

QUESTION 2**21 marks****Ignore taxation.**

Comb Holdings Ltd ('Comb') is listed on the Johannesburg Stock Exchange. Comb has a 31 December financial year end. Comb prides itself on the design, manufacture and retail of innovative equipment within the mining industry. Comb has been working on the design of a new solar-powered model of its best-selling air-handling equipment AirComb2000, called Solar AirComb. The Solar AirComb will be more eco-friendly than the AirComb2000 and allow customers to use the equipment in remote mining districts across Africa where access to electricity and oil supplies is often problematic and unreliable.

Comb has manufacturing plants in Johannesburg and Port Elizabeth. Comb further plans to open two additional manufacturing plants in Nigeria and Kenya within the next three years. Comb has an extensive sales force to sell the products as well as a team of service engineers to service the products.

All costs incurred in respect of the Solar AirComb design and manufacturing project up to 31 December 2014 were expensed. The costs specifically allocated to the Solar AirComb project were as follows:

Costs incurred in respect of the Solar AirComb Project	FY2014	FY2013
	R	R
Rental of office space	1 200 000	1 050 000
Attendance of International Solar Power Convention	500 000	400 000
Salaries of staff on the team (working full time on the project)	2 300 000	2 100 000
Sponsor programme at a university for engineering students researching solar power	1 500 000	1 000 000
Prototype design	2 500 000	3 000 000
Total	8 000 000	7 550 000

On 2 January 2015 the Solar AirComb team gave a presentation on a prototype model and feasibility study to management, during which the team stated the following:

- The current AirComb2000 that Comb manufactures will be modified to incorporate the solar power source;
- A local supplier has been identified who will be able to manufacture the Comb solar power design at a competitive price; and
- According to an analysis of the current customer base and target customers, approximately 1 000 units can be sold per annum in the short term at a considerable margin. The margin is due to the innovative technology used in the Solar AirComb that competitors would take at least another three years to develop.

Immediately after the presentation management approved the project and secured additional funding from the Development Corporation.

During the six months ended 30 June 2015 Comb incurred the following additional expenditure in respect of the Solar AirComb project:

Cost description	R
Final prototype model design	3 200 000
Designs of moulds for new product	500 000
Training of staff to service the Solar AirComb equipment	2 800 000
Testing of pre-production prototype	3 000 000
Total	9 500 000

During FY2015 management concluded that the requirements of par. 57 of IAS 38 *Intangible Assets* had been met with effect from 2 January 2015 and accordingly capitalised R25 050 000 to Intangible assets: New product development. This included all costs incurred during the development of the Solar AirComb equipment. The intangible asset was ready for use in the manner intended by management on 1 July 2015. Management estimated that its useful life was five years from this date.

The following journal entries were processed in FY2015:

	Dr.	Cr.
	R	R
Intangible assets: New product development	25 050 000	
Administrative expenses (P/L)		25 050 000
<i>Capitalisation of costs: Solar AirComb</i>		
Administrative expenses (P/L)	2 505 000	
Accumulated amortisation: New product development		2 505 000
<i>Amortisation of Solar AirComb development costs from 1 July 2015 (25 050 000 / 5 x 6 /12)</i>		

**INITIAL TEST OF COMPETENCE, JUNE 2016
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QUESTION 2 – REQUIRED	Marks	
	Sub-total	Total
Critically discuss the recognition and measurement of Intangible assets: New product development, in FY2015.	20	
<ul style="list-style-type: none"> • Include any correcting journal entry(ies) that you consider appropriate. • Ignore closing entries. 		
<i>Communication skills – clarity of expression</i>	1	21
Total		21