Session 4

Intangible Asset in Software Development

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Intangible Asset

An intangible asset is an **identifiable** non-monetary **asset** without physical substance. [MPSAS 31.16]

Identifiable [MPSAS 31.19]

| Separable | **Capable of being separated or divided from the entity** and sold, transferred, licensed, rented, or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so |

OR

| Binding arrangements | Including rights from **contracts or other legal rights**, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations. |

Intangible Asset (cont'd)

Assets are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity. [MPSAS 1.7]
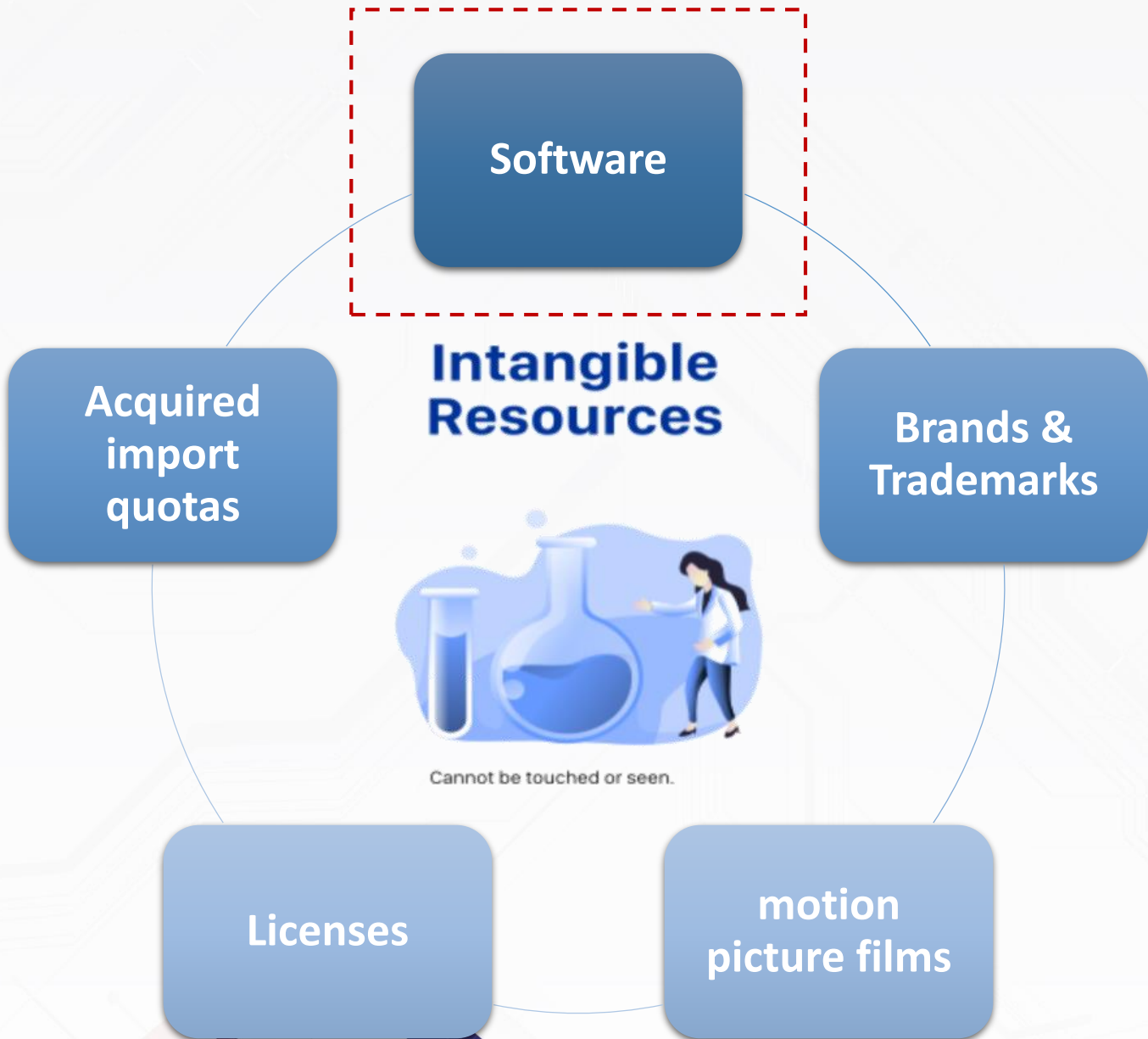
[MPSAS 31.21]

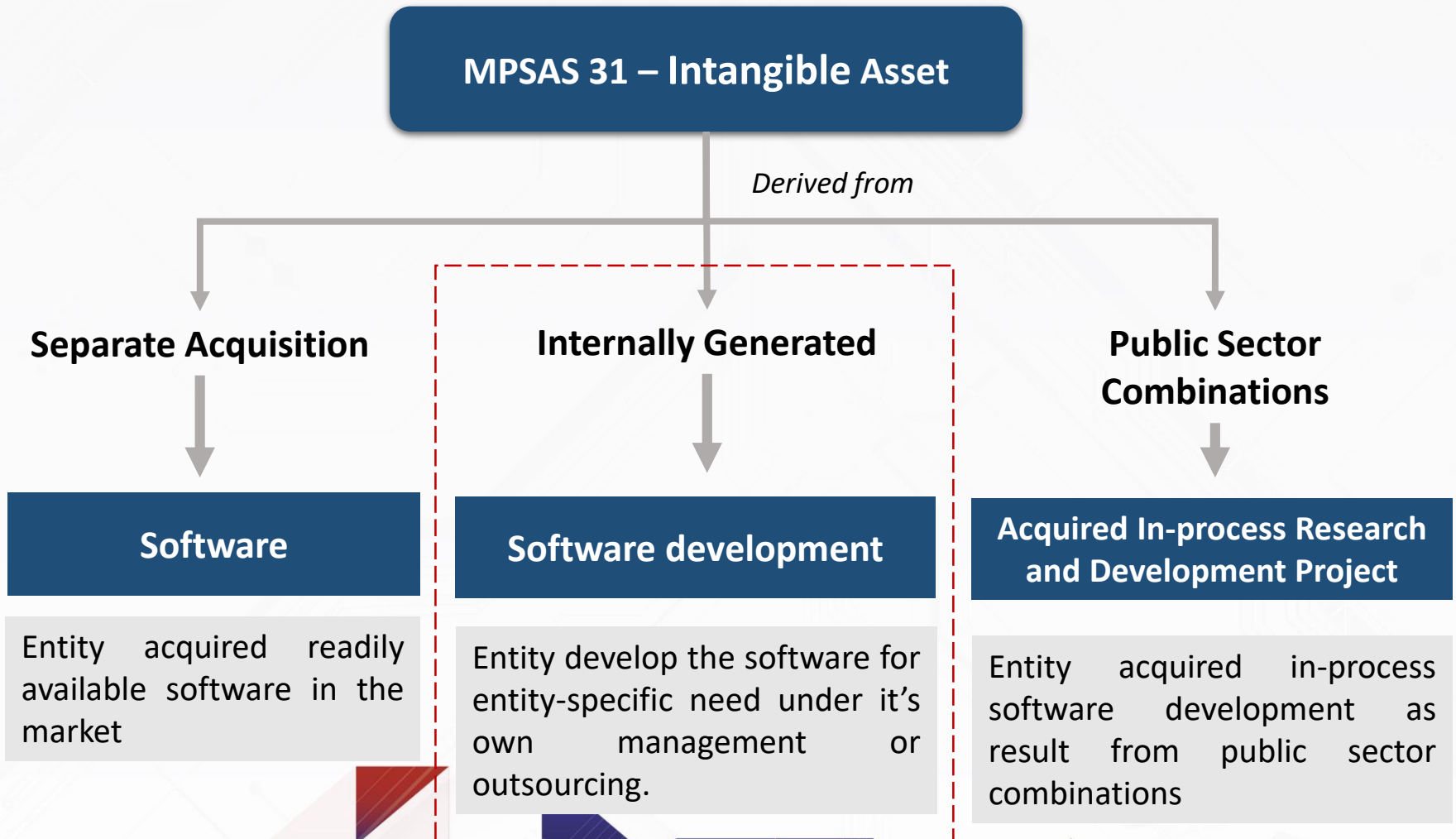| Control over resources | **Power to obtain** the future economic benefits or service potential flowing from the underlying resource and to **restrict the access** of others to those benefits or that service potential. |

| Future economic benefits or service potential | The future economic benefits or service potential flowing from an intangible asset may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity |

[MPSAS 31.25]

Software

Acquired import quotas

Intangible Resources

Brands & Trademarks

Cannot be touched or seen.

Licenses

motion picture films

Accounting treatment for Software

MPSAS 31 – Intangible Asset

Derived from

Separate Acquisition	Internally Generated	Public Sector Combinations
Software	**Software development**	**Acquired In-process Research and Development Project**
Entity acquired readily available software in the market	Entity develop the software for entity-specific need under it's own management or outsourcing.	Entity acquired in-process software development as result from public sector combinations

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Software…

Annual Subscription

An annual license will allow the customer to use the licensed software for one year. After the one year period ends, the software will no longer function unless a new license is purchased

Perpetual license

Perpetual license will allow the customer to use the licensed software indefinitely

Identifiable component in software development

Intangible component

Software is a set of instructions, data or programs used to operate computers and execute specific tasks.
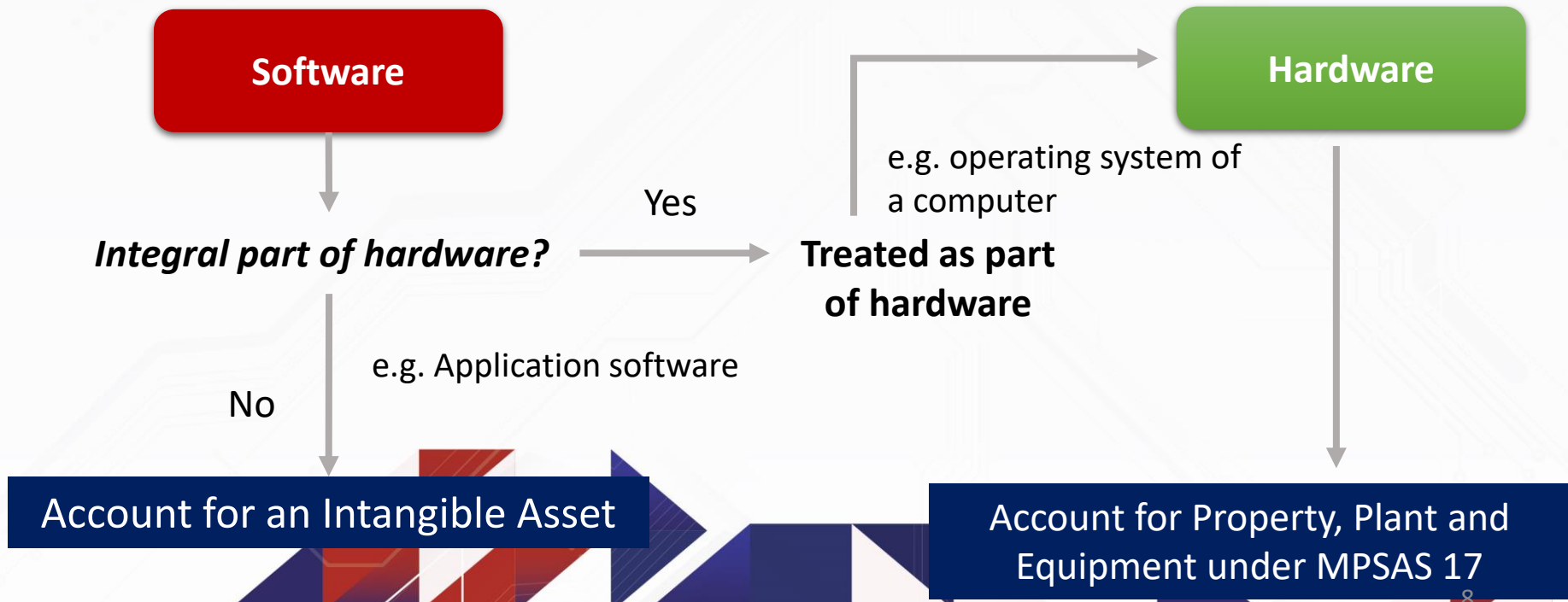
Tangible component

Hardware is the physical aspects of a computer and related devices.

Accounting for Tangible and Intangible component

Software may be contained in or on a physical substance such as a compact disc, computer or server. In determining whether an asset that incorporates both intangible and tangible elements should be treated under MPSAS 17 - *Property, Plant, and Equipment*, or as an intangible asset, **an entity uses judgement to assess which element is more significant**. [MPSAS 31.7]

Software

Hardware

Integral part of hardware? → Yes → **Treated as part of hardware**

e.g. operating system of a computer

No

e.g. Application software

Account for an Intangible Asset

Account for Property, Plant and Equipment under MPSAS 17

Accounting for Intangible Component

Entity shall account the intangible component in software development as intangible asset under MPSAS 31 if, and only if, an entity can demonstrate:

Meet the definition of IA

Satisfy the recognition criteria

(a) It is probable that the expected future economic benefits or service potential that are attributable to the asset will flow to the entity; and

(b) The cost or fair value of the asset can be measured reliably

Identifying Research and Development Phase

Research phase	Development phase	Operation phase
Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding	Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.	Asset is in the condition necessary for it to be capable of operating in the manner intended by management

Brainstorming and planning

Requirements and feasibility analysis.

Design

Development & coding

Integration and testing

Deployment

Data Migration

Training

Operations and maintenance

Time

Recognition and Measurement

Research phase	Development phase	Operation phase
Expenditure on research (or on the research phase of an internal project) shall be **recognized as an expense** when it is incurred. [MPSAS 31.52]	Expenditure incurs in development phase shall be **recognized as intangible asset** if, and only if, an entity can demonstrate all six(6) conditions specified in paragraph 55 of MPSAS 31. Recognition of costs in the carrying amount of an intangible asset ceases when the asset is in the condition necessary for it to be capable of operating in the manner intended by management. [MPSAS 31.7]	Expenditure on an intangible item shall be recognized as an expense when it is incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria. [MPSAS 31.66]

Expenditure on an intangible item that was initially recognized as an expense under this Standard shall not be recognized as part of the cost of an intangible asset at a later date. [MPSAS 31.70]

Time →

Development phase – recognition conditions

The six(6) recognition condition of internally generated intangible asset

Technical feasibility of completing the intangible asset

Intention to complete the intangible asset and use or sell it

Ability to use or sell the intangible asset

How the intangible asset will **generate probable future economic benefits or service potential.** Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset

The availability of **adequate technical, financial and other resources** to complete the development and to use or sell the intangible asset

Its **ability to measure reliably** the expenditure attributable to the intangible asset during its development
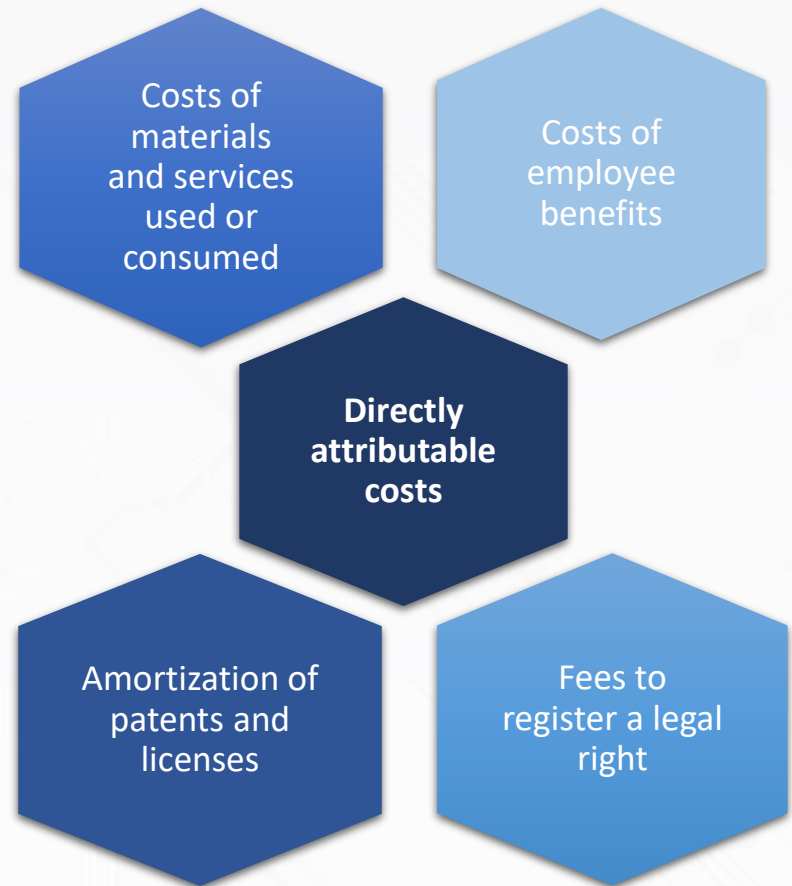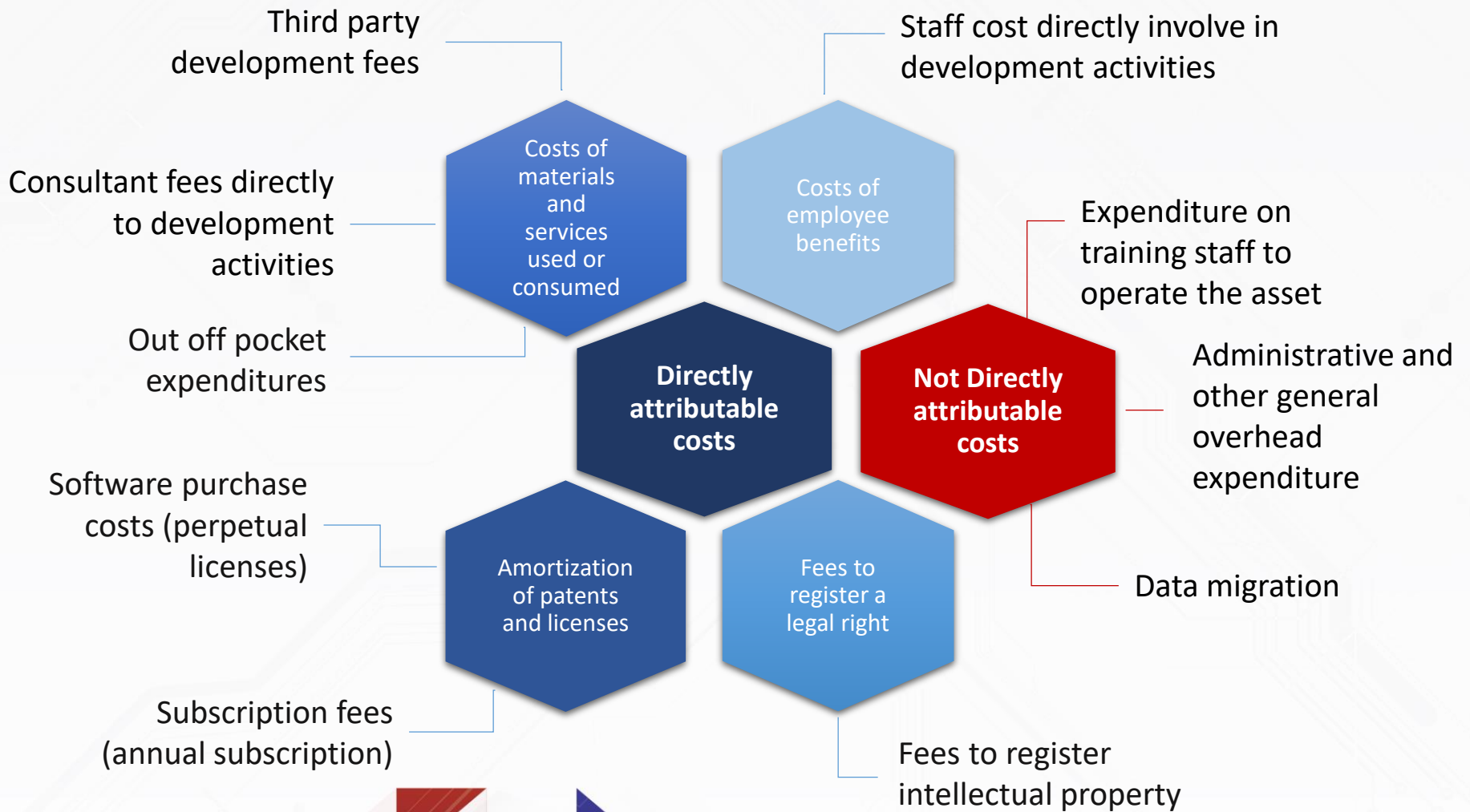
How to demonstrate?

- Entity assesses the future economic benefits or service potential to be received from the asset using the principles in either MPSAS 21 or MPSAS 26 as appropriate

- Operating plan showing the technical, financial, and other resources needed and the entity's ability to secure those resources.

- Availability of external finance by obtaining a lender's or funder's indication of its willingness to fund the plan

- Entity's costing systems can often measure reliably the cost of generating an intangible asset internally

Measurement – Cost elements

The cost of an internally generated intangible asset is the **sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria**. [MPSAS 31.63]

The cost of an internally generated intangible asset comprises all **directly attributable costs** necessary to create, produce, and prepare the asset to be capable of operating in the manner intended by management. [MPSAS 31.64]

Costs of materials and services used or consumed

Costs of employee benefits

Directly attributable costs

Amortization of patents and licenses

Fees to register a legal right

Third party development fees

Consultant fees directly to development activities

Out off pocket expenditures

Software purchase costs (perpetual licenses)

Subscription fees (annual subscription)

Staff cost directly involve in development activities

Expenditure on training staff to operate the asset

Administrative and other general overhead expenditure

Data migration

Fees to register intellectual property

Directly attributable costs

Not Directly attributable costs

Costs of materials and services used or consumed

Costs of employee benefits

Amortization of patents and licenses

Fees to register a legal right

Recoverability of the Carrying Amount - Impairment Losses

- **If it is no longer probable that a project will be completed, stop capitalizing the costs associated with it, and conduct impairment testing on the costs already capitalized**.
- The cost at which the asset should then be carried is the lower of its **carrying amount** or **the recoverable service amount/recoverable amount** of an asset. Unless there is evidence to the contrary, the usual assumption is that uncompleted software has no fair value.

To determine whether an intangible asset measured under the cost model is impaired, an entity applies either MPSAS 21 or MPSAS 26, as appropriate.

Those Standards explain when and how an entity reviews the carrying amount of its assets, how it determines the recoverable service amount or recoverable amount of an asset, as appropriate, and when it recognizes or reverses an impairment loss. [MPSAS 31.110]

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