

# Practical considerations on Valuation and Impairment -intangibles

Presentation by:

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# Presentation agenda



- ☐ Introduction to IAS 38
- ☐ Recognition of intangible assets
- ☐ Measurement/Valuation and Impairment of intangibles
- ☐ Q&A

# Introduction



## ◆ Asset

- A resource controlled by the entity as a result of past events,
- From which future economic benefits are expected to flow to the entity

## ◆ Intangible asset

- An identifiable non-monetary asset without physical substance

# Introduction



## ◆ Intangible asset- examples:

- ✓ patented technology, computer software
- ✓ trademarks, trade dress, internet domains
- ✓ video and audiovisual material (e.g. TV programmes)
- ✓ customer lists
- ✓ mortgage servicing rights
- ✓ licensing, royalty and standstill agreements
- ✓ import quotas
- ✓ franchise agreements
- ✓ customer and supplier relationships (including customer lists)
- ✓ marketing rights

# Introduction



**Identifiable criterion is met when  
an intangible item:**

**Arises from contractual or  
other legal rights**

**or**

**Is separable**

# Introduction



## ◆ Control criterion is met when:

**Legal rights  
that are  
enforceable in  
a court of law**

**Exchange  
transactions  
for the same  
or similar item  
(= separable)**

**Other**

# Recognition of intangibles



## Separate acquisition

**Intangible item should be recognised if:**

- a) It meets the definition of an intangible asset
- b) Probable future economic benefits, and
- c) Cost can be measured reliably

## Business combination

**Intangible item should be recognised if:**

- a) It meets the definition of an intangible asset

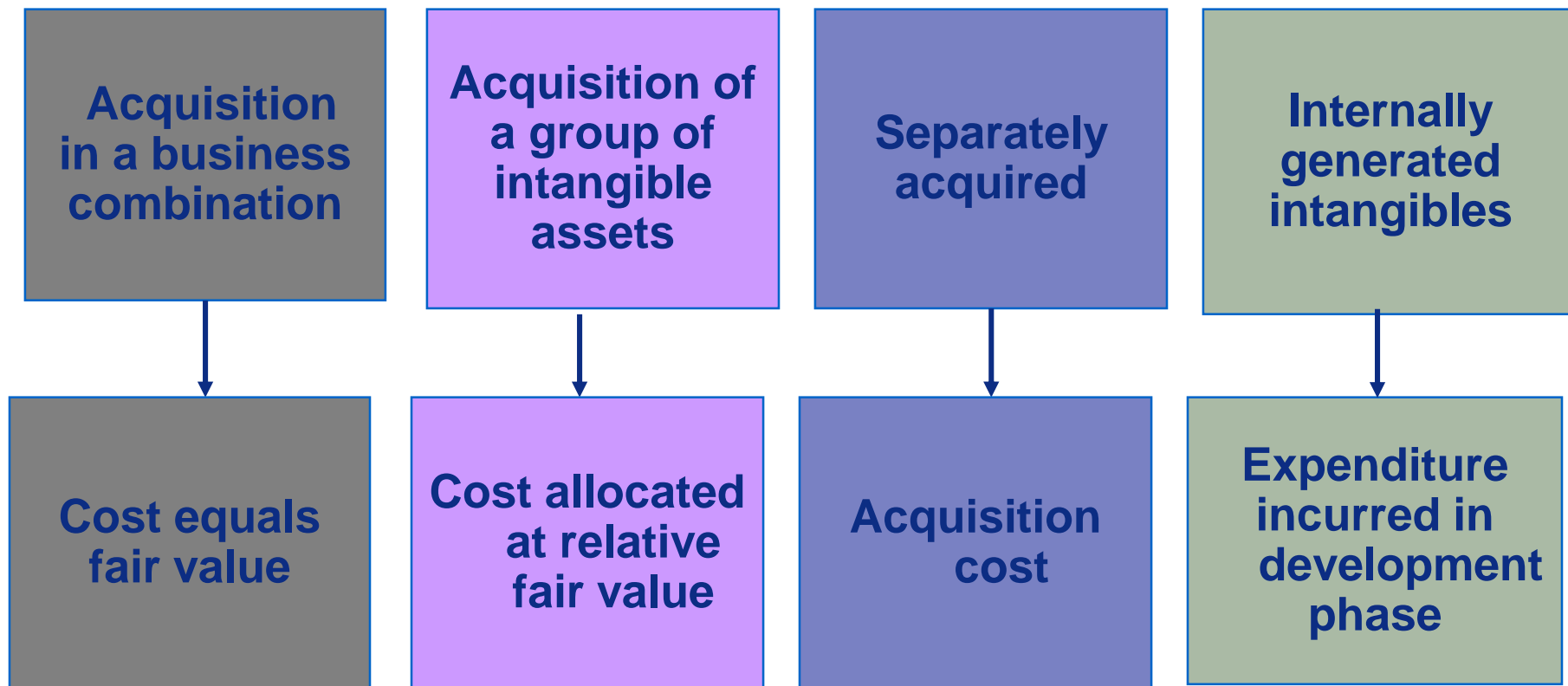
### **Intangible assets acquired separately:**

- The probability criterion (b) is always considered to be satisfied.
- The reliable measurement criterion (c) is *usually* satisfied in a *separate acquisition*

# Initial measurement



**... at cost**





# Subsequent measurement



## Cost Model

### Cost less

- amortisation (if any) and
- impairment losses (if any)

## Revaluation Model

### Revalued amount less

- amortisation (if any) and
- impairment losses (if any)

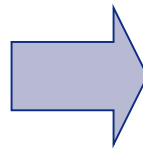
Active Market  
required !

# Useful life



## ◆ Factors to consider in determining useful life

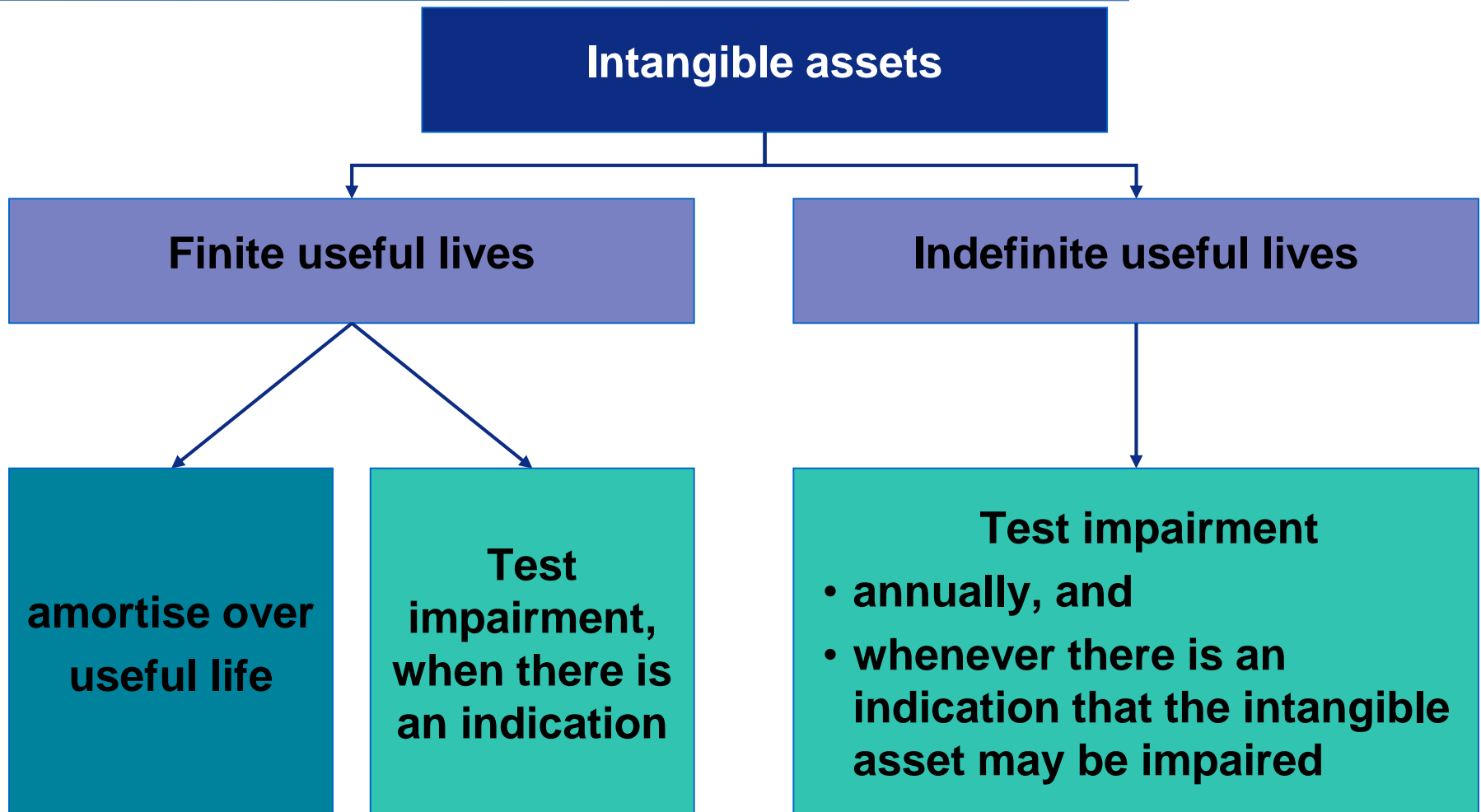
- Expected usage, life cycles, obsolescence, industry stability, competitor activity
- Period of control and legal limits, such as expiry dates
- Contractual terms and renewal periods



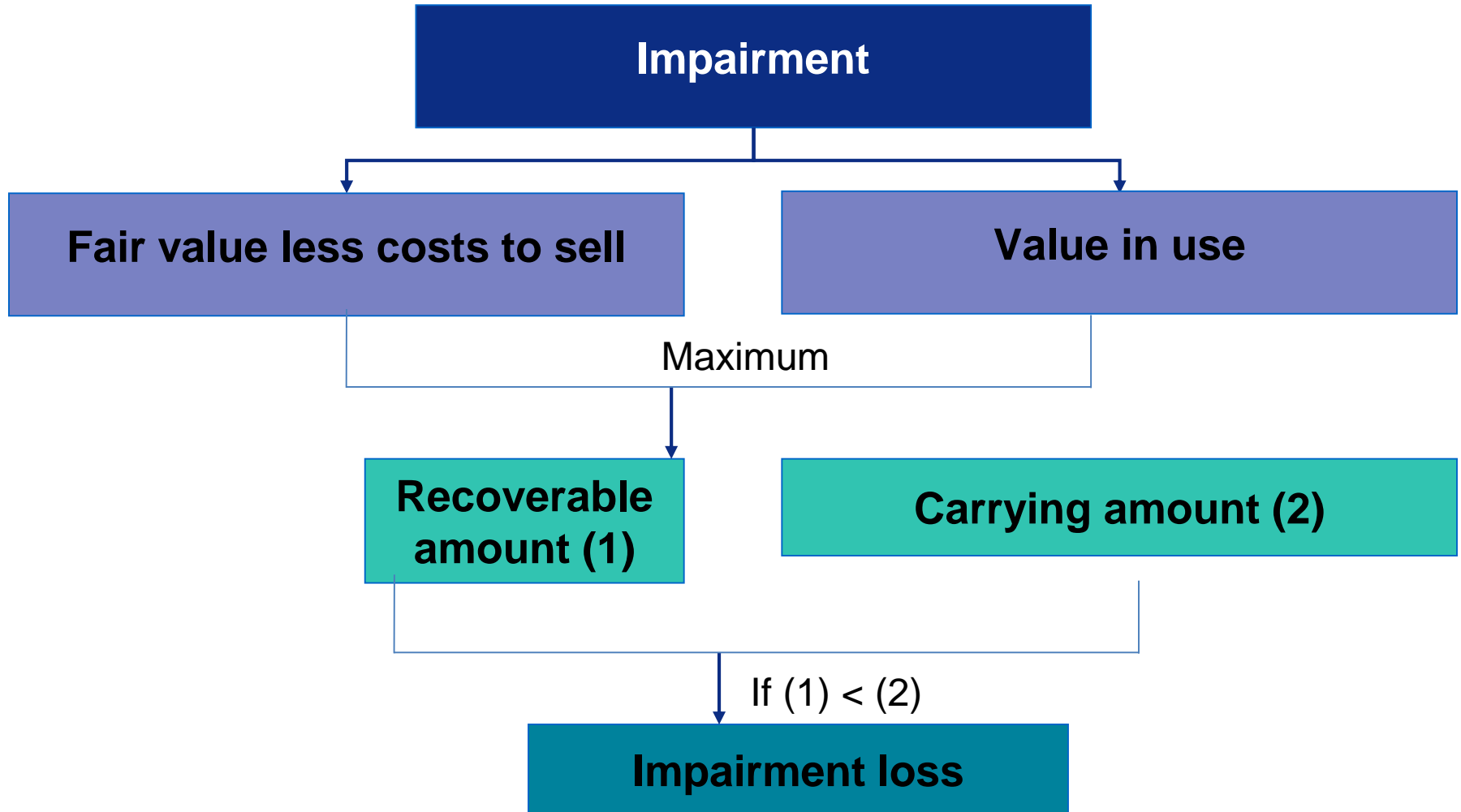
## ◆ Finite or indefinite?

- Indefinite when no foreseeable limit on period of cash inflows
- Indefinite does not mean infinite
- Do not consider planned future expenditure in excess of that required to maintain standard of performance

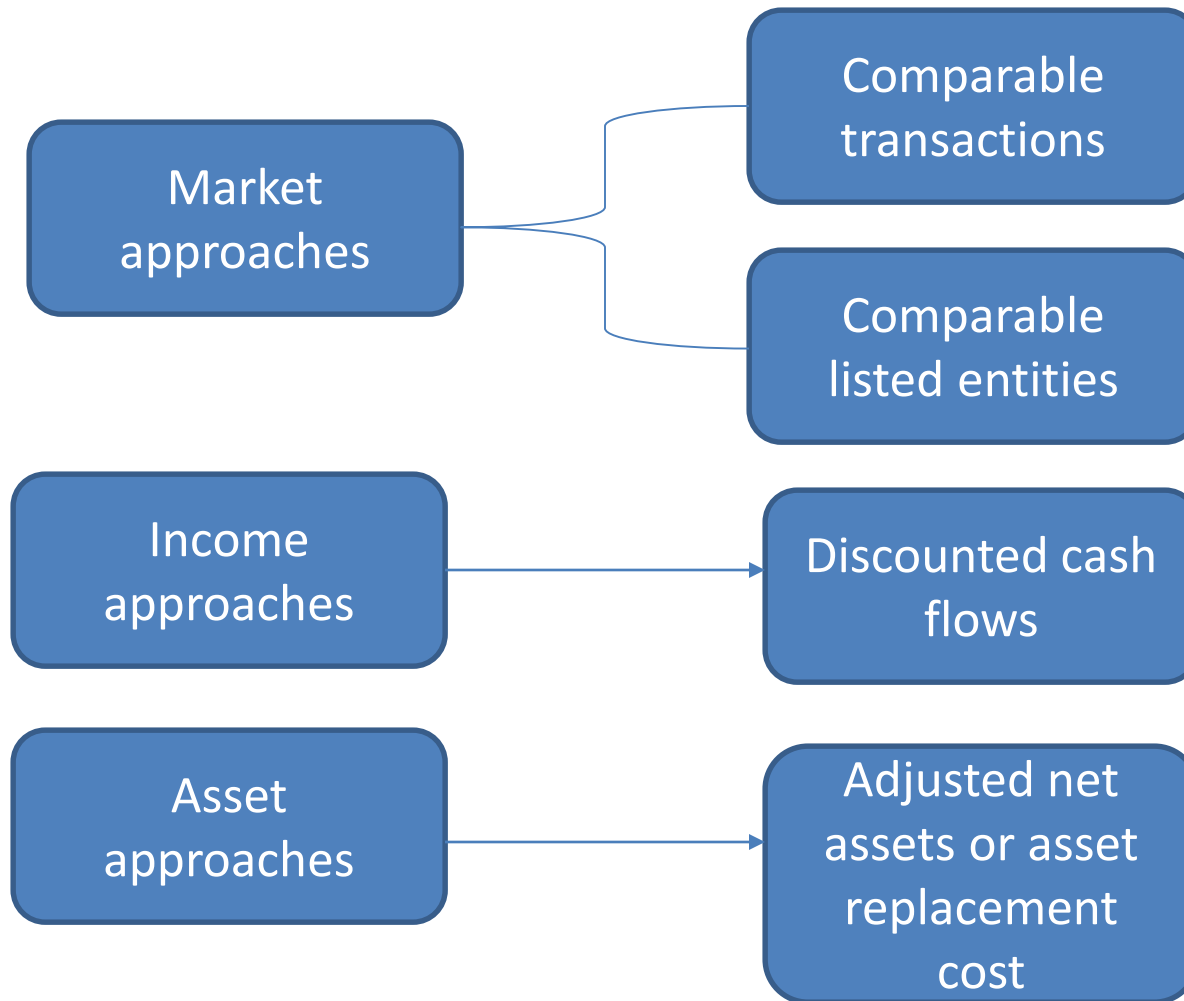
# Amortisation and impairment



# Impairment



# Valuation of intangible assets



# Intellectual property



## *Exists in three forms*

1. *Patents* – the right to exclude others from commercial exploitation of an invention for a period of 20 years in Kenya. A patent must be novel, non-obvious, and disclosed in sufficient detail so as to allow others to perform the claimed invention upon expiration of the monopoly right.
2. *Trademarks* – the right to exclude others from using a name or image associated with the delivery of a good or service for the life of its use. A trademark can be signified by the letters “™”. For maximum protection, trademarks are registered and, when examined and allowed, are indicated by the symbol ®.

# Intellectual property



## *Exists in three forms- cont'd*

3. *Copyrights* –the right to commercially control the use and distribution of a creative work or compilation. (**Literary, musical or artistic work other than photographs**) Lasts until 50 years after the death of its author or creator (In case of sound records, broadcasts - 50 *years* after the *year* in which the first recording was made). Copyrights can be registered are indicated by the symbol ©.

# Example 1



Company Y buys a five year licence to use technology owned by Company Z

1. Y agrees to pay a minimum amount of 200, 25% of which is due immediately on signing the agreement and the remaining 75% due one year later.
2. In addition to the minimum payment, Y agrees to pay Z 10% of the future revenues that will be generated with the licence technology.
3. Y's best estimate of the revenues expected to be generated if 1,000 for each year of the five years.

Question: Determine the cost of the intangible asset



# Example 2



Using example 1 above in which Company Y buys a five year licence to use technology owned by Company Z to generate revenue. assume Y pays a one-off payment of KES 10,000,000 and the following additional information:

1. Y amortises the intangible asset over the five years
2. At the start of year 3, competitors enter the market cutting down Y's market share from 100% to 40%
3. Y estimates the reduction in annual revenues to be from KES 15m per year to KES 6m per year for the next 3 years.
4. Direct cost related to generating the revenue is approx. KES 4.5m
5. Y's WACC is 10%

Question:

Determine whether the intangible asset is impaired or not.

# Example 3



A direct-mail marketing company acquires a customer list and expects that it will be able to derive benefit from the information on the list for at least one year, but no more than three years.

Question:

1. Determine the accounting policy
2. What would be a potential impairment indicators

# Example 4



The product protected by the patented technology is expected to be a source of net cash inflows for at least 15 years. The entity has a commitment from a third party to purchase that patent in five years for 60 per cent of the fair value of the patent at the date it was acquired, and the entity intends to sell the patent in five years.

Question:

1. Determine useful life
2. What would be a potential impairment indicators

# Example 5



The broadcasting licence is renewable every 10 years if the entity provides at least an average level of service to its customers and complies with the relevant legislative requirements. The licence may be renewed indefinitely at little cost and has been renewed twice before the most recent acquisition. The acquiring entity intends to renew the licence indefinitely and evidence supports its ability to do so. Historically, there has been no compelling challenge to the licence renewal. The technology used in broadcasting is not expected to be replaced by another technology at any time in the foreseeable future. Therefore, the licence is expected to contribute to the entity's net cash inflows indefinitely.

Question:

1. Determine useful life
2. Frequency of impairment

# Interactive Session



# Contacts



Thank you

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