GROUP OF 100

POLICY STATEMENT
INTANGIBLE ASSETS

June 2005

The Group of 100 first issued a Statement of Principles on Intangible Assets in 1994 in which it expressed the view that goodwill should not normally be amortised but rather should be subject to an annual impairment test. This approach to accounting for purchased goodwill is now required under IASB Standards and Australian equivalents to IASB Standards.

This Policy Statement is prepared in the context of the Group of 100's policy on adoption of IASB Standards with effect from 2005, the IASB/AASB research project on intangible assets leading to a review of AASB 138/IAS 38 'Intangible Assets' and the heightened awareness of the significance of intangible assets to the value of a business.

This Policy Statement deals with intangible assets as defined and included within the scope of AASB 138/IAS 38 and, as such, does not deal with purchased or internally developed goodwill. AASB 138/IAS 38 define an intangible asset as "an identifiable non-monetary asset without physical substance". Consistent with the scope of AASB 138/IAS 38 this Policy Statement does not deal with mineral rights and expenditure on the exploration for, or development and extraction of, minerals, oil, natural gas and similar non-regenerative resources.

The Group of 100 believes that:

- there should be a uniform accounting treatment for intangible assets. As a general principle all non-monetary assets (both tangible and intangible) should be treated in the same way. As with other assets, intangible assets should be treated uniformly irrespective of whether recognition and measurement derives from event-driven activities such as initial public offerings, privatisations or business combinations or whether the asset is internally generated/self-constructed;

- the lack of a consistent approach to accounting for intangible assets on a global basis erodes the credibility and comparability of financial reports and the credibility of the accounting profession. This is particularly the case where entities possessing the same or similar characteristics and assets are treated differently; and

- the use of additional note disclosure as a method of reporting intangible assets is not an adequate substitute for recognition given that disclosure and recognition have differing impacts on users' perceptions and the measurement of ratios and other variables including key performance indicators.

1. Recognition and Measurement

The G100 believes that recognition of intangible assets that satisfy recognition criteria will lead to improved financial reporting because:

- intangible assets are an important component of the value of many entities;
- recognition of intangible assets will reduce the uncertainty about firm value;
- information about intangible assets is value-relevant;
- the recognition of value-relevant information about intangible assets enhances the relevance and usefulness of financial reports;

- the absence of such value-relevant information decreases the information content of financial reports and results in potential loss of efficiency because users of financial reports are not properly informed of the assets of an entity; and
- recognition of intangible assets will mitigate the level of information asymmetry between insiders and outside (less informed) investors.

a. Initial recognition and measurement:

- An asset must be recognised where the expenditures made satisfy the definition of an asset and meet the criteria for recognition of an asset.

  Under the AASB/IASB 'Framework for the Preparation and Presentation of Financial Statements' an asset is defined as a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity. The Framework indicates that the future economic benefits embodied in an asset may flow to the entity in a number of ways including its use singly or in combination with other assets in the production of goods or services to be sold by the entity, its exchange for other assets, its use to settle a liability or distribution to the owners of the entity.

  The Framework specifies that an asset is recognised when it is probable that any future economic benefits associated with the asset will flow to the entity and the asset has a cost or value that can be measured with reliability.

- Intangible assets should only be recognised when they can be measured reliably and it is probable that future economic benefits associated with the asset will flow to the enterprise. To satisfy this criteria it is necessary that :

  ~ the role performed by the intangible asset will enhance the economic benefits which will flow to the entity in the future; and
  ~ the entity will be in a position to enjoy those benefits.

- Intangible assets should be initially recognised at cost as defined in AASB 138/IAS 38 when acquired either individually or by way of business combination, by way of contribution or internally generated. It is noted that for intangible assets recognised in a business combination and those received by way of contribution the cost is determined by reference to fair values. AASB 138/IAS 38 define cost as 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 recognized in accordance with the specific requirements of other Standards.

b. Subsequent measurement:

- In accordance with the general principle that all non-monetary assets should be treated in a consistent way, an entity should be permitted to revalue intangible assets at fair value, provided that the fair value can be measured reliably. Preferably, as for other non-monetary assets, fair value should be determined by reference to an active secondary market for that type of intangible asset or by the use of a generally accepted method of valuation under the fair value hierarchy which is robust, verifiable and transparent.

- AASB 138/IAS 38 'Intangible Assets' provides that, subsequent to initial recognition, an intangible asset shall be measured on either the cost basis or the fair value basis. However, AASB 138/IAS 38 adopt different criteria for revaluation of intangible assets (the existence of an active and liquid market) than does AASB 116/IAS 16 'Property, Plant and Equipment' in respect of other non-current assets. The G100 believes that this difference should be removed so that all non-current assets should be subject to the same revaluation rules. Additionally, the criteria in AASB 138/IAS 38 for establishing when fair value is regarded as reliably measurable for purposes of subsequent measurement differ from the criteria in AASB 138/IAS 38 for when fair value is regarded as reliably measurable in other circumstances (such as on initial recognition in a business combination). The G100 believes that this difference should be removed so that the criteria for establishing when fair value is reliably measurable are consistent within AASB 138/IAS 38. There is a range of valuation methods for determining the fair values of intangible assets which reflect a robust methodology which is verifiable and transparent. These include:

  ~ market based methods;
  ~ excess profits/premium pricing methods; and
  ~ royalty based methods.

  In addition, the use of fair value measurements and a hierarchy of approaches to determining fair values are used in respect of a variety of assets (and liabilities) and circumstances including financial instruments, property, plant and equipment and in the allocation of cost in a business combination. The use of methods that result in the determination of reliable information in respect of measuring these assets, and in business combinations in respect of acquired intangible assets, is also appropriate in respect of initially measuring intangible assets received by way of contribution.

- Revaluations, if undertaken, should be carried out on a regular and frequent basis.

- When an intangible asset is revalued the normal rules for revaluation as they apply to property, plant and equipment, should apply, namely :
  ~ the entire class of assets should be revalued;
  ~ an increase in value should be credited directly to shareholders' equity and not recycled (except to the extent that it reverses a revaluation decrease which has been previously recognised as an expense); and

~ a decrease in value should be recognised as an expense (except to the extent that it reverses a revaluation increase which has been previously credited to shareholders' equity).

2. Amortisation of Intangible Assets

Consistent with the principle that all non-monetary assets should be treated in a consistent manner the G100 believes that:

- Intangible assets should be amortised over their useful lives where the useful life is finite. Where an intangible asset is evidenced by contract or other agreement, amortisation should occur over a period no longer than the contract period, including renewal periods where renewal of the contract or licence is assured at a nominal cost.

- Those intangible assets that have an indefinite useful life should be accounted for on a similar basis to purchased goodwill and be subject to an impairment test approach.

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