IPSAS 31 Intangible Assets – as adopted by the Maltese Government

Guidelines

IPSAS Implementation Team

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Introduction

1. IPSAS 31 Intangible Assets – as adopted by the Maltese Government

1.1 These guidelines refer to the Intangible Assets accounting standard **as adopted by the Maltese Government**. This version is based on the original IPSAS 31 developed by the International Public Sector Accounting Standards Board (IPSASB). Modifications were made to bring the IPSAS closer to the local context. A summary of the significant differences with the original IPSAS 31 can be found as an Appendix to the standard, entitled **Comparison with IPSAS 31**.

2. Scope

2.1 These guidelines were prepared to enable the users to:

2.1.1 Develop a working-level knowledge of the principles contained in the accounting standard; and

2.1.2 Understand and appreciate the major challenges and benefits resulting from the implementation of IPSAS 31[1].

3. Target Audience

3.1 These guidelines are designed for financial and non-financial employees employed in Ministries and Departments of the Government of Malta.

4. Guidelines Structure

4.1 These guidelines shall provide a detailed overview of all the principles contained in the standard, including Intangible Asset classification, recognition and measurement, amortisation and impairment, derecognition, reporting and disclosure of Intangible Asset information.

[1] References to IPSAS 31 or any other IPSAS shall be taken as meaning 'as adopted by the Maltese Government'.

A. Intangible Assets Defined

1. Some assets held by ministries/departments are used for a considerable length of time. These assets may either be Property, Plant and Equipment, Investment Property, or Intangible Assets. These Guidelines refer to the latter category.

2. Intangible Assets are non-monetary assets which are ***without physical substance*** and ***identifiable*** (either being separable or arising from contractual or other legal rights).

3. When accounting for Intangible Assets, the following should be considered:

- *Is this item an asset?*
- *What is the item's value?*
- *How long will it be useful to us?*
- *Will it have any value after we are finished using it?*
- *How should we account for the reduction in its usefulness through time?*
- *How should we present all this in our financial statements?*

4. The **three critical attributes** to remember are:

Identifiability

- Is capable of being separated and sold, transferred, licenced, rented, or exchanged, either individually or as part of a package, or
- Arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

Control

- An entity controls an asset if it has power to obtain future economic benefit or service potential flowing from the underlying resource, and
- To restrict the access of others to those benefits.

Future Economic Benefits or Service Potential

- Revenue from sale of products, services or processes, or
- Cost savings, or
- Other benefits from use of an asset

<u>IPSAS Team Note:</u>

Intangible assets have no physical substance: although some assets may be contained in or on a physical substance, this physical substance is a secondary element of the asset and the asset is still considered as not having a physical substance. Examples include: licences printed on a paper document, application software on a CD and patents on a patent registration document.

B. Impact of Intangible Asset Standard Implementation

1. One of the major differences between the ***current cash-based accounting system*** and ***accruals-based accounting*** is the fact that currently costs incurred on intangible assets are expensed immediately upon there being a cash outlay.

2. The implementation of this standard compliments that of Property, Plant and Equipment; in fact, the benefits associated with the implementation of both these standards, the required changes in processes and the challenges foreseen as a result of this implementation are very similar for these two standards (please refer to *IPSAS 17 PP&E as adopted by MG Guidelines*).

C. Classification of Intangible Asset

1. IPSAS 17 defines a class of Property, Plant and Equipment as follows: *'a grouping of assets of a similar nature or function in an entity's operations that is shown as a single line-item for the purpose of reporting value and providing disclosure in the financial statements.'*

2. This concept also holds when classifying intangible assets. Central Government entities should present Intangible Assets in the following four classes in the Notes to the Financial Statements:

- Computer Software & Websites
- Trademarks, Copyrights and Patents
- Licences and Royalties
- Other[2]

IPSAS Team Note:

1. **Goodwill**: goodwill is not being considered in the classification of intangible assets. Unlike the other intangible assets, goodwill is an **unidentifiable** intangible asset that cannot exist independently, nor can it be sold, purchased, or transferred separately without carrying out the same transactions as a whole.

2. **Development Expenditure (refers to assets in the course of development):** this expenditure may be considered as a separate class and may be eligible for capitalisation if it satisfies the conditions stipulated on IPSAS 31 (section 55). Note that once these assets are completed, they are to be placed within the respective category and no amortisation is to be charged on such assets.

[2] The class 'other' should be used in specific circumstances as determined by the pertinent government body.

2.1 **Computer Software and Websites**:

2.1.1 Acquired Computer Software and Websites – the user is acquiring the rights (the licence) to use the software in accordance with a licencing agreement. This software is substantially used in the form it was purchased without material changes.

2.1.1.1 A software licence is a legal instrument governing the use or redistribution of software.

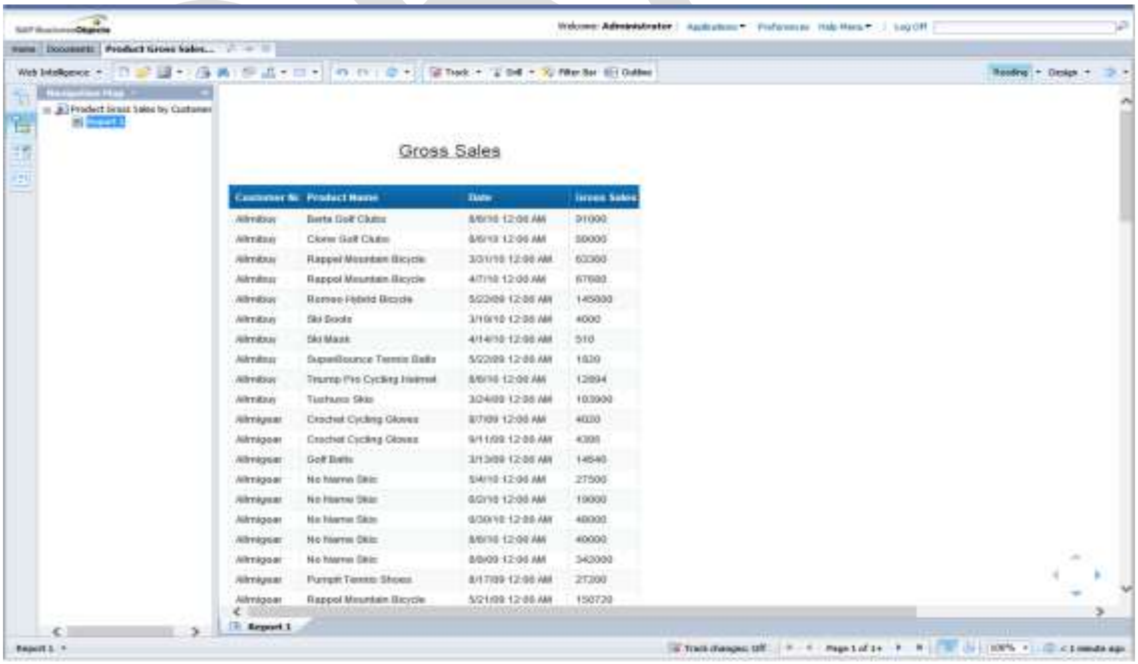
A typical software licence grants an end-user permission to use one or more copies of software in ways where such a use would otherwise potentially constitute copyright infringement of the software owner's exclusive rights under copyright law.

IPSAS Team Note:

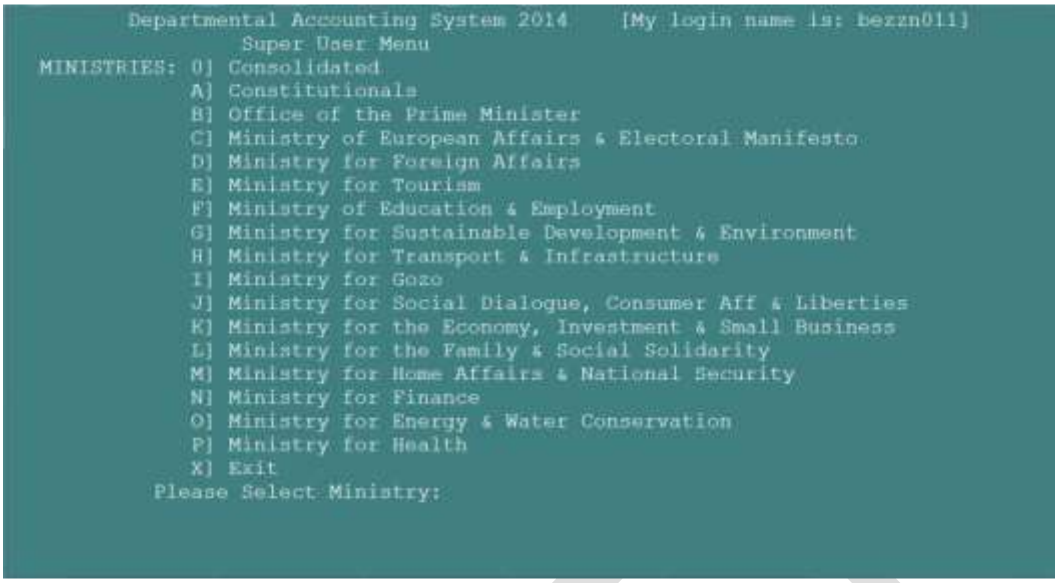
Software is considered as PP&E and not as an intangible asset when it is an integral part of the hardware without which the hardware cannot operate e.g. Operating systems

2.1.1.2 Examples of software licences used by Government include:

- Departmental Accounting System (DAS)
- Business Objects



Business Objects

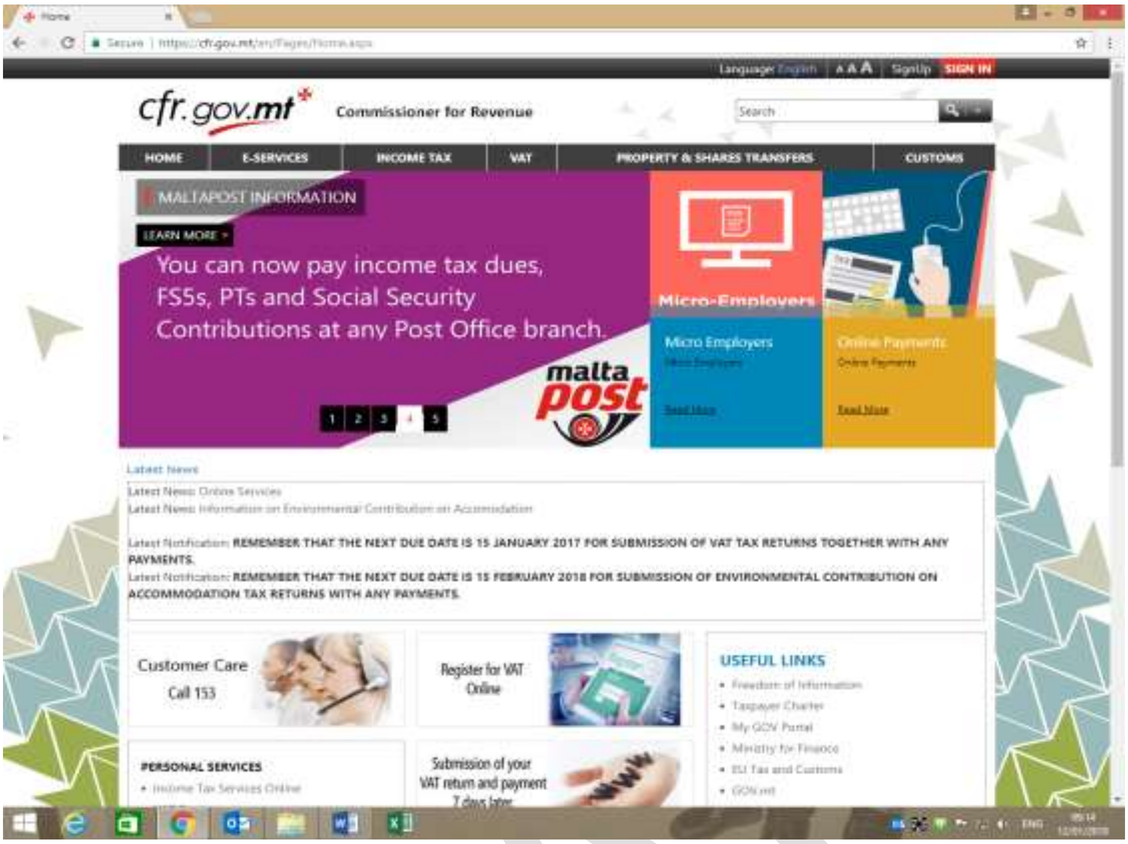


Departmental Accounting System (DAS)

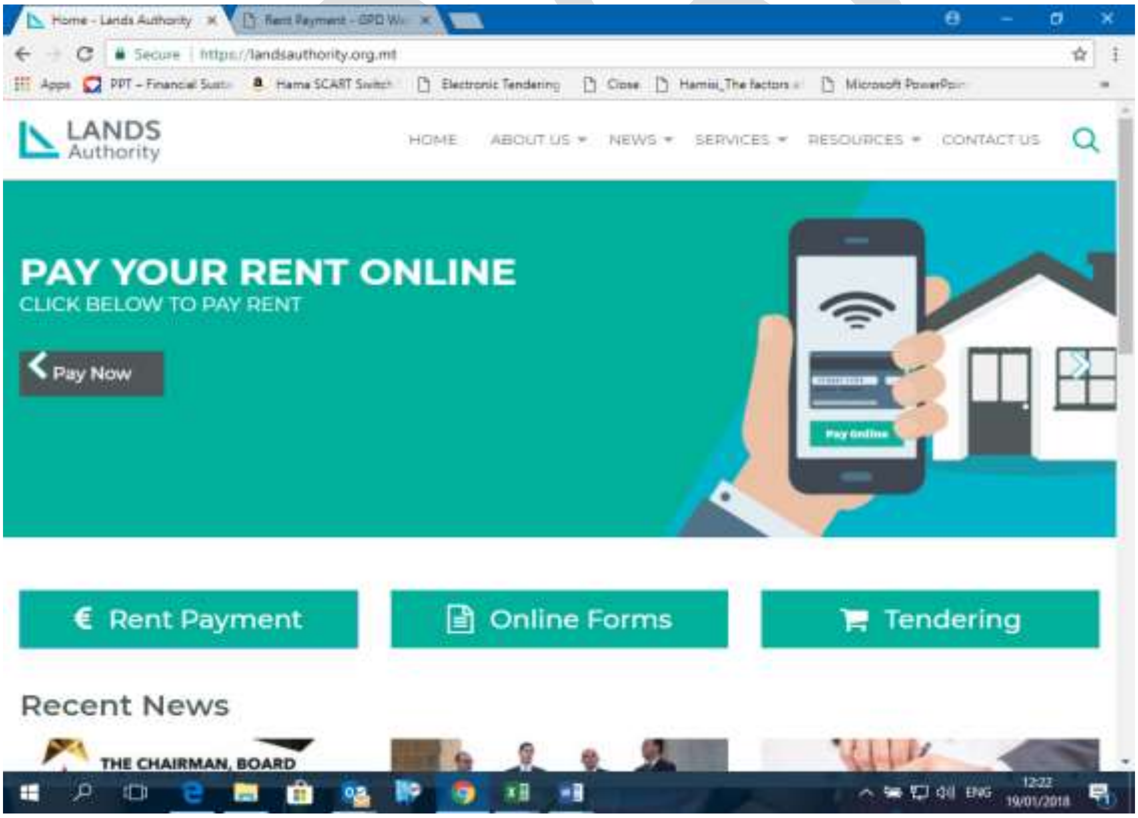
2.1.2 Internally Developed Software and Websites – these are specifically designed to cater for the specific needs of the Central Government Entity.

2.1.2.1 Examples of internally developed websites include:

- CFR On-line Payments (https://cfr.gov.mt/en/Pages/Home.aspx)
- Lands Authority (former GPD) On-line Rent Payments (https://landsauthority.org.mt/)



CFR On-line Payments



Lands Authority (former GPD) On-line Rent Payments

<u>IPSAS Team Note:</u>

Determining whether a <u>website</u> can be capitalised as an intangible asset:

It is important to note that an entity will need to demonstrate how the website will generate probable future economic benefits or service potential, in order to capitalise the website as an intangible asset.

If the entity **cannot** demonstrate this, all expenditure on such a website should be recognised as an expense when it is incurred.

If it is difficult for an entity to demonstrate that probable future economic benefits or service potential will be generated from a website developed **solely or primarily to promote and advertise its own products or services**; all costs on developing such a website shall be recognised as an **expense**.

2.2 **Trademarks, copyrights and patents**

2.2.1 These include:

2.2.1.1 Internet domains;

2.2.1.2 Newspaper mastheads;

2.2.1.3 Trademarks (recognisable signs, designs or expressions which identify products or services of a particular source from those of others);

2.2.1.4 Copyrights (legal rights created by the law of a country, that grant the creator of an original work exclusive rights to its use and distribution, usually for a limited time, with the intention of enabling the creator, such as the photographer of a photograph or the author of a book, to receive compensation for their intellectual effort); and

2.2.1.5 Patents (a set of exclusive rights granted by a sovereign state to an inventor or assignee for a limited period of time in exchange for detailed public disclosure of an invention. An invention is a solution to a specific technological problem and is a product or a process).

gov.mt

Government Internet Domain

'Gazzetta tal-Gvern' masthead

tm

Trademark

2.3 **Licences (except those software related) and Royalties**

2.3.1 A licence is "an authorisation (by the licensor) to use the licenced material (by the licensee)."

2.3.2 A royalty is a usage-based payment made by one party (the "licensee") to another (the "licensor") for the right to ongoing use of an asset, sometimes an intellectual property (IP). Royalties are typically agreed upon as a percentage of gross or net revenues derived from the use of an asset or a fixed price per unit sold of an item of such, but there are also other modes and metrics of compensation.

3. Intangible Heritage Assets

3.1 Some intangible assets are described as intangible heritage assets because of their cultural, environmental, or historical significance.

3.2 Examples of intangible heritage assets include recordings of significant historical events and rights to use the likeness of a significant public person on, for example, postage stamps or collectible coins.

3.3 Certain characteristics, including the following, are often displayed by intangible heritage assets (although these characteristics are not exclusive to such assets):

3.3.1 Their value in cultural, environmental, and historical terms is unlikely to be fully reflected in a financial value based purely on a market price;

3.3.2 Legal and/or statutory obligations may impose prohibitions or severe restrictions on disposal by sale;

3.3.3 Their value may increase over time; and

3.3.4 It may be difficult to estimate their useful lives, which in some cases could be several hundred years.

<u>IPSAS Team Decisions</u>

Recognition of intangible heritage assets:

Recognition of intangible heritage assets on the balance sheet is **required** in cases where the entity can reliably determine the cost or value of the heritage asset.

If the cost or value **cannot** be reliably measured, the entity may, following agreement with the pertinent government body, not recognise these assets but disclose, in the notes to the Financial Statements, a **description** of such intangible heritage assets held by the entity.

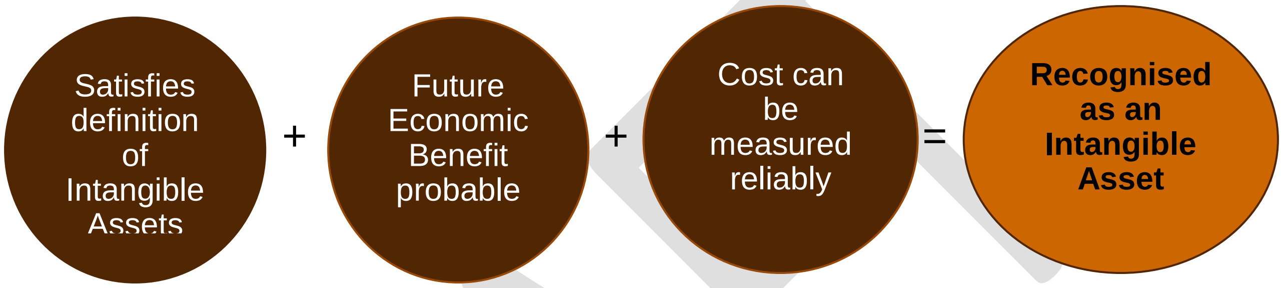
D. Recognition of an Intangible Asset

1. IPSAS 31 states that an intangible asset shall be recognised if, and only if:

   1.1 It is probable that future economic benefits or service potential associated with the item will flow to the entity; and

   1.2 The cost or fair value of the item can be measured reliably.

2. The **recognition criteria** for any expenditure on intangible items to be capitalised as an asset shall be based on the above definition, summarised as follows:



3. **Capitalisation** is the recognition of a non-current asset in the Statement of Financial Position.

4. Adequate **documentation** of whether to capitalise or expense costs should be maintained.

   4.1 **Example 1: Capitalisation of intangible assets**

   The Ministry for Justice, Culture and Local Government acquires copyright to the original recordings of a famous singer. The agreement with the singer allows the Ministry to record and re-record the singer for a period of 5 years. During the initial six-month period of the agreement, the singer is very sick and consequently cannot record. The studio time that was blocked by the Ministry had to be paid even during the period the singer could not sing. The following costs were incurred by the Ministry:

   i) Legal cost of acquiring the copyrights €15m

   ii) Operational losses (studio time lost etc.) during start-up period €3m

   iii) Massive advertising campaign to launch the artist €2m

   Required: which of the above items is a cost that is eligible for capitalisation as an intangible asset?

Solution:

i) Legal cost of acquiring the copyrights can be capitalised as this cost is directly linked to the acquisition of asset, in this case the copyright.
ii) Operation losses are not allowed to be capitalised as these are not directly linked to the acquisition of asset, in this case the copyright.
iii) Advertising campaign costs are not allowed to be capitalised.

4.2 Example 2: Capitalisation of intangible assets

An educational institution, providing distance learning courses to students, reproduces all the study material and relevant textbooks necessary for the completion of the course on a specific website. Participating students pay a fee which grants them access to the website contents necessary for their studies. This website **qualifies for recognition** as an intangible asset as the **future economic benefits** can be demonstrated by the **fees generated.**

The same institution has **another website** providing information to prospective students regarding the study programme and fees. It is difficult to demonstrate that future economic benefits or service potential are probable, as the **website** is **solely intended** to **promote** the **products** and **services** of the institution. The costs related to this website should therefore be **expensed**.

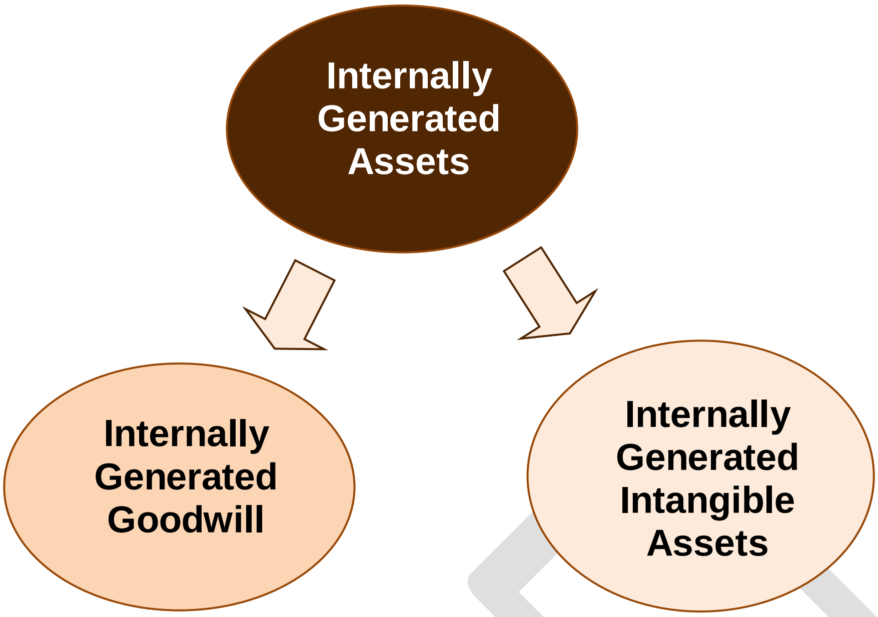
IPSAS Team Note:

The following expenses should **not** be capitalised:

- Expenditure on start-up activities
- Expense of training
- Expenses on advertising and promotional activities
- Expenditure on relocating or reorganising part or all of an entity

5. No **capitalisation threshold** shall be set. All assets falling within the above-mentioned classification (computer software and websites, trademarks, copyrights and patents, licences and royalties) that meet the said criteria shall be capitalised as Intangible Assets.

6. Recognition of **Internally Generated Assets:**



6.1 Internally Generated **Goodwill**:

6.1.1 Internally generated goodwill shall not be recognised as an asset, as it is **not** an identifiable resource controlled by the entity, which can be measured reliably at cost.

6.2 Internally Generated **Intangible Assets**:

6.2.1 Internally generated brands, mastheads, publishing titles and other similar items are not recognised as intangible assets since their expenditure cannot be determined separately from the cost of developing the business as a whole and therefore are not separately identifiable.

6.2.2 In order to determine whether an internally generated intangible asset qualifies for recognition, the generation of the asset is divided into two phases:

6.2.2.1 **Research phase**: the “planned investigation” carried out for gaining knowledge. Expenditure incurred during this phase should be written off as an **expense** as and when incurred, because it is not possible to demonstrate that an asset exists in this phase that will generate future economic benefits. Examples include:

- activities aimed at gaining new knowledge;
- the search, evaluation and selection of applications of research findings; and
- the formulation, design, evaluation and selection of possible alternatives for new or improved materials, devices, products, systems and processes.

6.2.2.2 **Development phase**: already obtained knowledge from research phase is applied in formulation of intangible assets. Development expenditure may be **recognised** as an intangible asset when, and only when, **all** of the following can be demonstrated:

- technical feasibility has been established;
- intention to produce and complete such asset exists in the entity;
- ability to use or sell the assets (i.e. under the control of the entity);
- availability of sufficient technical, financial and other resources to complete the development of the asset;
- expected future benefits can be measured reliably; and
- cost of the asset during the development phase can be measured reliably.

The following are **examples** of development costs that can be **capitalised**:

- staff time (including project managers) directly related to developing or testing the asset in the development phase;
- contractor and supplier expenses involved in the development and/or testing the asset;
- depreciation of software licences and computers specifically required to develop or test the asset;
- the costs of data migration but only for test data used for system testing; and
- initial pilot system to test feasibility prior to developing the final system to be capable of being used by the entity.

The following are examples of costs that are considered **expenses** and should **not** be capitalised:

- staff time not directly related to the project for example attending training;
- training and developing user manuals;
- post implementation reviews;
- data migration outside of system testing; and
- administration costs not directly related to development.

6.2.3 Example 3: Internally Generated Software – to capitalise or expense?

(The purpose of the tables hereunder is to illustrate examples of expenditure to assist in clarifying their meaning. It is not intended to be a comprehensive checklist of expenditure that might be incurred).

Capitalise	Examples
External direct costs of materials	Costs of producing product masters
Payroll & payroll related costs for employees working directly on the project (including coding, testing and software setup), and for employees spending >50% of their time on the project during the program instruction stage	Salaries Benefits (exclude meals, alcohol, moral related expenses) Bonuses
Interest costs incurred while developing software	Interest expense
Upgrades and enhancements that increase functionality of existing internal-use software, including major revisions of third party products	Cost of software upgrade resulting in additional functionality such as adding new functions, features, and content and updating graphics Installation costs as described for new software
Data conversion	Costs to develop or obtain software that allows for access or conversion of old data by new systems
Fees to register a legal right	–––
Amortisation of patents and licences that are used to generate the intangible assets	–––

Expense	Examples
Research and development	Undertaking feasibility studies Defining hardware and software specifications Purchased or leased computer software used in research & development (R&D)
Conceptual formulation of alternatives	Decision whether to develop a new system or to correct problems of existing system
Evaluation of alternatives	Functions to be performed by software
Determination of existence of needed technology	–––
Final selection of alternatives	–––
Identified inefficiencies and initial operating deficits incurred before the intangible asset achieves planned performance	–––
Training costs	End-user training salaries Training employees to operate the software/website Materials such as user manuals
Selling, administrative and other general overhead expenditure, unless it can be directly attributed to preparing the intangible asset for use to operate in the manner intended by management	Support staff salaries (non–dedicated) Space Utilities Telephone Overhead costs Supplies Equipment (desktop support)
Implementation costs	Customer support efforts Help desk Internal and external training Maintenance costs
Data conversion costs	Purging / cleaning existing data Reconciliation / balancing of old data and data in new system

Expense	Examples
Upgrades & enhancements	Internal costs External costs incurred under agreements related to specific upgrades and enhancements that do not increase functionality, i.e., those costs which merely extend the useful life are considered maintenance activities
Maintenance	Portion of software contracts attributable to maintenance contracts Direct expenses Correction of errors Minor updates to keep software current Unspecified upgrades

6.2.4 Example 4: Expense, Intangible Asset or PP&E

A department develops a new IT software programme to record customer details. The department incurred the following costs to develop the new software:

i) €6,500 consultant fees to search and evaluate off the shelf systems;
ii) €3,000 in employee expenses to select the final off the shelf system;
iii) €4,000 in employee expenses to design the changes required to the off the shelf system;
iv) €12,000 in employee expenses to construct and test the new software;
v) €7,000 for new terminals to replace old terminals that did not have the capacity to handle the new software;
vi) €800 to promote the new software to staff; and
vii) €2,800 in training staff to operate the new asset.

Required: which of the above items is expensed, capitalised as an Intangible Asset or as a PP&E?

Solution

i) expense €6,500 consultant fee as it was incurred in the research stage;
ii) expense €3,000 employee expenses to select the final off the shelf system;

iii) capitalise as an Intangible Asset €4,000 employee expenses to design changes required to the off-the-shelf system;
iv) capitalise as an Intangible Asset €12,000 employee expenses to construct and test the new system;
v) recognise as PP&E (property, plant and equipment) €7,000 new terminals;
vi) expense €800 to promote new software to staff; and
vii) expense €2,800 training of staff to operate the new asset.

To summarise:

	Expense	Intangible Asset	PP&E
RESEARCH PHASE			
Consultants Fees	X		
Staff Costs	X		
DEVELOPMENT PHASE			
Off the shelf System		X	
Consultants Fees – Design & Construction		X	
Equipment Other (printers, PC's etc.)			X
Data Migration (outside of system testing)	X		
Staff Costs - Development		X	
Staff Costs - Testing		X	
IMPLEMENTATION STAGE			
Training - Staff Costs	X		
Promotional Costs	X		
Manuals	X		

<u>IPSAS Team Note</u>

Software upgrades: departments wishing to upgrade their software will need to determine whether the upgrade should be **expensed** or **capitalised**, and if capitalised, at what value.

- ✓ Updates and minor upgrades as part of a maintenance agreement should be expensed.
- ✓ Major upgrades that meet the definition and recognition criteria of intangible assets and increase the capacity or efficiency or extend the application's useful life should be capitalised.
- ✓ When a department capitalises the software upgrade, it should derecognise the carrying amount of the software replaced and recognise the cost of the new (upgrade) software on the acquisition date.

6.2.5 Example 5: Software Upgrades

Currently a department is using software Infospeed version 2.1 which was purchased 20 months ago. During the current financial year an upgraded version was introduced on the market, Infospeed version 2.1XT, which provides additional features. This is not a compulsory upgrade and entities have to purchase the software separately. This department decided to upgrade to Infospeed version 2.1XT and bought the new software in December. This will replace Infospeed version 2.1.

<u>Scenario A</u> - if upgrading to 2.1XT costs the same to all buyers, including those upgrading from 2.1:

The department should recognise Infospeed version 2.1 as an intangible asset on purchase and then amortise the software over its useful life. Upon purchase of Infospeed version 2.1XT, the carrying amount of Infospeed version 2.1 is de-recognised and the cost of Infospeed version 2.1XT capitalised and amortised over its useful life.

<u>Scenario B</u> - if the cost of upgrade is discounted (as department was a license holder of 2.1):

The department should add the upgrade cost on to the existing carrying amount of Infospeed version 2.1 (this would represent an additional cost to enhance an existing intangible asset), and a re-assessment of the remaining useful life may be necessary.

6.2.6 Example 6: Software Upgrades

Three years ago a department purchased 'Easy Soft' Software from ABC Ltd; the purchase included a 5-year maintenance agreement against a fixed monthly maintenance fee. Under this agreement, any updates and minor upgrades are performed at no additional cost.

The department shall capitalise 'Easy Soft' Software as an intangible asset on purchase and amortise it over its useful life. Updates and minor updates provided as part of the maintenance agreement will not be capitalized and the maintenance fee must be expensed when incurred.

<u>Case Study – Capitalise or Expense?</u>

The Ministry for Transport and Infrastructure created a new department which will be specifically providing basic engineering and operational support services to aircraft manufacturers in a stride to try to boost the sector in Malta. This new department received a request from a well-known aircraft manufacturer (MyAir) to help develop new designs for ducting the air conditioning of their aircraft.
The department identified this as an opportunity to launch such a product with the aim of attracting MyAir and other similar companies to Malta. For this project the funds needed aggregated to €1 million**.** The Ministry was willing to fund the project.

The expenditure incurred in pursuance of the department's research and developments projects was the following, in chronological order: -

- January 28, 2007: Paid €175,000 towards salaries of technicians.
- March 31, 2007: Incurred €250,000 towards cost of developing duct plan and producing the test model.
- June 15, 2007: Paid an additional €300,000 for revising the ducting process to ensure that product could be introduced in the market in line with EU requirements.
- August 15, 2007: Developed at a cost of €80,000 the first model and tested it with the air conditioners to ensure its compatibility.
- October 30, 2007: Individuals from MyAir and from other aircraft manufacturers were invited to a conference for the introduction of this new product. Cost of the conference was €50,000.
- December 5, 2007: The development phase was completed and a cash flow budget was prepared.

Required: What is the proper accounting treatment for the various costs incurred in the year 2007?

Solution

Treatments of various cost incurred during 2007 depends on whether these costs can be capitalised or expensed as per IPSAS 31. Based on the criteria prescribed (as described in section D, paragraph 6.2.2.2. of these Guidelines), these conclusions can be drawn: -

- ✓ It could be argued that the technical feasibility criterion was established at the end of August 2007, when the first prototype was produced.
- ✓ The intention to sell or use criterion was met at the end of August 2007 when the sample was tested with the air-conditioning components to ensure it functions.
- ✓ But it was not until October 2007 that the product marketability was established. The reason is attributable to the fact that the entity had doubts about the new models being compatible with air conditioners and that the sample would need further testing, had it not functioned.
- ✓ In October 2007, the existence of a market was clearly established.
- ✓ The financial feasibility and funding criterion was also clearly met as there was clear backing from the respective Ministry.
- ✓ One assumes that the newly formed department was able to measure its costs reliably, although this point was not addressed thoroughly in the question.

Expensed: the costs incurred **before October 2007** €175,000 + €250,000 + €300,000 + €80,000 = **€805,000.**
Capitalised: the costs incurred **after October 2007** except **conference costs of €50,000;** these are **expensed** because they are **independent** from the **development process**.

Based on the above, there are no costs to capitalise.

E. Measurement of Intangible Assets

1. IPSAS 31 An Intangible Asset may be acquired by means of:

1.1 **Exchange Transactions**: In this case its initial cost at the date of acquisition shall be measured at cost.

1.2 **Non-Exchange Transactions**: In this case its initial cost at the date of acquisition shall be measured at its fair value as at that date.

IPSAS Team Note

Exchange transactions: transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange (e.g. acquisition of software licences).

Non-exchange transactions: transactions in which one entity either receives value from another entity without directly giving approximately equal value in exchange, or gives to another entity without directly receiving approximately equal value in exchange (e.g. donation of an intangible heritage asset e.g. rights to historical movies).

Fair Value: the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Active market: a market in which all of the following conditions exist

- The items traded in the market are homogeneous;
- Willing buyers and sellers can normally be found at any time; and
- Prices are available to the public.

2. Measurement - **Separate Acquisition**

2.1 **Exchange** Transactions:

2.1.1 The initial costs at the date of acquisition would generally **include**:

i) the purchase price, including import duties, non-refundable purchase taxes after deducting trade discounts and rebates; and

ii) any directly attributable cost necessary to get the asset ready for its intended use, such as

- costs of employee benefits arising directly from bringing the asset to its working condition;
- professional fees arising directly from bringing the asset to its working condition; and
- costs of testing whether the asset is functioning properly

2.1.2 The following costs should be **excluded**:

2.1.2.1 Costs of introducing a new product or service (including costs of advertising and promotional activities);

2.1.2.2 Costs of conducting operations in a new location or with a new class of users of a service (including costs of staff training); and

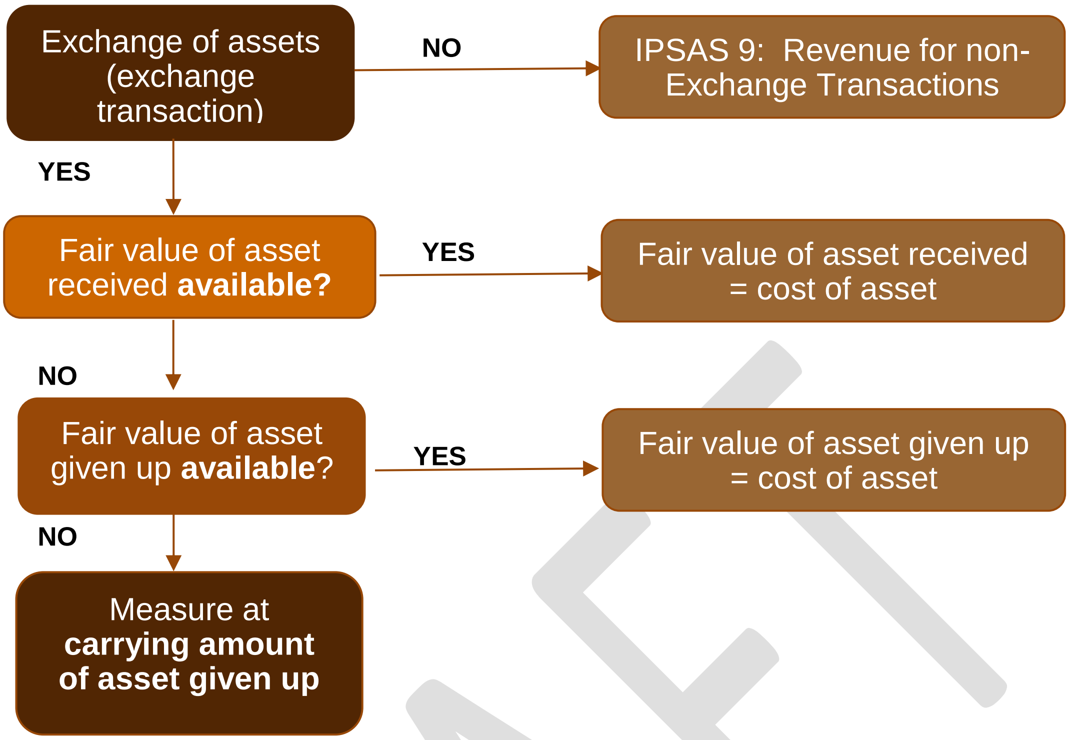
2.1.2.3 Administration and other general overhead costs.

2.1.3 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, therefore the following costs are also **excluded**:

2.1.3.1 Costs incurred while an asset capable of operating in the manner intended by management has yet to be brought into use; and

2.1.3.2 Initial operating deficits, such as those incurred while demand for the asset's output builds up.

2.1.4 Exchange Transactions for a **non-monetary asset**:



2.1.4.1 Example 7: Exchange Transactions for non-monetary assets

A department acquired a licence which meets the definition and recognition criteria of an intangible asset. This department acquired this licence in exchange for I.T. equipment. At transaction date the fair value of the licence was €12,000, the fair value of the I.T. equipment was €10,000 and the carrying amount of the I.T. equipment in the department's records was €9,000(original cost €11,000, and accumulated depreciation €2,000). The licence is recorded as an acquisition of an intangible asset. The I.T. equipment needs to be derecognised.

i) The department should initially recognise the licence acquired **at its fair value of** €12,000.

The journal entry would be as follows:

Debit Software Licences	€12,000
Debit Accumulated Depreciation (I.T. Equipment)	€2,000
Credit I.T. Equipment	€11,000
Credit Gain on sale of asset	€3,000

ii) Had the department **not** been able to reliably measure the fair value of the **licence**, then the licence would be initially recognised at the fair value of the I.T. equipment exchanged, that is at €10,000.

The journal entry would be as follows:

Debit Software Licences	€10,000
Debit Accumulated Depreciation (I.T. Equipment)	€2,000
Credit I.T. Equipment	€11,000
Credit Gain on sale of asset	€1,000

iii) Had the department **not** been able to reliably measure the fair value of either of the **licence** or the **I.T. equipment**, then the licence would have been initially recognised at the carrying amount of the I.T. equipment exchanged, that is at €9,000.

The journal entry would be as follows:

Debit Software Licences	€9,000
Debit Accumulated Depreciation (I.T. Equipment)	€2,000
Credit I.T. Equipment	€11,000

2.2 **Non-Exchange** Transactions:

2.2.1 The initial costs at the date of acquisition shall be measured at its fair value as at that date. For example, a Malta Literary Award Prize winner (a private citizen), may bequeath his or her personal papers, including the copyright to his or her publications to Government in a non-exchange transaction.

2.2.2 Fair Value is determined by reference to an active market (refer to IPSAS Team Note above [section E]).

3. Measurement - **Internally Generated Asset**

3.1 **Costs** of an Internally Generated Asset

3.1.1 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 (refer to section D, paragraph 6.2.3 to determine which costs should be recognised as part of the asset and which costs are to be expensed).

4. Measurement - **Subsequent Measurement**

4.1 <u>Cost Model vs. Revaluation Model:</u>

4.1.1 An entity shall apply the **cost model** as its accounting policy.

4.1.2 The revaluation model shall only apply in specific circumstances as determined by the pertinent government body. These circumstances mainly include rare cases were subsequent to recognition, there are assets whose fair value can be measured reliably (i.e. for which an active market exists). In such instances the asset can be carried at revalued amount less any accumulated amortisation and any accumulated impairment losses.

4.1.3 The chosen policy shall apply to an entire class of the asset.

4.1.4 An active market exists for only a few types of intangible assets and the revaluation model can only be used where such a market exists. For example, an active market cannot exist for brands, newspaper mastheads, film rights, patents, or trademarks, because each such asset is unique. Although such unique intangibles may be bought and sold, the prices are negotiated between individual buyers and sellers rather than quoted on an active market. The price paid for an asset in one transaction may not be a good guide to the fair value of another asset.

4.2 Cost Model

4.3 Revaluation Model

Fair Value − **Accumulated Amortisation & Accumulated Impairment losses** = **Carrying Amount**

4.3.1 Example 8: The Revaluation Model

A department acquired a licence, which meets the definition and recognition criteria of an intangible asset, at an initial cost of €15,000. The licence was purchased on 1 January 2009 and had a useful life of five years (the entity uses the straight-line method of amortisation). On 31st December 2010, the market value of the licence was €20,000. As at 31st December 2010, the accumulated amortisation amounted to €6,000.

Required: journal entries to reflect the revaluation of the Intangible Asset.

Solution

The journal entries would be as follows:

Debit Accumulated Amortisation	€6,000
Credit Intangible Asset	€6,000
Being the elimination of accumulated amortisation against the cost of the asset	

Debit Intangible Asset	€11,000
Credit Revaluation Surplus	€11,000
Being the increase in value following the revaluation of the licence value	

The revaluation increase is to be credited directly to the revaluation surplus. However, the increase shall be recognised in surplus or deficit to the extent that it reverses a revaluation decrease of the same class of assets previously recognised in surplus or deficit.

The revaluation surplus included in net assets/equity shall be transferred directly to accumulated surpluses or deficits when the assets are derecognised. Transfers from revaluation surplus to accumulated surpluses or deficits are not made through surplus or deficit.

Note that a *revaluation decrease* shall be recognised in surplus or deficit. However, the decrease shall be recognised directly in net assets/equity to the extent of any credit balance in the revaluation surplus in respect of that asset. The decrease recognised directly in net assets/equity reduces the amount accumulated in net assets/equity under the heading of revaluation surplus.

F. Amortisation

1. **Amortisation** is the systematic allocation of the amortisable amount of an intangible asset over its useful life.

> Systematic allocation means that the amortisation is charged according to a consistent policy and method (e.g. the straight line method).

2. The **Amortisable Amount** is the cost of an asset, or other amount substituted for cost, less its residual value.

3. The **Value** of an asset is reduced during its life because of:

   3.1 usage over the passage of time,
   3.2 contractual considerations, and
   3.3 technological outdating.

4. **Residual Value** is the estimated amount that an entity would currently receive from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Cost/Fair Value − **Residual Value** = **Amortisable Amount**

> **Recommended Accounting Practice** is to use a residual value of zero, unless at the end of the asset's usefulness to the department the residual value is likely to be significant.

4.1 **Example 9: Residual value**

A department acquired a patent that expires in 20 years. The product protected by the patented technology is expected to be a source of net cash inflows for at least 20 years. The patent would be amortised over its 20-year useful life to a nil residual value. If there is any indication that the patent is impaired at any reporting date, the patent would be reviewed for impairment.

4.2 **Example 10: Residual value**

On 1 January 2011 a department acquired a patent for €70,000 that expires in 20 years. The product protected by the patented technology is expected to be a source of net cash inflows for at least 20 years. The department has a commitment from ABC Ltd to purchase that patent in eight years for 50 per cent of the amount that the department paid for the patent (i.e. €35,000), and the department intends to sell the patent to ABC Ltd in eight years.
The patent has an economic life of 20 years and a useful life of eight years to the department.

5. The depreciable amount would be amortised over its eight-year useful life, with a residual value estimated at the present value of 50 per cent of the patent's fair value at the date it was acquired. If there is any indication that the patent is impaired at any reporting date, the patent would be reviewed for impairment. The **Useful life of an asset** can either be the **period** over which an asset is expected to be available for use by an entity or the number of production or similar **units** expected to be obtained from the asset by an entity.

5.1 An entity assesses the useful life or service potential of an intangible asset as either indefinite or finite.

5.1.1 **Indefinite useful life**: When there is no foreseeable limit to the period over which an asset is expected to generate net cash inflows or service potential for the entity; these intangible assets are not amortised.

<u>IPSAS Team Note</u>:

- '**Indefinite**' does **not** mean '**infinite**'.
- The useful life of an intangible asset reflects only that level of future maintenance expenditure required to maintain the asset at its <u>standard of performance</u> assessed at the time of estimating the asset's useful life, and the entity's ability and intention to reach such a level. A conclusion that the useful life of an intangible asset is **indefinite** should <u>not</u> depend on planned future expenditure in <u>excess</u> of that required to maintain the asset at that standard of performance.

5.1.2 **Finite useful life**: in this case the entity shall assess the length of, or number of production or similar units constituting, that useful life. Where an intangible asset arises from contractual rights or legal rights, the useful life of the intangible asset should not exceed the period of the contractual or legal rights, but may be shorter. If there is a specified term that the contract or legal right can be renewed without incurring significant cost, then the useful life should include the renewal period.

5.2 **Example 11: Useful life vs. Economic life of an intangible asset**

A department acquires software under licence for seven years—the shortest licence period offered by the licensor. The department expects to use the software for only the first five years of the licence period, while it develops its own tailor-made software. The best estimate of the useful life of the software held under licence is 5 years. The fact that the department has the right to use the software for seven years does not extend its useful life beyond the period over which the department expects to use the asset. Therefore, useful life is 5 years and the cost of the licence shall be amortised over 5 years.

5.3 Examples of factors to consider in determining an asset's expected useful life:

- ❖ Expected usage by the entity
- ❖ Product life cycles
- ❖ Rate of technical or commercial change
- ❖ Industry stability
- ❖ Legal restrictions
- ❖ Whether the useful life is dependent on the useful lives of other assets

6. Amortisation of an Intangible Asset:

6.1 Amortisation commences when the asset is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by management;

6.2 Amortisation continues even though the asset is idle, unless it is classified as held for sale. Amortisation shall cease when the asset is derecognized. Therefore, amortization does not cease when the asset becomes idle or is retired from active use and held for disposal/sale unless the asset is fully depreciated.

6.3 **Example12: Amortisation of a patented formula**

On 1 February 2011 a department purchased a patented formula. The patented formula was available for use on this date. However, the department only started producing inventory using the patented formula on 1 April 2011 because the department did not have the appropriate plant and equipment in place to begin production. The department should begin amortisation of the patent from 1 February 2011 that is when it was available for use.

7. Amortisation of an Intangible Asset: method

7.1 The amortisation method shall reflect the pattern in which the asset's future economic benefits or service potential is expected to be consumed by the entity.

7.2 The entity shall apply the **straight line method of amortisation**. Other methods may only be applied in specific circumstances as determined by the pertinent government body.

7.3 The department shall charge a full-year's amortisation expense in the year of acquisition and no amortisation expense in the year in which the asset is derecognised.

8. Straight Line Amortisation Method

8.1 The straight line method amortises cost evenly throughout the useful life of the fixed asset. Straight line amortisation is calculated as follows:

Amortisable Amount ÷ **Useful Life** = **Amortisation per annum**

8.2 **Example 13: the straight line method**

An asset has a useful life of 20 years.
Cost of the asset is €50,000.
Residual Value is €10,000.
Amortisable Amount is €50,000 - €10,000 = €40,000.
Annual amortisation cost will be 40,000/20 = **€2,000**

9. Amortisation Rates

9.1 The following are the useful lives and respective amortisation rates applicable to the Intangible Assets held by ministries and departments.
In some cases, a range is being presented as there may be assets within the same classification having different useful lives and therefore different amortisation rates.

Description of Asset	Useful Life (years)	Amortisation % Rate
Acquired software and websites	5 - 10	10 - 20
Internally developed software and websites	5 - 10	10 - 20
Trademarks, copyrights and patents	According to respective agreement or applicable law	According to respective agreement or applicable law
Licences and royalties	According to respective agreement – usually 10 – 20 yrs.	According to respective agreement – usually 5 - 10

10. Amortisation - Accounting Entries

10.1 At every accounting period, the amortisation of the intangible asset is expensed to the Statement of Financial Performance and credited to the Accumulated Amortisation account on the Statement of Financial Position.

Debit	Amortisation Expense (on the Statement of Financial Performance)
Credit	Accumulated Amortisation (on the Statement of Financial Position)

10.2 Accumulated amortisation is deducted from the respective asset's cost/fair value to arrive at the net book value that appears on the face of the Statement of Financial Position.

10.3 **Example 14: Accounting Entries**

The Ministry for Education and Employment purchased a software package for €5,000 on 1 January 2011. It had a useful life of five years over which it generated sales of €2,000 annually and incurred annual direct costs amounting to €900.

10.3.1 **Scenario A – incorrect approach:** If this Ministry expensed the entire cost of the software package in the year of acquisition, its Statement of Financial Performance for the five years would be as follows:

Statement of Financial Performance	2011	2012	2013	2014	2015
	€	€	€	€	€
Sales	2,000	2,000	2,000	2,000	2,000
Cost of Sales	(900)	(900)	(900)	(900)	(900)
Cost of software package	(5,000)	-	-	-	-
Net (Deficit)/ Surplus	(3,900)	1,100	1,100	1,100	1,100

10.3.1.1 The Statement of Financial Performance of this Ministry shows a net deficit in the first year, unlike the other subsequent years, even though the sales generated and the cost of sales were constant during this five-year period.

10.3.1.2 Furthermore, although this Ministry earned revenue from the use of the software package over the five-year period, this software package will not appear as an intangible asset on its Statement of Financial Position.

10.3.2 **Scenario B – correct approach**. If the Ministry capitalised the cost of the software package as an intangible asset and amortised the cost over five years (the useful life of the asset), its Statement Financial Position and Statement of Financial Performance would be as follows:

Statement of Financial Position	2011	2012	2013	2014	2015
	€	€	€	€	€
Intangible Assets	5,000	5.000	5,000	5,000	5,000
Accumulated Amortisation	(1,000)	(2,000)	(3,000)	(4,000)	(5,000)
Net Book Value	4,000	3,000	2,000	1,000	Nil

Statement of Financial Performance	2011	2012	2013	2014	2015
	€	€	€	€	€
Sales	2,000	2,000	2,000	2,000	2,000
Cost of Sales	(900)	(900)	(900)	(900)	(900)
Cost of software package (amortisation)	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)
Net Surplus	100	100	100	100	100

10.3.2.1 The matching of costs to the corresponding periods of economic benefits in **Scenario B** presents a more balanced view of the surplus generated by the department. Using the above example, the following double entries will be recorded in respect of amortisation:

Amortisation Expense Account						
Debit		€		Credit		€
2011	Accumulated Amortisation	1,000		2011	Statement of Financial Performance	1,000
2012	Accumulated Amortisation	1,000		2012	Statement of Financial Performance	1,000
2013	Accumulated Amortisation	1,000		2013	Statement of Financial Performance	1,000
2014	Accumulated Amortisation	1,000		2014	Statement of Financial Performance	1,000
2015	Accumulated Amortisation	1,000		2015	Statement of Financial Performance	1,000

Accumulated Amortisation Account						
Debit		€	Credit		€
2011	Balance c/d	1,000	2011	Amortisation Expense	1,000
		1,000	2011		1,000
2012	Balance c/d	2,000	2012	Balance b/d	1,000
				Amortisation Expense	1,000
		2,000	2012		2,000
2013	Balance c/d	3,000	2013	Balance b/d	2,000
				Amortisation Expense	1,000
		3,000	2013		3,000
2014	Balance c/d	4,000	2014	Balance b/d	3,000
				Amortisation Expense	1,000
		4,000	2014		4,000
2015	Balance c/d	5,000	2015	Balance b/d	4,000
				Amortisation Expense	1,000
		5,000	2015		5,000

G. Impairment

1. Impairment is the loss in the future economic benefits or service potential of an asset, over and above amortisation. Impairment reflects a decline in the utility of an asset to the entity that controls it. For example, a new software version will have a direct impact on the value of the software currently in use.

2. At each reporting date, the entity needs to assess (in accordance with IPSAS 21 on Impairment of Non-cash-generating Assets and IPSAS 26 on Impairment of Cash-generating Assets) whether or not there is an indication that an intangible asset might be impaired. If there is an indication of impairment, then the recoverable amount or recoverable service amount should be determined respectively.

> IPSAS Team Note:
>
> An intangible asset with an **indefinite useful life** must be assessed for impairment annually **and** whenever there is an indication that the asset may be impaired.

3. When assets are carried at cost under the cost model, any impairment loss or reversal of impairment loss is recognised in surplus or deficit.

4. When in specific circumstances assets are carried at revalued amounts, an impairment loss is treated as a revaluation decrease – i.e. the impairment is recognised in the revaluation reserve to the extent of a revaluation surplus available beyond which the amount is recognised in surplus or deficit.

5. When compensation is expected from third parties for intangible assets that were impaired, lost or given up, it is included in surplus or deficit when the compensation amount becomes receivable.

H. Derecognition

1. Derecognition of an intangible asset is the removal of an intangible asset from the Statement of Financial Position.

2. Situations determining removal of an intangible asset – an intangible asset is derecognised:

- On disposal for example: sold, donated, scrapped, transferred etc.
- When no future economic benefits or service potential are expected from its use or disposal.

3. Gains and losses from derecognition of intangible assets

3.1 The gain or loss arising from the derecognition of an intangible asset is determined as follows:

Net Disposal Proceeds − **Carrying Amount** = **Gain / (Loss)**

3.2 The gain or loss is recognised in surplus or deficit when the asset is derecognised.

3.3 **Example 15: Derecognition of intangible assets**

A software package that originally cost €25,000 and had accumulated amortisation on it of €16,000 was disposed of during the year for €8,000 cash. How should the disposal be accounted for in the financial statements?

Solution

The asset cost of €25,000 and its associated amortisation of €16,000 should be removed from the Statement of Financial Position and transferred to a disposal account. The cash received of €8,000 is recorded as a cash receipt and credited to the disposal account. The balance on the disposal account is the gain or loss on disposal which should be recorded in the Statement of Financial Performance:

In this example, the loss on disposal is:

Carrying amount at disposal date (€25,000 – €16,000)	€9,000
Disposal proceeds	€8,000
Loss on disposal	**€1,000**

Net Disposal Proceeds
€8,000

-

Carrying Amount
(€25,000 – €16,000) = €9,000

=

Gain / (Loss)
-€1,000

4. Example 16: Accounting for Intangible Assets

Department A acquired a new accounting software to process daily transactions and compile various relevant financial reports. Department A needs 6 licences to use this software (*version 1.1.2010)* as six members of staff will work on the system. One licence costs € 2,000, and therefore €12,000 were paid on 1 January 2010 for these 6 licences.

Note:
- The reporting date is 31 December.
- The license fees have a lifetime of 3 years, following which they are subject to renewal with a 15% increase in fees.

The accounting treatment shall be as follows:
The accounting software is recognised as an intangible asset on acquisition date. The licence fees paid are capitalised and amortised over a period of 3 years starting from 1 January 2010.

The journal entries will be as follows for the **first year**:

1 January 2010	Debit	Credit
	€	€
Software Licences *[€2,000 x 6]*	12,000	
Bank		12,000
Being the recognition of software acquired and paid.		

31 December 2010	Debit	Credit
	€	€
Amortisation *[€12,000/3]*	4,000	
Accumulated amortisation		4,000
Being the recognition of amortisation of the software licence fees.		

Assuming that Department A renewed the licence fees for the six users on 1 January 2014, the carrying amount of the expired licence fees will be derecognised and upon renewal the new cost of the licence fees will be recognised:

1 January 2014	Debit	Credit
	€	€
Accumulated amortisation (old licence fees) *[€4,000 x 3]*	12,000	
Software Licence fees (old licence fees)		12,000
Software Licence fees (renewed) *[increase of 15%, €12,000 x 1.15 = €13,800]*	13,800	
Bank		13,800
Being derecognition of the carrying amount of the 'old' licence fees and recognition of the renewed licence fees.		

31 December 2014	Debit	Credit
	€	€
Amortisation *[€13,800/3]*	4,600	
Accumulated amortisation		4,600
Being the amortisation of the renewed licence fees.		

On 31 December 2014, the software distributor launched an upgrade to version 1.1.2010 - version 1.1.2014.

Department A decided to purchase the new software (as it had additional features and new functionalities).

The new software was acquired on 1 January 2015. €15,000 (full price) were paid for the acquisition of six licences having a lifetime of 3 years.

Note:
In some cases, the 'Upgrade price' may be discounted for holders of an older version.
In this case, the new carrying amount should be the lower of:
a) The cost of the new software, had a full price been paid;
b) The amount paid + carrying amount of previous software version.
A reassessment of the remaining useful life may be necessary.

As Department A is effectively replacing the original accounting software purchased, the carrying amount, on acquisition date of the new software, should be derecognised and the cost of the new software capitalised. The journal entries are as follows:

1 January 2015	**Debit**	**Credit**
	€	€
Accumulated amortisation (old version)	4,600	
Software Licence fees (old version)		4,600
Software Licence fees (upgraded version) (€2,500 x 6)	15,000	
Bank		15,000
Being derecognition of the carrying amount of 'old version' licence fees and the recognition of 'upgraded version' licence fees.		

31 December 2015	**Debit**	**Credit**
	€	€
Amortisation – licence fees (€15,000/3)	5,000	
Accumulated amortisation		5,000
Being amortisation of 'upgraded' software licence fees.		

I. Disclosure and Reporting of Intangible Assets

1. IPSAS 31 provides that the disclosures concerning intangible assets must be made in the following components of the financial statements:

- Statement of Financial Position – shows all items of assets and liabilities as at the end of the financial period and shows a breakdown of the net asset position.
- Statement of Financial Performance – shows all items of revenue and expense recognised in a financial period and the surplus or deficit of total revenues against expenses.
- Statement of Cash Flows – shows how cash was used by the department during the period, and linking the two previous financial statements; and
- Notes to the Financial Statements – shows important and useful details of the summary information provided in the Financial Statements.

1.1 **Statement of Financial Position**

1.1.1 At the end of the reporting period, the total of the carrying amount of all Intangible Assets is shown as a "Non-current Asset" in the Statement of Financial Position.

1.1.2 The different classes of Intangible Assets are only presented (i.e. shown) in the Notes, not on the face of the Financial Statements.

1.1.3 Comparative figures (previous year amounts) will not be provided in the first year of IPSAS compliance but a reconciliation between beginning and ending balances of Intangible Assets for the first year of IPSAS compliance is still required in the Notes to the Financial Statements.

1.1.4 The following extract illustrates how Intangible Assets should be reported on the face of the **Statement of Financial Position**:

Statement of Financial Position as at 31st December 2013 (extract)				
NON CURRENT ASSETS	Notes	2013 (€)	2012 (€)	
Receivables from Exchange Transactions		X	X	IPSAS 1.88 (h)
Investments		X	X	IPSAS 1.88 (e)
Intangible assets	41	X	X	IPSAS 1.88 (c)
Property, plant and equipment	40	X	X	IPSAS 1.88 (a)
		X	X	IPSAS 1.70

1.2 **Statement of Financial Performance**

1.2.1 Disclosure in the Statement of Financial Performance related to Intangible Assets include amortisation and impairment losses and losses/gains on disposal in the "Expenses" section of that statement (if material, impairment losses can be shown as a separate line item, otherwise they can be recorded under "Other expenses").

1.2.2 Gains from sale of Intangible Assets shall not be classified as revenue. Gains are deducted from expenses.

1.2.3 The following extract illustrates how Intangible Assets should be reported on the face of the **Statement of Financial Performance**:

Statement of Financial Performance for the year ended 31st December 2013 (extract)				
	Notes	2013 (€)	2012 (€)	
Expenses				IPSAS 1.109 - 112
Wages, salaries & employee benefits		x	x	
Supplies and consumables used		x	x	
Depreciation and amortization expense	25	x	x	
Impairment of PP&E and Intangible Assets		x	x	
General expenses		x	x	
Total expenses		x	x	

1.3 Statement of Cash Flows

1.3.1 The following extract illustrates how Intangible Assets should be reported on the face of the Statement of Cash Flows:

Statement of Cash Flows for the year ended 31st December 2013 (extract)				
	Notes	2013 (€)	2012 (€)	
Cash flows from investing activities				IPSAS 2.18, IPSAS 2.31
Purchase of property, plant, equipment and intangible assets		X	X	IPSAS 2.25 (a)
Proceeds from sale of property, plant and equipment and intangible assets		X	X	IPSAS 2.25 (b)
Decrease in non-current receivables		X	X	
Increase in investments		X	X	IPSAS 2.25 (c)
Net cash flows used in investing activities		X	X	

1.4 Notes to the Financial Statements

An entity shall disclose the following for each class of intangible assets, distinguishing between internally generated intangible assets and other intangible assets:

(a) Whether the useful lives are **indefinite or finite** and, if finite, **the useful lives or the amortisation rates used**;

(b) The **amortisation methods used** for intangible assets with finite useful lives;

(c) The **gross carrying amount** and any **accumulated amortisation** (aggregated with accumulated impairment losses) at the beginning and end of the period;

(d) **The line item(s)** of the statement of financial performance in which any amortisation of intangible assets is included;

(e) A **reconciliation** of the carrying amount at the beginning and end of the period showing:

(i) **Additions**, indicating separately those from internal development and those acquired separately;

(ii) Increases or decreases during the period resulting from **revaluations**;

(iii) **Impairment losses** recognized in surplus or deficit during the period;

(iv) **Impairment losses reversed** in surplus or deficit during the period;

(v) Any **amortisation** recognized during the period;

(vi) **Net exchange differences** arising on the translation of the financial statements into the presentation currency, and on the translation of a foreign operation into the presentation currency of the entity; and

(vii) **Other changes** in the carrying amount during the period, for example disposal.

An entity shall also disclose:

(a) For an intangible asset assessed as having an indefinite useful life, **the carrying amount of that asset and the reasons supporting the assessment of an indefinite useful life**. In giving these reasons, the entity shall describe the factor(s) that played a significant role in determining that the asset has an indefinite useful life.

(b) **A description, the carrying amount, and remaining amortisation period** of any individual intangible asset that is material to the entity's financial statements.

(c) For **intangible assets acquired through a non-exchange transaction** and initially recognized at fair value:

(i) The fair value initially recognized for these assets;

(ii) Their carrying amount; and

(iii) Whether they are measured after recognition under the cost model or the revaluation model (if one of the abovementioned specific circumstances).

(d) The existence and carrying amounts of **intangible assets whose title is restricted** and the carrying amounts of **intangible assets pledged as security** for liabilities.

(e) The amount of **contractual commitments** for the acquisition of intangible assets.

If intangible assets are accounted for **at revalued amounts** (i.e. the asset in question is one of those very specific cases), an entity shall disclose the following:

(a) By class of intangible assets:

(i) The effective date of the revaluation;

(ii) The carrying amount of revalued intangible assets; and

(iii) The carrying amount that would have been recognized had the revalued class of intangible assets been measured after recognition using the cost model;

(b) The **amount of the revaluation surplus** that relates to intangible assets at the beginning and end of the reporting period, indicating the changes during the reporting period and any restrictions on the distribution of the balance to owners; and

(c) The **methods and significant assumptions** applied in estimating the assets' fair values.

Other general disclosures:

An entity shall disclose the aggregate amount of **research and development expenditure** recognized as an expense during the period.

As previously mentioned (Section C4) if the cost or value of **Intangible Heritage Assets** cannot be reliably determined, the Financial Statements shall **disclose a description** of such intangible heritage assets held by the entity.

<u>Example</u> – extract of the Notes to the Financial Statements

Significant accounting policies - Intangible assets

3. Intangible Assets

Intangible assets acquired separately are initially recognised at cost. The cost of intangible assets acquired in a non-exchange transaction is their fair value at the date of the exchange.
Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses.

3.1 Internally generated computer software
Software development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalised only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits or service potential is probable, and Government intends to and has sufficient resources to complete development and to use or sell the asset.

The expenditure capitalised includes the cost of materials, direct labour and overheads that are directly attributable to preparing the asset for its intended use. Other development expenditure is not capitalised and is reflected in surplus or deficit in the period in which the expenditure is incurred.

3.2 Software Licences
Software licences that are identifiable or arise from contractual or other legal rights are recognised as intangible assets if it is probable that the expected future economic benefits or service potential that is attributable to the asset will flow to the entity and the cost of the asset can be measured reliably.

Example – extract of the Notes to the Financial Statements (contd.)

3.3 Subsequent expenditure

Subsequent expenditure is capitalised only when it increases the future economic benefits or service potential embodied in the specific asset to which it relates. All other expenditure is reflected in surplus or deficit in the period in which the expenditure is incurred.

3.4 Amortisation

Amortisation is calculated over the cost of the asset, or other amount substituted for cost, less its residual value.

Amortisation is recognised in surplus or deficit on a straight-line basis over the estimated useful lives of intangible assets, from the date that they are available for use, since this most closely reflects the expected patterns of consumption of the future economic benefits or service potential embodied in the asset.

The useful life of the intangible assets is assessed as either finite or indefinite. Intangible assets with a finite life are amortised over their useful life as follows:

Internally generated computer software	10 years
Software licences	5 years

The amortisation period and the amortisation method, for an intangible asset with a finite useful life, are reviewed at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate.

Intangible assets with a finite useful life are assessed for impairment whenever there is an indication that the asset may be impaired.

Intangible assets with indefinite useful lives are not amortised, but are tested annually for impairment, and more frequently whenever there is an indication that the asset may be impaired.

3.5 Derecognition

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in surplus or deficit when the asset is derecognised.

Example – extract of the Notes to the Financial Statements (contd.)

	Internally generated computer software	Software licences	Total
	€	€	€
Cost			
At 1 January 2012	11,000,000	3,000,000	14,000,000
Additions	500,000	-	500,000
At 31 December 2013	**11,500,000**	**3,000,000**	**14,500,000**
At 1 January 2013	11,500,000	3,000,000	14,500,000
Additions	500,000	1,000,000	1,500,000
At 31 December 2014	**12,000,000**	**4,000,000**	**16,000,000**
Amortisation and impairment			
At 1 January 2012	3,300,000	1,800,000	5,100,000
Amortisation	1,150,000	600,000	1,750,000
At 31 December 2013	**4,450,000**	**2,400,000**	**6,850,000**
At 1 January 2013	4,450,000	2,400,000	6,850,000
Amortisation	1,200,000	800,000	2,000,000
Impairment	-	100,000	100,000
At 31 December 2014	**5,650,000**	**3,300,000**	**8,950,000**
Net Book Values			
At 31 December 2014	**6,350,000**	**700,000**	**7,050,000**
At 31 December 2013	**7,050,000**	**600,000**	**7,650,000**

Glossary

''Accruals-based accounting'' Accruals-based accounting is a system of accounting based on the accrual principal, under which revenue is recognised (recorded) when earned, and expenses are recognised when incurred.

''Amortisable amount'' Amortisable amount is the cost of an asset, or other amount substituted for cost, less its residual value.

''Amortisation'' Amortisation is the systematic allocation of the amortisable amount of an asset over its useful life.

''Asset'' An asset is a resource presently controlled by the entity as a result of a past event and from which future economic benefits or service potential are expected to flow to the entity.

''Carrying amount (aka Net Book Value)'' The carrying amount is the amount at which an asset is recognised after deducting any accumulated amortisation and impairment losses.

''Cash-based accounting'' Cash-based accounting is an accounting method in which income is recorded when cash is received, and expenses are recorded when cash is paid.

''Central Government Entities (CGEs)'' The term CGEs refers only to ministries and departments of the Government of Malta.

''Class of Intangible Assets'' A Class of Intangible Assets is a grouping of assets of a similar nature or function in an entity's operations that is shown as a single line-item for the purpose of reporting value and providing disclosure in the financial statements.

''Derecognition'' Derecognition of Intangible Assets is the removal of an intangible asset from the Statement of Financial Position.

''Development'' 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.

''Fair Value'' Fair Value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

''Impairment'' Impairment is the loss in the future economic benefits or service potential of an asset, over and above amortisation. Impairment reflects a decline in the utility of an asset to the entity that controls it.

''Intangible Assets'' Intangible Assets are non-monetary assets which are without physical substance and identifiable (either being separable or arising from contractual or other legal rights).

''International Public Sector Accounting Standards (IPSAS)'' IPSAS are a set of accrual-based accounting standards issued by the IPSAS Board for use by public sector entities around the world in the preparation of financial statements.

''Intangible Heritage Assets'' Intangible Heritage Assets are assets having a cultural, environmental, or historical significance.

''Research'' is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

''Residual value'' Residual value is the estimated amount that an entity would currently receive from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

''Resource'' A resource is an item with service potential or the ability to generate economic benefits. Physical form is not a necessary condition of a resource. The service potential or ability to generate economic benefits can arise directly from the resource itself or from the rights to use the resource.

''Service Potential'' Service potential is the capacity to provide services that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating net cash inflows.

''Useful life'' Useful life is the period over which an asset is expected to be available for use by an entity, or the number of production or similar units expected to be obtained from the asset by an entity.

Amendments to draft Guidelines

Amendments[3] made to the original draft guidelines:
Section C [paras 2, 2.1, 3 IPSAS Team Decisions]
Section D [paras 6.2.3, example 6.2.5]
Section E [1 IPSAS Team Note, 2.1.4.1, 2.2, 3, 4]
Section F [paras 6, 7]
Section H [paras 3, 3.3 example 15, 4 example 16]
Section I [para 1.4(e)]

[3] *Only the most significant amendments have been included*