OREGON ACCOUNTING MANUAL

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Division **Chief Financial Office**		REFERENCE/AUTHORITY ORS 293.590 GASB Statement No. 31 GASB Statement No. 51	
Policy Owner Statewide Accounting and Reporting Services			
SUBJECT Capital Assets – Intangible Assets		**APPROVED SIGNATURE** *George Naughton, Chief Financial Officer* *Signature on file*	

PURPOSE
This policy provides guidance on accounting for intangible assets, including internally generated intangible assets. The financial reporting requirements for both tangible and intangible capital assets appear in **OAM 15.60.10**, *Capital Assets – Classification and Capitalization*.

APPLICABILITY
This policy applies to all state agencies included in the State's annual financial statements, except those agencies specifically exempted by **OAM 01.05.00**.

This policy does not apply to the following intangible assets:

   a. Assets acquired or created primarily for **obtaining income or profit**.

   b. Assets resulting from **lease transactions** reported by lessees.

   c. **Goodwill** created through the combination of a government and another entity.

FORMS/EXHIBITS/INSTRUCTIONS
None.

DEFINITION
An **intangible asset** is an asset that possesses *all* of the following characteristics:

   a. It lacks physical substance. It may be contained in or on an item with physical substance, for example, software stored on a compact disc; it may be closely associated with another item that has physical substance, for example, the underlying land in the case of a right-of-way easement.

   b. It is non-financial in nature, meaning it is not in monetary form and it does not represent a claim or right to assets or a prepayment.

   c. It has an initial useful life of more than one year.

Common types of intangible assets:

- Right-of-way easements

- Other types of easements

- Land use rights, such as mineral, water, or timber rights

- Patents, copyrights, and trademarks

- Computer and website software – purchased, internally generated, or acquired through licensing agreements

Click here for **definitions**.

EXCLUSIONS AND SPECIAL SITUATIONS
None.

POLICY

101.   Agency management must ensure the proper accounting and reporting of capital assets that meet the definition of intangible assets as defined in GASB 34 and amended by GASB 51.

102.   In addition to the specific provisions of this policy, an agency must apply the general guidance contained in **OAM 15.60.10**, *Capital Assets – Classification and Capitalization*; **OAM 15.60.20**, *Depreciation and Amortization*; and **OAM 15.60.25**, *Capital Asset Impairments* to its accounting and reporting of intangible assets.

103.   The state's capitalization threshold is $5,000. Record intangible assets that cost $5,000 or more and have a useful life of more than one year in the appropriate capital asset general ledger (GL) accounts. Expense intangible assets costing less than $5,000 according to **OAM 15.55.00,** *Non-Capital Assets*.

104.   Consider land use rights, such as easements, water rights, timber rights and mineral rights, obtained through the purchase or donation of land as "bundled" with the land; do not record them as separate assets.

105.   Account for a land use right obtained by lease, contract or other similar agreement (without acquiring the underlying land) as a separate intangible asset. Record the obligation to make payments over the life of the agreement as a long-term liability.

106.   Account for and report intangible assets acquired or created primarily for obtaining income or profit as investments.

107.   Capitalize software acquired through a licensing agreement as an intangible asset, even if the license agreement refers to the arrangement as a lease. Record the obligation to make payments over the life of the agreement as a long-term liability.

108.   When a computer software system consists of more than one module or component, apply the guidance in this policy to each individual component or module separately rather than the system as a whole.

109.   Amortize intangible assets with limited lives on a straight-line basis according to **OAM 15.60.20**. Do not amortize intangible assets with indefinite lives.

110. When an agency sells or retires an intangible asset, remove the asset and accumulated amortization from the GL control accounts and subsidiary property ledger and recognize any gain or loss arising from the disposition.

111. In addition to this policy, Statewide IT Policy 107-004-010, *Information Technology Asset Inventory and Management*, applies to *all* IT assets, including intangible IT assets.

PROCEDURES

Recognition

112. Recognize an intangible asset *only* if it is identifiable. Consider an intangible asset as identifiable if it is either (1) separable, meaning the asset is capable of being separated from the agency and sold, transferred, licensed, etc.; or (2) the asset arises from contractual or other legal rights.

Land Use Rights Bundled with Property

113. Ownership of property comprises a bundle of rights that includes the right to control the use of the property. Do not report land use rights such as easements, water rights, timber rights and mineral rights obtained through the purchase or donation of land as separate assets. Although the individual rights included in the bundle of rights are separable and intangible in nature, collectively they represent the ownership of the land.

Land Use Rights Accounted for Separately

114. Account for land use rights obtained by lease, contract or other similar agreement (without acquiring the underlying land) as separate intangible assets. Record the agency's obligation to make payments over the life of the agreement as a long-term liability. Land use rights that may be obtained from a third party through a legal agreement include:

    a. The right to access land, such as an easement

    b. The right to explore or exploit natural resources, such as timber, mineral, or water rights

115. A developer may donate a right-of-way easement along with infrastructure assets. Report the easement as a separate asset rather than as infrastructure. Also, report the easement at estimated fair value based on what it would have cost to acquire the asset had it not been donated. Do not arbitrarily assign a nominal value to the easement.

Intangible Assets Acquired or Created to Obtain Income

116. Assets acquired or created primarily to obtain income or profit are not subject to this policy. For example, this policy does not apply to a copyright acquired or created by an agency that the agency uses primarily to generate royalty income.

117. However, when an agency uses an intangible asset, such as a trademark, both in its operations and to obtain revenues, professional judgment is required. To determine the primary purpose of the intangible asset, consider the amount of revenue expected to be generated versus the service capacity gained by using the intangible asset in the agency's operations.

Internally Generated Intangible Assets

118.   Consider intangible assets "internally generated" if the agency or an entity contracted by the agency creates or produces the assets. Also, consider assets acquired from a third party as internally generated if the assets require more than minimal additional effort on the part of the agency to achieve the desired service capacity.

119.   Under the "specified-conditions" approach, an agency capitalizes outlays associated with the development of internally generated intangible assets only when all of the following conditions occur:

   a.   The agency has determined the specific objective of the project and the service capacity expected upon completion of the project.

   b.   The agency has determined that it is technologically feasible to complete the project.

   c.   The agency has demonstrated that it intends to complete the project (or in the case of a multiyear project, to continue development of the intangible asset).

   This approach provides a safeguard against the capitalization of outlays that may become impaired in the future because the agency terminated the project.

120.   Expense outlays incurred *prior* to meeting the above criteria. Capitalize outlays incurred *subsequent* to meeting the criteria.

Internally Generated Computer Software

121.   When an agency develops computer software in-house, by agency personnel or by a third-party contractor, consider it internally generated. Commercially available software (purchased or licensed from a third party) that requires more than minimal additional effort to put it into operation is also internally generated.

122.   The following three stages represent activities associated with developing and installing internally generated computer software:

Preliminary Project Stage	Application Development Stage	Post-implementation/ Operation Stage
Conceptual formulation of alternatives	Design of chosen path, including software configuration and software interfaces	Application training
Evaluation of alternatives	Coding	Software maintenance
Determination of existence of needed technology	Installation to hardware	
Final selection of alternatives	Testing, including parallel processing phase	

123. <u>Preliminary Project Stage:</u> When a computer software project is in the preliminary project stage, agencies should take the following actions:

   a. Decide how to allocate resources – e.g., determine if programmers should develop a new accounts receivable subsidiary system or direct their efforts toward correcting existing problems in the current accounts receivable system.

   b. Determine the performance requirements for the computer software project – e.g., through a user needs analysis.

   c. Determine the systems requirements for the computer software project and if the technology needed to achieve performance goals exists.

   d. Explore alternative means of achieving specific performance goals – e.g., evaluating internal development of the computer software against purchase and modification of commercially available software.

   e. Select a vendor, if an agency chooses to purchase software.

   f. Select a consultant to assist in software development or installation.

124. For internally generated computer software, consider the criteria in paragraph 119 to be met only when *both* of the following actions have occurred:

   a. The activities in the preliminary project stage are complete, and

   b. Management implicitly or explicitly authorizes and commits to fund the software project (at least currently in the case of a multiyear project).

   Accordingly, expense outlays connected with activities in the preliminary project stage as incurred. For commercially available software that the agency will modify and consider internally generated, consider (a) and (b) above to have occurred when the agency commits to purchase or license the computer software.

125. <u>Application Development Stage:</u> Once the agency meets the criteria in paragraph 124, capitalize outlays related to activities in the application development stage. Capitalization stops no later than the point at which the computer software is substantially complete and operational.

126. Data conversion costs qualify as an activity of the application development stage *only* to the extent data conversion is necessary to make the computer software operational. Otherwise, treat data conversion as an activity of the post-implementation operation stage. Data conversion activities include purging or cleansing of existing data, conversion of data from the old system to the new system, and reconciliation of the data from the old system to the data in the new system.

127. <u>Post-Implementation/Operation Stage:</u> Expense outlays associated with activities in the post-implementation/operation stage as incurred.

128. The activities within the stages of development of internally generated computer software may occur in a different order than discussed above. For example, training staff to use the new system may occur during the application development stage. Regardless of the order of activities, base the decision to capitalize or expense outlays on the nature of the activity, not the timing of its occurrence.

Software Modifications, Upgrades, or Enhancements

129.   Capitalize outlays for modification of computer software already in operation according to paragraphs 124 and 125 above, if the modification results in any of the following:

   a.   An increase in the functionality of the computer software; e.g., the software performs tasks that it was previously incapable of performing.

   b.   An increase in the efficiency of the software; e.g., an increase in the level of service provided by the software without the ability to perform additional tasks.

   c.   An extension of the estimated useful life of the software.

        NOTE: Modifications that extend useful life alone without adding capacity or efficiency are rare events. Generally, an extension of useful life is the result of underestimating the original useful life. When determining the useful life, consider how maintenance activities may affect the serviceability of the software.

   If the software modification does not result in any of these outcomes, account for the modification as maintenance and expense the related outlays as incurred.

130.   In theory, outlays for a maintenance contract that covers required maintenance and any unspecified upgrades should be allocated between the upgrades that meet the conditions discussed in 129 and all other upgrades/maintenance provided by the vendor. As a practical matter, agencies may choose to establish a policy that treats all unspecified upgrades as maintenance and expense the related costs as incurred.

Computer Software with Multiple Components

131.   An agency may enter into a licensing agreement for computer software with multiple components that the agency considers internally generated (e.g., the license to use the software; modifications to meet the agency's requirements; training; routine systems maintenance; and rights to future upgrades and modifications). The agency must allocate the outlays associated with the agreement among all the individual elements based on the guidance in this policy. For example, capitalize outlays to obtain the software license as part of the application development stage and expense outlays to train the users as part of the post-implementation/operation stage.

Software Licensing Agreements

132.   Software licensing agreements are not subject to **OAM 15.60.30**, *Leases,* even if the agreement is referred to as a "lease". Agencies must capitalize the software and report it as an intangible asset. They must also record a long-term liability to recognize the obligation to make annual payments over the life of the contract.

Software Licenses Purchased as a Bundle

133.   If a large number of software licenses are purchased all at one time and installed on individual PC's, and the cost of each separate license is less than the state's capitalization threshold, treat the entire cost as a period expense. However, if the software licenses are purchased as part of a "server install" and all of the licenses are installed on one server (computer) that individual users can access, capitalize the entire purchase as a single asset if the total cost is $5,000 or more.

Capitalized Interest

134.   When a proprietary fund finances the acquisition of an internally generated intangible asset, the interest capitalization requirements discussed in **OAM 15.60.10** apply. Interest capitalization starts on the date of the borrowing and continues until the date that the asset is ready for its intended use. Interest earned during this period on unspent borrowings reduces the amount the agency capitalizes. *Capitalized interest is not included as part of the cost of assets purchased with resources from governmental funds.*

Useful Life

135.   The useful life of an intangible asset that arises from contractual or legal rights must not exceed the legal term of the rights. Consider renewal periods when determining the useful life of an intangible asset, if the agency plans to seek a renewal and the anticipated costs will be minimal. If the expected outlay for renewal is more than minimal, the agency must account for the resulting transaction as a new intangible asset.

136.   Consider an intangible asset to have an indefinite life, if there are no legal, contractual, regulatory, technological, or other factors that limit the useful life of the asset. A permanent right-of-way easement is an example of an intangible asset with an indefinite life. Do not amortize intangible assets with indefinite lives. If changes occur that cause the useful life of an intangible asset no longer to be indefinite, the agency must test the asset for impairment. Amortize the carrying value of the intangible asset, if any, following the recognition of an impairment loss over the remaining estimated useful life of the asset.

Impairment

137.   When testing an intangible asset for impairment, apply the provisions of **OAM 15.60.25,** *Capital Asset Impairments*. In addition to the examples included in OAM 15.60.25, a common indicator of impairment occurs when the agency stops development due to a change in priorities. Report internally generated intangible assets impaired by development stoppage at the lower of carrying value or fair value.

Sample Transactions

138.   An agency internally develops a computer software program for their accounts receivable system. Total outlays through final acceptance testing were $6,000, which the agency paid from its Special Revenue fund. The useful life of the software is three years. The agency decides to take a full year of amortization in the year the software is placed in service using the straight-line method. After year two, the agency determines that the software is permanently impaired and of no future use to the agency. Its fair value is zero. The agency makes the following entries:

<u>Special Revenue Fund</u>

Generic entry to record expenditure using comptroller object 5300 – Information Tech Network Software >= $5k.

DR Expenditure (C/O 5300)	6,000	
CR Cash		6,000

TC 545: To capitalize software using comptroller object 5300 - Information Tech Network Software >= $5k.

DR 0817 Data Processing Software	6,000	
DR 3074 Change in Capital Assets	6,000	
CR 3018 Invested in Capital Assets		6,000
CR 3600 GAAP Expenditure Offset-Capital Outlay (C/O 5300)		6,000

TC 542: To record amortization of software for year one and two using comptroller object 7478 - Amortization Expense-Software.

DR 3018 Invested In Capital Assets	2,000	
DR 3600 GAAP Expenditure Offset (C/O 7478)	2,000	
CR 3074 Change in Capital Assets		2,000
CR 0868 Accumulated Amortization–DP Software		2,000

TC 545R: To recognize the impairment loss using comptroller object 7510 - Gain/Loss on Capital Asset Impairment.

DR 3018 Invested in Capital Assets	2,000	
DR 3600 GAAP Expenditure Offset (C/O 7510)	2,000	
CR 0817 Data Processing Software		2,000
CR 3074 Change in Capital Assets		2,000

TC 532: To remove remaining book value.

DR 0868 Accumulated Amortization-Data Processing Software	4,000	
CR 0817 Data Processing Software		4,000

139.   Assume that the $6,000 payment in the Special Revenue fund is the first installment on a five-year software licensing agreement that totals $30,000.

TC 545: To capitalize the software licensing agreement using comptroller object 5300 - Information Tech Network Software >= $5k.

DR 0817 Data Processing Software	30,000	
DR 3074 Change in Capital Assets	30,000	
CR 3018 Invested in Capital Assets		30,000
CR 3600 GAAP Expenditure Offset-Capital Outlay (C/O 5300)		30,000

TC 459R: To record the remaining obligation under the contract.

DR 3600 GAAP Expenditure Offset-Capital Outlay (C/O 5300)	24,000	
CR 1715 Lease/Purchase Contracts Payable		24,000

TC 459: To reduce the obligation in subsequent years for payments made on the contract.

DR 1715 Lease-Purchase Contracts Payable	6,000	
CR 3600 GAAP Expenditure Offset-Capital Outlay (C/O 5300)		6,000