

Exposure Draft

Accounting Standard (AS) 38

Intangible Assets

Last date for the comments: November 2, 2018



Issued by

Accounting Standards Board

The Institute of Chartered Accountants of India

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(The Indian Accounting Standards (Ind AS), as notified by the Ministry of Corporate Affairs in February, 2015, have been applicable to the specified class of companies. For other class of companies, i.e., primarily the unlisted companies having net worth less than Rs. 250 crores, Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, have been applicable. However, the Ministry of Corporate Affairs has requested the Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI) to upgrade Accounting Standards, as notified under Companies (Accounting Standards) Rules, 2006, to bring them nearer to Indian Accounting Standards. Accordingly, the Accounting Standards Board (ASB) of ICAI has initiated the process of upgradation of these standards which will be applicable to all companies having net-worth less than Rs. 250 crores including non-corporate entities.

In this direction, the ASB has finalised AS 38, Intangible Assets. For formulating AS 38 Ind AS 38, Intangible Assets, has been taken as the base. Major differences between draft AS 38 and Ind AS 38 are given in Appendix 1 of the AS 38. Similarly, major differences between draft AS 38 and AS 26 are given in Appendix 2 of AS 38.

Following is the Exposure Draft of the Accounting Standard (AS) 38, Intangible Assets, issued by the Accounting Standards Board of the Institute of Chartered Accountants of India, for comments. The Board invites comments on any aspect of this Exposure Draft. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

How to Comment

Comments can be submitted using one of the following methods so as to receive not later than November 2, 2018:

1. Electronically: Visit the link <http://www.icai.org/comments/asb/>
2. Email: Comments can be sent at commentsasb@icai.in
3. Postal: Secretary, Accounting Standards Board,
The Institute of Chartered Accountants of India, ICAI Bhawan,
Post Box No. 7100, Indraprastha Marg, New Delhi – 110 002

Further clarifications on any aspect of this Exposure Draft may be sought by email to asb@icai.in.

Accounting Standard (AS) 38

Intangible Assets

(This Accounting Standard includes paragraphs set in **bold** type and plain type, which have equal authority. Paragraphs in bold type indicate the main principles.)

Objective

- 1 The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires specified disclosures about intangible assets.

Scope

- 2 **This Standard shall be applied in accounting for intangible assets, except:**
 - (a) **intangible assets that are within the scope of another Standard;**
 - (b) **financial assets, as defined in AS 109, *Financial Instruments*;**
 - (c) **the recognition and measurement of exploration and evaluation assets;**
 - (d) **expenditure on the development and extraction of minerals, oil, natural gas and similar non-regenerative resources, and**
 - (e) **intangible assets arising in insurance entity from contracts with policyholders.**
- 3 If another Standard prescribes the accounting for a specific type of intangible asset, an entity applies that Standard instead of this Standard. For example, this Standard does not apply to:
 - (a) intangible assets held by an entity for sale in the ordinary course of business (see AS 2, *Inventories*, and AS 11, *Construction Contracts*).
 - (b) deferred tax assets (see AS 12, *Income Taxes*).
 - (c) leases that are within the scope of AS 17, *Leases*.
 - (d) assets arising from employee benefits (see AS 19, *Employee Benefits*).

- (e) financial assets as defined in AS 109. The recognition and measurement of some financial assets are covered by AS 110, *Consolidated Financial Statements*, AS 27, *Separate Financial Statements*, and AS 28, *Investments in Associates and Joint Ventures*.
 - (f) goodwill acquired in a business combination (see AS 103, *Business Combinations*).
 - (g) [Refer Appendix 1].
 - (h) non-current intangible assets classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with AS 105, *Non-current Assets Held for Sale and Discontinued Operations*.
 - (i) [Refer Appendix 1].
- 4 Some intangible assets may be contained in or on a physical substance such as a compact disc (in the case of computer software), legal documentation (in the case of a licence or patent) or film. In determining whether an asset that incorporates both intangible and tangible elements should be treated under AS 16, *Property, Plant and Equipment*, or as an intangible asset under this Standard, an entity uses judgement to assess which element is more significant. For example, computer software for a computer-controlled machine tool that cannot operate without that specific software is an integral part of the related hardware and it is treated as property, plant and equipment. The same applies to the operating system of a computer. When the software is not an integral part of the related hardware, computer software is treated as an intangible asset.
- 5 This Standard applies to, among other things, expenditure on advertising, training, start-up, research and development activities. Research and development activities are directed to the development of knowledge. Therefore, although these activities may result in an asset with physical substance (eg a prototype), the physical element of the asset is secondary to its intangible component, ie the knowledge embodied in it.
- 6 In the case of a finance lease, the underlying asset may be either tangible or intangible. After initial recognition, a lessee accounts for an intangible asset held under a finance lease in accordance with this Standard. Rights under licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights are excluded from the scope of AS 17, and are within the scope of this Standard.
- 7 Exclusions from the scope of a Standard may occur if activities or transactions are so specialised that they give rise to accounting issues that may need to be dealt with in a different way. Such issues arise in the accounting for expenditure on the exploration for, or development and extraction of, oil, gas and mineral deposits in extractive industries and in the case of insurance contracts. Therefore, this

Standard does not apply to expenditure on such activities and contracts. However, this Standard applies to other intangible assets used (such as computer software), and other expenditure incurred (such as start-up costs), in extractive industries or by insurers.

- 7AA The amortisation method specified in this Standard does not apply to an entity that opts to amortise the intangible assets arising from service concession arrangements in respect of toll roads recognised in the financial statements for the period ending immediately before the beginning of the first upgraded AS reporting period as per the exception given in AS 101.

Definitions

- 8 The following terms are used in this Standard with the meanings specified:

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

An *asset* is a resource:

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

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

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

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

Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.

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

***Fair value* is the value as defined under AS 113, *Fair Value Measurement*.**

An *impairment loss* is the amount by which the carrying amount of an asset exceeds its recoverable amount.

An *intangible asset* is an identifiable non-monetary asset without physical substance.

***Monetary assets* are money held and assets to be received in fixed or determinable amounts of money.**

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

The *residual value* of an intangible asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

***Useful life* is:**

- (a) the period over which an asset is expected to be available for use by an entity; or**
- (b) the number of production or similar units expected to be obtained from the asset by an entity.**

Intangible assets

- 9 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.
- 10 Not all the items described in paragraph 9 meet the definition of an intangible asset, ie, identifiability, control over a resource and existence of future economic benefits. If an item within the scope of this Standard does not meet the definition of an intangible asset, expenditure to acquire it or generate it internally is recognised as an expense when it is incurred. However, if the item is acquired in a business combination, it forms part of the goodwill recognised at the acquisition date (see paragraph 68).

Identifiability

- 11 The definition of an intangible asset requires an intangible asset to be identifiable to distinguish it from goodwill. Goodwill recognised in a business combination is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised. The future economic benefits may result from synergy between the identifiable assets acquired or from assets that, individually, do not qualify for recognition in the financial statements.
- 12 **An asset is identifiable if it either:**
- (a) **is separable, i.e., is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or**
 - (b) **arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.**

Control

- 13 An entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way.
- 14 Market and technical knowledge may give rise to future economic benefits. An entity controls those benefits if, for example, the knowledge is protected by legal rights such as copyrights, a restraint of trade agreement (where permitted) or by a legal duty on employees to maintain confidentiality.
- 15 An entity may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits from training. The entity may also expect that the staff will continue to make their skills available to the entity. However, an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.

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

Future economic benefits

- 17 The future economic benefits flowing from an intangible asset may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity. For example, the use of intellectual property in a production process may reduce future production costs rather than increase future revenues.

Recognition and measurement

- 18 The recognition of an item as an intangible asset requires an entity to demonstrate that the item meets:
- (a) the definition of an intangible asset (see paragraphs 8–17); and
 - (b) the recognition criteria (see paragraphs 21–23).

This requirement applies to costs incurred initially to acquire or internally generate an intangible asset and those incurred subsequently to add to, replace part of, or service it.

- 19 Paragraphs 25–32 deal with the application of the recognition criteria to separately acquired intangible assets, and paragraphs 33–43 deal with their application to intangible assets acquired in a business combination. Paragraph 44 deals with the initial measurement of intangible assets acquired by way of a government grant, paragraphs 45–47 with exchanges of intangible assets, and paragraphs 48–50 with the treatment of internally generated goodwill. Paragraphs 51–67 deal with the initial recognition and measurement of internally generated intangible assets.

- 20 The nature of intangible assets is such that, in many cases, there are no additions to such an asset or replacements of part of it. Accordingly, most subsequent expenditures are likely to maintain the expected future economic benefits embodied in an existing intangible asset rather than meet the definition of an intangible asset and the recognition criteria in this Standard. In addition, it is often difficult to attribute subsequent expenditure directly to a particular intangible asset rather than to the business as a whole. Therefore, only rarely will subsequent expenditure—expenditure incurred after the initial recognition of an acquired intangible asset or after completion of an internally generated intangible asset—be recognised in the carrying amount of an asset. Consistently with paragraph 63, subsequent expenditure on brands, mastheads, publishing titles, customer lists and items similar in substance (whether externally acquired or internally generated) is always recognised in profit or loss as incurred. This is because such expenditure cannot be distinguished from expenditure to develop the business as a whole.
- 21 **An intangible asset shall be recognised if, and only if:**
- (a) **it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and**
 - (b) **the cost of the asset can be measured reliably.**
- 22 **An entity shall assess the probability of expected future economic benefits using reasonable and supportable assumptions that represent management’s best estimate of the set of economic conditions that will exist over the useful life of the asset.**
- 23 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.
- 24 **An intangible asset shall be measured initially at cost.**

Separate acquisition

- 25 Normally, the price an entity pays to acquire separately an intangible asset will reflect expectations about the probability that the expected future economic benefits embodied in the asset will flow to the entity. In other words, the entity expects there to be an inflow of economic benefits, even if there is uncertainty about the timing or the amount of the inflow. Therefore, the probability recognition criterion in paragraph 21(a) is always considered to be satisfied for separately acquired intangible assets.
- 26 In addition, the cost of a separately acquired intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.

- 27 The cost of a separately acquired intangible asset comprises:
- (a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
 - (b) any directly attributable cost of preparing the asset for its intended use.
- 28 Examples of directly attributable costs are:
- (a) costs of employee benefits (as defined in AS 19) arising directly from bringing the asset to its working condition;
 - (b) professional fees arising directly from bringing the asset to its working condition; and
 - (c) costs of testing whether the asset is functioning properly.
- 29 Examples of expenditures that are not part of the cost of an intangible asset are:
- (a) costs of introducing a new product or service (including costs of advertising and promotional activities);
 - (b) costs of conducting business in a new location or with a new class of customer (including costs of staff training); and
 - (c) administration and other general overhead costs.
- 30 Recognition of costs in the carrying amount of an intangible asset ceases when the asset is in the condition necessary for it to be capable of operating in the manner intended by management. Therefore, costs incurred in using or redeploying an intangible asset are not included in the carrying amount of that asset. For example, the following costs are not included in the carrying amount of an intangible asset:
- (a) costs incurred while an asset capable of operating in the manner intended by management has yet to be brought into use; and
 - (b) initial operating losses, such as those incurred while demand for the asset's output builds up.
- 31 Some operations occur in connection with the development of an intangible asset, but are not necessary to bring the asset to the condition necessary for it to be capable of operating in the manner intended by management. These incidental operations may occur before or during the development activities. Because incidental operations are not necessary to bring an asset to the condition necessary for it to be capable of operating in the manner intended by management, the

income and related expenses of incidental operations are recognised immediately in profit or loss, and included in their respective classifications of income and expense.

- 32 If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. The difference between this amount and the total payments is recognised as interest expense over the period of credit unless it is capitalised in accordance with AS 23, *Borrowing Costs*.

Acquisition as part of a business combination

- 33 In accordance with AS 103, *Business Combinations*, if an intangible asset is acquired in a business combination, the cost of that intangible asset is its fair value at the acquisition date. The fair value of an intangible asset will reflect market participants' expectations at the acquisition date about the probability that the expected future economic benefits embodied in the asset will flow to the entity. In other words, the entity expects there to be an inflow of economic benefits, even if there is uncertainty about the timing or the amount of the inflow. Therefore, the probability recognition criterion in paragraph 21(a) is always considered to be satisfied for intangible assets acquired in business combinations. If an asset acquired in a business combination is separable or arises from contractual or other legal rights, sufficient information exists to measure reliably the fair value of the asset. Thus, the reliable measurement criterion in paragraph 21(b) is always considered to be satisfied for intangible assets acquired in business combinations.

- 34 In accordance with this Standard and AS 103, an acquirer recognises at the acquisition date, separately from goodwill, an intangible asset of the acquiree, irrespective of whether the asset had been recognised by the acquiree before the business combination. This means that the acquirer recognises as an asset separately from goodwill an in-process research and development project of the acquiree if the project meets the definition of an intangible asset. An acquiree's in-process research and development project meets the definition of an intangible asset when it:

- (a) meets the definition of an asset; and
- (b) is identifiable, i.e., is separable or arises from contractual or other legal rights.

Intangible asset acquired in a business combination

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

intangible asset's fair value, there is a range of possible outcomes with different probabilities that uncertainty enters into the measurement of the asset's fair value.

- 36 An intangible asset acquired in a business combination might be separable, but only together with a related contract, identifiable asset or liability. In such cases, the acquirer recognises the intangible asset separately from goodwill, but together with the related item.
- 37 The acquirer may recognise a group of complementary intangible assets as a single asset provided the individual assets have similar useful lives. For example, the terms 'brand' and 'brand name' are often used as synonym for trademarks and other marks. However, the former are general marketing terms that are typically used to refer to a group of complimentary assets such as a trademark (or service mark) and its related trade name, formulas, recipes and technological expertise.

38-41 [Refer Appendix 1]

Subsequent expenditure on an acquired in-process research and development project

42 Research or development expenditure that:

(a) relates to an in-process research or development project acquired separately or in a business combination and recognised as an intangible asset; and

(b) is incurred after the acquisition of that project

shall be accounted for in accordance with paragraphs 54–62.

43 Applying the requirements in paragraphs 54–62 means that subsequent expenditure on an in-process research or development project acquired separately or in a business combination and recognised as an intangible asset is:

- (a) recognised as an expense when incurred if it is research expenditure;
- (b) recognised as an expense when incurred if it is development expenditure that does not satisfy the criteria for recognition as an intangible asset in paragraph 57; and
- (c) added to the carrying amount of the acquired in-process research or development project if it is development expenditure that satisfies the recognition criteria in paragraph 57.

Acquisition by way of a government grant

- 44 In some cases, an intangible asset may be acquired free of charge, or for nominal consideration, by way of a government grant. This may happen when a government transfers or allocates to an entity intangible assets such as airport landing rights, licences to operate radio or television stations, import licences or quotas or rights to access other restricted resources. An entity recognises both the intangible asset and the grant in accordance with AS 20, *Accounting for Government Grants*.

Exchanges of assets

- 45 One or more intangible assets may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The following discussion refers simply to an exchange of one non-monetary asset for another, but it also applies to all exchanges described in the preceding sentence. The cost of such an intangible asset is measured 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. The acquired asset is measured in this way even if an entity cannot immediately derecognise the asset given up. If the acquired asset is not measured at fair value, its cost is measured at the carrying amount of the asset given up.
- 46 An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows are expected to change as a result of the transaction. An exchange transaction has commercial substance if:
- (a) the configuration (ie risk, timing and amount) of the cash flows of the asset received differs from the configuration of the cash flows of the asset transferred; or
 - (b) the entity-specific value of the portion of the entity's operations affected by the transaction changes as a result of the exchange; and
 - (c) the difference in (a) or (b) is significant relative to the fair value of the assets exchanged.

For the purpose of determining whether an exchange transaction has commercial substance, the entity-specific value of the portion of the entity's operations affected by the transaction shall reflect post-tax cash flows. The result of these analyses may be clear without an entity having to perform detailed calculations.

- 47 Paragraph 21(b) specifies that a condition for the recognition of an intangible asset is that the cost of the asset can be measured reliably. The fair value of an intangible asset is reliably measurable if (a) the variability in the range of reasonable fair value measurements is not significant for that asset or (b) the

probabilities of the various estimates within the range can be reasonably assessed and used when measuring fair value. If an entity is able to measure reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

Internally generated goodwill

48 Internally generated goodwill shall not be recognised as an asset.

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

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

Internally generated intangible assets

51 It is sometimes difficult to assess whether an internally generated intangible asset qualifies for recognition because of problems in:

- (a) identifying whether and when there is an identifiable asset that will generate expected future economic benefits; and
- (b) determining the cost of the asset reliably. In some cases, the cost of generating an intangible asset internally cannot be distinguished from the cost of maintaining or enhancing the entity's internally generated goodwill or of running day-to-day operations.

Therefore, in addition to complying with the general requirements for the recognition and initial measurement of an intangible asset, an entity applies the requirements and guidance in paragraphs 52–67 to all internally generated intangible assets.

52 To assess whether an internally generated intangible asset meets the criteria for recognition, an entity classifies the generation of the asset into:

- (a) a research phase; and

(b) a development phase.

Although the terms ‘research’ and ‘development’ are defined, the terms ‘research phase’ and ‘development phase’ have a broader meaning for the purpose of this Standard.

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

Research phase

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

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

- 56 Examples of research activities are:

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

Development phase

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

- (a) **the technical feasibility of completing the intangible asset so that it will be available for use or sale.**
- (b) **its intention to complete the intangible asset and use or sell it.**
- (c) **its ability to use or sell the intangible asset.**

- (d) how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.**
 - (e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.**
 - (f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.**
- 58 In the development phase of an internal project, an entity can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits. This is because the development phase of a project is further advanced than the research phase.
- 59 Examples of development activities are:
- (a) the design, construction and testing of pre-production or pre-use prototypes and models;
 - (b) the design of tools, jigs, moulds and dies involving new technology;
 - (c) the design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production; and
 - (d) the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.
- 60 To demonstrate how an intangible asset will generate probable future economic benefits, an entity assesses the future economic benefits to be received from the asset using the principles in AS 36, *Impairment of Assets*. If the asset will generate economic benefits only in combination with other assets, the entity applies the concept of cash-generating units in AS 36.
- 61 Availability of resources to complete, use and obtain the benefits from an intangible asset can be demonstrated by, for example, a business plan showing the technical, financial and other resources needed and the entity's ability to secure those resources. In some cases, an entity demonstrates the availability of external finance by obtaining a lender's indication of its willingness to fund the plan.
- 62 An entity's costing systems can often measure reliably the cost of generating an intangible asset internally, such as salary and other expenditure incurred in securing copyrights or licences or developing computer software.

63 Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance shall not be recognised as intangible assets.

64 Expenditure on internally generated brands, mastheads, publishing titles, customer lists and items similar in substance cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognised as intangible assets.

Cost of an internally generated intangible asset

65 The cost of an internally generated intangible asset for the purpose of paragraph 24 is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria in paragraphs 21, 22 and 57. Paragraph 71 prohibits reinstatement of expenditure previously recognised as an expense.

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

- (a) costs of materials and services used or consumed in generating the intangible asset;
- (b) costs of employee benefits (as defined in AS 19) arising from the generation of the intangible asset;
- (c) fees to register a legal right; and
- (d) amortisation of patents and licences that are used to generate the intangible asset.

AS 23 specifies criteria for the recognition of interest as an element of the cost of an internally generated intangible asset.

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

- (a) selling, administrative and other general overhead expenditure unless this expenditure can be directly attributed to preparing the asset for use;
- (b) identified inefficiencies and initial operating losses incurred before the asset achieves planned performance; and
- (c) expenditure on training staff to operate the asset.

Example illustrating paragraph 65

An entity is developing a new production process. During 2017-2018, expenditure incurred was Rs.1,000, of which Rs.900 was incurred before 1 March 2018 and Rs.100 was incurred between 1 March 2018 and 31 March 2018. The entity is able to demonstrate that, at 1 March 2018, the production process met the criteria for recognition as an intangible asset. The recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be Rs.500.

At the end of 2018, the production process is recognised as an intangible asset at a cost of Rs.100 (expenditure incurred since the date when the recognition criteria were met, ie 1 March 2018). The Rs.900 expenditure incurred before 1 March 2018 is recognised as an expense because the recognition criteria were not met until 1 March 2018. This expenditure does not form part of the cost of the production process recognised in the balance sheet.

During 2018-19, expenditure incurred is Rs.2,000. At the end of 2019, the recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be Rs.1,900.

At the end of 2019, the cost of the production process is Rs.2,100 (Rs.100 expenditure recognised at the end of 2018 plus Rs.2,000 expenditure recognised in 2018-2019). The entity recognises an impairment loss of Rs.200 to adjust the carrying amount of the process before impairment loss (Rs.2,100) to its recoverable amount (Rs.1,900). This impairment loss will be reversed in a subsequent period if the requirements for the reversal of an impairment loss in AS 36 are met.

Recognition of an expense

68 Expenditure on an intangible item shall be recognised as an expense when it is incurred unless:

- (a) it forms part of the cost of an intangible asset that meets the recognition criteria (see paragraphs 18–67); or**
- (b) the item is acquired in a business combination and cannot be recognised as an intangible asset. If this is the case, it forms part of the amount recognised as goodwill at the acquisition date (see AS 103).**

69 In some cases, expenditure is incurred to provide future economic benefits to an entity, but no intangible asset or other asset is acquired or created that can be recognised. In the case of the supply of goods, the entity recognises such expenditure as an expense when it has a right to access those goods. In the case of the supply of services, the entity recognises the expenditure as an expense when it

receives the services. For example, expenditure on research is recognised as an expense when it is incurred (see paragraph 54), except when it is acquired as part of a business combination. Other examples of expenditure that is recognised as an expense when it is incurred include:

- (a) expenditure on start-up activities (ie start-up costs), unless this expenditure is included in the cost of an item of property, plant and equipment in accordance with AS 16. Start-up costs may consist of 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) or expenditures for starting new operations or launching new products or processes (ie pre-operating costs).
- (b) expenditure on training activities.
- (c) expenditure on advertising and promotional activities (including mail order catalogues).
- (d) expenditure on relocating or reorganising part or all of an entity.

69A An entity has a right to access goods when it owns them. Similarly, it has a right to access goods when they have been constructed by a supplier in accordance with the terms of a supply contract and the entity could demand delivery of them in return for payment. Services are received when they are performed by a supplier in accordance with a contract to deliver them to the entity and not when the entity uses them to deliver another service, for example, to deliver an advertisement to customers.

70 Paragraph 68 does not preclude an entity from recognising a prepayment as an asset when payment for goods has been made in advance of the entity obtaining a right to access those goods. Similarly, paragraph 68 does not preclude an entity from recognising a prepayment as an asset when payment for services has been made in advance of the entity receiving those services.

Past expenses not to be recognised as an asset

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

Measurement after recognition

72-73 [Refer Appendix 1]

74 After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortisation and any accumulated impairment losses.

75-87 [Refer Appendix 1]

Useful life

88 **The depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use.**

89 [Refer Appendix 1].

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

- (a) the expected usage of the asset by the entity and whether the asset could be managed efficiently by another management team;
- (b) typical product life cycles for the asset and public information on estimates of useful lives of similar assets that are used in a similar way;
- (c) technical, technological, commercial or other types of obsolescence;
- (d) 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;
- (e) expected actions by competitors or potential competitors;
- (f) the level of maintenance expenditure required to obtain the expected future economic benefits from the asset and the entity's ability and intention to reach such a level;
- (g) 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
- (h) whether the useful life of the asset is dependent on the useful life of other assets of the entity.

91 [Refer Appendix 1]

92 Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it will often be the case that their useful life is short. Expected future reductions in the selling price of an item that was produced using an intangible asset could indicate the expectation of technological or commercial obsolescence of the asset,

which, in turn, might reflect a reduction of the future economic benefits embodied in the asset.

- 92A Estimates of the useful life of an intangible asset generally become less reliable as the length of the useful life increases. This Standard adopts a presumption that the useful life of intangible assets is unlikely to exceed ten years.
- 92B In some cases, there may be persuasive evidence that the useful life of an intangible asset will be a specific period longer than ten years. In these cases, the presumption that the useful life generally does not exceed ten years is rebutted and the entity:
- (a) amortises the intangible asset over the best estimate of its useful life;
 - (b) estimates the recoverable amount of the intangible asset at least annually in order to identify any impairment loss (see paragraph 111A); and
 - (c) discloses the reasons why the presumption is rebutted and the factor(s) that played a significant role in determining the useful life of the asset (see paragraph 122(a)).
- 93 The useful life of an intangible asset may be very long but it is always finite. Uncertainty justifies estimating the useful life of an intangible asset on a prudent basis, but it does not justify choosing a life that is unrealistically short.

Example

A. An entity has purchased an exclusive right to generate hydro-electric power for sixty years. The costs of generating hydroelectric power are much lower than the costs of obtaining power from alternative sources. It is expected that the geographical area surrounding the power station will demand a significant amount of power from the power station for at least sixty years.

The entity amortises the right to generate power over sixty years, unless there is evidence that its useful life is shorter.

- 94 **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. The useful life of a reacquired right recognised as an intangible asset in a business combination is the remaining contractual period of the contract in which the right was granted and shall not include renewal periods.**

- 95 There may be both economic and legal factors influencing the useful life of an intangible asset. Economic factors determine the period over which future economic benefits will be received by the entity. Legal factors may restrict the period over which the entity controls access to these benefits. The useful life is the shorter of the periods determined by these factors.
- 96 Existence of the following factors, among others, indicates that an entity would be able to renew the contractual or other legal rights without significant cost:
- (a) there is evidence, possibly based on experience, that the contractual or other legal rights will be renewed. If renewal is contingent upon the consent of a third party, this includes evidence that the third party will give its consent;
 - (b) there is evidence that any conditions necessary to obtain renewal will be satisfied; and
 - (c) the cost to the entity of renewal is not significant when compared with the future economic benefits expected to flow to the entity from renewal.

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

Amortisation period and amortisation method

- 97 **The depreciable amount of an intangible asset shall be allocated on a systematic basis over its useful life. Amortisation shall begin when the asset is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortisation shall cease at the earlier of the date when the asset is:**
- a. **classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with AS 105 and**
 - b. **the date that the asset is derecognised.**

The amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used. The amortisation charge for each period shall be recognised in profit or loss unless this or another Standard permits or requires it to be included in the carrying amount of another asset.

- 97A As the future economic benefits embodied in an intangible asset are consumed over time, the carrying amount of the asset is reduced to reflect that consumption. This is achieved by systematic allocation of the cost of the asset, less any residual value, as an expense over the asset's useful life. Amortisation is recognised whether or

not there has been an increase in, for example, the asset's fair value or recoverable amount.

- 98 A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. The method used is selected on the basis of the expected pattern of consumption of the expected future economic benefits embodied in the asset and is applied consistently from period to period, unless there is a change in the expected pattern of consumption of those future economic benefits.
- 98A There is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. The revenue generated by an activity that includes the use of an intangible asset typically reflects factors that are not directly linked to the consumption of the economic benefits embodied in the intangible asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed. This presumption can be overcome only in the limited circumstances:
- (a) in which the intangible asset is expressed as a measure of revenue, as described in paragraph 98C; or
 - (b) when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.
- 98B In choosing an appropriate amortisation method in accordance with paragraph 98, an entity could determine the predominant limiting factor that is inherent in the intangible asset. For example, the contract that sets out the entity's rights over its use of an intangible asset might specify the entity's use of the intangible asset as a predetermined number of years (i.e. time), as a number of units produced or as a fixed total amount of revenue to be generated. Identification of such a predominant limiting factor could serve as the starting point for the identification of the appropriate basis of amortisation, but another basis may be applied if it more closely reflects the expected pattern of consumption of economic benefits.
- 98C In the circumstance in which the predominant limiting factor that is inherent in an intangible asset is the achievement of a revenue threshold, the revenue to be generated can be an appropriate basis for amortisation. For example, the right to operate a toll road could be based on a fixed total amount of revenue to be generated from cumulative tolls charged (for example, a contract could allow operation of the toll road until the cumulative amount of tolls generated from operating the road reaches Rs.100 million). In the case in which revenue has been established as the predominant limiting factor in the contract for the use of the intangible asset, the revenue that is to be generated might be an appropriate basis

for amortising the intangible asset, provided that the contract specifies a fixed total amount of revenue to be generated on which amortisation is to be determined.

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

Residual value

100 The residual value of an intangible asset shall be assumed to be zero unless:

(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or

(b) there is an active market (as defined in AS 109) 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.

- 101 The depreciable amount of an asset is determined after deducting its residual value. A residual value other than zero implies that an entity expects to dispose of the intangible asset before the end of its economic life.

- 102 An estimate of an asset's residual value is based on the amount recoverable from disposal using prices prevailing at the date of the estimate for the sale of a similar asset that has reached the end of its useful life and has operated under conditions similar to those in which the asset will be used. The residual value of an asset shall be reviewed at least at each financial year and, if expectations differ from previous estimates, the change in the asset's residual value shall be accounted for as a change in an accounting estimate in accordance with AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*.

- 103 The residual value of an intangible asset may increase to an amount equal to or greater than the asset's carrying amount. If it does, the asset's amortisation charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount.

Review of amortisation period and amortisation method

- 104 If there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the amortisation period**

and the amortisation method shall be reviewed to reflect the changed pattern. Such changes shall be accounted for as changes in accounting estimates in accordance with AS 8.

- 105 During the life of an intangible asset, it may become apparent that the estimate of its useful life is inappropriate. For example, the recognition of an impairment loss may indicate that the amortisation period needs to be changed.
- 106 Over time, the pattern of future economic benefits expected to flow to an entity from an intangible asset may change. For example, it may become apparent that a diminishing balance method of amortisation is appropriate rather than a straight-line method. Another example is if use of the rights represented by a licence is deferred pending action on other components of the business plan. In this case, economic benefits that flow from the asset may not be received until later periods.

107-110 [Refer Appendix 1]

Recoverability of the carrying amount—impairment losses

- 111 To determine whether an intangible asset is impaired, an entity applies AS 36. That Standard explains when and how an entity reviews the carrying amount of its assets, how it determines the recoverable amount of an asset and when it recognises or reverses an impairment loss.

Retirements and disposals

112 An intangible asset shall be derecognised:

(a) on disposal; or

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

113 The gain or loss arising from the derecognition of an intangible asset shall be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It shall be recognised in profit or loss when the asset is derecognised (unless AS 17 requires otherwise on a sale and leaseback). Gains shall not be classified as revenue.

114 The disposal of an intangible asset may occur in a variety of ways (e.g., by sale, by entering into a finance lease, or by donation). In determining the date of disposal of such an asset, an entity applies the criteria in AS 18, *Revenue*, for recognising revenue from the sale of goods. AS 17 applies to disposal by a sale and leaseback.

115 If in accordance with the recognition principle in paragraph 21 an entity recognises in the carrying amount of an asset the cost of a replacement for part of an intangible

asset, then it derecognises the carrying amount of the replaced part. If it is not practicable for an entity to determine the carrying amount of the replaced part, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or internally generated.

- 115A In the case of a reacquired right in a business combination, if the right is subsequently reissued (sold) to a third party, the related carrying amount, if any, shall be used in determining the gain or loss on reissue.
- 116 The consideration receivable on disposal of an intangible asset is recognised initially at its fair value. 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 in accordance with AS 18 reflecting the effective yield on the receivable.
- 117 Amortisation of an intangible asset does not cease when the intangible asset is no longer used, unless the asset has been fully depreciated or is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with AS 105.

Disclosure

General

- 118 An entity shall disclose the following for each class of intangible assets, distinguishing between internally generated intangible assets and other intangible assets:**
- (a) the useful lives or the amortisation rates used;**
 - (b) the amortisation methods used;**
 - (c) the gross carrying amount and the accumulated amortisation (aggregated with accumulated impairment losses) at the beginning and end of the period;**
 - (d) [Refer Appendix 1];**
 - (e) a reconciliation of the carrying amount at the beginning and end of the period showing:**
 - (i) additions, indicating separately those from internal development and through business combinations;**

- (ii) **assets classified as held for sale or included in a disposal group classified as held for sale in accordance with AS 105 and other disposals;**
- (iii) **[Refer Appendix 1];**
- (iv) **impairment losses recognised in profit or loss during the period in accordance with AS 36 (if any);**
- (v) **impairment losses reversed in the statement of profit and loss during the period (if any);**
- (vi) **amortisation recognised during the period; and**
- (vii) **[Refer Appendix 1]**
- (viii) **other changes in the carrying amount during the period.**

119 A class of intangible assets is a grouping of assets of a similar nature and use in an entity's operations. Examples of separate classes may include:

- (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, formulae, models, designs and prototypes; and
- (g) intangible assets under development.

The classes mentioned above are disaggregated (aggregated) into smaller (larger) classes if this results in more relevant information for the users of the financial statements.

120 An entity discloses information on impaired intangible assets in accordance with AS 36 in addition to the information required by paragraph 118(e)(iv)–(v).

121 AS 8 requires an entity to disclose the nature and amount of a change in an accounting estimate that has a material effect in the current period or is expected to have a material effect in subsequent periods. Such disclosure may arise from changes in:

- (a) the assessment of an intangible asset's useful life;
- (b) the amortisation method; or
- (c) residual values.

122 An entity shall also disclose:

- (a) if an intangible asset is amortised over more than ten years, the reasons why it is presumed that the useful life of an intangible asset will exceed ten years from the date when the asset is available for use. In giving these reasons, the entity shall describe the factor(s) that played a significant role in determining the useful life of the asset.**
- (b) [Refer Appendix 1]**
- (c) [Refer Appendix 1]**
- (d) the existence and carrying amounts of intangible assets whose title is restricted and the carrying amounts of intangible assets pledged as security for liabilities.**
- (e) the amount of contractual commitments for the acquisition of intangible assets.**

123-125 [Refer Appendix 1]

Research and development expenditure

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

127 Research and development expenditure comprises all expenditure that is directly attributable to research or development activities or that can be allocated on a reasonable and consistent basis to such activities (see paragraphs 66 and 67 for guidance on the type of expenditure to be included for the purpose of the disclosure requirement in paragraph 126).

Other information

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

- (a) a description of any fully amortised intangible asset that is still in use; and
- (b) [Refer Appendix 1].

Appendix A

Intangible Assets—Web Site Costs

This appendix is an integral part of the AS.

Issue

- 1 An entity may incur internal expenditure on the development and operation of its own web site for internal or external access. A web site designed for external access may be used for various purposes such as to promote and advertise an entity's own products and services, provide electronic services, and sell products and services. A web site designed for internal access may be used to store company policies and customer details, and search relevant information.
- 2 The stages of a web site's development can be described as follows:
 - (a) Planning – includes undertaking feasibility studies, defining objectives and specifications, evaluating alternatives and selecting preferences.
 - (b) Application and Infrastructure Development – includes obtaining a domain name, purchasing and developing hardware and operating software, installing developed applications and stress testing.
 - (c) Graphical Design Development – includes designing the appearance of web pages.
 - (d) Content Development – includes creating, purchasing, preparing and uploading information, either textual or graphical in nature, on the web site before the completion of the web site's development. This information may either be stored in separate databases that are integrated into (or accessed from) the web site or coded directly into the web pages.
- 3 Once development of a web site has been completed, the Operating stage begins. During this stage, an entity maintains and enhances the applications, infrastructure, graphical design and content of the web site.
- 4 When accounting for internal expenditure on the development and operation of an entity's own web site for internal or external access, the issues are:
 - (a) whether the web site is an internally generated intangible asset that is subject to the requirements of AS 38; and
 - (b) the appropriate accounting treatment of such expenditure.

- 5 This Appendix does not apply to expenditure on purchasing, developing, and operating hardware (eg web servers, staging servers, production servers and Internet connections) of a web site. Such expenditure is accounted for under AS 16. Additionally, when an entity incurs expenditure on an Internet service provider hosting the entity's web site, the expenditure is recognised as an expense under paragraph 88 of AS 1 and the *Framework for the Preparation and Presentation of Financial Statements* issued by The Institute of Chartered Accountants of India when the services are received.
- 6 AS 38 does not apply to intangible assets held by an entity for sale in the ordinary course of business (see AS 2 and AS 11) or leases that fall within the scope of AS 17. Accordingly, this Appendix does not apply to expenditure on the development or operation of a web site (or web site software) for sale to another entity. When a web site is leased under an operating lease, the lessor applies this Appendix. When a web site is leased under a finance lease, the lessee applies this Appendix after initial recognition of the leased asset.

Accounting Principles

- 7 An entity's own web site that arises from development and is for internal or external access is an internally generated intangible asset that is subject to the requirements of AS 38.
- 8 A web site arising from development shall be recognised as an intangible asset if, and only if, in addition to complying with the general requirements described in paragraph 21 of AS 38 for recognition and initial measurement, an entity can satisfy the requirements in paragraph 57 of AS 38. In particular, an entity may be able to satisfy the requirement to demonstrate how its web site will generate probable future economic benefits in accordance with paragraph 57 (d) of AS 38 when, for example, the web site is capable of generating revenues, including direct revenues from enabling orders to be placed. An entity is not able to demonstrate how a web site developed solely or primarily for promoting and advertising its own products and services will generate probable future economic benefits, and consequently all expenditure on developing such a web site shall be recognised as an expense when incurred.
- 9 Any internal expenditure on the development and operation of an entity's own web site shall be accounted for in accordance with AS 38. The nature of each activity for which expenditure is incurred (eg training employees and maintaining the web site) and the web site's stage of development or post-development shall be evaluated to determine the appropriate accounting treatment. For example:
- (a) the Planning stage is similar in nature to the research phase in paragraphs 54-56 of AS 38. Expenditure incurred in this stage shall be recognised as an expense when it is incurred.

- (b) the Application and Infrastructure Development stage, the Graphical Design stage and the Content Development stage, to the extent that content is developed for purposes other than to advertise and promote an entity's own products and services, are similar in nature to the development phase in paragraphs 57-64 of AS 38. Expenditure incurred in these stages shall be included in the cost of a web site recognised as an intangible asset in accordance with paragraph 8 of this Appendix when the expenditure can be directly attributed and is necessary to creating, producing or preparing the web site for it to be capable of operating in the manner intended by management. For example, expenditure on purchasing or creating content (other than content that advertises and promotes an entity's own products and services) specifically for a web site, or expenditure to enable use of the content (eg a fee for acquiring a licence to reproduce) on the web site, shall be included in the cost of development when this condition is met. However, in accordance with paragraph 71 of AS 38, expenditure on an intangible item that was initially recognised as an expense in previous financial statements shall not be recognised as part of the cost of an intangible asset at a later date (eg if the costs of a copyright have been fully amortised, and the content is subsequently provided on a web site).
- (c) expenditure incurred in the Content Development stage, to the extent that content is developed to advertise and promote an entity's own products and services (eg digital photographs of products), shall be recognised as an expense when incurred in accordance with paragraph 69(c) of AS 38. For example, when accounting for expenditure on professional services for taking digital photographs of an entity's own products and for enhancing their display, expenditure shall be recognised as an expense as the professional services are received during the process, not when the digital photographs are displayed on the web site.
- (d) the Operating stage begins once development of a web site is complete. Expenditure incurred in this stage shall be recognised as an expense when it is incurred unless it meets the recognition criteria in paragraph 18 of AS 38.

10 A web site that is recognised as an intangible asset under paragraph 8 of this Appendix shall be measured after initial recognition by applying the requirements of paragraphs 74 of AS 38. The best estimate of a web site's useful life should be short.

Illustration I

Illustrative Application of the Accounting Standard to Internal Use Computer Software

This illustration, which does not form part of the Accounting Standard, provides illustrative application of the principles laid down in the Standard to internal use software and web-site costs. Its purpose is to illustrate the application of the Accounting Standard to assist in clarifying its meaning.

Computer software for internal use can be internally generated or acquired.

Internally Generated Computer Software

1. Internally generated computer software for internal use is developed or modified internally by the entity solely to meet the needs of the entity and at no stage it is planned to sell it.
2. The stages of development of internally generated software may be categorised into the following two phases:
 - Preliminary project stage, i.e., the research phase
 - Development stage

Preliminary project stage

3. At the preliminary project stage the internally generated software should not be recognised as an asset. Expenditure incurred in the preliminary project stage should be recognised as an expense when it is incurred. The reason for such a treatment is that at this stage of the software project an entity cannot demonstrate that an asset exists from which future economic benefits are probable.
4. When a computer software project is in the preliminary project stage, entities are likely to:
 - (a) Make strategic decisions to allocate resources between alternative projects at a given point in time. For example, should programmers develop a new payroll system or direct their efforts toward correcting existing problems in an operating payroll system.
 - (b) Determine the performance requirements (that is, what it is that they need the software to do) and systems requirements for the computer software project it has proposed to undertake.
 - (c) Explore alternative means of achieving specified performance requirements.

For example, should an entity make or buy the software. Should the software run on a mainframe or a client server system.

- (d) Determine that the technology needed to achieve performance requirements exists.
- (e) Select a consultant to assist in the development and/or installation of the software.

Development Stage

- 5. An internally generated software arising at the development stage should be recognised as an asset if, and only if, an entity can demonstrate all of the following:
 - (a) the technical feasibility of completing the internally generated software so that it will be available for internal use;
 - (b) the intention of the entity to complete the internally generated software and use it to perform the functions intended. For example, the intention to complete the internally generated software can be demonstrated if the entity commits to the funding of the software project;
 - (c) the ability of the entity to use the software;
 - (d) how the software will generate probable future economic benefits. Among other things, the entity should demonstrate the usefulness of the software;
 - (e) the availability of adequate technical, financial and other resources to complete the development and to use the software; and
 - (f) the ability of the entity to measure the expenditure attributable to the software during its development reliably.
- 6. Examples of development activities in respect of internally generated software include:
 - (a) Design including detailed program design - which is the process of detail design of computer software that takes product function, feature, and technical requirements to their most detailed, logical form and is ready for coding.
 - (b) Coding which includes generating detailed instructions in a computer language to carry out the requirements described in the detail program design. The coding of computer software may begin prior to, concurrent with, or subsequent to the completion of the detail program design.

At the end of these stages of the development activity, the entity has a working

model, which is an operative version of the computer software capable of performing all the major planned functions, and is ready for initial testing ("beta" versions).

- (c) Testing which is the process of performing the steps necessary to determine whether the coded computer software product meets function, feature, and technical performance requirements set forth in the product design.

At the end of the testing process, the entity has a master version of the internal use software, which is a completed version together with the related user documentation and the training materials.

Cost of internally generated software

- 7. The cost of an internally generated software is the sum of the expenditure incurred from the time when the software first met the recognition criteria for an intangible asset as stated in paragraphs 21 and 22 of this Standard and paragraph 5 above. An expenditure which did not meet the recognition criteria as aforesaid and expensed in an earlier financial statements should not be reinstated if the recognition criteria are met later.
- 8. The cost of an internally generated software comprises all expenditure that can be directly attributed or allocated on a reasonable and consistent basis to create the software for its intended use. The cost include:
 - (a) expenditure on materials and services used or consumed in developing the software;
 - (b) the salaries, wages and other employment related costs of personnel directly engaged in developing the software;
 - (c) any expenditure that is directly attributable to generating software; and
 - (d) overheads that are necessary to generate the software and that can be allocated on a reasonable and consistent basis to the software (For example, an allocation of the depreciation of fixed assets, insurance premium and rent). Allocation of overheads are made on basis similar to those used in allocating the overhead to inventories.
- 9. The following are not components of the cost of an internally generated software:
 - (a) selling, administration and other general overhead expenditure unless this expenditure can be directly attributable to the development of the software;
 - (b) clearly identified inefficiencies and initial operating losses incurred before software achieves the planned performance; and

- (c) expenditure on training the staff to use the internally generated software.

Software Acquired for Internal Use

- 10. The cost of a software acquired for internal use should be recognised as an asset if it meets the recognition criteria prescribed in paragraphs 21 and 22 of this Standard.
- 11. The cost of a software purchased for internal use comprises its purchase price, including any import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities) and any directly attributable expenditure on making the software ready for its use. Any trade discounts and rebates are deducted in arriving at the cost. In the determination of cost, matters stated in paragraphs 25 to 47 of the Standard need to be considered, as appropriate.

Subsequent expenditure

- 12. Entities may incur considerable cost in modifying existing software systems. Subsequent expenditure on software after its purchase or its completion should be recognised as an expense when it is incurred unless it meets the recognition criteria in paragraph 18 of the Standard.

Amortisation period

- 13. The depreciable amount of a software should be allocated on a systematic basis over the best estimate of its useful life. The amortisation should commence when the software is available for use.
- 14. As per this Standard, there is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. However, given the history of rapid changes in technology, computer software is susceptible to technological obsolescence. Therefore, it is likely that useful life of the software will be much shorter, say 3 to 5 years.

Amortisation method

- 15. The amortisation method used should reflect the pattern in which the software's economic benefits are consumed by the entity. If that pattern can not be determined reliably, the straight-line method should be used. The amortisation charge for each period should be recognised as an expenditure unless another Accounting Standard permits or requires it to be included in the carrying amount of another asset. For example, the amortisation of a software used in a production process is included in the carrying amount of inventories.

Appendix 1

Note: This Appendix is not a part of the Accounting Standard. The purpose of this Appendix is only to bring out the major differences, if any, between Accounting Standard (AS) 38 and the corresponding Indian Accounting Standard (Ind AS) 38, Intangible Assets.

Comparison with Ind AS 38, Intangible Assets

1. Accounting Standard (AS) corresponding to Ind AS 106, *Exploration for and Evaluation of Mineral Resources*, will not be formulated. Accordingly, reference of Ind AS 106 in paragraph 2(c) has been deleted in AS 38.
2. Accounting Standard (AS) corresponding to Ind AS 104, *Insurance Contracts*, will not be formulated. In order to clarify the position in this regard, intangible assets arising in insurance entity from contracts with policyholders have been specifically excluded from the scope of AS 38. Consequently, paragraph 2(e) has been added and paragraph 3(g) is deleted.
3. Paragraphs 3(a), 114 and 116 are modified and 3(i) is deleted in AS 38 since it has been decided to formulate AS 11, *Contractor Contracts*, and AS 18, *Revenue*, corresponding to Ind AS 11 and Ind AS 18 respectively and not to formulate AS corresponding to Ind AS 115.
4. Paragraph 44 is modified in AS 38 to align it with the provisions of AS 20, *Government Grants*.
5. Ind AS 38 permits an entity to choose either the cost model or the revaluation model as its accounting policy, whereas in AS 38 revaluation model is not permitted. Accordingly, following paragraphs are 'Deleted' in AS 38. In order to maintain consistency with paragraph numbers of Ind AS 38, the paragraph numbers have been retained in AS 38:
 - (a) Paragraph 72-73
 - (b) Paragraphs 75-87 and related headings
 - (c) Paragraph 118(e)(iii)
 - (d) Paragraph 124-125 and related headings
6. Ind AS 38 recognizes that the useful life of an intangible asset can even be indefinite subject to fulfillment of certain conditions, in which case it should not be amortised but should be tested for impairment. AS 38 is based on the assumption that the useful life of an intangible asset is always finite and included a rebuttable presumption that the useful life cannot exceed ten years from the date the asset is available for use. Accordingly, following paragraphs are 'Deleted' in AS 38:
 - (a) paragraph 89

- (b) paragraph 91
- (c) paragraphs 107-110

In order to maintain consistency with paragraph numbers of Ind AS 38, the paragraphs number have been retained in AS 38.

Consequent to above, following paragraphs are 'Modified' in AS 38:

- (a) paragraph 88 and 90
- (b) paragraph 104
- (c) paragraph 122(a)

7. An example is added after paragraph 92B in AS 38 to provide guidance about useful life of intangible assets.
8. Ind AS 38 encourages an entity to disclose a brief description of significant intangible assets controlled by the entity but not recognised as assets because they did not meet the recognition criteria in this Standard or because they were acquired or generated before this standard was effective. However, AS 38 does not contain this requirement. Accordingly, paragraph 128(b) is 'Deleted' in AS 38. In order to maintain consistency with paragraph numbers of Ind AS 38, the paragraphs number have been retained in AS 38.
9. Following paragraph numbers appear as 'Deleted' in Ind AS 38. In order to maintain consistency with paragraph numbers of Ind AS 38, the paragraphs number have been retained in AS 38:
 - (a) Paragraph 38-41
10. AS 38 requires less disclosures since it is considered to be too onerous to disclose the provisions contained in Ind AS 38. Accordingly, paragraphs 118(d) and 118(e)(vii), 122(b)-(c), 123 and 128 are deleted. However, in order to maintain consistency with Ind AS 38, paragraph numbers have been retained in AS 38.
11. An Illustration is included in AS 38 to provide guidance on Application of Accounting Standard to Internal use Computer Software.

Appendix 2

Note: This Appendix is not a part of the Accounting Standard. The purpose of this Appendix is only to bring out the major differences, if any, between Accounting Standard (AS) 26, Intangible Assets and Accounting Standard (AS) 38, Intangible Assets

Comparison with AS 26, Intangible Assets

1. AS 38 contains scope exclusion with regard to the amortization method for intangible assets arising from service concession arrangements in respect of toll roads recognised in the financial statements before the beginning of the first upgraded AS reporting period.

AS 26 (paragraph 5) provides that accounting issues of specialised nature that arise in respect of accounting for discount or premium relating to borrowings and ancillary costs incurred in connection with the arrangement of borrowings, share issue expenses and discount allowed on the issue of shares are excluded from Standard. AS 38 does not include any such exclusion specifically as these are covered by other Accounting Standards.

2. AS 26 defines an intangible asset as an identifiable non-monetary asset without physical substance held for use in the production or supply of goods or services, for rental to others, or for administrative purposes whereas in AS 38, the requirement for the asset to be held for use in the production or supply of goods or services, for rental to others, or for administrative purposes has been removed from the definition of an intangible asset. (Paragraph 8 of AS 38)
3. AS 38 provides detailed guidance in respect of identifiability (paragraphs 11 and 12 of AS 38). AS 26 did not define 'identifiability', but stated that an intangible asset could be distinguished clearly from goodwill if the asset was separable, but that separability was not a necessary condition for identifiability.
4. As per AS 38, in the case of separately acquired intangibles, the criterion of probable inflow of expected future economic benefits is always considered satisfied, even if there is uncertainty about the timing or the amount of the inflow. However, there was no such provision in AS 26. (Paragraph 25 of AS 38)
5. In AS 38, there is a rebuttable presumption that an amortization method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. AS 38 allows use of revenue based method of amortisation of intangible asset, in a limited way. AS 26 did not specifically deal with revenue based amortisation method. (Paragraph 98A of AS 38)
6. Under AS 38, if payment for an intangible asset is deferred beyond normal credit terms, the difference between this amount and the total payments is recognised as

interest expense over the period of credit unless it is capitalised as per AS 23. However, there was no such provision in AS 26. (Paragraph 32 of AS 38)

7. AS 38 deals in detail in respect of intangible assets acquired in a business combination. On the other hand, AS 26 referred only to intangible assets acquired in an amalgamation in the nature of purchase and did not refer to business combinations as a whole.
8. AS 38 provides guidance for the treatment of subsequent expenditure on an in-process research and development project acquired in a business combination whereas AS 26 was silent regarding the treatment of such expenditure. (Paragraphs 42 and 43 of AS 38)
9. AS 38 require recognition of subsequent expenditure as intangible assets if it meets the definition of intangible assets and recognition criteria laid down in the standard (refer paragraph 18 and 20). AS 26 provided separate guidance for recognition of subsequent expenditure as intangible assets which was primarily based on generation of future economic benefits in excess of its originally assessed standard of performance (refer paragraph 59 of AS 26).
10. In AS 38, guidance is available on cessation of capitalisation of expenditure (Paragraph 30 of AS 38), de-recognition of a part of an intangible asset (Paragraph 115 of AS 38) and useful life of a reacquired right in a business combination (Paragraph 94 of AS 38). There was no such guidance in AS 26 on these aspects.
11. AS 38 provides more guidance on recognition of intangible items recognised as expense. AS 38 clarifies that in respect of prepaid expenses, recognition of an asset would be permitted only upto the point at which the entity has the right to access the goods or upto the receipt of services. Further, unlike AS 26, mail order catalogues have been specifically identified as a form of advertising and promotional activities which are required to be expensed.
12. AS 38 (paragraph 94) acknowledges that the useful life of an intangible asset arising from contractual or legal rights maybe shorter than the legal life. AS 26 does not include such a provision.
13. As per AS 26 (paragraph 73), there will rarely, if ever, be persuasive evidence to support an amortisation method for intangible assets that results in a lower amount of accumulated amortisation than under straight-line method. AS 38 does not contain any such provision.
14. Under AS 38, the residual value is reviewed at least at each financial year-end and, if expectations differ from previous estimates. If it increases to an amount equal to or greater than the asset's carrying amount, amortisation charge is zero unless the residual value subsequently decreases to an amount below the asset's carrying

amount. However, AS 26 specifically required that the residual value is not subsequently increased for changes in prices or value.

15. As per AS 38 (paragraph 104), change in the method of amortisation is a change in accounting estimate whereas as per AS 26, this was a change in accounting policy.
16. AS 38 also requires certain additional disclosures as compared to AS 26.
17. AS 38 does not deal with the assets 'held for sale' because the treatment of such assets is covered in Ind AS 105, *Non-current Assets Held for Sale and Discontinued Operations*. AS 26 dealt with accounting for intangible assets retired from active use and held for sale.