

Capitalization of internally developed software

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US Chapter of ICAN

Topics to be covered

- Definition of Internal-Use Software
- Capitalization Criteria
- Stages of Software Capitalization
- Capital or Operating Expenditures
- Amortization
- Impairment / Abandonment
- Responsibility

Definition of Internal-Use Software

- Per ASC 350-40, internal-use software has both of the following characteristics:
 - The software is internally developed, acquired, or modified solely to meet the entity's internal needs.
 - During the software's development or modification, no substantive plan exists or is being developed to license or sell the software externally.
- Per ASU 2015-05, SaaS (Software as a Service) is considered internal use software, since the customer has no contractual right to take possession of the software or run the software on its own hardware or contract with a third party to host the software, and is subject to the rules of ASC 350-40.

Capitalization Criteria

- Software cost is greater than \$10,000 (per Organization's policy)
- The software has an expected useful life of greater than 12 months.
- Capitalization of qualifying costs should begin when both occur:
 - Preliminary project phase is completed
 - Management, with relevant authority, implicitly or explicitly authorizes and commits funding to a computer software project and it is probable that the project will be completed and the software used to perform the function intended
- Capitalization should cease no later than the point at which a computer software project is substantially completed and ready for its intended use. ASC 350-40-25-14 indicates that “ready for its intended use” occurs after all substantial testing is completed.

Stages of Software Capitalization

**INTANGIBLE ASSETS
CAPITALIZED SOFTWARE**

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

Capital or Expense Expenditures

The following table summarizes company policy regarding the capitalization of specific costs during the software development:

ITEM	CAPITAL	EXPENSE
Design of software, configuration, interfaces, data mapping and coding – internal labor costs and fringe, or external labor and other costs	X	
Software licenses acquired	X	
Software configuration	X	
Travel costs associated directly with software development	X	
Support services (desktop services, helpdesk)		X
Internal and external training costs, including travel costs		X
Maintenance		X
General and Administrative costs		X
Research and Development Cost		X

Amortization

- In accordance with GAAP and company policy, the cost of internal use software should be amortized on a straight-line basis, beginning with the software is available for its intended use, generally between 3-5 years. Exceptions are to be approved by the responsible authority (Controller). The ASC 350-40-35-5 observes that useful lives are often short because of the speed of technological change. All depreciation of software should be reflected in the P&L line item titled “amortization”.

Impairment / Abandonment

- Software is subject to impairment testing when a triggering event occurs that suggests software may be impaired. If internal-use software ceases to be used, or it is no longer probable that software under construction will be placed in service, entity must record software at zero carrying value unless a FMV greater than zero can be shown.

Responsibility:

- Policy owner (Controller/Director)
- Responsible party (Manager/Sr Accountants)

Thank you