Appendix 2 – Illustrative example: costs to expense and capitalise

Thresholds for capitalisation of expenditure will vary between entities, but will usually be documented in the entity’s Accountable Authority Instructions and/or accounting policies and operational guidance. Paragraphs 51-67 of [AASB 138](https://aasb.gov.au/pronouncements/accounting-standards/) and paragraphs 16-22A of [AASB 116](https://aasb.gov.au/pronouncements/accounting-standards/) provide further guidance on capitalisation of costs.

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| **Scenario:**An entity develops a new IT software program to record customer details. The entity incurred the following costs to develop the new software:1. $5,000 consultant fees to search and evaluate off-the-shelf systems
2. $2,000 in employee expenses to select the final off-the-shelf system
3. $3,000 in employee expenses to design changes required to the off-the-shelf system
4. $10,000 in employee expenses to construct and test the new software
5. $5,000 for new terminals to replace old terminals that did not have the capacity to handle the new software
6. $500 to promote the new software to staff
7. $2,000 in training staff to operate the new asset.
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| **Treatment of costs – expense or capitalisation**Assuming the requirements to capitalise are met, these costs would be treated as follows:1. expense $5,000 consultant fee—as it was incurred in the research phase
2. expense $2,000 employee expenses—as it was incurred in the research phase
3. capitalise $3,000 employee expenses—as it is directly attributable and was incurred in the development phase
4. capitalise $10,000 employee expenses—as it is directly attributable and was incurred in the development phase
5. recognise $5,000 as property, plant and equipment under [AASB 116](https://aasb.gov.au/pronouncements/accounting-standards/)
6. expense $500 as it is an operating expense incurred in the implementation phase
7. expense $2,000 as it is an operating expense incurred in the implementation phase.
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