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An Analysis of Intangible Asset Accounting Under Indian Accounting Standard AS-26

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Abstract: *This paper summarizes the accounting and disclosure treatment of Intangible assets under the rules promulgated by the set standard for Intangible assets in India. In India, this issue is dealt by the AS-26, "Intangible Assets", issued by the Institute of Charted Accountant (ICAI), the apex accounting institute of India. This standard was issued in 2002 and came into effect from 1-April-2003 and is mandatory for all enterprises.*

Keywords: AS - 26, Intangible assets, Recognition, Research and Development, Disclosure.

I. INTRODUCTION

The increasing importance and share of intangible assets in the balance sheet has augmented the need of accurate accounting and disclosure of Intangible Assets in the financial statements.In India, this issue is dealt by the AS-26, "Intangible Assets", issued by the Institute of Charted Accountant (ICAI), the apex accounting institute of India. This standard was issued in 2002 and came into effect from 1-April-2003 and is mandatory for all enterprises. This standard covers all type of intangible assets except- Intangible assets that are covered by another accounting standards.

- Financial assets.
- Mineral rights and expenditure on the exploration for, or development and extraction of minerals, oil, natural gas and similar non-regenerative resources. Intangible assets arising in insurance enterprises from contracts with policyholders and Expenditure in respect of termination benefits. This standard is used in combination with standards which deals with those issues which are not covered by AS26. For example, this standard does not deal with lease that fall under AS-19, Leases; goodwill arising on an amalgamation (AS-14, Accounting for Amalgamation) and goodwill arising on consolidation (AS-21, Consolidated Financial Statements); deferred tax assets (AS-22, Accounting for Taxes on Income) and lastly intangible assets held by an enterprise for sale in the ordinary course of business (AS-2, Valuation of Inventories and AS-7, Accounting for Construction Contracts). The emphasis of this chapter is mainly on AS-26. Other standards have also been referred where necessary.

RATIONAL OF THE PAPER

The main objective of this paper is to comprehend and abridge the accounting treatment of intangible assets given in AS-26.This paper has tried to emerge with significant points of AS-26 in a simplified manner.

Accounting standard- 26

This statement addresses the issues of accounting of Intangible assets acquired individually or acquired in a business combination. It also addresses how goodwill and other Intangible assets should be accounted initially and subsequently in the financial statements. The introduction of this standard is an attempt towards recognition and proper valuation of the economic benefits generated by intangible assets. Because of this standard the firms are now able to identify and value their valuable intangible assets, which were used to combine under the heading goodwill. Moreover, it has uniformed the accounting treatment for the intangible assets. The driving force behind this standard is the need of fair valuation of intangible assets as they have taken an important place in the financial statements.

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Recognition of intangible asset

An intangible asset can be recognized if it meets the definition and recognition criteria given in the standard. This standard has laid down a proper recognition criteria for intangible assets. According to this standard an intangible asset should be recognized if It is probable that the future economic benefits generated by an intangible asset will flow to the enterprise and The cost of the asset can be measured reliably. Considerable amount of judgement is required by the firm to ascertain the degree of certainty attached with the flow of economic benefits. After understanding when we can recognize an intangible asset, the next step is how to recognize these assets i.e. how to value them. An intangible asset should be measured initially at cost. Standard has divided the recognition part of intangibles into two parts ─ primary recognition and secondary recognition. Under primary recognition intangible assets are valued on the basis on which they have acquired or internally generated. Acquisition can be By way of purchase. By way of amalgamation. By way of government grant By way of exchange for another asset and By way of exchange for shares Standard has given different treatment under different types of acquisition which is discussed in the following section.

PRIMARY RECOGNITION

Separate acquisition: This kind of acquisition provides the most accurate intangible cost analysis. The standard states that the cost of an intangible asset is equal to the purchase price plus taxes, installation costs, trade discount, and any other directly related charges. It is capitalized in the books of accounts after cost estimate. Acquisition as a component of an amalgamation: Intangible assets purchased as part of an amalgamation must be reported in accordance with AS-14, Accounting for Amalgamation. worth should be assigned to identifiable intangible assets based on their fair worth on the date of amalgamation (if there was an active market) or the amount the business would have paid in an arm's length transaction (if there was no active market), according to AS-14 standard. It is not appropriate to identify a business separately if its worth cannot be accurately assessed. It must be a part of Goodwill. Acquisition by government grant: The government sometimes gives businesses intangible assets like import permits, airport landing rights, etc. for free or at a small cost. These intangibles are classified as intangible assets that were obtained via government grants. These kinds of intangible assets are accounted for using AS-12, Accounting for Government Grants.

This guideline states that intangible assets that are obtained for free via government grants should be valued at their nominal amount, while those that are obtained for a nominal amount through government grants should be valued at the purchase cost. It is also necessary to incorporate additional costs made in order to prepare the asset for usage. Acquisition by asset exchange: In this instance, an intangible asset is purchased in whole or in part in return for another asset. According to AS-10, Accounting for Fixed Assets, the cost of certain kinds of intangible assets is calculated. This guideline states that the value should be determined at the fair value of the item that was acquired or at the fair value of the asset that was given up, whichever is more obvious. Consider a lower value for intangible assets if fair value is not immediately apparent. Acquired goodwill: Acquired goodwill is the goodwill that results from an acquisition. Positive or negative acquired goodwill is possible. It is necessary to capitalize positive goodwill and display it as an asset on the balance sheet. With the exception of goodwill resulting from merger, goodwill must be evaluated for impairment on an annual basis under this standard. According to AS-14, Accounting for Amalgamation, this goodwill will be repaid over a period of three to five years.

Simply put, negative goodwill is charged to shareholder equity's capital reserve account. Internally produced goodwill is the term used to describe expenses that an organization incurs in order to create future economic advantages but that do not match the recognition requirements to be recognized as intangible assets. It is thus impossible to measure with any degree of accuracy. As a result, goodwill created internally shouldn't be recorded as an asset. Internally generated intangible assets: These are intangible assets that are produced by the organization via the two-phase process of research and development in its own right. These two stages of development serve as the foundation for accounting for internally created intangible assets.

Certain internally created intangible assets are expressly excluded from recognition under this standard because their costs cannot be accurately determined. Brands, mastheads, publication titles, and customer lists are examples of these intangible assets that are created internally. The financial accounts do not reflect these assets. The procedure outlined

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in this standard will be used to recognize any remaining internally created intangible assets in the books. The two stages of expenditure on self-generated intangible assets are the research phase and the development phase. The division of the generation process into two stages is crucial because it determines which phase's expenses will be recorded as internally created intangible assets in the book of accounts. Phase of Research: Research refers to a systematic research for knowledge acquisition.

No tangible asset development occurs during the research phase. We learn how to create a new product, service, gadget, system, etc. at this phase. Since no asset comes into physical existence from which future economic benefits can be determined, expenditures made during this period cannot be classified as intangible assets. Consequently, in accordance with AS-26, such expenses shall be deducted from the profit and loss statement at the time of incurrence. Phase of Development: Development is the use of previously acquired research information. The results of the research phase were presented in its current form at this phase. This statement states that if an internally developed intangible asset meets the following requirements, it may be recognized: An organization should show that completing an intangible asset is technically feasible. The company must demonstrate that it intends to finish the intangible asset; sufficient resources must be available (in every way) to finish the intangible asset; and the company must provide specifics on the likely future financial gains.

It must show that there is a market for the product that may be produced using that intangible asset or via internal usage of that asset. The development cost is capitalized in the book of accounts if all of the aforementioned requirements are met. The standard, however, does not specify the maximum amortization time. The price of an intangible asset created domestically The total of all expenses spent since the intangible asset first satisfies the requirements for recognition as an intangible asset is the cost of internally created intangible assets. Except for staff training costs, losses suffered prior to an asset's scheduled performance, selling, administrative, and general overheads unless directly related, all costs are included in the cost.

Secondary recognition

Subsequent expenditures are those which are done in later years of usage of an intangible asset. Standard has recognized that if the subsequent expenditure improves the performance of the asset beyond a standard performance then that expenditure should be capitalized if it can be measured. Otherwise, that expenditure should be transferred to profit and loss account. Expenditures which are not measurable should not be recognized. Consistent with above discussion, subsequent expenditure on brands, mastheads, publishing titles, customer list is always recognized as an expense. The above classification is depicted with the help of the following flowchart:-

Measurement subsequent to initial recognition

Measuring the carrying value of intangible assets for later years comes after they have been identified and recognized in the financial accounts. Intangible assets must be valued at the conclusion of each accounting period, just like physical assets. Depending on their useful life, intangible assets must either be amortized or assessed for impairment. For the following measurement of intangible assets, this standard has selected the cost model. In contrast to other nations, Indian businesses are not offered the choice of a cost or revaluation model.

Intangible assets should be carried at the following cost, according the cost model: Amortization and impairment losses accrued over time In line with AS-26 The methodical distribution of an intangible asset's depreciable amount throughout the course of its useful life is known as amortization. The difference between an asset's carrying value and its recoverable value is known as impairment loss. More knowledge of the amortization process, the life of an intangible asset, and scrap value is necessary to comprehend the idea of "subsequent recognition." The next section discusses each of these ideas using the guidelines provided by this standard. The Amortization Method AS-26 states that "the amortization method should reflect the pattern in which the enterprise is to consume the asset's economic benefits."

According to the standard, if the pattern of economic benefits cannot be accurately determined, a straight line technique should be used. Amortization may be done using the production unit approach, the straight line method, and the declining balance method. Unless there is a shift in the pattern of economic advantages, the technique to be chosen should be consistent with the pattern of economic benefit consumption and should be used year after year.

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Amortization is recorded as a cost, much like depreciation. Amortization is included in the carrying value of an intangible asset if it is used in the production process, such as in the case of inventories. Scrap value or residual value The standard states that unless there is an active market or a third party commits to buying it at the end of its useful life, scrap value shall be presumed to be zero. However, in accordance with Section 205 of the Companies Act 1956, a corporation that uses the written down value technique must submit 5% of the cost as scrap value. "The period over which the depreciable amount of an intangible asset should be allocated is known as the amortization period."asset and the goodwill valued at the time of the merger by the impairment loss amount. However, the impairment loss should be recorded in accordance with AS-28's requirements if it results from certain events or circumstances.

Retirement and disposal

When an intangible asset is disposed of or no longer projected to generate income in the future, it should be taken off the balance sheets. When an asset is sold or retired, any profit or loss should be moved to the profit and loss account. DISCLOSE Specific rules for the disclosure of information pertaining to intangible assets have been provided by the standard. It is necessary to first distinguish domestically created intangible assets from other types of intangible assets. The financial accounts should therefore provide the following details on intangible assets in accordance with AS-26: A useful existence. Technique of amortization. The total quantity of carrying assets and the total amount of amortization at the start and finish of the period. A modification to the accounting rules concerning intangible assets and its impact on financial statements. When the amortization term exceeds ten years, the reasons are disclosed. Total amount of R&D that was recorded as a cost for the time period.

Transitional provisions

This section outlines the process by which a business may transition from its previous accounting policy for the accounting of intangible assets to a new accounting policy that does, and how this change would impact the financial statements. For instance, how a business might change its accounting policy from one that does not amortize intangible assets to one that does. In this section, the following situations have been covered.

The enterprise should remove the carrying amount of an intangible asset from the balance sheet by making a corresponding adjustment in the opening balance of revenue reserves if the period determined under this standard has ended (1-04-2003) and the enterprise is adhering to a policy of not amortizing an intangible asset or amortizing over a period longer than the period determined under this standard. The company must recast the carrying amount as if the cumulative amortization had been determined in accordance with the guidelines of this standard if the period has not ended and the company policy is not to amortize an intangible asset. The initial balance of revenue reserves must be adjusted accordingly.

Over the remaining time, the revised carrying amount is to be amortized. It is recommended that the enterprise amortize the carrying amount of the intangible asset over the remaining period determined by the enterprise's accounting policy if the remaining period is shorter than the balance of the period determined by this standard. The business must restate the carrying amount as though the accumulated amortization had been computed in accordance with the provisions of this standard if, in accordance with its accounting policy, the remaining period is longer than the balance of the period as determined by this standard. The initial balance of revenue reserves must be adjusted accordingly . Over the remaining time, the revised carrying amount is to be amortized. II. Final Thoughts It is clear from the discussion above that the AS-26 has adequately addressed a wide range of topics pertaining to the accounting and disclosure of intangible assets. When and how to recognize intangible assets, their subsequent recognition, the best amortization technique to use, the best amortization term, how to show intangible assets on the balance sheet, and other concerns were all addressed by the standard. This statement has helped Indian businesses with accurate intangible asset declaration and accounting, which in turn helps with accurate business valuation. A company's investors, banks, government, tax authorities, and other interested parties all depend on accurate value.

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