

# Scientific Herald of Uzhhorod University

Series "Physics"

Journal homepage: <https://physics.uz.ua/en>

Issue 55, 2847–2854

Received: 01.11.2023. Revised: 24.02.2024. Accepted: 18.03.2024



DOI: 10.54919/physics/55.2024.284ep7

## Intangible assets of an enterprise: Peculiarities of auditing and display in accounting

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### Abstract

**Relevance.** The research relevance is determined by the rapid development and introduction of intangible assets in enterprises causing issues of their proper accounting and subsequent audit.

**Purpose.** The research aims to analyse the accounting of intangible assets of the enterprise and to consider the peculiarities of their audit.

**Methodology.** The analysis method was used to establish that problems in accounting for intangible assets arise at each of its stages, which is ultimately reflected in the final stage of work with intangible assets – audit problems. The deduction method was used to establish that the double-entry accounting system significantly limits the completeness of information on intangible assets.

**Results.** According to the results of the research, as of 2023, the enterprises of Azerbaijan apply an international approach in the accounting of intangible assets. In addition to characteristic features of intangible assets and their nature, inaccuracies in international standards concerning intangible assets are the root cause of incorrect accounting and create many problems in their accounting and further audit. These problems impede stakeholder information and reduce confidence in financial reporting and subsequent decisions to develop the company's competitive advantage in the market.

**Conclusions.** The practical significance of this study is determined the findings of the study help businesses to avoid the most common errors in accounting for intangible assets, improve their management efficiency, minimise risks and make informed decisions to achieve long-term sustainability and success in the market.

**Keywords:** stakeholder; international standards; audit problems; financial display; financial documentation.

### Introduction

In the current operating environment, Azerbaijani enterprises devote considerable attention to intangible assets, i.e., those assets of the enterprise that do not have a tangible component [1]. Their main feature is that they

provide entrepreneurs with the opportunity to utilise a wide range of resources, which can affect the increase in the market value of the company, increasing the potential for future growth [2]. But the problem is that the specificity of intangible assets as an object of accounting has difficulties

### Suggested Citation:

Musayeva N, Atakishiyeva N, Mammadova U. Intangible assets of an enterprise: Peculiarities of auditing and display in accounting. *Sci Herald Uzhhorod Univ Ser Phys.* 2024;(55):2847-2854. DOI: 10.54919/physics/55.2024.284ep7

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in displaying in the accounting of international and Azerbaijani standards. This requires a more detailed analysis of the order of their reflection in accounting for effective use in the economic activity of the enterprise. In turn, this state of affairs leads to the analysis of the peculiarities of the audit of intangible assets. Since intangible assets occupy a significant place in the formation of the value of the enterprise, the studied problem is quite relevant and appropriate. Following the relevance of the research topic, as of 2023, many studies have been conducted to investigate various aspects of accounting for intangible assets and methodological issues of developing their audit.

Y.T. Peng et al. [3] identified a significant advantage of intangible assets for businesses. The most important advantage is that intangible assets can act as an additional choice of the company as a financing tool when companies face financial difficulties. However, enterprises face significant problems in accounting for such assets. Ž. Savickaitė [4] revealed a significant gap between the book value and market value that intangible assets create in a company. Similar conclusions were also reached by D. Dancaková et al. [5]. However, in the process of the study, researchers were able to identify an interesting fact about the relationship between intangible assets and the market valuation of companies. Companies are still not sufficiently motivated to disclose the actual value of the expenditure on the studied assets in their financial statements due to the persistent conservatism of the accounting standards they follow. Y.U. Rozmatovna [6], while investigating the improvement of accounting and auditing of intangible assets, determined that difficulties in accounting for intangible assets appear at each of the accounting transactions: book entry, amortisation, and write-off. A.A. Prabhawa and M. Nasih [7] focused on investigating the relationship between intangible assets and audit fees. Through an empirical study, the scholars were able to find that auditors charge higher fees to companies with a higher proportion of intangible assets on the balance sheet. There are several reasons for this: the valuation process is more complex, subjectivity is present, and time costs are significant.

Nevertheless, analysing the majority of conducted research it is possible to note gaps in research concerning accounting and audit of intangible assets of Azerbaijani enterprises. The research relevance is determined by the lack of similar studies. The study of this issue will reveal the peculiarities and problems faced by enterprises in the Republic of Azerbaijan. Besides, modern requirements in the field of accounting of intangible assets, including International Financial Reporting Standards (IFRS), put more and more strict requirements on the correct reflection and audit of such assets. The study will draw attention to the existing problems of accounting and IFRS concerning intangible assets of enterprises. The research aims to conduct a detailed analysis of the reflection of intangible assets in the accounting of the enterprise, as well as to consider specific aspects related to their audit, considering international standards of valuation and accounting and current trends in economic development.

## Materials and Methods

Previous studies related to the topic were analysed, and categorical concepts within the topic were identified for a more accurate understanding of the subject area and identification of patterns. The research objects in the studies of Azerbaijani, English, Spanish, Ukrainian, and Chinese authors were also analysed. Primarily to fulfil the objectives of the study for a more accurate understanding of the subject area and identification of regularities with the help of the method of hermeneutics was studied the definition of the concept of “intangible assets”, its features, and characteristics. The subsequent research consisted of a thorough analysis of the content of international standards on accounting for intangible assets [1]. The main provisions and requirements that regulate the accounting of intangible assets in Azerbaijan were considered.

The main choice in determining the research design was to orient the study towards the deductive research method appropriate to the study. This method was used to draw logical conclusions based on the standards studied and the analyses conducted. This approach contributed to the systematisation and structuring of information, as well as the formation of valid and balanced conclusions. Thus, the analysis of international standards on accounting for intangible assets, conducted using the deductive research method, was an important component of this study. It provided a thorough understanding of the features and requirements governing the accounting for intangible assets and allowed for the formulation of appropriate conclusions and recommendations. The study applied the comparative method, examined inaccuracies, and discrepancies and put forward perceived accounting problems based on such inaccuracies. Each of the steps in the accounting process was investigated using the generalisation method to better understand the inaccuracies that arise initial recognition, valuation, and amortisation.

In the course of the research, the peculiarities of intangible assets audit were identified using analysis. Then, by reasoning from general to particular and vice versa, the problems that accompany both accounting and auditing of intangible assets in Azerbaijani enterprises were identified. Using a similar method, the problems related to incomplete and insufficient information on intangible assets, the complexity of their valuation and amortisation, as well as insufficient standardisation of accounting and auditing processes were investigated. For this purpose, various sources of information were analysed, including scientific articles, books, journal publications, and other studies related to the topic and purpose of the research. The abstract-logical method was used to form conclusions based on the findings. Earlier in the research, the main problems and inaccuracies in accounting and auditing of intangible assets were identified, and at the final stage recommendations and solutions to overcome them were proposed. In addition, an important component of the use of the abstract-logical method was the consideration of possible consequences and effects of the recommendations on the activities of enterprises in the future. This made it possible to propose more meaningful and sustainable solutions that consider potential risks and benefits when implementing changes in

the practice of accounting for intangible assets and their audit.

**Results**

With the ever-increasing pressure of corporate competition and continuous changes in the economic environment, the importance of intangible assets in enterprises is becoming more and more apparent [8]. Almost all enterprises have intangible assets, but they may not always be correctly recognised in accounting. Often, accountants do not know how to properly value them and take them on the balance sheet, and it is intangible assets that give a firm a competitive advantage and significantly affect its market value [9; 10]. Accounting for intangible assets consists of many step-by-step processes, starting with the identification and classification of intangible assets and ending with their audit, which were analysed in more detail

during the study. The international accounting standard for intangible assets is IFRS, namely International Accounting Standard 38 (IAS 38), which are financial reporting standard used by firms in more than 130 countries [11; 12]. Azerbaijan uses one approach to the definition and classification of intangible assets: IFRS. Therefore, further in the paper, aspects of this approach will be considered at each of the stages, to determine the peculiarities and identify the problems of accounting and auditing of intangible assets for Azerbaijani enterprises.

Under IFRS, specifically IAS 38 Intangible Assets, an intangible asset is defined as an identifiable non-monetary asset that has no physical substance [1]. This can therefore include trademarks, development costs associated with research and development, patents, goodwill, and similar items, where anything that a company can physically own is a legal document rather than a physical item (Table 1).

**Table 1.** Intangible asset types

| Category         | Examples   |
|------------------|--|
| Contract-bound   | Licences, royalties, licensing and franchising agreements, rights to use resources (water, mineral, air), and employment contracts |
| Technology-bound | Technologies, patents, software, databases, know-how   |
| Art-bound        | Literary, artistic and musical works, video and audiovisual materials  |
| Marketing-bound  | Rights in marks for goods and services, non-competition agreements   |
| Client-bound     | Client lists and client contracts, contractual and non-contractual relationships with clients                                      |

Source: H. Mohammadzadeh [13], A.A. Prabhawa and M. Nasih [7].

Concerning the data in Table 1, five categories of intangible assets can be identified. As such, marketing-related intangible assets are words, phrases, and symbols that distinguish or identify a company (product, service), increasing its competitiveness. Customer-related intangible assets are the values created by a company’s interaction with customers, such as customer loyalty, brand reputation, customer base and customer information. Art-related intangible assets are legally represented copyrights held by individuals over their creations and expressions. Contract-related intangible assets represent the rights and obligations arising from contractual relationships. Technology-related intangible assets are intellectual resources, which may also include technical documentation, product design and processes, research, and development, as well as patent portfolios and licences to use technology [7].

The challenge in classifying intangible assets is also caused by the fact that some intangible assets have a general purpose, such as a trademark, while others are introduced for a specific purpose and are specific to a particular situation, such as a patented machine that solves a particular production problem [14]. IFRS refer to three main aspects when defining intangible assets: identification, control, and future benefits [1]. Initial recognition acts as the next step in the accounting process. Recognising an object as an intangible asset is still a serious practical and theoretical problem [6]. Since according to IFRS an intangible asset is recognised if it will generate future economic benefits and if the value of the asset can be measured reliably [1]. The next step is to determine the value of intangible assets. Several approaches can be distinguished. While intangible assets

are acquired by the company, the value is initially recognised at cost. When assessing the value of intangible assets, the cost consists of two aspects: purchase costs and related costs. If intangible assets are acquired as a result of a business combination, they are measured at fair value. Fair value is determined based on the current market value of the assets, considering supply and demand factors, risk assessment and other relevant factors. If intangible assets are acquired in exchange (a so-called “unequal exchange transaction”), they are measured at the fair value of the assets given up or promised to be given up or at the fair value of the intangible assets exchanged if measurable and reliable [1].

Under IFRS, internally generated intangible assets are categorised as intangible assets that cannot be capitalised. This means that the costs of developing or creating such intangible assets, such as research and development of new products or technologies, are generally not recognised as assets in accounting. Instead of being capitalised, the costs of creating such intangible assets are usually expensed immediately by IFRS cost principles. This means that intangible asset losses on impairment are not recognised as assets and are not subject to valuation on the balance sheet. This approach assumes that the creation of some intangible assets, such as ideas, knowledge or skills, does not have reliable future economic benefits or specific value in the market to capitalise them and account for them as assets on the company’s balance sheet. Amortisation of intangible assets is calculated under IFRS using the method of apportioning the cost over the expected useful life of the asset. This method is called the proportional amortisation method, which provides a more accurate reflection of the cost of use of intangible assets over their useful life and

allows for evenly distribution of the costs of assets in the financial statements of the company. The essence of the proportional amortisation method is that the costs of an intangible asset that are not capitalised and expensed are spread evenly over the expected useful life of the asset. Thus, each reporting period during the useful life of the asset includes an equal proportion of the costs of the asset. For intangible assets that do not have a finite useful life or that are not time-limited, amortisation is not applied following IFRS. Intangible assets with finite lives are also subject to pro-rata allocation under IFRS. It is also worth considering that IFRS provides requirements for this type of disclosure, namely useful lives, amortisation method, and losses, which are given in a note [1].

The double entry system dictates an equity credit must also be recognised if an asset is recorded as a debit on the balance sheet. If the asset is created through the expenditure of cash or in-kind, this credit is easily interpreted as investors' cash (or in-kind) given up for investment in the hope of adding value. However, if recognition of an intangible asset – organisational capital, market power, customer loyalty – is offered in the absence of such expenditure, the credit should be an increase in investors' claims on the assets. That is, if the accounting system is to account for the cash-to-cash cycle, it records only those assets that result from expenditures. This restriction on expenses in no way excludes cases where a firm invests in, for example, the acquisition of knowledge capital or customer lists. It does, however, exclude things like social capital. Which is a significant problem for the firm. An analysis of the accounting treatment of intangible assets is important not only to accountants, the accounting standard setters but also to many who are in favour of greater recognition of intangible assets: they are also interested in providing the best information to investors. The common ground is also shared by those responsible for financial reporting, management, corporate boards, and their audit committees [15].

The audit of intangible resources is a study to identify and assess the key intangible resources of an enterprise and analyse the dynamics of their relationship [16]. The requirements of International Standards on Auditing (ISA) stipulate the collection of audit evidence on which the opinion formulation process is based. ISA 500 "Evidence" defines that regarding the procedures for obtaining evidence among others belong to analytical procedures, according to ISA 520 "Analytical procedures" are defined as estimates of financial information made based on analysing the expected relationships between financial and non-financial data, covering the necessary examination of identified deviations or relationships that are inconsistent with other relevant information or significantly different from the expected values. Therefore, the audit of intangible assets initially consists of a review by independent auditors of documentation, both accounting and legal. In the audit of accounting documentation, the following points are checked first of all: the primary documents about the entry of the intangible asset on the books, the correct reflection of the amounts in the books and records and the correctness of the calculation of the initial value of intangible assets. At check of legal documentation, the following moments are checked: presence of authorisation documents which give the right of display of intangible assets, correct

carrying out of operations. Thus, the process of auditing transactions with intangible assets is based primarily on legal support, and not only on finding out the correctness and legality of accounting.

Among all possible assets of an enterprise, auditing intangible assets is the most complex. For example, goodwill, which acts as an intangible asset requires a large amount of time and specialists in a narrow field of study to assess its fair value. That is, another characteristic feature of auditing intangible assets is the increase in audit risk [17]. Finding errors in the accounting of intangible assets during the audit process by specialists may indicate imperfect accounting. However, such imperfection is primarily due to inaccuracies in the legislation that accountants rely on to account for intangible assets. According to N. Hellman [18], normative accounting research on accounting for intangible assets is relatively underdeveloped. At each of the steps considered in the study, auditors can find errors: misclassification, calculation of historical cost, amortisation, asset write-offs, and workflow. But, as a result of the study, it became clear that the most important problem is the lack of an approved effective methodology for their valuation. What is important in the audit process is that independent auditors provide error correction measures for enterprises but with the condition of subsequent re-audits, which allows enterprises to improve their accounting.

## Discussion

Following the conducted research, it should be noted that recently in modern conditions of functioning of enterprises, both internationally in general and in Azerbaijan in particular, researchers are increasingly covering various aspects of accounting and auditing of intangible assets, which present as of today significant difficulties and problems, despite the developed accounting standards. The problems and questions posed by theorists and practitioners of intangible assets are almost always formulated from an accounting perspective. The problem of intangible assets is universally regarded as an accounting problem [19-21]. In exploring international accounting standards for intangible assets, researchers R. Barker et al. [15] identified that the problems are rooted in the specialised accounting for intangible assets required by IFRS. There are inconsistencies between accounting for tangible and intangible assets without a clear basis.

Y.U. Rozmatovna [6] established in the study of the peculiarities of accounting for intangible assets that accounting for intangible assets has problems that can be conditionally divided into those that can be traced in all long-term assets, as well as those that can be identified as specific problems only for this type of assets. Accounting for intangible assets is often accompanied by problems that are common for most long-term assets: determination of initial value, and determination of useful life. But there are also problems specific only to intangible assets: the lack of possibility of their identification due to the lack of physical form. As a consequence, the difficulty arises in establishing the estimated value (especially if intangible assets are transferred on a gratuitous basis) and useful life [22; 23]. The researcher also noted the problems at three stages: accounting, amortisation, and disposal. Having analysed the international accounting standards for intangible assets

in the course of this study, it was possible to establish problems not only at the three stages but at each of the stages of accounting for intangible assets.

Considering the criteria that identify intangible assets, it can be concluded that their application can be ambiguous and requires a case-by-case assessment. An example of an intangible asset that requires a case-by-case assessment may be software developed by a company for its internal needs [24]. In some cases, this software may be recognised as an intangible asset if it has the long-term potential to generate economic benefits for the company. However, in other cases, if the software has a limited scope and the expected benefit from its use is small, it may be treated as a current expense and not recognised as an intangible asset [25]. Thus, determining the status of software as an intangible asset requires an assessment of its specific characteristics, the purposes for which it is used and the potential economic benefit to the company. A problem in the classification of intangible assets should also be noted here. Although intangible assets are assets without physical substance, many of them contribute significantly to market value, they do not meet the recognition criteria of traditional accounting standards [5; 26-28]. Different types of intangible assets require their accounting principle, method of valuation and revaluation of value. The initial difficulty of categorisation affects their further accounting and, consequently, auditing.

The study determined that significant problems occur in determining the value of intangible assets. A similar conclusion was reached by A.L. Niculita et al. [19] as a result of a study where they noted the narrow problem of calculating a certain type of intangible value. Reflecting the value of intangible assets comes with the following problem: market value, which can then be broken down into other elements. That said, knowledge and the processes that produce and integrate it are not adaptive. Market value can be influenced by many factors, such as market supply and demand, competition, industry changes and other external factors, which creates difficulties in accurately estimating it [29-31]. In addition, the knowledge and processes that form intangible assets are often unique and difficult to customise and value. For example, intellectual property, brands, or technological know-how may be unique to a particular company and have no direct analogue in the market [32]. This makes the process of valuing and determining their value more complex and requires specialised knowledge and methodologies. Looking at the problems that arise during the accounting of intangible assets, it can be concluded that their audit is also accompanied by significant difficulties. Auditing intangible assets involves different challenges than auditing tangible assets: they do not require physical verification but have a complex level of calculations [7; 33].

M.A. Jawad [20] explores the challenges of modern intangible asset auditing, citing the fact that confidence in the auditor increases the credibility of financial statements due to the high level of assurance. Absolute confidence in audit cannot be achieved for three reasons: the need for prudence, the use of necessary parameters for any accounting system and the internal control system. Auditors must be prudent in their conclusions and judgements [34]. They can perform extensive testing,

testing and data analysis, but there are still limitations that may restrict the completeness of information available to auditors when auditing intangible assets. Some events may be hidden, unpredictable or undetectable due to limited data availability. Auditors evaluate a company's financial statements in light of certain auditing standards and methodologies [35]. However, there is a possibility that these standards may not be ideal or may not consider all the characteristics of a particular company. Auditors may rely on information provided by the company, but incorrect or insufficient data may lead to inaccurate results [36]. Auditors depend on the effectiveness of a company's accounting systems and internal controls. If a company has weak or ineffective systems, this can increase the risk of errors, fraud, or misstatements in the financial statements that may go undetected by auditors, which is the challenge of auditing intangible assets [37-39].

Key audit issues have been studied by N. Abu and R. Jaffar [21]. The researchers found that frequent audits of intangible assets devalue a company's goodwill and also devalue the intangible assets themselves. Firstly, repeated audits can cause negative perceptions from stakeholders such as investors, creditors, and partners, who may see it as a sign of a company's lack of reliability or non-compliance. This may lead to a decline in the company's credibility and goodwill. Secondly, repeated audits can cause cost and time pressures for the company as they require additional resources and time from its staff and management [40; 41]. This may divert resources away from the company's core operations and development, as well as increase the cost of audit services. As a result, the value of intangible assets may be diminished in the eyes of the market, especially if these costs and time burdens are felt to be inefficient and unjustified [42-44].

After analysing all the aforementioned problems and difficulties encountered during the accounting of intangible assets, it is possible to identify the main tasks through which it will be possible to improve the accounting process, which in turn will affect the audit of intangible assets of enterprises. Firstly, it is important to provide the personnel of the enterprise with the necessary information and special knowledge to work with intangible assets. Secondly, the correct determination of the initial value of various types of intangible assets. Thirdly, determining the need for revaluation of intangible assets, and, accordingly, the methods of their valuation. Among other important tasks: the correct accrual of amortisation, which implies the exact establishment of the term of exploitation; determination of the possibility of accounting for the costs of their maintenance; formation of complete and reliable information on the presence and movement of intangible assets. Thus, it becomes clear that the need to solve accounting problems arises in all types of accounting operations. This leads to the idea that it is important to revise the legislative and regulatory framework, which is used by enterprises in the process of working with intangible assets.

## **Conclusions**

Summarising the results, it can be stated that, being quite a relevant and promising area for development, intangible assets need not only regular study of accounting and auditing aspects but also constant study of the regulatory

and legal aspects. The conducted research allowed to draw the following conclusions. The nature of intangible assets and their peculiarities initially make it difficult to carry out accounting without errors. They have no physical form, and their value can be determined based on estimation of future benefits and income streams. This requires the use of subjective estimates and assumptions, which can lead to inaccuracies and discrepancies in accounting. Analysing the conducted research, it can be concluded that international standards have their inaccuracies. This may cause additional difficulties not only in accounting but also in the audit of intangible assets. In this regard, a significant problem today is the improvement of international standards.

Double-entry accounting focuses primarily on recording financial transactions and tangible assets, which limits the completeness and accuracy of information about intangible assets. This can result in underestimation and under-reporting of their value and contribution to the success of the enterprise. Based on the analysis, the problem in legislation and inaccuracies in international standards is the starting point of all subsequent inaccuracies in accounting at each stage, and consequently

the audit of intangible assets of enterprises in Azerbaijan. Ambiguities in legislation can lead to different interpretations and practices, which creates risks of incorrect reflection and valuation of intangible assets in the financial statements. This in turn makes it difficult for stakeholders to make informed decisions and reduces confidence in the financial statements of enterprises. Given the aspects discussed in the study and the conclusions drawn about the multitude of problems in both accounting and auditing of intangible assets, it can be assumed that a promising area for further research is to investigate solutions for accounting for intangible assets that differ from recognition in the balance sheet. As well as their subsequent comparison with current practice following IFRS.

### Acknowledgements

None.

### Conflict of Interest

None.

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## Нематеріальні активи підприємства: Особливості аудиту та відображення в обліку

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### Анотація

**Актуальність.** Актуальність дослідження визначається стрімким розвитком і впровадженням нематеріальних активів на підприємствах, що зумовлює питання їх належного обліку та подальшого аудиту.

**Мета.** Метою дослідження є аналіз обліку нематеріальних активів підприємства та розгляд особливостей їх аудиту.

**Методика.** За допомогою методу аналізу встановлено, що проблеми в обліку нематеріальних активів виникають на кожному з його етапів, що в кінцевому підсумку відображається на завершальному етапі роботи з нематеріальними активами - проблемах аудиту. Методом дедукції встановлено, що система подвійного запису суттєво обмежує повноту інформації про нематеріальні активи.

**Результати.** За результатами дослідження встановлено, що станом на 2023 рік підприємства Азербайджану застосовують міжнародний підхід в обліку нематеріальних активів. Окрім характерних особливостей нематеріальних активів та їхньої природи, неточності в міжнародних стандартах щодо нематеріальних активів є першопрчиною некоректного обліку і створюють багато проблем в їхньому обліку та подальшому аудиті. Ці проблеми ускладнюють інформування зацікавлених сторін і знижують довіру до фінансової звітності та подальших рішень, спрямованих на розвиток конкурентних переваг компанії на ринку.

**Висновки.** Практична значущість даного дослідження визначається тим, що результати дослідження допомагають підприємствам уникнути найбільш поширених помилок в обліку нематеріальних активів, підвищити ефективність управління ними, мінімізувати ризики та приймати обґрунтовані рішення для досягнення довгострокової стійкості та успіху на ринку.

**Ключові слова:** стейкхолдер; міжнародні стандарти; проблеми аудиту; фінансове відображення; фінансова документація.