

<b>NDH</b>	Topics in Accounting: Capitalization of Intangible Assets The NDH Group, Ltd. <i>Authoritative text related to the concepts presented here include:          FASB Statement No. 142 – Goodwill and Other Intangible Assets</i>
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**Overview & Objective** – The purpose of this TIA is to review current GAAP as it applies to the capitalization of costs incurred for the *establishment* of intangibles or when such assets are *purchased*. As a general framework, intangible assets are distinguished as either “by purchase,” or “by internal development” and then as “identifiable,” or “unidentifiable.”

**General Application** – Broadly speaking there are two classifications of long-lived assets: tangible and intangible. The former maintains physical substance while the latter does not. As costs for tangible assets are capitalized and reported on a company’s Balance Sheet, so to are certain and specific intangible assets. Recognizing the costs associated with creating a portfolio of usable intangibles, and their future benefit to the firm, provides competitive advantages. These advantages are seen in the form of future cash-flows from operations, licensing agreements, and in the event of a company sale (others abound). Companies seeking to add value to their future operations and enhance their exit strategy work to enhance these “unseen” assets by allocating resources, management focus, and R & D efforts to their development. A general framework for accounting for the cost of intangibles follows (FASB Statement No. 142).

**Classification of Intangible Assets** – Intangibles must be classified according to one of four alternatives as listed below.

<b>Classification of Intangible Assets</b>				
<b>Acquired</b>	<b>By Purchase</b>		<b>By Internal Development</b>	
<b>Type</b>	<b>Identifiable</b>	<b>Unidentifiable</b>	<b>Identifiable</b>	<b>Unidentifiable</b>
<b>Examples</b>	<ul style="list-style-type: none"> <li>• Trademarks</li> <li>• Service Marks</li> <li>• Trade Names</li> <li>• Copyrights</li> <li>• Patents</li> <li>• Customer Lists</li> <li>• Franchise Fee</li> </ul>	<ul style="list-style-type: none"> <li>• Goodwill</li> </ul>	<ul style="list-style-type: none"> <li>• Trademarks</li> <li>• Service Marks</li> <li>• Trade Names</li> <li>• Copyrights</li> <li>• Patents</li> <li>• Proprietary Info</li> </ul>	<ul style="list-style-type: none"> <li>• HR Functions</li> <li>• Employee Training</li> <li>• Quality Process</li> <li>• Design of Quality Product</li> </ul>

**Determining If Capitalization of Identifiable Intangibles Applies** – Costs of developing identifiable intangibles are capitalized if they meet any one of the following tests. Note: As seen below not all costs associated with the development of intangibles are capitalized! Internally developed unidentifiable intangibles are expensed as well as development costs.

1. **Provides Future Cash-Flows** – Provides for distinct future cash flows.
2. **Provides Legal Rights** – Gives legal rights to its owner conveyed by a contract.
3. **Exchangeable** – Can be independently exchanged (sold).

**Determining Treatment of Costs Associated with Intangible Assets** – For each class of intangible, costs are treated somewhat differently (general rule above applies).

- **By Purchase** – If the intangible asset is purchased and...
  - **Identifiable**
    - \* Costs are capitalized
    - \* Costs are amortized over their useful life
    - \* Costs are reviewed annually for impairment
  - **Unidentifiable**
    - \* Costs are capitalized
    - \* Costs are reviewed annually for impairment
- **Internally Developed** – If the intangible asset is internally developed and...
  - **Identifiable**
    - \* Costs are capitalized
    - \* Costs are amortized over their useful life
    - \* Costs are reviewed annually for impairment
  - **Unidentifiable**
    - \* Costs are expensed as incurred

**Determining What Costs to Capitalize** – Only certain costs *associated with developing* intangible assets are capitalized. Examples of those include the following:

- **Acquisition** cost of a purchased intangible.
- Legal fees related to *establishing* the intangible.
- Filing costs related to *establishing* the intangible.
- Other costs related to *establishing* the intangible.
- Other **direct and indirect costs associated with *developing* the product or process are NOT capitalized (I.E. *Development Costs*)**. They are expensed as R & D costs (FASB Statement No2).

**Further Instruction & Use** – For further information regarding capitalization of intangible assets contact your Account Executive or call The NDH Group, Ltd. at 312.461.0505.