State of Louisiana

Division of Administration

Office of Statewide Reporting and Accounting Policy

May 27, 2009

OSRAP MEMORANDUM 09-34

TO: Fiscal Officers
              All State Entities

FROM: Afranie Adomako, CPA
              Director

SUBJECT: Implementation of GASB Statement No. 51

In June 2007, the Governmental Accounting Standards Board (GASB) issued Statement No. 51 (GASB 51), *"Accounting and Financial Reporting for Intangible Assets."* This pronouncement requires that all intangible assets subject to the provisions of this statement be classified as capital assets. GASB 51 is effective for periods beginning after June 15, 2009 (State fiscal year 2010). This memorandum summarizes the provisions of GASB 51 and provides an update to the Office of Statewide Reporting and Accounting Policy's (OSRAP) capitalization and depreciation policy for intangible assets.

An **intangible asset** is an asset with an initial life that extends beyond a single reporting period, lacks physical substance, and is nonfinancial in nature. Existing authoritative guidance related to capital assets should be applied to intangible assets subject to GASB 51. Intangible assets include easements, water rights, timber rights, patents, trademarks, and computer software which can be purchased or licensed or internally generated.

The provisions in GASB 51 do not apply to (a) intangible assets acquired or created primarily for the purpose of obtaining income or profit, (b) assets created as a result of capital lease transactions reported by lessees, or (c) goodwill created through the combination of a government and another entity (GASB 51, paragraph 3).

Per paragraph 6 of GASB 51, an intangible asset should only be recognized if it is identifiable. An asset is identifiable if it is separable; i.e., the asset is capable of being separated and sold, transferred, licensed, etc., or if the asset arises from contractual or other legal rights, regardless of whether rights are separable.

Intangible assets are amortized over their useful lives. The useful life of an intangible asset that arises from contractual or legal rights should not exceed the legal term of the rights. Renewal periods should be considered in determining the useful life if there is evidence that renewal will be sought and achieved and the cost of the renewal is nominal in relation to the level of service capacity expected to be obtained through the renewal. An intangible asset is not amortized if the asset has an indefinite useful life. An intangible asset should be considered to have an indefinite

useful life if there are no legal, contractual, regulatory, technological, or other factors that limit the useful life of the asset (GASB 51, paragraph 16). For example, a permanent right-of-way easement would have an indefinite useful life.

GASB 51, paragraph 7, states "Intangible assets are considered internally generated if they are created or produced by the government or an entity contracted by the government, or if acquired from a third-party but require more than minimal incremental effort on the part of the government to begin to achieve their expected level of service capacity." Commercially available software that is purchased or licensed, but modified by using more than minimal effort before being put into operation is also considered internally generated.

GASB 51 uses an approach called the Specified Conditions Approach for internally generated intangible assets, in which outlays are capitalized when incurred once specified conditions are fulfilled (paragraph 46 (c)). Outlays incurred up to that point are expensed as incurred. GASB 51 groups the activities involved in developing and installing internally generated computer software into the following stages (GASB 51, paragraph 10):

   a. Preliminary Project Stage: includes the conceptual formulation and evaluation of alternatives, the determination of the existence of needed technology, and final selection of alternatives for development of software. Outlays associated with activities in this stage should be expensed as incurred.

   b. Application Development Stage: includes the design of the chosen path (consisting of software configuration and interfaces), coding, installation to hardware, and testing (including parallel processing). Also includes licensing of commercially available software (GASB 51, paragraph 65).

   c. Post-Implementation/Operation Stage: includes application training and software maintenance. Outlays associated with activities in this stage should be expensed as incurred.

Only data conversion necessary to make the computer software operational is considered to be part of the application development stage; otherwise, it is part of the post-implementation/operation stage.

Outlays incurred related to the development of internally generated intangible assets should be capitalized only upon the occurrence of all the following, per paragraph 8 of GASB 51:

   a. Determination of the specific objective of the project and the nature of the service capability to be provided by the asset.

   b. Demonstration of the technological feasibility for completing the project.

   c. Demonstration of the current intention, ability, and presence of effort to complete or continue development of the asset.

These criteria could be considered to be met when both (1) the activities in the preliminary project stage are completed, and (2) management implicitly or explicitly authorizes and commits to funding the project (at least currently in the case of a multi-year project). These two conditions can be considered satisfied when the government commits to purchase or license the software.

Outlays incurred prior to meeting all of the above should be expensed as incurred, but once these criteria have been met, outlays related to activities in the application development phase should begin to be capitalized. Capitalization should continue until the computer software is substantially complete and operational. Outlays subsequent to that point should be considered part of the post-implementation/operation stage, and should be expensed as incurred.

While a project is in the application development stage, it is considered to be similar to construction in progress for tangible assets. As such, the asset is being developed and is not depreciated (for tangible assets) or amortized (for intangible assets). Once the project is substantially complete and begins to provide service utility, depreciation or amortization will begin. For internally generated computer software, this will occur when the project is in the post implementation/operation stage. The amount of amortization charged each year will be the capitalized cost of the project divided by the estimated useful life.

Generally, the provisions of GASB Statement 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, should be applied to determine impairment of intangible assets. A common indicator of impairment for internally generated intangible assets is developmental stoppage (GASB 51, paragraph 18).

Provisions of this statement should be retroactively applied except for intangible assets with unlimited useful lives or those that are internally generated. Per GASB 51, paragraph 21, if determining the actual historical cost of these intangible assets is not practical due to insufficient records, the estimated historical cost for these intangible assets acquired in fiscal years ending after June 30, 1980 should be reported.

OSRAP's current policy states that all entities capitalize purchased computer software costing $1 million or more, while only colleges and universities capitalize internally developed computer software (also costing $1 million or more). However, due to the implementation of GASB 51, effective July 1, 2009 (for FY 2010 reporting), OSRAP's policy on software capitalization is hereby revised to state that the **capitalizable costs of internally generated computer software or purchased or licensed computer software that must be more than incrementally modified will include costs that would clearly fall under the application development stage.** These items include: the design of the chosen path (including software configuration and software interfaces), coding, installation to hardware, testing (including the parallel processing phase), and data conversion (only to the extent required to make the software operational). The capitalization threshold will remain at $1 million. Preliminary Project Stage costs and Post Implementation/Operation Stage costs should be expensed.

As part of the implementation of the standard, OSRAP needs to identify all intangible assets owned by the state. We have provided a survey for you to complete on the following page. If you have any questions, contact Ms. Inga Kimbrough at (225) 219-4444 or at Inga.Kimbrough@la.gov.

AA:ik

Information Sheet for Intangible Assets – GASB 51

Agency Name:_____

Contact Name:_____

Contact Job Title: _____

Contact Number:_____

Contact Email:_____

Please list all individual intangible assets in your agency valued at $100,000 or greater except for computer software. Only list purchased or licensed computer software of $1 million or more. Internally generated software does not have to be listed at this time.

Note: Intangible assets that were created specifically with intention to sell should not be reported. For example, if an agency developed a patent with the intention of selling the patent, it should not be reported.

Type of Intangible Asset[1]	Date Acquired (if known)	Name or Description	Useful Life (if known)[2]	Value[3]

[1]**Types of Intangible Assets** include right-of-way easements, other easements, websites, copyrights, patents, trademarks, and computer software which can be purchased or licensed or internally generated. Intangible assets such as timber, gas, water or mineral rights that were acquired as a result of purchasing or owning the land on which they exist do not need to be reported since the value of those rights is included in the cost of the land.

[2]**Useful Life** should be stated in number of years and should represent the period over which the intangible will be used up or until the intangible expires, whichever is shorter.   An intangible's life is **"indefinite"** if there are no legal, contractual, regulatory, technological or other limiting factors. OSRAP would appreciate your input.

[3]**Value**, as it relates to this standard, is defined as either the purchase price or costs to develop the asset. This would include costs such as legal fees to register a trademark. The value should not be the current market value or include goodwill unless the goodwill was incurred as part of the purchase of the asset. In the event that an intangible asset has been donated, the estimated fair value at the time of acquisition should be recorded. If the value of the intangible asset cannot be determined, **"unknown"** should be listed.

Email to Inga.Kimbrough@la.gov or fax to (225) 342-1053, attention Inga Kimbrough.