluation and final selection of applications of research findings or other knowledge;
- the search for alternatives for materials, devices, products, processes, systems or services; and
- the formulation, design, evaluation and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.

The development phase includes 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:

- the design, construction and testing of pre-production or pre-use prototypes and models;
- the design of tools, jigs, moulds and dies involving new technology;
- the design, construction and operation of a pilot plant that is not of a scale that would be economically viable for commercial production; and
- the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

Expenditures on both research and development activities are recognised as an expense when incurred, unless they form part of the cost of another asset that meets the recognition criteria in another section of the *IFRS for SMEs*.

18.15 As examples of applying the preceding paragraph, an entity shall recognise expenditure on the following items as an expense and shall not recognise such expenditure as intangible assets:

(a) internally generated brands, logos, publishing titles, customer lists and items similar in substance.

(b) start-up activities (ie start-up costs), which include establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (ie pre-opening costs) and expenditure for starting new operations or launching new products or processes (ie pre-operating costs).

(c) training activities.

(d) advertising and promotional activities.

(e) relocating or reorganising part or all of an entity.

(f) internally generated goodwill.

Examples – expenditures recognised as an expense or as an intangible asset

Ex 34 **In 20X1 a candle manufacturer incurred the following expenses on raw materials and labour to invent a new wax that enables candles to burn for substantially longer:**

- **CU1,000 on experimenting with chemicals to discover enhanced wax compounds**
- **CU3,000 to evaluate the suitability of the different wax compounds invented**
- **CU1,500 to patent registration costs for the most effective wax compound discovered**
- **CU2,300 to develop and test the pre-production prototypes**
- **CU5,000 on an initial commercial production run (half of the output was sold by the end of the reporting period—31 December 20X1)**
- **CU 2,000 on advertising the new product.**

The following amounts will be recognised as expenses in the determination of the entity's profit or loss for the year ended 31 December 20X1:

- CU6,300 for research and development costs (ie CU1,000 experimentation costs + CU3,000 evaluation costs + CU2,300 development and testing costs)
- CU2,500 for cost of goods sold (ie CU5,000 ÷ 2 half of the goods produced were sold during the reporting period)
- CU2,000 for selling expenses (ie advertising costs).

Furthermore:

- An intangible asset must be recognised at a cost of CU1,500 for the acquired patent. The patent qualifies for recognition even though it was purchased as part of the creation of internally generated intangible assets. This is because paragraph 18.4(a) is always considered satisfied for intangible assets that are separately acquired. The patent would be amortised in accordance with paragraphs 18.18–18.24. If there is any indication that the patent is impaired at the reporting date, it must be tested for impairment in accordance with Section 27 *Impairment of Assets*.

- at 31 December 20X1 inventory (asset) includes CU2,500 cost of production (ie CU5,000 ÷ 2 because half of the goods produced were on hand at the end of the reporting period). The CU2,500 includes material and labour costs only. Consequently, the cost of the inventory is increased to include a systematic allocation of fixed and variable production overheads (see Section 13 *Inventories*).

Ex 35 **An entity has established a substantial list of customers over time. The list is considered to be very valuable to the entity.**

On 1 January 20X1 the entity acquired a customer list from another entity for CU100,000. Management could sell the externally acquired customer list to third parties. In 20X1 the entity estimates that it incurred a further CU10,000 staff costs in maintaining and developing this externally acquired customer list.

The entity may not recognise an intangible asset for the internally generated customer list, because Section 18 specifically prohibits an entity from recognising internally generated intangible assets (see paragraph 18.15(a)). The costs of establishing the list cannot be distinguished from the cost of developing the business as a whole.

The externally acquired customer list must be measured at CU100,000 on initial recognition because it meets the recognition criteria in paragraph 18.4. Note that the list meets the definition of an intangible asset because it is separable (it can be sold to a third party).

However, the additional CU10,000 incurred in maintaining and developing the externally acquired customer list must be recognised as an expense in the determination of profit or loss for the year. Subsequent expenditure on customer lists (whether externally acquired or internally generated) is always recognised in profit or loss as incurred (see paragraph 18.14). This is because such expenditure cannot be distinguished from expenditure to develop the business as a whole and hence does not satisfy the recognition criteria in paragraph 18.4.

Ex 36 **On 20 February 20X1 an entity held an event to officially open its new retail outlet. The event cost CU20,000 and generated much favourable publicity. In February 20X1, before the new retail outlet was opened, the entity hired and trained new sales staff at a cost of CU30,000.**

The cost of the pre-opening staff training and the opening function must be recognised as expenses in the determination of profit of the period in which the expenses were incurred (see paragraph 18.15(b) and (c)).

Ex 37 **On 31 December 20X1 an entity placed an advertisement for its products in a local newspaper. The newspaper advertisement cost the entity CU20,000 which the entity paid on 1 December 20X1. Although the advertisement will only appear in the 31 December 20X1 newspaper, the entity expects that the advertisement will continue to generate additional sales of its products in January 20X2.**

The entity has a 31 December year-end.

The cost of the newspaper advertisement (CU20,000) must be recognised as an expense in the determination of profit for the period ended 31 December 20X1 (ie when the advertisement was published (see paragraph 18.15(d)). It cannot be deferred and recognised as an expense over the period of additional sales.

Ex 38 **In June 20X1 an entity employed external consultants at a cost of CU20,000 to reorganise its internal operating policies and procedures. The reorganisation will take three months and is expected to reduce operating costs significantly for the foreseeable future.**

The costs of reorganisation must be recognised as an expense in the determination of profit or loss in the period in which the external consultants provide their services (ie in the year ended 20X1), rather than during the period in which the entity expects to benefit from reduced operating costs. The expenditure does not qualify to be recognised as an intangible asset (see paragraph 18.15(e)).

18.16 Paragraph 18.15 does not preclude recognising a prepayment as an asset when payment for goods or services has been made in advance of the delivery of the goods or the rendering of the services.

Example – prepayments

Ex 39 **On 31 December 20X1 an entity paid CU10,000 for a full page advertisement featuring the entity's products in a local newspaper. The advertisement will appear in the 20 January 20X2 edition of the local newspaper. The entity has a 31 December financial year-end.**

As at 31 December 20X1 the entity must present the CU10,000 advertising costs paid to the local newspaper in advance as an asset (prepaid expense). The prepayment asset will be recognised as an expense on 20 January 20X2 when the advertisement is featured in the local newspaper (ie the service is received).

The advertising expenditure does not qualify to be recognised as an intangible asset at any time (see paragraph 18.15(d)).

Past expenses not to be recognised as an asset

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

Measurement after recognition

18.18 An entity shall measure intangible assets at cost less any accumulated **amortisation** and any accumulated **impairment losses**. The requirements for amortisation are set out in this section. The requirements for recognition of impairment are set out in Section 27 *Impairment of Assets*.

Example – measurement after initial recognition

Ex 40 On 1 January 20X1 an entity acquired a franchise licence for CU500,000. Management measured the amortisation of the licence at CU100,000 per year.

At 31 December 20X3 in response to the entry into the market of a competing franchisor the entity assessed the recoverable amount of the franchise licence at CU180,000.

Description	*Calculation or reason*	*CU*	*Reference to IFRS for SMEs*
Cost	Purchase price at 1 January 20X1	500,000	18.10(a)
Amortisation in 20X1	CU500,000 depreciable amount ÷ 5 years	(100,000)	18.22 and 18.23
Carrying amount at 31 December 20X1	CU500,000 cost less CU100,000 accumulated amortisation	**400,000**	18.18
Amortisation in 20X2		(100,000)	18.22 and 18.23
Carrying amount at 31 December 20X2	CU500,000 cost less CU200,000 accumulated amortisation	**300,000**	18.18
Amortisation in 20X3		(100,000)	18.22 and 18.23
Carrying amount at 31 December 20X3 before impairment	CU500,000 cost less CU300,000 accumulated amortisation	**200,000**	18.18
Impairment	CU200,000 carrying amount before impairment less CU180,000 recoverable amount	(20,000)	18.25
Carrying amount at 31 December 20X3 after impairment	Impaired to recoverable amount	**180,000**	18.18

Amortisation over useful life

18.19 For the purpose of this IFRS, all intangible assets shall be considered to have a finite useful life. 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.

Notes

The useful life of an asset is:

- the period over which an asset is expected to be available for use by an entity;

or

- the number of production or similar units expected to be obtained from the asset by an entity.

An intangible asset's useful life is not necessarily the same as its economic life. An asset's economic life is the period during which the asset produces economic benefits, no matter who uses those benefits at the time. The useful life is the period when the asset is used by the entity. If the entity has an intangible asset that has an economic life of ten years, but the entity intends to sell the asset after six years, the useful life will be six years and not ten years. It would be necessary to estimate the residual value at the end of six years.

Many factors are considered in determining the useful life of an intangible asset, including:

- the expected usage of the asset by the entity;
- typical product life cycles for the asset and public information about estimates of useful lives of similar assets that are used in a similar way;
- technical, technological, commercial or other types of obsolescence;
- the stability of the industry in which the asset operates and changes in the market demand for the products or services output from the asset;
- expected actions by competitors or potential competitors;
- the level of maintenance expenditure required to obtain the expected future economic benefits from the asset and the entity's ability and intention to achieve such a level;
- the period of control over the asset and legal or similar limits on the use of the asset, such as the expiry dates of related leases; and
- whether the useful life of the asset is dependent on the useful life of other assets of the entity.

The useful life of an intangible asset does not reflect planned future expenditure in excess of that required to maintain the intangible asset at its standard of performance assessed at the time of estimating the asset's useful life. The useful life reflects the level of future maintenance expenditure required to maintain the asset at its standard of performance assessed, provided that the entity has the ability and intention to carry out such maintenance.

Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Consequently, it is likely that their useful life is short.

If there is an indication that the useful life of an intangible asset has changed since the most recent reporting date then, in accordance with paragraph 18.24, the entity reviews its estimates of the assets useful life and accounts for any change therein as a change in accounting estimate prospectively in accordance with paragraph 10.16.

18.20 If an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall be presumed to be ten years.

Examples – determination of the useful life of an intangible asset

Ex 41 **An entity acquires a computer program under licence for five years—the shortest licence period offered by the licensor. The entity expects to use the software for only the first three years of the licence period, while it develops its own bespoke (custom-made) software.**

The best estimate of the useful life of the software held under licence is 3 years. The fact that the entity has the right to use the software for five years does not extend its useful life beyond the period over which the entity expects to use the asset.

Ex 42 **An entity in the business of direct-mail marketing 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 entity intends to add customer names and other information to the list in the future as it expands the business.**

Management must determine their best estimate of the useful life of the customer list, which may be, for example, 18 months. Although the entity 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.

Ex 43 **An entity acquired an airline route authority between two cities. The route authority 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 about renewals. 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 (eg 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.**

Because the facts and circumstances support the acquiring entity's ability to continue providing air service indefinitely between the two cities, the entity may be unable to make a reliable estimate of the useful life of the intangible asset. Consequently, the useful life is presumed to be 10 years (see paragraph 18.20).

Ex 44 **An entity acquired a broadcasting licence that expires in five years. Thereafter the broadcasting licence is renewable every ten years, on condition that 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. Consequently, the licence is expected to contribute to the entity's net cash inflows indefinitely.**

Because the facts and circumstances support the acquiring entity's ability to continue renewing the broadcasting licence so as to contribute to the entity's net cash inflows indefinitely, the entity may be unable to make a reliable estimate of the useful life of the intangible asset. Consequently, the useful life is presumed to be 10 years (see paragraph 18.20).

Ex 45 **The facts are the same as in example 44. However, the licensing authority subsequently decides that it will no longer renew broadcasting licences, but instead will auction the licences. At the time that 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 presumed to be 10 years. The useful life of the acquired licence would be re-estimated and the entity would conclude that it is the remaining three years until expiration.

Note: the change in the legal environment is an impairment indicator and hence the licence must be tested for impairment in accordance with Section 27 *Impairment of Assets*.

Amortisation period and amortisation method

18.21 An entity shall allocate the **depreciable amount** of an intangible asset on a systematic basis over its useful life. The amortisation charge for each period shall be recognised as an expense, unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

18.22 Amortisation begins when the intangible asset is available for use, ie when it is in the location and condition necessary for it to be usable in the manner intended by management. Amortisation ceases when the asset is derecognised. The entity shall choose an amortisation method that reflects the pattern in which it expects to consume the asset's future economic benefits. If the entity cannot determine that pattern reliably, it shall use the straight-line method.

Notes – amortisation of an intangible asset

Depreciable amount

The depreciable amount of an intangible asset with a finite useful life is its cost, or other amount substituted for cost (in the financial statements), less its residual value. The depreciable amount is usually cost less residual value. Another amount may be substituted for cost when an entity used fair value or a previous GAAP revaluation as a deemed cost for an intangible asset on first-time adoption of the *IFRS for SMEs* (see paragraphs 35.10(c) and 35.10(d) of Section 35 *Transition to the IFRS for SMEs*).

Residual value

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. However, the useful life of an intangible asset is zero unless particular criteria are satisfied (see paragraph 18.23).

Amortisation period

Amortisation begins when the asset is available for use, which is not necessarily the date at which the intangible asset is brought into use. Amortisation of an intangible asset does not cease when the intangible asset is no longer used, unless the asset has been fully amortised or has been derecognised.

Amortisation method

The entity must choose an amortisation method that reflects the pattern in which it expects to consume the asset's future economic benefits. If the entity cannot determine that pattern reliably, it must use the straight-line method.

What does the IASB mean by 'the pattern in which it expects to consume the asset's future economic benefits'? Every asset on an entity's statement of financial position represents a bundle of future economic benefits. Those benefits may be direct, as in the case of cash flows from a financial instrument, or indirect, as in the case of benefits derived from an item of office furniture. With intangible assets the objective of the amortisation method is to approximate the pattern in which the bundle of economic benefits diminishes over time. There are several methods that can be used to allocate amortisation over the asset's estimated useful life. The three most common methods are:

- The straight-line method: the asset's depreciable amount is allocated evenly over its useful life. Hence, straight-line amortisation results in a constant amortisation charge over the useful life of the asset. The straight-line basis is the default method. It is also the most appropriate method where the future economic benefits are consumed over time (eg it is often appropriate for licences and franchises).
- The reducing balance (diminishing balance) method: the annual amortisation charge is a fixed percentage of the opening carrying amount. This results in more amortisation in earlier years than under the straight-line basis. It would be appropriate if future benefits from the intangible asset are expected to be greater in the earlier years of the asset's expected useful life (eg this may be the case for an acquired customer relationship intangible asset).
- The unit of production method: the asset's depreciable amount is allocated over its useful life based on the asset's usage, activity or units produced instead of the passage of time.

Recognition of amortisation

Amortisation is usually recognised in profit or loss. However, sometimes the future economic benefits embodied in an asset are consumed in producing other assets. In this case, the amortisation charge constitutes part of the cost of the other asset and is included in that other asset's carrying amount. For example, the amortisation of intangible assets used in a production process is included in the carrying amount of inventories (see Section 13 *Inventories*).

Examples – amortisation of an intangible asset

Ex 46 **The facts are the same as in example 42—an entity in the business of direct-mail marketing 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 entity intends to add customer names and other information to the list in the future as it expands the business.**

If diminishing returns are expected from using the customer list over management's best estimate of its useful life (ie 18 months), the reducing balance method of amortisation would be used.

If the entity cannot reliably determine the pattern in which it expects to consume the customer list's future economic benefits then it would amortise the customer list using the straight-line method over 18 months (ie management's best estimate of its useful life).

The amortisation charge (expense) is recognised in profit or loss.

The entity must assess at each reporting date whether there is any indication that the customer list is impaired. If any such indication exists, the entity shall review the customer list for impairment in accordance with Section 27 *Impairment of Assets* (see paragraph 18.18).

Ex 47 **The facts are the same as in example 45.**

The acquired licence would be amortised over its remaining three-year useful life. The entity must assess at each reporting date whether there is any indication that the acquired licence is impaired. If any such indication exists, the entity shall review the acquired licence for impairment in accordance with Section 27 *Impairment of Assets* (see paragraph 18.18).

The straight-line basis is used for amortisation unless another amortisation method better reflects the pattern in which the entity expects to consume the asset's future economic benefits, and if the entity can determine the pattern of benefits reliably.

Ex 48 **An entity develops a formula for manufacturing a type of cleaning product. The entity purchases a patent to protect the formula. The patented formula is used to produce the cleaning products. The patented formula is expected to have a three-year useful life because the entity expects that it will take three years to develop a superior formula.**

The patented formula will be amortised over its three-year useful life. As the cleaning products are produced using the patented formula, the amortisation of the patent will be included in the cost of the cleaning products (see Section 13 *Inventories*).

If any impairment indicators exist the entity shall review the patented formula for impairment in accordance with Section 27 *Impairment of Assets* (see paragraph 18.18).

The straight-line basis is used for amortisation unless another amortisation method better reflects the pattern in which the entity expects to consume the asset's future economic benefits, and if the entity can determine the pattern of benefits reliably.

Ex 49 **On 1 February 20X1 an entity purchases a patented formula. The patented formula is available for use on this date. However the entity only starts producing inventory using the patented formula on 1 April 20X1 because the entity did not have the appropriate plant and equipment in place to begin production.**

The entity should begin amortisation of the patent from 1 February 20X1.

Note: if the entity has the ability to determine the pattern in which it expects to consume the future economic benefits from the patented formula, and the entity believes that the unit of production method of amortisation better reflects the pattern in which it expects to consume the asset's future economic benefits, then it may be that the amortisation charge allocated to the period from 1 February 20X1 to 1 April 20X1 would be zero.

Residual value

18.23 An entity shall assume that the **residual value** of an intangible asset is 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 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.

Notes

Residual value is the estimated amount that an entity would currently obtain from disposal of an 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. That definition can be restated as a simple question. If the asset was at the end of its useful life today, and was in the condition expected at the end of useful life, what would the company receive today from selling the asset (net of disposal costs)?

An active market is a market in which all the following conditions exist:

- the items traded in the market are homogeneous;
- willing buyers and sellers can normally be found at any time; and
- prices are available to the public.

It is uncommon for an active market with the characteristics described above to exist for an intangible asset, although this may happen. For example, in some jurisdictions, an active market may exist for freely transferable taxi licences, fishing licences or production quotas. However, an active market cannot exist for brands, newspaper mastheads, music and film publishing rights, patents or trademarks, because each such asset is unique. Furthermore, although intangible assets are bought and sold, contracts are negotiated between individual buyers and sellers, and prices are often not available to the public because the negotiations are done privately.

A residual value other than zero implies that an entity expects to dispose of the intangible asset before the end of its economic life.

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. However if the residual value subsequently decreases to an amount below the asset's carrying amount, amortisation should once more be applied.

Examples – residual value

Ex 50 **An entity acquired a 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 patent would be amortised over its 15-year useful life to a nil residual value. If there is any indication that the patent is impaired at any reporting date, the patent would be reviewed for impairment in accordance with Section 27 *Impairment of Assets*.

Ex 51 **On 1 January 20X1 an entity acquired for CU100,000 a 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 amount that the entity paid for the patent, and the entity intends to sell the patent to that party in five years.**

The patent has an economic life of 15 years and a useful life of five years to the entity. The depreciable amount would be amortised over its five-year useful life, with a residual value estimated at the present value of 60 per cent of the patent's fair value at the date it was acquired (eg at the date of acquisition the residual value is the present value of CU60,000 = CU37,255[(6)]). If there is any indication that the patent is impaired at any reporting date, the patent would be reviewed for impairment in accordance with Section 27 *Impairment of Assets*.

Ex 52 **On 1 January 20X1 an entity acquired a five-year taxi licence in an active market for CU10,000. The taxi licence is expected to be a source of net cash inflows for at least five years. However, the entity expects to sell the taxi licence in the active market in three years. On 1 January 20X1 taxi licences with a two-year remaining useful life were trading at CU2,500. The active market for taxi licences is expected to continue to exist for the foreseeable future.**

The depreciable amount of the taxi licence at 1 January 20X1 is CU7,500 (= CU10,000 carrying amount less CU2,500 estimated residual value). Consequently, CU7,500 should be amortised over the licence's three-year useful life. At each reporting date, if there is a significant change in the market price for taxi licences with a two-year remaining useful life then the residual value should be updated (see paragraph 18.24).

If there is any indication that the licence is impaired at any reporting date, the taxi licence would be reviewed for impairment in accordance with Section 27 *Impairment of Assets*.

[(6)] Assuming a discount rate of 10 per cent per year, the residual value measured at the date of acquisition = CU37,255 (ie CU60,000 ÷ 1.1^5 = CU60,000 × 0.620921).

Review of amortisation period and amortisation method

18.24 Factors such as a change in how an intangible asset is used, technological advancement, and changes in market prices may indicate that the residual value or useful life of an intangible asset has changed since the most recent annual **reporting date**. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, amortisation method or useful life. The entity shall account for the change in residual value, amortisation method or useful life as a change in an **accounting estimate** in accordance with paragraphs 10.15–10.18.

Note

Intangible assets are tested for impairment in accordance with Section 27 *Impairment of Assets*. In accordance with paragraph 27.10, if there is an indication that an intangible asset may be impaired, this may indicate that the entity should review its remaining useful life, amortisation method or residual value, even if no impairment loss is recognised for the asset.

Example – review of amortisation period and amortisation method

Ex 53 **On 1 January 20X1 an entity acquired a patent-protected medicine formula for CU500,000. Management estimated the useful life of the intangible asset to be 20 years (which is the remaining period of the patent) and its residual value at nil. Furthermore, management believed that the straight-line method reflects the pattern in which it expects to consume the intangible asset's future economic benefits.**

At the entity's 31 December 20X5 financial year-end, new information arose that caused management to reconsider its initial assessment of the amortisation period of the intangible asset. To encourage the development of the local pharmaceutical industry, the government extended the term of all local medical patents. Management now estimates the useful life of the formula to be 25 years (measured from the date of acquisition). Management continues to believe that the straight-line method reflects the pattern in which it expects to consume the asset's future economic benefits.

The amortisation expense recognised in the year ended 31 December 20X5 is CU19,048, which was determined as follows:

Dr	Inventories or profit or loss (amortisation expense)	CU19,048[(a)]	
	Cr Accumulated amortisation		CU19,048

To record amortisation expense for the year ended 31 December 20X5.

(a) CU400,000[(b)] ÷ 21 years' remaining useful life at the beginning of the current reporting period = CU19,048

(b) CU500,000 cost less (4 years × CU25,000[(c)] annual amortisation) = CU400,000 carrying amount at 1 January 20X5 (ie 31 December 20X4)

(c) Annual amortisation = CU500,000 ÷ 20 years = CU25,000

Ex 54 **On 1 January 20X1 an entity paid a system developer CU50,000 for an on-line system through which its customers can place orders. The entity estimated that the system would have a five-year life and amortised the cost accordingly. Unfortunately, the system never worked as anticipated and customer use declined considerably after the first year because of ongoing system problems resulting in incorrect orders. After two years, the entity replaced the custom-developed system with a generic software package available in the market. The entity concluded that the entire CU50,000 expenditure was worthless from the beginning and decided to write it off retrospectively, in the year of acquisition, as a correction of an error (see paragraph 10.21(a)).**

The entity accounts for the change in useful life of the customer order system as a change in an accounting estimate in accordance with paragraphs 10.15–10.18. The amortisation in the first two years in which the custom-developed system was used was based on an assessment of future benefits coming from that system. After two years, the assessment of future benefits changed.

A prior period error results from failure to take into account information that was available at the time. Until the end of the second year, the best available information was that the system would provide future benefits. Consequently, this is a change of accounting estimate, and not a correction of a prior period error.

Note: because there was an indication in 20X1 that future benefits were likely to be lower than expected, an impairment test would be carried out at 31 December 20X1 in accordance with Section 27 *Impairment of Assets*.

Recoverability of the carrying amount—impairment losses

18.25 To determine whether an intangible asset is impaired, an entity shall apply Section 27. That section 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. *[Refer: Section 27 Impairment of Assets]*

Note

If there is an indication that an intangible asset may be impaired, this may indicate that the entity should review its remaining useful life, amortisation method or residual value, even if no impairment loss is recognised for the asset (see paragraph 27.10).

Retirements and disposals

18.26 An entity shall derecognise an intangible asset, and shall recognise a gain or loss in profit or loss:

(a) on disposal, or

(b) when no future economic benefits are expected from its use or disposal.

Notes

The disposal of an intangible asset may occur in a variety of ways (eg by sale, by entering into a finance lease or by donation). In determining the date of disposal of such an asset, an entity applies the criteria in Section 23 *Revenue* for recognising revenue from the sale of goods (see paragraph 23.10).

The gain or loss arising from derecognising an intangible asset is determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It is recognised in profit or loss when the asset is derecognised (unless the transaction results in a sale and leaseback, in which case Section 20 *Leases* specifies the treatment of the gain or loss).

If payment for the intangible asset is deferred, the consideration received is recognised initially at the cash price equivalent. The difference between the nominal amount of the consideration and the cash price equivalent is recognised as interest revenue.

Examples – derecognition of an intangible asset

Ex 55 **On 14 December 20X5 an entity sold an item of computer software. The purchaser took immediate delivery of the software.**

The entity must derecognise the intangible asset on 14 December 20X5 when the risks and rewards of ownership of the software passed to the purchaser, assuming all the other conditions in paragraph 23.10 are met.

Ex 56 **An entity sells cardboard boxes made out of a special type of cardboard, which the entity has protected by purchasing a patent. In late 20X4 an entity experienced several complaints from customers that they had received batches of defective cardboard boxes. This led to several important customers cancelling their future orders.**

In May 20X5, because of a significant drop in the level of sales, the entity temporary halted production of its patented cardboard boxes. Expecting that the customers would return and that demand for cardboard boxes would increase in the foreseeable future, the entity did not dispose of its cardboard manufacturing operations.

On 30 June 20X6 management discovered that a competitor had developed a new type of cardboard that customers believed was superior to the entity's patented product. As a result, management gave up hope that sales would improve to the extent that it could recommence manufacturing cardboard boxes. Management therefore decided that the associated tangible and intangible assets (including the patent) should be scrapped.

The entity has a year-end of 31 December.

The entity must derecognise the patent on 30 June 20X6. From this date no future economic benefits are expected from its use or disposal.

The reduction in expected future economic benefits (ie reduction in sales) due to customers cancelling their orders in late 20X4 is an impairment indicator, and hence the cardboard manufacturing operations should be tested for impairment under Section 27 *Impairment of Assets* on 31 December 20X4. The subsequent significant drop in the level of sales is also an impairment indicator, and the cardboard manufacturing operations should therefore be tested again for impairment on 31 December 20X5.

Note: if expected future benefits are reduced, this is an impairment indicator. However, if no future benefits are expected, this results in derecognition of the asset.

Disclosures

18.27 An entity shall disclose the following for each class of intangible assets:

(a) the useful lives or the amortisation rates used.

(b) the amortisation methods used.

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

(d) the line item(s) in the **statement of comprehensive income** (and in the **income statement**, if presented) in which any amortisation of intangible assets is included.

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

(i) additions.

(ii) disposals.

(iii) acquisitions through business combinations.

(iv) amortisation.

(v) impairment losses.

(vi) other changes.

This reconciliation need not be presented for prior periods.

Notes

A class of intangible assets is a grouping of assets of a similar nature and use in an entity's operations (see the Glossary). The following are examples of separate classes of intangibles:

(a) brand names;

(b) mastheads and publishing titles;

(c) computer software;

(d) licences and franchises;

(e) copyrights, patents and other industrial property rights, service and operating rights;

(f) recipes, formulas, models, designs and prototypes; and

(g) intangible assets under development.

Example – disclosures for each class of intangible assets

Ex 57 **An entity could disclose information about intangible assets in its financial statements as follows:**

Note 1 Accounting policies

Intangible assets other than goodwill

Intangible assets, other than goodwill, are measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged so as to allocate the cost of assets less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives of intangible assets are:

- Patents 20 years
- Formulas 10 years
- Computer software 3 years

Note 4 Intangible assets other than goodwill

	Patents	*Formulas*	*Computer software*	*Total*
	CU'000	*CU'000*	*CU'000*	*CU'000*
Cost	10,000	13,000	4,400	27,400
Accumulated amortisation	(4,400)	(3,200)	(2,300)	(9,900)
Carrying amount at 1 January 20X2	**5,600**	**9,800**	**2,100**	**17,500**
Additions	–	2,000	1,000	3,000
Acquired in a business combination	5,000	4,000	2,000	11,000
Disposals	(1,400) [a]	(1,200) [d]	(300) [g]	(2,900)
Amortisation	(730)	(1,700)	(2,250)	(4,680)
Impairment	–	(600)	–	(600)
Carrying amount at 31 December 20X2	**8,470**	**12,300**	**2,550**	**23,320**
Cost	13,000 [b]	16,000 [e]	6,400 [h]	35,400
Accumulated amortisation	(4,530) [c]	(3,700) [f]	(3,850) [i]	(12,080)

Note: the following calculations illustrate the workings only and would not comprise part of the actual disclosures in the financial statements.

Calculations (in CU000)

(a) CU2,000 cost less CU600 accumulated amortisation

(b) CU10,000 cost + CU5,000 acquired in business combination less CU2,000[a] cost of disposed

items
(c) CU4,400 accumulated amortisation at 1 January 20X2 + CU730 annual amortisation less CU600[(a)] accumulated amortisation of disposed items
(d) CU3,000 cost less CU1,800 accumulated amortisation
(e) CU13,000 cost + CU2,000 additions + CU4,000 acquired in business combination less CU3,000[(d)] cost of disposed items
(f) CU3,200 accumulated amortisation at 1 January 20X2 + CU1,700 annual amortisation + CU600 impairment loss recognised on 20X2 less CU1,800[(d)] accumulated amortisation of disposed items
(g) CU1,000 cost less CU700 accumulated amortisation
(h) CU4,400 cost + CU1,000 additions + CU2,000 acquired in business combination less CU1,000[(g)] cost of disposed items
(i) CU2,300 accumulated amortisation at 1 January 20X2 + CU2,250 annual amortisation less CU700[(g)] accumulated amortisation of disposed items

18.28 An entity shall also disclose:

(a) a description, the carrying amount and remaining amortisation period of any individual intangible asset that is **material** to the entity's **financial statements**.

(b) for intangible assets acquired by way of a government grant and initially recognised at fair value (see paragraph 18.12):

(i) the fair value initially recognised for these assets, and

(ii) their carrying amounts.

(c) the existence and carrying amounts of intangible assets to which the entity has restricted title or that are pledged as security for liabilities.

(d) the amount of contractual commitments for the acquisition of intangible assets.

Example – other disclosures

Ex 58 **An entity could present disclosures about intangible assets as follows:**

Note 4 Intangible assets other than goodwill

At 31 December 20X5 the entity's taxi licence was pledged as security for a CU80,000 loan from entity B. This pledge also existed at 31 December 20X4.

In December 20X5 the entity signed an agreement to acquire a brand name from entity A on 31 March 20X7 for CU90,000. The entity had no contractual commitments for the acquisition of intangible assets at 31 December 20X4.

18.29 An entity shall disclose the aggregate amount of research and development expenditure recognised as an expense during the period (ie the amount of expenditure incurred internally on research and development that has not been capitalised as part of the cost of another asset that meets the recognition criteria in this IFRS).

Example – disclosures of research and development

Ex 59 **An entity could disclose research and development expenditure as follows:**

Note 3 Profit before tax

The following items have been recognised as expenses (income) in determining profit before tax:

	20X2	**20X1**
	CU	CU
Research and development costs	100,000	120,000

SIGNIFICANT ESTIMATES AND OTHER JUDGEMENTS

Applying the requirements of the *IFRS for SMEs* to transactions and events often requires judgement. Information about significant judgements and key sources of estimation uncertainty are useful in assessing the financial position, performance and cash flows of an entity. Consequently, in accordance with paragraph 8.6, an entity must disclose the judgements that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements. Furthermore, in accordance with paragraph 8.7, an entity must disclose information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Other sections of the *IFRS for SMEs* require disclosure of information about particular judgements and estimation uncertainties. Some of the judgements in accounting for intangible assets are set out below.

Recognition

In most cases little difficulty is encountered in identifying intangible assets. However, in a business combination, significant judgement may be required to identify all intangible assets that must be recognised separately in the accounting for the business combination. Failure to do so will result in the understatement of separately identified intangible assets and the overstatement of goodwill, with the effect that the intangible may be amortised over an incorrect period.

Measurement

An entity shall measure an intangible asset at its cost at initial recognition. In most cases little difficulty is encountered in determining the cost of an intangible asset. However, significant judgements in measuring the cost of an intangible asset at initial recognition may include:

- If payment for the item is deferred beyond normal credit terms—estimating the discount rate at which to discount all future payments to arrive at the present value that will be included in the cost of the intangible asset.
- If the item is acquired in an exchange transaction—measuring fair value when an active market does not exist for the asset received, or for the asset given up, and also judging whether the fair value can be measured reliably.
- If the item is acquired in a business combination—measuring the fair value of the intangible asset when an active market does not exist for the asset acquired, and also judging whether the fair value can be measured reliably.
- If the item is acquired by way of government grant—measuring the fair value of the intangible asset when an active market does not exist for the asset acquired.

Significant judgements in accounting for the amortisation of an intangible asset may include:

- estimating the useful life of the item and;

- determining the appropriate amortisation method that reflects the pattern in which the entity expects to consume the intangible asset.

Significant judgements in accounting for the impairment of an intangible asset may include:

- assessing whether there is any indication that an item may be impaired; and
- if there is an indication that the item may be impaired—measuring the recoverable amount of the intangible asset (see Module 27 *Impairment of Assets*).

COMPARISON WITH FULL IFRSs

A high-level overview of differences between the requirements at 9 July 2009 of accounting and reporting property, plant and equipment in accordance with full IFRSs (see IAS 38 *Intangible Assets*) and the *IFRS for SMEs* (see Section 18 *Intangible Assets other than Goodwill*) includes:

- The *IFRS for SMEs* is drafted in simple language and includes significantly less guidance on how to apply the principles.
- Full IFRSs require all research costs to be charged to expense when incurred, but development costs incurred after the project is deemed to be commercially viable are to be capitalised. The *IFRS for SMEs* requires all research and development costs to be recognised as expenses.
- Full IFRSs presume that the reliable measurement recognition criterion is always satisfied for intangible assets acquired in a business combination. The *IFRS for SMEs* provides an exception for an intangible asset acquired in a business combination that arises from legal or other contractual rights when its fair value cannot be measured reliably because either it is not separable from goodwill or it is separable from goodwill but there is no history or evidence of exchange transactions for the same or similar assets, and estimating fair value otherwise would be dependent on immeasurable variables.
- Full IFRSs require indefinite-lived intangible assets to be carried at cost less impairment loss, if any. The *IFRS for SMEs* considers all intangible assets (including indefinite-lived intangible assets) to have finite lives. It requires all intangible assets (ie including indefinite-lived intangible assets) to be amortised.
- Full IFRSs permit an option to use the revaluation model for the measurement of intangible assets after initial recognition. The *IFRS for SMEs* does not.
- Full IFRSs require an annual review of residual value, useful life and amortisation method of intangible assets. The *IFRS for SMEs* requires a review *only* if there is an indication that there has been a significant change since the last annual reporting date.
- Full IFRSs (see IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*) allow a choice of methods in accounting for intangible assets acquired by way of government grants. The *IFRS for SMEs* (see Section 24 *Government Grants*) prescribes a single method of accounting for government grants.

For differences related to impairment testing see Module 27 *Impairment of Assets*.

Module 18 – Intangible Assets other than Goodwill

TEST YOUR KNOWLEDGE

Test your knowledge of the requirements for accounting and reporting intangibles other than goodwill in accordance with the *IFRS for SMEs* by answering the questions below.

Once you have completed the test check your answers against those set out below this test.

Assume that all amounts are material.

Mark the box next to the most correct statement.

Question 1

An intangible asset (other than goodwill) is:

☐ (a) an identifiable asset without physical substance.

☐ (b) a non-monetary asset without physical substance.

☐ (c) an identifiable non-monetary asset without physical substance.

Question 2

An intangible asset is identifiable when:

☐ (a) it is separable (ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or liability).

☐ (b) it 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.

☐ (c) either (a) or (b) applies.

☐ (d) none of the above.

Question 3

An entity must measure intangible assets after initial recognition:

☐ (a) at fair value.

☐ (b) at fair value or at cost less any accumulated amortisation and any accumulated impairment losses (same accounting policy for all items in the same class of intangible asset).

☐ (c) at fair value or at cost less any accumulated amortisation and any accumulated impairment losses (elected on an item-by-item basis).

☐ (d) at cost less any accumulated amortisation and any accumulated impairment losses.

Question 4

The cost of an intangible asset at initial recognition is measured at its fair value when:

- ☐ (a) it is internally generated.
- ☐ (b) it is acquired as part of a business combination.
- ☐ (c) it is acquired by way of a government grant.
- ☐ (d) all of (a)–(c) above.
- ☐ (e) both (b) and (c) above.
- ☐ (f) none of the above.

Question 5

An entity acquired a trademark for a leading consumer product. The trademark has a remaining legal life of five years but is renewable every ten years at little cost. The acquiring entity intends to renew the trademark continuously and evidence supports its ability to do so. An analysis of (i) product life cycle studies, (ii) market, competitive and environmental trends, and (iii) brand extension opportunities provides evidence that the trademarked product will generate net cash inflows for the acquiring entity for an indefinite period. The useful life of the intangible asset is:

- ☐ (a) five years—the initial period of the contractual rights.
- ☐ (b) presumed to be 10 years—if the entity is unable to make a reliable estimate of its finite useful life.
- ☐ (c) 15 years—the initial period of the contractual rights plus a renewal period.
- ☐ (d) five years—the period of the contractual rights, but with no amortisation charges, as it is expected to generate cash flows for a indefinite period.

Question 6

On 31 December 20X2 entity A sold a brand name to entity B for CU250,000. Entity A estimates that it cost CU100,000 to develop the brand name during 20X1. Entity B estimates that it spent CU50,000 in maintaining and developing the brand name in 20X3.

On 31 December 20X3 entity C gained control over entity B in a business combination, when the fair value of the brand was estimated at CU400,000.

For the purpose of this example, ignore amortisation.

The brand name must be recognised:

- ☐ (a) on 31 December 20X1 by entity A at CU100,000; on 31 December 20X2 by entity B at CU250,000; on 31 December 20X3 by entity C (in its consolidated financial statements) at CU400,000.
- ☐ (b) on 31 December 20X1 by entity A at nil; on 31 December 20X2 by entity B at CU300,000; on 31 December 20X3 by entity C (in its consolidated financial statements) at CU400,000.
- ☐ (c) on 31 December 20X1 by entity A at nil; on 31 December 20X2 by entity B at CU250,000; on 31 December 20X3 by entity C (in its consolidated financial statements) at CU400,000.

Question 7

On 1 January 20X1 an entity acquired a taxi licence for CU95,000, including CU5,000 non-refundable purchase taxes. The purchase agreement provided that payment must be made in full on 31 December 20X1. Legal fees of CU2,000 were incurred in acquiring the taxi licence and paid on 1 January 20X1.

An appropriate discount rate is 10 per cent per year.

On 1 January 20X1 the entity shall measure the initial cost of the taxi licence at:

☐ (a) CU102,000.

☐ (b) CU97,000.

☐ (c) CU88,364.

☐ (d) CU107,000.

Question 8

On 1 January 20X1 an entity acquired a patent for CU100,000. At 31 December 20X1 management:

- assessed the patent's useful life at 20 years from the date of acquisition
- assessed that the entity will consume the patent's future economic benefits evenly over 20 years from the date of acquisition
- assessed the fair value of the patent at CU130,000.

The entity shall measure the carrying amount of the patent on 31 December 20X1 at:

☐ (a) CU100,000.

☐ (b) CU95,000.

☐ (c) CU130,000.

☐ (d) CU123,500.

Question 9

On 31 December 20X5 the entity reassessed the patent described in Question 8 as follows:

- the patent's useful life at 14 years from the date of acquisition
- the entity will consume the patent's future economic benefits evenly over 14 years from the date of acquisition
- the recoverable amount (fair value less costs to sell) of the patent at CU70,000.

The entity shall measure the carrying amount of the patent on 31 December 20X5 at:

☐ (a) CU72,000.

☐ (b) CU100,000.

☐ (c) CU64,286.

☐ (d) CU70,000.

Question 10

On 1 January 20X1 an entity (a publisher) acquired a competitor's publishing title for CU30,000. On 1 January 20X4 the entity commenced publishing using the new title.

On 31 December 20X8 the entity decided to sell the publishing title and took actions that make its sale within 12 months highly probable. The publishing title was sold on 31 March 20X9.

The entity shall account for the publishing title as:

☐ (a) an intangible asset (other than goodwill) from the date of acquisition (1 January 20X1) to 31 December 20X8 and as an inventory (asset held for sale in the ordinary course of business) from 31 December 20X8 to the date of disposal (31 March 20X9).

☐ (b) an item of inventory from the date of acquisition (1 January 20X1) to the date of disposal (31 March 20X9).

☐ (c) an intangible asset (other than goodwill) from the date of acquisition (1 January 20X1) to the date of disposal (31 March 20X9).

☐ (d) none of the above.

Module 18 – Intangible Assets other than Goodwill

Answers

Q1 (c) see paragraph 18.2

Q2 (c) see paragraph 18.2(a) and (b)

Q3 (d) see paragraph 18.18

Q4 (e) see paragraphs 18.9, 18.11 and 18.12

Q5 (b) see paragraphs 18.19 and 18.20

Q6 (c) see paragraphs 18.14 (entity A), 18.10 (entity B) and 18.11 (entity C).

Q7 (c) calculation—(CU95,000 purchase price including refundable taxes) ÷ 1.1 = CU86,364 present value of the purchase price + CU2,000 direct costs (legal fees) = CU88,364

Q8 (b) calculation—CU100,000 cost less (CU100,000 depreciable amount ÷ 20 years useful life × 1 year in use) accumulated amortisation = CU95,000

Q9 (d) calculation—CU100,000 cost less [CU20,000 accumulated amortisation at the beginning of the reporting period + (CU80,000 remaining depreciable amount ÷ 10 years remaining useful life × 1 year in use since the beginning of the current reporting period) = CU8,000 accumulated amortisation] = CU72,000 carrying amount before impairment testing. The significantly reduced assessment of the assets useful life would trigger an impairment test. The impairment test would require the carrying amount of the asset be reduced by a further CU2,000 to its recoverable amount CU70,000.

Q10 (c) see paragraphs 18.4 and 18.26(a). The decision to sell an intangible asset does not in itself change the classification of the intangible asset to inventory.

Module 18 – Intangible Assets other than Goodwill

APPLY YOUR KNOWLEDGE

Apply your knowledge of the requirements for accounting and reporting intangibles other than goodwill in accordance with the *IFRS for SMEs* by solving the case studies below.

Once you have completed the case studies check your answers against those set out at the end of this test

Case study 1

SME D incurred the following expenditures in establishing its taxi business in a local city:

Date	*CU*	*Additional information*
1 May 20X1	1,500	General start-up costs
30 June 20X1	7,000	Legal costs directly attributable to the acquisition of the taxi licences
30 June 20X1	100,000	Payment to the taxi licensing authority for the taxi licences, including CU10,000 refundable purchase taxes
1 July 20X1	100	Printing business cards of the drivers
1 July 20X1	20,000	Payment for an advertisement to be published every day for the next 12 months in a local daily newspaper

At 31 December 20X1 SME D made the following assessments:

- Economic life of the taxi licence: five years from 30 June 20X1 (the date of acquisition)
- Residual value of the taxi licences: nil
- The entity expects to consume the taxi licences' future economic benefits evenly over five years from the date of acquisition
- There is no indication that the taxi licences might be impaired.

The taxi drivers own their own vehicles, which they operate under SME D's taxi licences.

Prepare accounting entries to record the information set out above in the accounting records of SME D for the year ended 31 December 20X1.

Ignore all forms of taxation.

Answer to case study 1

1 May 20X1

Dr	Profit or loss (expenses)	CU1,500	
	Cr Cash		CU1,500

To recognise start-up costs incurred for the taxi operations.

30 June 20X1

Dr	Intangible asset (taxi licence)—cost	CU7,000(A)	
	Cr Cash		CU7,000

To recognise legal costs directly attributable to the acquisition of the taxi licences.

Dr	Intangible asset (taxi licence)—cost	CU90,000(A)	
Dr	Receivable—refundable purchase taxes	CU10,000	
	Cr Cash		CU100,000

To recognise the acquisition of the taxi licences.

1 July 20X1

Dr	Profit or loss (operating expenses)	CU100	
	Cr Cash		CU100

To recognise as an expense the costs of printing business cards for the taxi drivers.

Dr	Prepaid expenses (asset)	CU20,000	
	Cr Cash		CU20,000

To recognise advertising costs paid on 1 July 20X1 for the twelve months ending 30 June 20X2.

For the year ended 31 December 20X1

Dr	Profit or loss (operating expenses)	CU10,000	
	Cr Prepaid expenses (asset)		CU10,000

To recognise an expense for advertising prepaid on 1 July 20X1 for the six months ending 31 December 20X1.

Dr	Profit or loss (operating expenses)	CU9,700(a)	
	Cr Intangible asset (taxi licences)—accumulated amortisation		CU9,700

To recognise amortisation of taxi licences from the date when the asset was ready for use (for the six month period ended 31 December 20X1).

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) CU97,000[(b)] cost ÷ 5 year useful life = CU19,400 amortisation for a year.

Amortisation for 6 months = CU9,700 (ie CU19,400 ÷ 12 months × 6 months).

(b) ∑A = CU97,000 cost of intangible asset—taxi licences.

Case study 2

On 1 January 20X4 SME F acquired a trademark for a line of products in a separate acquisition from a competitor for CU300,000. SME F expected to continue marketing the line of products using the trademark indefinitely. An analysis of (i) product life cycle studies, (ii) market, competitive and environmental trends, and (iii) brand extension opportunities provides evidence that the line of trademarked products may generate net cash inflows for the acquiring entity for an indefinite period. Because management is unable to estimate the useful life of the trademark SME F amortises the cost of the trademark over 10 years (ie its presumed useful life) using the straight-line method.

In 20X7 a competitor unexpectedly revealed a technological breakthrough that is expected to result in a product, that when launched by the competitor, will extinguish demand for SME F's patented product-line. Demand for SME F's patented product-line is expected to remain strong until December 20X9, when the competitor is expected to launch its new product.

On 31 December 20X7 SME F assessed the recoverable amount of the trademark at CU50,000. SME F intends to continue manufacturing the patented products until 31 December 20X9.

SME F has a 31 December financial year-end.

Prepare accounting entries to record the information set out above in the accounting records of SME F from 1 January 20X4 to 31 December 20X7.

Ignore all forms of taxation.

Answer to case study 2

1 January 20X4

Dr	Intangible asset (trademark)—cost	CU300,000	
	Cr Cash		CU300,000

To recognise the acquisition of the trademark in a separate acquisition.

For the year ended 20X4

Dr	Profit or loss (operating expenses)—amortisation of trademark	CU30,000[(a)]	
	Cr Intangible asset (trademark)—accumulated amortisation and accumulated impairment		CU30,000

To recognise the annual amortisation of the trademark during the period.

For the year ended 20X5

Dr	Profit or loss (operating expenses)—amortisation of trademark	CU30,000[(a)]	
	Cr Intangible asset (trademark)—accumulated amortisation and accumulated impairment		CU30,000

To recognise the annual amortisation of the trademark during the period.

For the year ended 20X6

Dr	Profit or loss (operating expenses)—amortisation of trademark	CU30,000[(a)]	
	Cr Intangible asset (trademark)—accumulated amortisation and accumulated impairment		CU30,000

To recognise the annual amortisation of the trademark during the period.

For the year ended 31 December 20X7

Dr	Profit or loss (operating expenses)—amortisation of trademark	CU70,000[(b)]	
	Cr Intangible asset (trademark)—accumulated amortisation and accumulated impairment		CU70,000

To recognise the annual amortisation of the trademark during the period.

At 31 December 20X7

Dr	Profit or loss (operating expenses)—impairment of trademark	CU90,000[(c)]	
	Cr Intangible asset (finite life trademark)—accumulated amortisation and accumulated impairment		CU90,000

To recognise the impairment loss for the trademark.

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) CU300,000 cost ÷ 10 years useful life = CU30,000 amortisation per year.

(b) CU210,000 carrying amount (ie CU300,000 cost less (CU30,000 amortisation per year × 3 years since acquisition)) ÷ 3 years remaining useful life (31 December 20X9 less 1 January 20X7) = CU70,000 amortisation per year.

(c) CU140,000 carrying amount (ie CU300,000 cost less (CU30,000 amortisation per year × 3 years since acquisition until 31 December 20X6) less CU70,000 amortisation for the year 20X7) less CU50,000 recoverable amount = CU90,000 impairment loss.

Case study 3

At 1 January 20X5 (the beginning of the comparative reporting period) SME J, an Internet service provider, owned the following intangible assets:

Description	*Additional information*
Internet domain name	Acquired in a separate acquisition on 1 January 20X4 for CU300,000. The entity is unable to make a reliable estimate of the useful life.
Software	Internally developed. Estimated useful life—ten years from date of development. Remaining useful life—five years.
Customer list	Acquired in a separate acquisition on 1 January 20X4 for CU100,000. Estimated useful life—five years from date of acquisition.
Ringtones	Internally developed. Estimated useful life—three years from date of development.

On 30 June 20X6 SME J acquired ringtones (sometimes called jingles) developed by an independent third party for CU20,000. The useful life of the jingles is expected to be three years from the date of acquisition.

On 30 September 20X6 SME J acquired 60 per cent of the issued share capital of SME K in a business combination when the fair value of SME K's identifiable intangible assets were:

Description	*CU*	*Additional information*
Internet domain name	500,000	Unable to make a reliable estimate of the useful life.
Software	600,000	Internally developed. Estimated remaining useful life = ten years.
Customer list	400,000	Internally generated. Estimated remaining useful life = five years.
Advertising contracts	500,000	Five-year contracts (all contracts started on 1 October 20X5) for customers' advertisements to appear in a designated space on SME K's website.
In-process research and development	80,000	Various current research and development projects to enhance the value of the services offered by the entity.

In the last quarter of 20X6 SME K incurred CU10,000 on research and development. No projects were completed during the period.

At 31 December 20X6 SME J confirmed its previous assessments of the group's intangible assets.

Draft an extract showing how the intangible assets could be presented and disclosed in the consolidated financial statements of SME J Group for the year ended 31 December 20X6.

Answer to case study 3

Extract from SME J group's consolidated statement of financial position at 31 December 20X6:

	Note	*20X6*	*20X5*
Intangible assets	4	CU2,267,917	CU300,000

Extract from the notes to SME J group's 31 December 20X6 consolidated financial statements:

Note 1 Accounting policies

Intangible assets other than goodwill

Intangible assets are measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged so as to allocate the cost of assets less their residual values over their estimated useful lives, using the straight-line method. Internet domain names are presumed to have a useful life of ten years because their useful life cannot be estimated reliably. The estimated useful lives of other intangible assets are estimated to be:

- Advertising contracts 5 years
- Software 10 years
- Customer lists 5 years
- Ringtones 3 years

Note 4 Intangible assets other than goodwill (*amounts in CU*)

	Internet domain name	*Software*	*Customer lists*	*In-process research and development*	*Advertising contracts*	*Ringtones*	*Total*
Carrying amount at 31 December 20X5	240,000	– [h]	60,000	–	–	– [h]	300,000
Cost	300,000	–	100,000	–	–	–	400,000
Accumulated amortisation	(60,000) [a]	–	(40,000) [c]	–	–	–	(100,000)
Additions	–	–	–	–	–	20,000	20,000
Acquired in a business combination	500,000	600,000	400,000	80,000	500,000	–	2,080,000
Amortisation	(42,500) [a]	(15,000) [b]	(40,000) [c]	– [e]	(31,250) [f]	(3,333) [g]	(132,083)
Carrying amount at 31 December 20X6	697,500	585,000	420,000	80,000	468,750	16,667	2,267,917
Cost	800,000	600,000	500,000	80,000	500,000	20,000	2,500,000
Accumulated amortisation	(102,500)	(15,000)	(80,000)	–	(31,250)	(3,333)	(232,083)

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) CU300,000 cost ÷ 10 years = CU30,000 amortisation per year of Internet domain name acquired on 1 January 20X4.

CU500,000 cost ÷ 10 years × 3 ÷ 12 months (ie 30 September to 31 December 20X6) = CU12,500 amortisation of Internet domain name acquired in a business combination.

Until 31 December 20X5: CU30,000 × 2 years = CU60,000 amortisation of Internet domain name.

In 20X6: CU30,000 + CU12,500 = CU42,500 amortisation of Internet domain name in 20X6.

(b) CU600,000 cost ÷ 10 years × 3 ÷ 12 months (ie 30 September to 31 December 20X6) = CU15,000 amortisation of software.

(c) Until 31 December 20X5: CU20,000[(d)] × 2 years = CU40,000 amortisation of customer lists.

In 20X6: CU20,000[(d)] + CU20,000[(d)] = CU40,000 amortisation of customer lists in 2006.

(d) CU100,000 cost ÷ 5 years = CU20,000 amortisation per year of customer lists acquired on 1 January 20X4.

CU400,000 cost ÷ 5 years × 3 ÷ 12 months (ie 30 September to 31 December 20X6) = CU20,000 amortisation of customer lists acquired in a business combination.

(e) The entity will start amortising the in-process research and development that it acquired in a business combination when it is developed (ie ready for use as intended by management).

(f) CU500,000 cost ÷ 4 years remaining useful life × 3 ÷ 12 months (ie 30 September to 31 December 20X6) = CU31,250 amortisation of advertising contract intangible asset.

(g) CU20,000 cost ÷ 3 years remaining useful life × 6 ÷ 12 months (ie 30 June to 31 December 20X6) = CU3,333 amortisation of ringtones.

(h) Internally generated intangible assets are never recognised under Section 18.