State of Vermont
Department of Finance & Management
Intangible Assets Guide

Purpose and Objective

The purpose of this document is to provide guidance, to State of Vermont (State) financial accounting and capital asset management personnel, in accounting and reporting intangible assets.

The objective of the guide is to identify the information needed to properly report intangible assets in the fund and government-wide financial statements.

Accounting Principles and Policies

The State prepares its financial statements in accordance with Generally Accepted Accounting Principles (GAAP) prescribed by the Governmental Accounting Standards Board (GASB). GAAP requires the State to report the ending balance of capital assets (net of accumulated depreciation), depreciation expense, and net assets invested in capital assets (net of accumulated depreciation and related debt) on the face of the financial statements. GASB Statement No. 34 - *Basic Financial Statements – and Managements Discussion and Analysis-for State and Local Governments,* brought about significant changes to governmental financial statement, including the changes to the accounting and reporting of capital assets. GAAP for capital assets also includes GASB Statement No. 42 – *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries,* and GASB Statement No. 51 - *Accounting and Financial Reporting of Intangible Assets*. The issuance of GASB No. 51 was prompted by the many questions about how to identify and report intangible assets that arose from inclusion of the concept of intangible assets in GASB No. 34. (http://www.gasb.org)

All intangible assets subject to the provisions of Statement No. 51 should be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capitals assets, including the areas of recognition, measurement, amortization, impairment, presentation, and disclosures should be applied to intangible assets, as applicable. An intangible asset should be recognized in the statement of net assets only if it is identifiable.

An intangible asset is considered identifiable when either of the following conditions is met:

A) the asset is separable, that is, the asset is capable of being separated or divided from the State and sold, transferred, licensed, rented, or exchanged, either individually or together with a related contract, asset, or liability; or
B) the asset arises from contractual or other legal rights, regardless of whether those rights are transferable or separate from the entity or from other rights and obligations.

It‟s **not an intangible asset** if any of the following occur:

A) if the assets are acquired or created primarily for the purpose of directly obtaining income of profit,
B) assets resulting from capital lease transactions reported by the lessees, or
C) goodwill created through the combination of the State and another entity.

GASB No. 51 requires that all intangible assets acquired in fiscal years ending after June 30, 1980 (and still in use), to be classified as capital assets and reported at historical cost in the State"s financial statements. As stated in GASB No. 51, intangible assets with indefinite useful lives and internally generated intangible asset (IGIA) will not be required, but are permitted, to be retroactively reported (put into service between June 30, 1980 and June 30, 2009). Finance and Management has opted to **NOT** report these assets retroactively. The requirements of the Statement were effective for financial statements for periods beginning after June 15, 2009 (i.e. July 1, 2009).

Definitions

Amortization - The systematic allocation of the cost of intangible assets over its estimated useful life, comparable to Depreciation in capitalized assets.

Capital Assets –Assets of a relatively permanent nature with a life expectancy of more than one reporting period and costs with a minimum threshold whose identity does not change with use. The unit must be identifiable and separately accounted for. Capital assets include land, buildings and improvements, improvements other than buildings, machinery and equipment, capital leases, and intangible assets

Capitalization – To record the cost as an asset that is subject to depreciation (amortization for intangible assets) over its estimated useful life, rather than as an expense for one accounting period.

Construction-in-Process (CIP) – The cost of construction or development work undertaken, but not yet completed that will result in a capitalized asset; sometimes referred to as Work-in-Process (WIP).

Copy Right – An intellectual property that is a right as a legal device that provides the owner the right to control how a creative work is used. A copyright is comprised of a number of exclusive rights, including the right to make copies, authorize others to make copies, make derivative works, sell and market the work, and perform the work.

Commercial Off-The-Shelf Software (COTS) - COTS products are designed to be easily installed and to interoperate with existing system components. Almost all software bought by the average computer user fits into the COTS category: operating systems, office product suites, word processing, and e-mail programs are some examples.

Depreciation – The systematic allocation of the cost of a depreciable capitalized asset (less salvage value) over its estimated useful life. A depreciable capitalized asset is one which decays or loses its usefulness with the passage of time. Most capitalized assets are depreciable. Land, easements, construction-work-in-progress, museums, collections of art and library are typically not depreciated.

Donated Asset – An asset received as a gift from an individual or non-State entity; donated assets are valued at fair-market value at the time of acquisition.

Easements – An easement is a right to use or an interest in land that is owned by another entity or individual. Examples of easements include conservation easements, which prohibit certain types of development, and right of way easements, which allow for the use of land in some manner. Easements are typically inexhaustible in nature and therefore would not be amortized.

Fair Market Value – Cost to acquire an item in its current condition through an "arm‟s-length" transaction; costs may be determined based on an appraisal price of the selling price of an equivalent item on the open market.

Infrastructure – Infrastructure assets are those assets typically long-lived stationary in nature and be preserved for a significantly greater number of years than most capital assets. Examples of infrastructure assets includes Roads, bridges, dams, drainage systems, weigh stations, rest areas, water and sewage systems, parking lots, lighting systems and highway ramps.

Infrastructure Systems – Infrastructure systems are infrastructure assets that are stationary in nature and involve several components of assets that work together for a singular purpose. Examples include railroad stations and railroad lines, airport buildings and runways and water canals, locks and ports.

Intangible Asset – An intangible asset is a legal right with the following characteristics:

- lacks physical substance,
- useful life is more than one reporting year, and meets the capitalization threshold, and
- nonfinancial in nature (has value but not in a monetary form such as cash, receivables or investments).

Examples include patents, copyrights, trademarks, easements, software (including websites), rights to natural resources (water, timber and mineral rights), and similar assets.

Intellectual Property – An intangible asset is considered an intellectual property when human minds create an end product that has "protective" rights. Such items can be a motto, logo, symbol, literary work, or invention. See trademarks, copyrights and patents.

Internally Generated Intangible Asset (IGIA) – Intangible assets are considered internally generated if they are created or produced by the State or an entity contracted by the State, or if they are acquired from a third party by requiring more than „minimal incremental effort‟ on the part of the State to begin to achieve their expected level of service capacity. An example of IGIA is internally generated/developed software.

Internally Generated/Developed Software – Internally Generated Software is software that is internally generated by the State or by an entity contracted by the State, or is purchased software from a third party that requires more than „minimal incremental effort‟ to achieve expected service capacity. For example, licensed financial accounting software (VISION) that the State modifies to add special capabilities would be considered internally generated asset.

Land Use Rights – Right to use water source or to remove timber, minerals or other resources from land that is not owned by the State. Land use rights associated with property owned by the State should not be separately recorded as intangible assets.

Minimal Incremental Effort – It"s a term used to identify whether software is determined to be an intangible asset. When commercially available software is purchased or licensed by an entity and modified using more than „minimal incremental effort" before being put into operation, the software should be considered internally generated. Professional judgment must be used to determine what is considered „minimal incremental effort". As a general rule, if you have to change coding of commercial off-the-shelf software (COTS), then you have satisfied the requirement of applying more than a „minimal incremental effort". However, customizing COTS to interact and communicate with existing State systems would NOT be considered more than a „minimal incremental effort".

Patent – A patent, an intellectual property that is a legal right to exclude others from making, using, manufacturing, or selling an invention in the United States (or importing the invention into the U.S.). Patents have a definitive useful life.

Purchased/Licensed Software – Software purchased or licensed from a third party that does not require more than minimum incremental effort to achieve expected service capacity; sometimes referred to as COTS software. Purchased or licensed software is an intangible asset and must be capitalized if it meets the capitalization threshold and useful life criteria.

Right-of-way – Right of way is a strip of land occupied or intended to be occupied by (for example) a street, crosswalk, railroad, road, electric transmission line, oil or gas pipeline, water supply main, sanitary sewer, storm drain, or any other special use.

Trademark – Trademark is an intellectual property that is a distinctive name, symbol, motto, or design that legally indentifies an entity or its products and services. Trademarks have a definitive useful life.

Useful Life – Period of time over which a capital asset provides future economic benefit in performing the function for which it was purchased.

Websites – Website is a set of interconnected WebPages, usually including a homepage, generally located on the same server, and prepared and maintained as a collection of information by a person, group or organization.

Working Papers - Documents prepared or obtained by the department in performing an examination of a financial record. The working papers may be subject to examination by an auditor to determine the accuracy of the reported costs of an asset.

Capitalization Thresholds and Useful Life

Asset Classification	Minimum Acquisition Cost	Useful Life	Amortizable	Examples/comments
Easements, Right-of-Ways, Land Use Rights	No Minimum	No Minimum	NO (if permanent, otherwise YES)	Record separately from associated asset; except land use rights on state-owned land should not be separately recorded
Intellectual Property	$5,000	No Minimum	YES (generally)	Trademarks, Copyrights patents
Internally Generated Intangible Asset	$150,000	> 1 year	YES	Examples include internally generated software, websites, patents, copyrights, etc. Cost includes in house payroll and fringe benefits expense for State personnel's time devoted to a project.

Those intangible assets which have no legal, contractual, regulatory, technological, or other factors limiting their useful life should be considered to have an indefinite useful life. A permanent right-of-way easement, for example, should be considered to have an indefinite useful life. An intangible asset with indefinite useful life should not be amortized unless its useful life is subsequently determined to no longer be indefinite due to a change in circumstances.

Intangible assets with an indefinite useful life (e.g. permanent right-of-way easement, water rights), like land, are capitalized but should not be amortized. If conditions change and the useful life is no longer indefinite, the asset should be tested for impairment. Any remaining carrying value should begin to be amortized over the remaining useful life. This change should be treated as a change in accounting estimate. Therefore, the old asset would need to be retired and a new asset set up in AM.

For State owned land, the land use rights (e.g. easements, water, mineral, and timber rights) already included in the tangible land should not be broken out and valued individually. These rights are considered part of the ownership of the land, and would only be valued individually if they are purchased separately from the land.

Working Papers

In terms of departmental tracking and reporting, working papers are an essential source document(s) to offer support for determining if an item is reportable and if so, the reporting costs, terms and life expectancy of intangible assets. Working papers may include the original source(s) document of data for each item and amount, such as invoices; the purchase price of intangible assets acquired, as in fair market value at date of acquisition for donated assets; forms, contracts, leases and land records, especially for right-of-ways, easements and land use rights; payroll records for reporting on internally generated computer software; and any other documents that supports the valuation of the intangible asset.

Upon review of the working papers, a department"s accounting or capital asset manager can determine the quality of the work performed. Included in the working papers are schedules, analyses, transcriptions, memos and confirmation results related to the assets. These working papers serve as the basis of the work performed and supports a department"s decisions in the asset"s evaluation.

Tracking and Reporting of Intangible Asset

Acquisition Costs

Intangible assets can be purchased, licensed, acquired through nonexchange transactions, or internally generated. The acquisition cost of an intangible asset is based on actual cost or fair market value and is the capitalized amount recorded in the VISION Asset Management module (AM). Following are general guidelines for determining the acquisition cost for the most common acquisition methods:

A) Purchase: Invoice price plus necessary ancillary costs to place the asset into its intended location.
B) Donated or Gifted: Fair Market value at time of acquisition plus ancillary charges required acquiring the asset.
C) Constructed or Internally Generated: Direct cost of materials, components, contracted services, professional fees & services, in-house employee payroll and fringe benefit costs directly allocable to the project.

It should be noted that extended maintenance agreements (e.g. software) paid at the same time as the asset, are to be included as part of the asset"s acquisition cost and capitalized. If an extended maintenance agreement is invoiced and paid annually, then these costs will be considered expensed as incurred.

If acquisition costs are not readily available, historical cost estimation methods can be used. For example, costing methods can use the standard costing which involves using historical sources, such as sales catalogs or advertisements, to establish the average cost of obtaining the same or similar assets. Further, a quote from a manufacturer as to the cost at the time of purchase may be used as well.

The price level index method can be used which deflates the current costs of the same or similar asset using an appropriate price index. Annual price levels are measured in terms of the Gross National Product Implicit Price Deflators (GNP Deflators) for government purchases of goods/services. GNP Deflators can be found at the following website. BEA National Economic Accounts

Internally Generated Intangible Asset

If an intangible asset is created or produced in-house by the State, or by an entity contracted by the State (generally a combination of both), or acquired from a third party (e.g. commercial off-the-shelf purchase) and more than a „minimal incremental effort" is required by the State to achieve the software"s expected service capacity, then the asset should be considered an internally generated intangible asset. You will need to use professional judgment as to what is considered „minimal incremental effort". As a general rule, if you have to change coding of the

COTS, then you have satisfied the requirement of applying more than a „minimal incremental effort". However, customizing the software to interact and communicate with existing agency systems would not be considered more than a „minimal incremental effort".

Capitalization of any development costs cannot take place until **ALL** of the following three criteria have been met:

A) The specific objective and the nature of the service capacity expected from the asset upon completion of the project can be determined. In other words, if you can document what the intended purpose is or end result of the project then you have satisfied this first criterion.
B) The technical or technological feasibility for completing the project in order to provide its expected service capacity can be demonstrated. If your department can show that contracted consultants or in house employees have the skills, competence, and knowledge to complete the project, then this second criteria will have been met.
C) The current intention, presence of effort, and ability to complete the project, or, in the case of a multiyear project, continue development of the intangible asset can be demonstrated. For example, has management approved the project, or in the case of a multiyear project, has funding been committed to the project?

Generally IGIA is customarily software, however, websites, intellectual properties, such as copyrights, trademarks and patents can be intangible assets that were developed in-house as well.

<u>Internally Generated Computer Software</u>
The activities involved in developing and installing internally generated computer software can be grouped into the following three stages:

Project Stage	**Associated Activities**	**Accounting Treatment**
PRELIMINARY	Concept formulation; evaluation of alternatives; feasibility	**EXPENSE**
APPLICATION DEVELOPMENT	Application design; configuration of interfaces; coding; installation to hardware; testing	**CAPITALIZE**
POST-IMPLEMENTATION AND OPERATIONS	Application training; software maintenance	**EXPENSE**

Data conversion should be considered an activity of the Post-Implementation/Operation Stage unless it is necessary to make the computer software operational, in which case, data conversion should be considered part of the Application Development Stage.

Modifications of computer software already in operation should be capitalized if the project cost meets the $150,000 threshold and any of the following criteria:

A) there is an increase in functionality (able to perform tasks it was previously incapable of performing),

B) there is an increase in efficiency (level of service has increased without the ability to perform additional tasks), or
C) the useful life has been extended.

If none of these conditions apply, then the modification costs in question should be expensed as maintenance.

In calculating the total costs of an IGIA, in-house payroll will be required to be tracked in some manner. Finance & Management recommends that departments use a VISION Project ID on all expenditure transactions to allow easy summarization of the costs for IGIA, including positive reporting using the project ID on payroll time and expense forms for hours worked and expenses allocated to the IGIA project.

Intangible Asset CIP Costs

Per fiscal year end closing instructions, departments with CIP must complete the Construction in Process form located on the CAFR and Year-End Closing page on the Finance & Management webite. The complete form must be emailed to VISION.CAFR@vermont.gov. Please read the FY Year End Closing Instructions for all capital asset closing requirements.

Impairment Indicator

GASB No. 42 identifies a common indicator of impairment for an internally generated intangible asset is development stoppage, such as stoppage of development of computer software due to a change in the priorities of management. Internally generated intangible assets impaired from development stoppage should be reported at the lower of carrying value or fair value.

Adding Intangible Assets to VISION

Intangible Assets are entered into the VISION Asset Management Module as you would for tangible capital assets. Profiles, categories, and asset class for the intangible assets are listed below. Please read the FY Year End Closing Instructions for all capital asset closing requirements.

PROFILES	PROFILE DESCR	CATEGORIES	CATEGORY DESCR	CLASS
IRIGHTOFWA	Right of Way	LAND	Land	Intangible
ILANDUSE	Land Use Rights	LAND	Land	Intangible
IEASEMENT	Easement	LAND	Land	Intangible
ITRADEMRKD	Trademark - Depreciable	OINTD	Other Intangibles - Depr	Intangible
ICPYRIGHTD	Copyright - Depreciable	OINTD	Other Intangibles - Depr	Intangible
IPATENTD	Patent - Depreciable	OINTD	Other Intangibles - Depr	Intangible
ITRADEMRK	Trademark - Non Depreciable	OINTN	Other Intangibles - Non Depr	Intangible
ICOPYRIGHT	Copyright - Non Depreciable	OINTN	Other Intangibles - Non Depr	Intangible
IPATENT	Patent - Non Depreciable	OINTN	Other Intangibles - Non Depr	Intangible

ISOFTWAR10	Software - 10 yr Depreciable	SFTWD	Computer Software - Depr	Intangible
ISOFTWAR3	Software - 3 yr Depreciable	SFTWD	Computer Software - Depr	Intangible
ISOFTWAR5	Software - 5 yr Depreciable	SFTWD	Computer Software - Depr	Intangible
IWEBSITE3	Website - 3 yr Depreciable	SFTWD	Computer Software - Depr	Intangible
IWEBSITE5	Website - 5 yr Depreciable	SFTWD	Computer Software - Depr	Intangible

Departments should contact FINOPS if the default useful life of the related intangible asset is other than 3, 5, or 10 years for software.

Amortization is computed using the straight-line method. When applicable, AM will calculate prior period amortization for all periods (months) prior to the current period, when the transaction date is changed to reflect an in service date in an earlier period. The prior period amortization will be reflected on PDP journals.

Contact Financial Operations for assistance if the asset should have a different profile.

For assistance in processing intangible assets in VISION Asset Management, Call Jamie Sheltra at 828-0670 or email at Jamie.Sheltra@vermont.gov

For accounting inquiries related to intangible assets call Peggy Brooks at 828-1467 or email at Peggy.Brooks@vermont.gov