Urgent Issues Group

Interpretation 132 July 2004

Intangible Assets – Web Site Costs



Australian Government

Australian Accounting Standards Board

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PREFACE

Reasons for Issuing UIG Interpretation 132

The Australian Accounting Standards Board (AASB) is implementing the Financial Reporting Council's policy of adopting the Standards of the International Accounting Standards Board (IASB) for application to reporting periods beginning on or after 1 January 2005. The AASB has decided it will continue to issue sector-neutral Standards, that is, Standards applicable to both for-profit and not-for-profit entities, including public sector entities. Except for Standards that are specific to the not-for-profit or public sectors or that are of a purely domestic nature, the AASB is using the IASB Standards as the "foundation" Standards to which it adds material detailing the scope and applicability of a Standard in the Australian environment. Additions are made, where necessary, to broaden the content to cover sectors not addressed by an IASB Standard and domestic, regulatory or other issues.

The same approach applies to UIG pronouncements. This Interpretation is part of the set of Australian equivalents to each International Accounting Standard (IAS), International Financial Reporting Standard (IFRS) and Interpretation of the IASB (collectively defined by the IASB as IFRSs). This set includes UIG Interpretations that correspond to the IASB Interpretations originated by the International Financial Reporting Interpretations Committee (IFRIC) or the former Standing Interpretations Committee (SIC).

Main Features of this Interpretation

This Interpretation is applicable to annual reporting periods beginning on or after 1 January 2005. To promote comparability among the financial reports of Australian entities, early adoption of this Interpretation is not permitted.

Application of this Interpretation will begin in the first annual reporting period beginning on or after 1 January 2005 in the context of adopting all Australian equivalents to IFRSs. The requirements of Accounting Standard AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*, the Australian equivalent of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, must be observed. AASB 1 requires prior period information, presented as comparative information, to be restated as if the requirements of this Interpretation had always applied. This differs from previous Australian requirements where changes in accounting policies did not require the restatement of the income statement and balance sheet of the preceding period.

The Interpretation specifies that a web site developed by an entity for its own use is an internally generated intangible asset, and therefore subject to the

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recognition and measurement requirements of AASB 138 *Intangible Assets*. It identifies various stages in the development of the web site, and sets out whether costs incurred by the entity during the various development stages and the operation of the web site can be included in the cost of the web site as an intangible asset. For example, all expenditure on developing a web site solely or primarily for promoting and advertising an entity's own products and services is required to be recognised as an expense when incurred. As a general rule, costs incurred during the planning stage are recognised as an expense whereas other costs are recognised as an intangible asset if, and only if, the entity is able to demonstrate in accordance with AASB 138 that the web site will generate probable future economic benefits.

Comparison with Superseded Requirements

UIG Interpretation 132 supersedes Abstract 37 Accounting for Web Site Costs. Although the requirements are substantially similar, there are some differences between the pronouncements. For example, Interpretation 132 requires all costs incurred in the planning stage to be expensed when incurred, whereas Abstract 37 indicated that some planning stage costs potentially could be recognised as an asset, such as the costs of documenting the specifications of the web site, including the technology to be adopted to achieve the desired functionalities.

A further difference is that Abstract 37 indicated that some costs incurred during the operation stage potentially could be recognised as an asset if they extended the originally assessed standard of performance of the web site. However, Interpretation 132 applies the general asset recognition criteria to determining the treatment of subsequent expenditure relating to the web site (based on the requirements of AASB 116 *Property, Plant and Equipment*), and concludes that it would be rare for costs incurred in the operating stage to be recognised as an asset.

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COMPARISON WITH INTERNATIONAL PRONOUNCEMENTS

UIG Interpretation 132 is equivalent to Standing Interpretations Committee Interpretation SIC-32 *Intangible Assets – Web Site Costs*, issued by the IASB. Paragraphs that have been added to this Interpretation (and do not appear in the text of the equivalent SIC Interpretation) are identified with the prefix "Aus", followed by the number of the relevant SIC paragraph and decimal numbering.

Entities that comply with Interpretation 132 will simultaneously be in compliance with SIC-32.

International Public Sector Accounting Standards (IPSASs) are issued by the Public Sector Committee of the International Federation of Accountants. There is no specific IPSAS dealing with accounting for intangible assets at present.

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URGENT ISSUES GROUP INTERPRETATION 132

INTANGIBLE ASSETS – WEB SITE COSTS

ISSUE

- 1. An entity may incur internal expenditure on the development and operation of its own web site for internal or external access. A web site designed for external access may be used for various purposes such as to promote and advertise an entity's own products and services, provide electronic services, and sell products and services. A web site designed for internal access may be used to store company policies and customer details, and search relevant information.
- 2. The stages of a web site's development can be described as follows:
 - Planning includes undertaking feasibility studies, defining objectives and specifications, evaluating alternatives and selecting preferences;
 - (b) Application and Infrastructure Development includes obtaining a domain name, purchasing and developing hardware and operating software, installing developed applications and stress testing;
 - (c) Graphical Design Development includes designing the appearance of web pages; and
 - (d) Content Development includes creating, purchasing, preparing and uploading information, either textual or graphical in nature, on the web site before the completion of the web site's development. This information may either be stored in separate databases that are integrated into (or accessed from) the web site or coded directly into the web pages.
- 3. Once development of a web site has been completed, the Operating stage begins. During this stage, an entity maintains and enhances the applications, infrastructure, graphical design and content of the web site.
- 4. When accounting for internal expenditure on the development and operation of an entity's own web site for internal or external access, the issues are:

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- (a) whether the web site is an internally generated intangible asset that is subject to the requirements of Accounting Standard AASB 138 *Intangible Assets*; and
- (b) the appropriate accounting treatment of such expenditure.
- 5. This Interpretation does not apply to expenditure on purchasing, developing, and operating hardware (e.g. web servers, staging servers, production servers and Internet connections) of a web site. Such expenditure is accounted for under AASB 116 *Property, Plant and Equipment.* Additionally, when an entity incurs expenditure on an Internet service provider hosting the entity's web site, the expenditure is recognised as an expense under AASB 101 *Presentation of Financial Statements*, paragraph 78, and the *Framework for the Preparation and Presentation of Financial Statements* when the services are received.
- 6. AASB 138 does not apply to intangible assets held by an entity for sale in the ordinary course of business (see AASB 102 *Inventories* and AASB 111 *Construction Contracts*) or leases that fall within the scope of AASB 117 *Leases*. Accordingly, this Interpretation does not apply to expenditure on the development or operation of a web site (or web site software) for sale to another entity. When a web site is leased under an operating lease, the lessor applies this Interpretation. When a web site is leased under a finance lease, the lessee applies this Interpretation after initial recognition of the leased asset.

CONSENSUS

- 7. An entity's own web site that arises from development and is for internal or external access is an internally generated intangible asset that is subject to the requirements of AASB 138.
- 8. A web site arising from development shall be recognised as an intangible asset if, and only if, in addition to complying with the general requirements described in AASB 138.21 for recognition and initial measurement, an entity can satisfy the requirements in AASB 138.57. In particular, an entity may be able to satisfy the requirement to demonstrate how its web site will generate probable future economic benefits in accordance with AASB 138.57(d) when, for example, the web site is capable of generating revenues, including direct revenues from enabling orders to be placed. An entity is not able to demonstrate how a web site developed solely or primarily for promoting and advertising its own products and services will generate probable future economic

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benefits, and consequently all expenditure on developing such a web site shall be recognised as an expense when incurred.

- 9. Any internal expenditure on the development and operation of an entity's own web site shall be accounted for in accordance with AASB 138. The nature of each activity for which expenditure is incurred (e.g. training employees and maintaining the web site) and the web site's stage of development or post-development shall be evaluated to determine the appropriate accounting treatment (additional guidance is provided in the Appendix to this Interpretation). For example:
 - (a) the Planning stage is similar in nature to the research phase in AASB 138.54-.56. Expenditure incurred in this stage shall be recognised as an expense when it is incurred;
 - **(b)** the Application and Infrastructure Development stage, the Graphical Design stage and the Content Development stage, to the extent that content is developed for purposes other than to advertise and promote an entity's own products and services, are similar in nature to the development phase in AASB 138.57-.64. Expenditure incurred in these stages shall be included in the cost of a web site recognised as an intangible asset in accordance with paragraph 8 of this Interpretation when the expenditure can be directly attributed and is necessary to creating, producing or preparing the web site for it to be capable of operating in the manner intended by management. For example, expenditure on purchasing or creating content (other than content that advertises and promotes an entity's own products and services) specifically for a web site, or expenditure to enable use of the content (e.g. a fee for acquiring a licence to reproduce) on the web site, shall be included in the cost of development when this condition is met. However, in accordance with AASB 138.71, expenditure on an intangible item that was initially recognised as an expense in previous financial statements shall not be recognised as part of the cost of an intangible asset at a later date (e.g. if the costs of a copyright have been fully amortised, and the content is subsequently provided on a web site):
 - (c) expenditure incurred in the Content Development stage, to the extent that content is developed to advertise and promote an entity's own products and services (e.g. digital photographs of products), shall be recognised as an expense when incurred in accordance with AASB 138.69(c). For

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example, when accounting for expenditure on professional services for taking digital photographs of an entity's own products and for enhancing their display, expenditure shall be recognised as an expense as the professional services are received during the process, not when the digital photographs are displayed on the web site; and

- (d) the Operating stage begins once development of a web site is complete. Expenditure incurred in this stage shall be recognised as an expense when it is incurred unless it meets the recognition criteria in AASB 138.18.
- 10. A web site that is recognised as an intangible asset under paragraph 8 of this Interpretation shall be measured after initial recognition by applying the requirements of AASB 138.72-.87. The best estimate of a web site's useful life shall be short.

Application

- Aus10.1 This Interpretation applies when AASB 138 applies.
- Aus10.2 This Interpretation applies to annual reporting periods beginning on or after 1 January 2005.
- Aus10.3 This Interpretation shall not be applied to annual reporting periods beginning before 1 January 2005.
- Aus10.4 The requirements specified in this Interpretation apply to the financial report where information resulting from their application is material in accordance with AASB 1031 *Materiality*.
- Aus10.5 When applicable, this Interpretation supersedes Abstract 37 Accounting for Web Site Costs, as issued in January 2001.
- Aus10.6 Abstract 37 remains applicable until superseded by this Interpretation.

DISCUSSION

11. An intangible asset is defined in AASB 138.8 as an identifiable nonmonetary asset without physical substance. AASB 138.9 provides computer software as a common example of an intangible asset. By analogy, a web site is another example of an intangible asset.

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- AASB 138.68 requires expenditure on an intangible item to be 12 recognised as an expense when incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria in AASB 138.18-.67. AASB 138.69 requires expenditure on start-up activities to be recognised as an expense when incurred. An entity developing its own web site for internal or external access is not undertaking a start-up activity to the extent that an internally generated intangible asset is created. The requirements and guidance in AASB 138.52-.67, in addition to the general requirements described in AASB 138.21 for recognition and initial measurement of an intangible asset, apply to expenditure incurred on the development of an entity's own web site. As described in AASB 138.65-.67, the cost of a web site recognised as an internally generated intangible asset comprises all expenditure that can be directly attributed and is necessary to creating, producing and preparing the asset for it to be capable of operating in the manner intended by management.
- 13. AASB 138.54 requires expenditure on research (or on the research phase of an internal project) to be recognised as an expense when incurred. The examples provided in AASB 138.56 are similar to the activities undertaken in the Planning stage of a web site's development. Consequently, expenditure incurred in the Planning stage of a web site's development is recognised as an expense when incurred.
- 14. AASB 138.57 requires an intangible asset arising from the development phase of an internal project to be recognised only if an entity can demonstrate fulfilment of the six criteria specified. One of the criteria is to demonstrate how a web site will generate probable future economic benefits (AASB 138.57(d)). AASB 138.60 indicates that this criterion is met by assessing the economic benefits to be received from the web site and using the principles in AASB 136 Impairment of Assets, which considers the present value of estimated future cash flows from continuing use of the web site. Future economic benefits flowing from an intangible asset, as stated in AASB 138.17, may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity. Therefore, future economic benefits from a web site may be assessed when the web site is capable of generating revenues. A web site developed solely or primarily for advertising and promoting an entity's own products and services is not recognised as an intangible asset, because the entity cannot demonstrate the future economic benefits that will flow. Consequently, all expenditure on developing a web site solely or primarily for promoting and advertising an entity's own products and services is recognised as an expense when incurred.
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- 15. Under AASB 138.21, an intangible asset is recognised if, and only if, it meets specified criteria. AASB 138.65 indicates that the cost of an internally generated intangible asset is the sum of expenditure incurred from the date when the intangible asset first meets the specified recognition criteria. When an entity acquires or creates content for purposes other than to advertise and promote an entity's own products and services, it may be possible to identify an intangible asset (e.g. a licence or a copyright) separate from a web site. However, a separate asset is not recognised when expenditure is directly attributed to creating, producing, and preparing the web site for it to be capable of operating in the manner intended by management the expenditure is included in the cost of developing the web site.
- 16. AASB 138.69(c) requires expenditure on advertising and promotional activities to be recognised as an expense when incurred. Expenditure incurred on developing content that advertises and promotes an entity's own products and services (e.g. digital photographs of products) is an advertising and promotional activity, and consequently recognised as an expense when incurred.
- 17. Once development of a web site is complete, an entity begins the activities described in the Operating stage. Subsequent expenditure to enhance or maintain an entity's own web site is recognised as an expense when incurred unless it meets the recognition criteria in AASB 138.18. AASB 138.20 explains that most subsequent expenditures are likely to maintain the future economic benefits embodied in an existing intangible asset rather than meet the definition of an intangible asset and the recognition criteria set out in AASB 138. In addition, it is often difficult to attribute subsequent expenditure directly to a particular intangible asset rather than to the business as a whole. Therefore, only rarely will subsequent expenditure expenditure incurred after the initial recognition of a purchased intangible asset or after completion of an internally generated intangible asset be recognised in the carrying amount of an asset.
- 18. An intangible asset is measured after initial recognition by applying the requirements of AASB 138.72-.87. The revaluation model in AASB 138.75 is applied only when the fair value of an intangible asset can be determined by reference to an active market. However, as an active market is unlikely to exist for web sites, the cost model applies. Additionally, as indicated in AASB 138.92, many intangible assets are susceptible to technological obsolescence, and given the history of rapid changes in technology, the useful life of web sites will be short.

Date of SIC's Consensus: [Deleted by the UIG]

Effective Date of SIC-32: [Deleted by the UIG]

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APPENDIX

This appendix is illustrative only and does not form part of the Interpretation. The purpose of the appendix is to illustrate examples of expenditure that occur during each of the stages described in paragraphs 2 and 3 of the Interpretation and illustrate application of the Interpretation to assist in clarifying its meaning. It is not intended to be a comprehensive checklist of expenditure that might be incurred.

EXAMPLE APPLICATION OF INTERPRETATION 132

Stage / Nature of Expenditure	Accounting treatment
Planning	
 undertaking feasibility studies defining hardware and software specifications evaluating alternative products and suppliers selecting preferences 	Recognise as an expense when incurred in accordance with AASB 138.54
Application and Infrastructure Development	
• purchasing or developing hardware	Apply the requirements of AASB 116
 obtaining a domain name developing operating software (e.g. operating system and server software) developing code for the application installing developed applications on the web server stress testing 	Recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the web site to operate in the manner intended by management, and the web site meets the recognition criteria in AASB 138.21 and AASB 138.57*

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Stage / Nature of Expenditure	Accounting treatment
Graphical Design Development	
• designing the appearance (e.g. layout and colour) of web pages	Recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the web site to operate in the manner intended by management, and the web site meets the recognition criteria in AASB 138.21 and AASB 138.57*
Content Development	
• creating, purchasing, preparing (e.g. creating links and identifying tags), and uploading information, either textual or graphical in nature, on the web site before the completion of the web site's development. Examples of content include information about an entity, products or services offered for sale, and topics that subscribers access	Recognise as an expense when incurred in accordance with AASB 138.69(c) to the extent that content is developed to advertise and promote an entity's own products and services (e.g. digital photographs of products). Otherwise, recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the web site to operate in the manner intended by management, and the web site meets the recognition criteria in AASB 138.21 and AASB 138.57*
Operating	
 updating graphics and revising content adding new functions, features and content registering the web site with search engines backing up data reviewing security access analysing usage of the web site 	Assess whether it meets the definition of an intangible asset and the recognition criteria set out in AASB 138.18, in which case the expenditure is recognised in the carrying amount of the web site asset

Stage / Nature of Expenditure	Accounting treatment
Other	
 selling, administrative and other general overhead expenditure unless it can be directly attributed to preparing the web site for use to operate in the manner intended by management clearly identified inefficiencies and initial operating losses incurred before the web site achieves planned performance (e.g. false-start testing) training employees to operate the web site 	Recognise as an expense when incurred in accordance with AASB 138.6570

* All expenditure on developing a web site solely or primarily for promoting and advertising an entity's own products and services is recognised as an expense when incurred in accordance with AASB 138.68.

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REFERENCES

Australia

The Urgent Issues Group discussed Issues Paper UIG/SIC 04/1 "Adoption of Various SIC Interpretations in Australia" in relation to this Interpretation at its meeting on 4 May 2004.

Accounting Standard AASB 101 Presentation of Financial Statements

Accounting Standard AASB 102 Inventories

Accounting Standard AASB 111 Construction Contracts

Accounting Standard AASB 116 Property, Plant and Equipment

Accounting Standard AASB 117 Leases

Accounting Standard AASB 136 Impairment of Assets

Accounting Standard AASB 138 Intangible Assets

Framework for the Preparation and Presentation of Financial Statements

International Accounting Standards Board

International Accounting Standard IAS 38 Intangible Assets

Standing Interpretations Committee Interpretation SIC-32 Intangible Assets – Web Site Costs