

LKAS 38 : Intangible Assets

AAT Level III FAR - Financial Reporting

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ACA, B.Sc. (Accounting) Sp. Hons., ACMA (SL), SAT, CIMA Passed Finalist,
Reading for MBA (PIM), CA and CIMA Prize Winner



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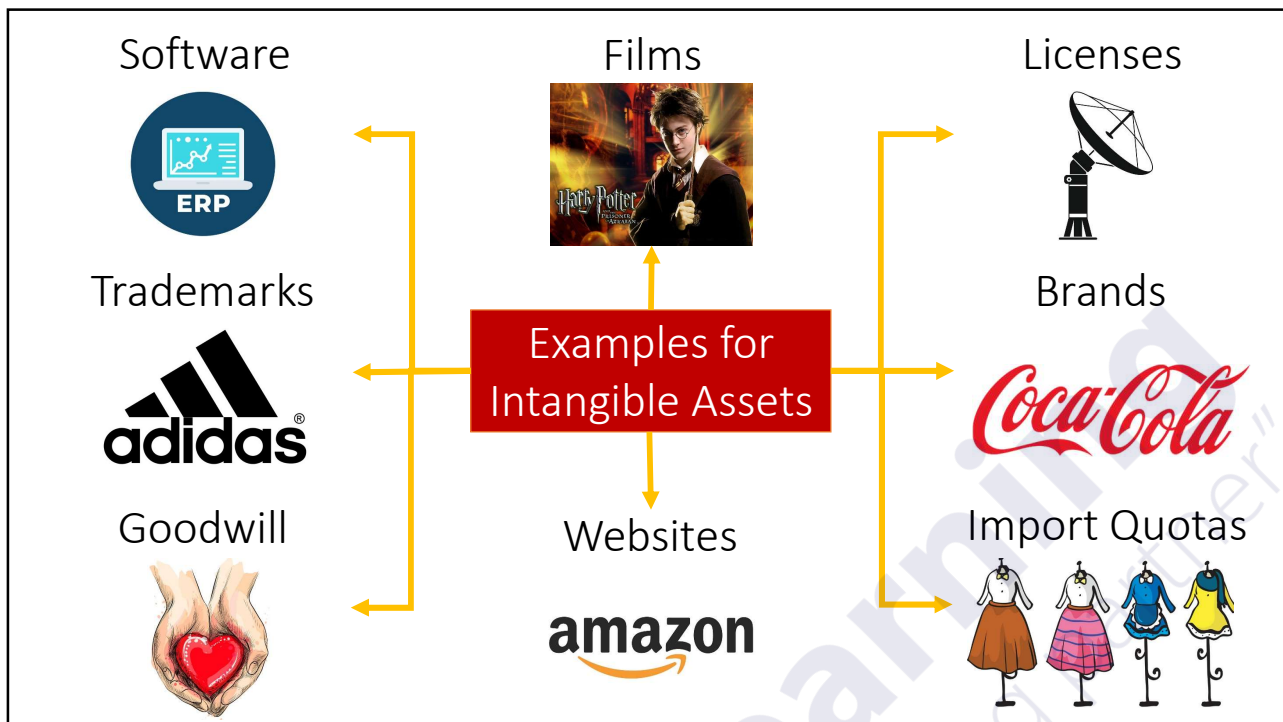
AAT Level 03

Financial Accounting and Reporting


Sandeepa Jayasekera

B.Sc. (Acct.) Hons. Gold Medal Winner, ACA, SAT, ACMA (UK), CGMA (UK), CA Prize Winner for AFR subject in Strategic Level II, CA First in Order of Merit Prize Winner in CAB II Level, CIMA Strategic Level Aggregate Prize Winner, MBA (PIM-SJP).

LKAS 38 Intangible Assets

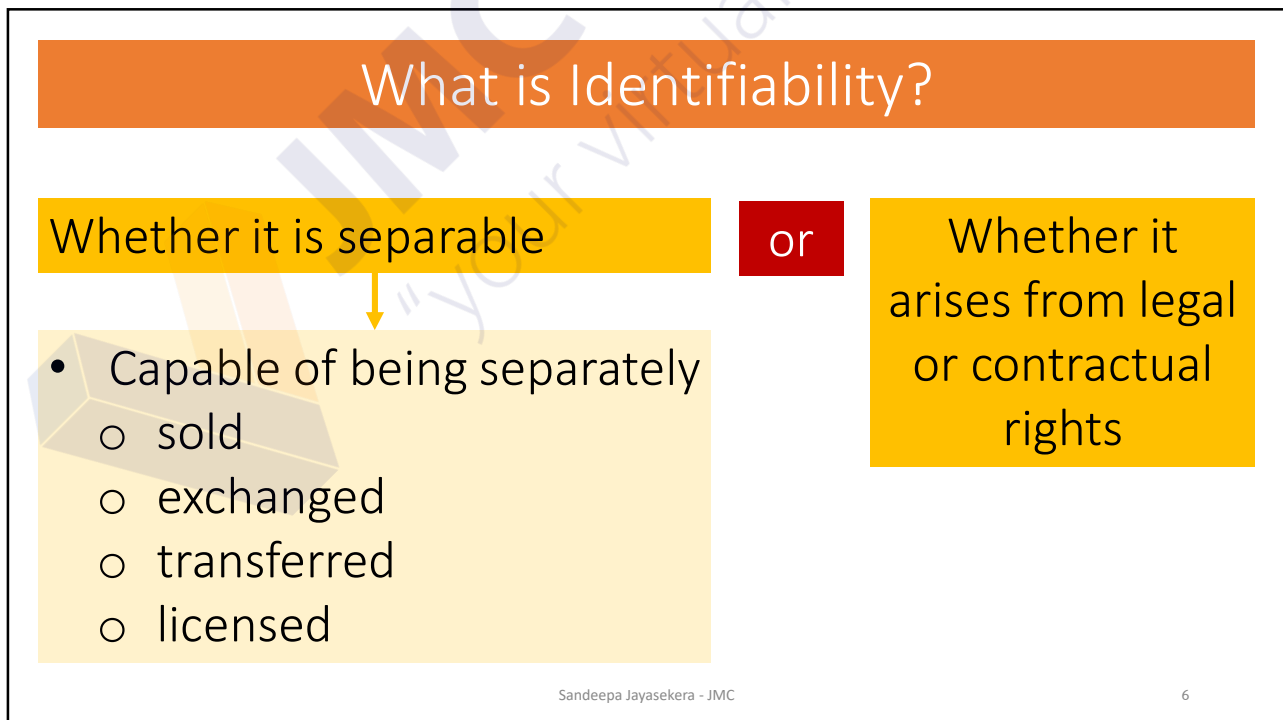
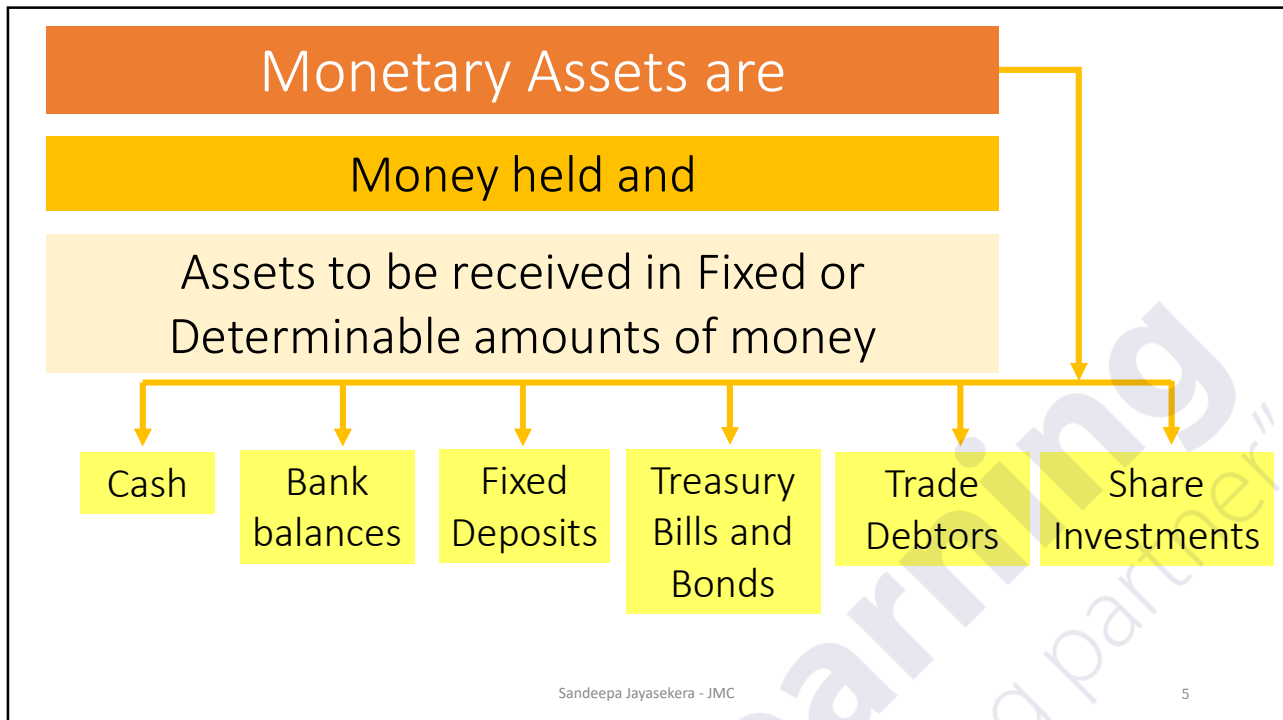


What is an Intangible Asset?



- Identifiable
- Non-monetary Asset
- Without
Physical Substance

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3 criteria needs to be satisfied to be an Intangible Asset

Identifiability

Controllability

Inflow of future economic benefits



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Question 01

Explain with reasons whether the following Intangible Assets come under the definition of Intangible Assets or not.

1.1 Patent purchased for Rs. 2 Mn

1.2 Customer List of an Audit Firm

1.3 Software purchased for Online Education at a cost of Rs. 100,000

1.4 Patent obtained on aeronautical technology

1.5 Rs.500,000 spent on training staff with expert technical knowledge

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Question 01

- 1.6 80% market share of Litro Gas Ltd. in the Gas Industry
- 1.7 Brand name developed by Coca Cola
- 1.8 Goodwill of a business
- 1.9 Website developed for customers to obtain information
- 1.10 lkman.lk website that generates income through sale of goods
- 1.11 Nokia brand name acquired by Microsoft

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When should Intangible Assets be recognized?

If it meets the Definition

When there is a probable inflow of future economic benefits

If the cost can be measured reliably



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2019 July Question No. 03

(a) State a criteria to be met to recognize an asset as an intangible asset. (02 marks)

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2022 January Question No. 04

The followings information was extracted from the books of Ganesh Ltd. for the year ended 31st March 2021:

- (1) The company has conducted a market research for the development of a new product in March 2021. An amount of Rs.1,500,000/- was paid to the research company for conducting the market research.
- (2) The company registered the patent right for the new product and cost of registration for patent right was Rs.200,000/-.
- (3) Over the past few years, the company has maintained a good relationship with existing key customers. During the year, the company incurred Rs.2 million on customer entertainment programmes to increase the sale of new product.

You are required to:

Explain whether each of the above costs could be recognized as an intangible asset as per LKAS 38 - Intangible Assets. (05 marks)

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2022 January Question No. 04

The followings information was extracted from the books of Ganesh Ltd. for the year ended 31st March 2021:

- (1) The company has conducted a market research for the development of a new product in March 2021. An amount of Rs.1,500,000/- was paid to the research company for conducting the market research.
- (2) The company registered the patent right for the new product and cost of registration for patent right was Rs.200,000/-.
- (3) Over the past few years, the company has maintained a good

Ways of Acquiring Intangible Assets and its Initial Cost

Purchase		As a part of a Business Combination	Internally generated Intangible Assets
Purchase Price	X	Fair Value at the Acquisition Date = Cost	Following internally generated assets are not recognized as Intangible Assets
(-) Trade Discounts	(X)		
(-) Rebates	(X)	Exchange of Assets	
Non-refundable Taxes	X	Fair Value of the New Asset	
Directly attributable costs of preparing the asset for its intended use	X	By way of a Government Grant	
		Fair Value at the Grant Date = Cost	<ul style="list-style-type: none"> • Goodwill • Brands • Copyright • Customer Lists

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Question 02

Fathima Ltd. purchased SAP ERP System. The expense incurred for it is as follows.

- Purchase Cost Rs. 10 Mn
- Trade Discount received 10%
- CESS Tax 15% (on purchase price net of discounts)
- Professional fee incurred Rs. 1 Mn
- Employee benefits of Rs. 1.9 Mn was paid for the SAP project team over the project implementation period

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Question 02

- Staff Training expense Rs. 1 Mn
- General overheads Rs. 0.5 Mn
- Internal Advertising expense Rs. 0.1 Mn

Compute the Cost of ERP System to be capitalized.

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2019 July Question No. 03

(b) EPL Ltd. has developed a new product during the year ended 31st March 2019 and started commercial operation in May 2019. Cost incurred for the new product during the year 2018/19 were as follows:

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2019 July Question No. 03

- (1) A research was done for the new product and incurred Rs.1 million during the year.
- (2) The company registered the patent right for the new product during the year and fee on registration for patent right was Rs.100,000/-.
- (3) Costs of Rs.300,000/- for advertising and promotional activities were spend on the new product.

You are required to:

Explain whether each of the above costs could be recognized as intangible assets as per LKAS 38 - Intangible Assets. (03 marks)

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How to recognise Internally generated Intangible Assets other than Internally generated Goodwill, Copyrights, Brand names and Customer Lists

Research

Development



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Research

- Planned investigation
- To gain new scientific and technical knowledge

Examples

- Activities aimed at obtaining new knowledge
- Search for evaluation and final selection of research findings
- Search for alternatives for production processes of material
- New or improved materials, processes

In the Research phase, **economic benefits do not** flow to the entity. Therefore, it is charged to the **P/L Account**.

Development



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Development

- Application of research findings or other knowledge
- To plan or design new or improved products or processes
- Before the start of commercial production or use

Examples

- Pre-production prototypes and models
- Design of tools, jigs and moulds involving new technology
- Design, construction and operation of a pilot plant that is not economically feasible for commercial production
- Design of alternative for new materials, devices, products or processes

Accounting Treatment for Development

Are these Criteria satisfied?

- **P** - Ability to generate **Probable** future economic benefits and the Existence of a market
- **R** - Availability of technical and financial **Resources** to use or sell the intangible asset
- **I** - **Intention** to Use or Sell the Intangible Asset
- **T** - **Technical Feasibility** to Use or Sell the Intangible Asset
- **A** - **Ability** to Use or Sell the Intangible Asset

Yes

Capitalise

No

Charge to
P/L Account

Expenses that can be included in Development Cost

Cost of **materials** used in generating the intangible assets

Directly attributable **salary** costs

Depreciation charge on Property, Plant and Equipment

Registration Fees, **Legal** Fees

Overheads attributed on an appropriate basis

2021 January Question No. 04

The followings information was extracted from the books of Das Ltd. for the year ended 31st March 2020:

(1) A cost of Rs. 2 million was incurred by the company during the year on a program to train employees. It is expected that the performance of the employees will be improved as a result of the training program.

(2) Das Ltd. developed a new product during the year and started its commercial operation on 01st June 2019. Before developing the new product, a research was conducted by the company incurring a cost of Rs. 3 million on 30th April 2019.

2021 January Question No. 04

You are required to:

- (a) Explain whether each of the above costs could be recognized as intangible asset as per LKAS 38 - Intangible assets. (03 marks)
- (b) State two(02) criteria to be met to recognize a development cost as an intangible asset. (02 marks)

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Question 03

On 01/01/20X1 Nizar Ltd. started to develop an accounting software.

During the first 6 months, the company incurred Rs. 1 Mn to obtain new technical knowledge.

On 01/07/20X1 the company started to develop the software for commercial use, by applying the knowledge gained.

The company incurred Rs. 1.5 for this phase.

Financial year ends on 31 December.

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Question 03

3.1 Define Research and Development.

3.2 Identify the Research and Development phases in this example.

3.3 Name the criteria that needs to satisfied to recognize development costs.

3.4 If the criteria required to be satisfied to recognize development costs were satisfied by 01/07/20X1, show how the total project cost of Rs. 2.5 Mn needs to be accounted.

3.5 On 01/02/20X2 it was identified that from the expenses relevant for the research phase, Rs. 200,000/- is relevant for the development phase. Can this be corrected?

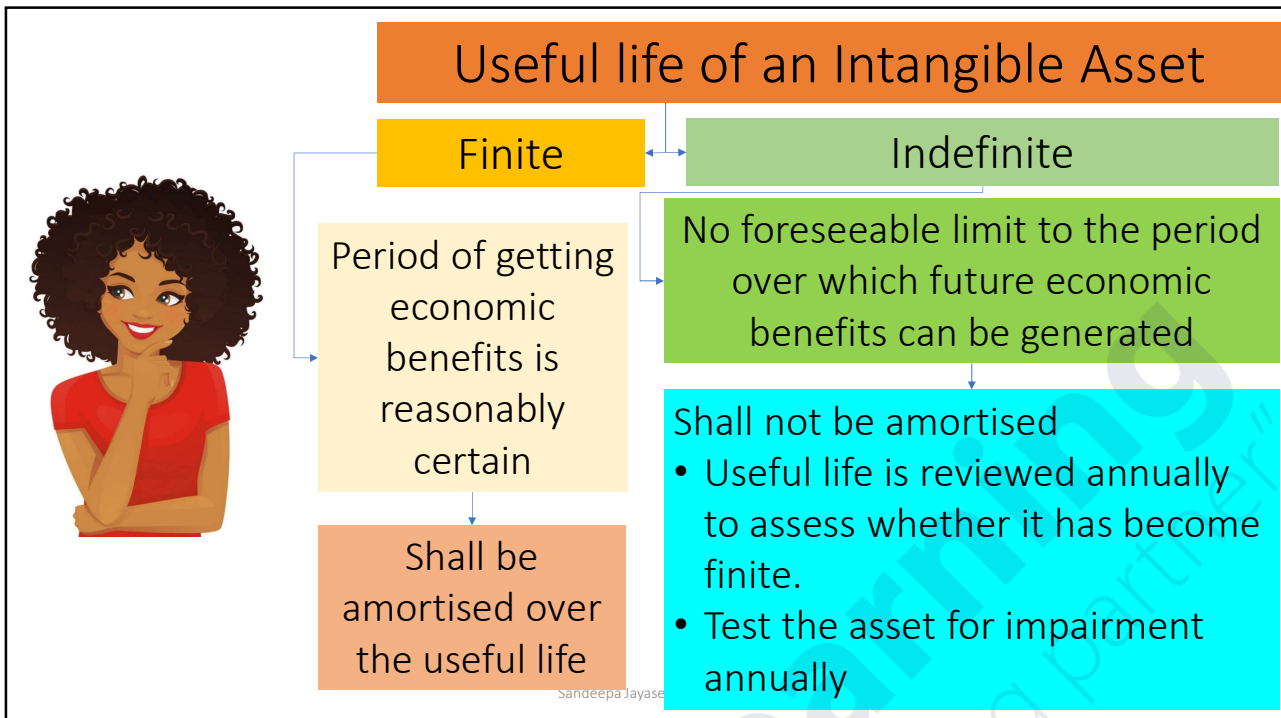
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Subsequent Measurement of Intangible Assets

Cost Model

Cost	XX
(-) Accumulated Amortisation	(X)
(-) Accumulated Impairment Losses	(X)
Net Book Value	XX

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Question 04

On 01/01/20X1 Khan Ltd. purchased a patent right at a cost of Rs. 10 Mn. Its useful life is 5 years. Residual value is zero.

Due a technical obsolescence it was noted that the patent right was impaired on 31/12/20X1.

The recoverable value was estimated as Rs. 7 Mn. There was no impact on the useful life.

Company's financial year ends on 31/12.

Question 04

1. Calculate the amortization for the year ended 31/12/20X1.
2. If the useful life is indefinite, explain how the above transaction should be accounted for.
3. Calculate the amortization for the year ended 31/12/20X2.

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Subsequent Measurement of Intangible Assets

Revaluation Model

Revalued Amount	XX
(-) Subsequent Accumulated Amortisation	(X)
(-) Subsequent Accumulated Impairment Losses	(X)
Net Book Value	XX

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Revaluation Model

- Revaluation Model can be applied if the fair value can be measured reliably by reference to an **active market**
- Active Market is a market in which transactions take place with sufficient frequency and volume
- This is more suitable for intangible assets such as software, quotas, licenses.
- When an asset is revalued, the entire class of that asset needs to be revalued.

Question 05

On 01/01/20X1 Isuru Ltd. purchased a quota to export garments at a cost of Rs. 20 Mn.

These types of quotas have an active market. Therefore, the company decided to use the revaluation model for subsequent measurement. The useful life is 5 years.

On 31/12/20X1 it was revalued at 22 Mn and on 31/12/20X2 it was revalued at Rs. 15 Mn.

Company's financial year ends on 31/12.

Question 05

1. Calculate the amortization for the year 20X1.
2. Calculate the revaluation gain/loss as at 31/12/20X1.
3. Explain the accounting treatment of revaluation gain/loss on 31/12/20X1.
4. Calculate the amortization for the year 20X2.
5. Calculate the revaluation gain/loss as at 31/12/20X2.
6. Explain the accounting treatment of revaluation gain/loss on 31/12/20X2.

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Derecognition of Intangible Assets

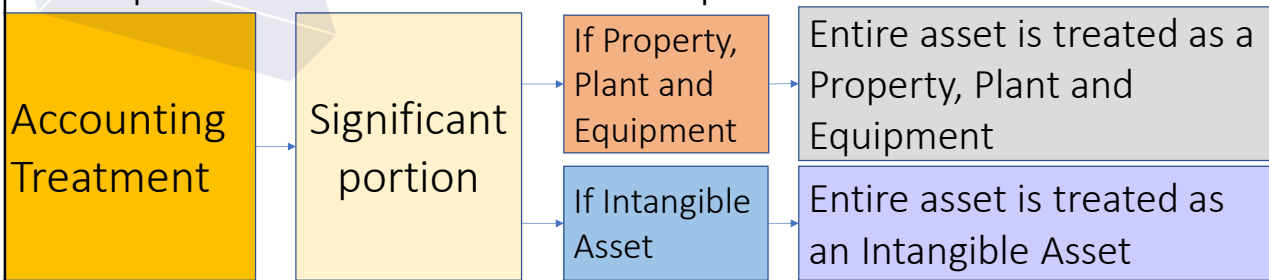
On Disposal

When future economic benefits are not being expected

Refer LKAS 16 on Accounting for Disposal profit/loss

Intangible Assets integrated in Property, Plant and Equipment

Example: Software installed in computers



Question 06

On 01/04/20X2 Madhavi Ltd. purchased a software at a cost of Rs. 2 Mn. Its useful life is 4 years.

The company exchanged this software with another new software on 31/03/20X3.

The market value of the new software is Rs. 2.5 Mn and its useful life is 5 years.

If the financial year ends on 31/3.

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Question 06

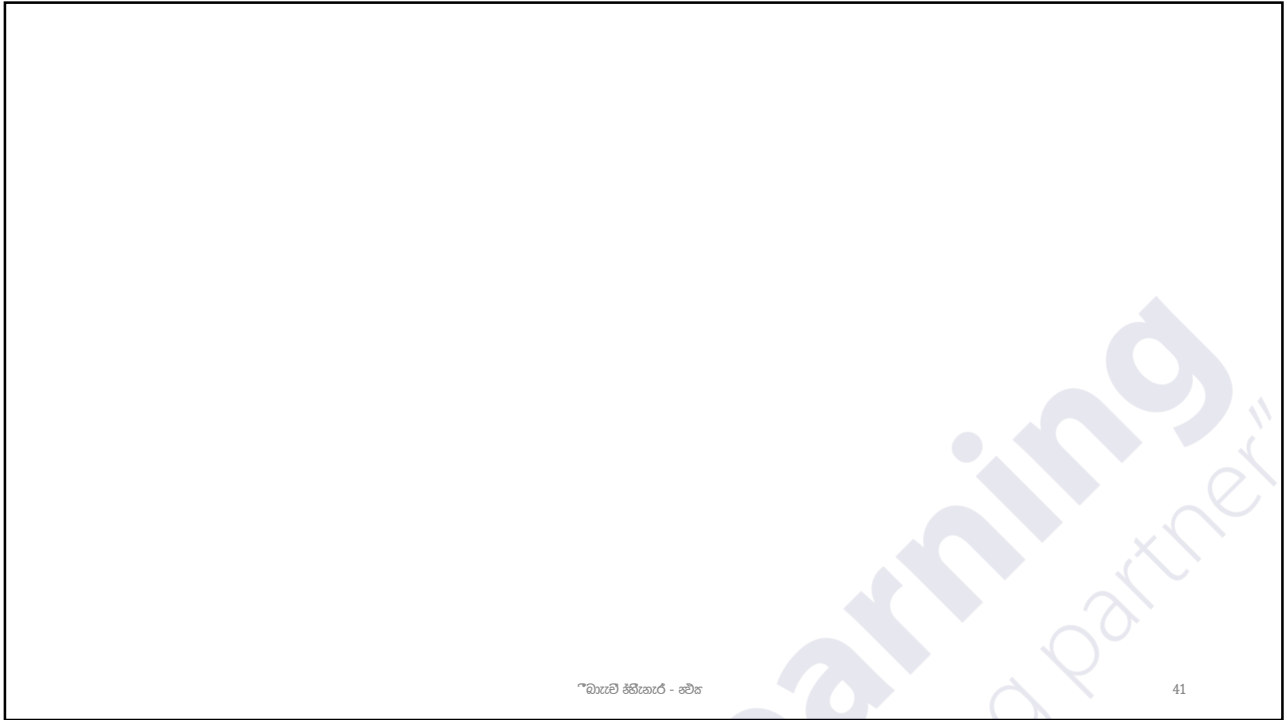
6.1 Calculate the amortization of old software for year ended 31/3/X3

6.2 Calculate the cost of new software

6.3 Calculate the exchange gain or loss

6.4 Calculate the amortization of new software for the year ended 31/3/X4

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