Customer's Accounting for Cloud Computing Arrangements—Background Information and Basis for Conclusions Accounting Guideline AcG-20

Foreword

In November 2022, the Accounting Standards Board (AcSB) released ACCOUNTING GUIDELINE AcG-20, Customer's Accounting for Cloud Computing Arrangements in Part II of the CPA Canada Handbook – Accounting. The AcSB has approved for publication the contents of this document setting out its rationale for the Guideline.

Background Information and Basis for Conclusions documents are sources of generally accepted accounting principles, as described in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100 in Part II of the Handbook. These documents are intended to help readers understand how the AcSB reached its conclusions, but they do not include explanations of requirements or guidance on the application of the relevant Section or Accounting Guideline.

November 2022

INTRODUCTION

1 This document summarizes how the Accounting Standards Board (AcSB) reached its conclusions as it developed ACCOUNTING GUIDELINE AcG-20, Customer's Accounting for Cloud Computing Arrangements in Part II of the CPA Canada Handbook – Accounting. This document also sets out the reasons the Board undertook the project to develop this Guideline, the process of research and deliberation, the key decisions made and the principal reasons for adopting the positions taken and rejecting others. Individual Board members gave some factors greater weight than other ones.

2 Nothing in this document is to be taken as overriding the requirements of the Handbook. However, the discussion may help readers understand how the AcSB developed AcG-20 and the Board's intent with respect to interpreting and applying this Guideline.

BACKGROUND

3 In March 2020, the AcSB considered its priorities related to projects for its domestic accounting standards. Based on input from its Private Enterprise Advisory Committee and Not-for-Profit Advisory Committee (Advisory Committees), the Board decided to add accounting for cloud computing arrangements from a customer's perspective to its workplan. The Board performed research to understand the nature of typical cloud computing arrangements and how they were accounted for. The Board also sought input to understand the accounting issues encountered by stakeholders and the usefulness of information provided to users of financial statements.

4 When it started the Cloud Computing Arrangements project, the AcSB heard from stakeholders two main financial reporting concerns:

(a) Expensing expenditures on implementation activities when the software in the cloud computing arrangement is not an enterprise's asset does not reflect the economic benefits an enterprise receives over time from implementing the software for use. Such expenditures can be quite significant.

(b) Determining the accounting for cloud computing arrangements involves a complex analysis, which can be difficult and costly to do for some private enterprises and not-for-profit organizations (NFPOs).

5 Through its research on this project and input from its Advisory Committees, the AcSB learned of other financial reporting issues stakeholders encountered when accounting for cloud computing arrangements. These issues are as follows:

(a) The lack of clarity as to which Section applies when accounting for a cloud computing arrangement, leading to the use of FINANCIAL STATEMENT CONCEPTS, Section 1000, to determine if an asset exists or GOODWILL AND INTANGIBLE ASSETS, Section 3064, to determine if an intangible asset exists in the arrangement.

(b) The control criterion in Section 3064 is challenging to apply in practice, especially for smaller private enterprises and NFPOs that may not have the time or resources to analyze if the arrangement contains an intangible asset.

(c) Allocating arrangement consideration to different elements in a cloud computing arrangement may be difficult to do when the vendor does not provide the information.

(d) Lack of guidance to account for subsequent changes to the software in a cloud computing arrangement (e.g., accounting for software upgrades and additional software modules).

(e) Insufficient disclosures for users to understand how the cloud computing arrangement is accounted for in the enterprise's financial statements. The lack of information provided to users affects the analysis of key ratios such as earnings before interest, tax, depreciation and amortization (EBITDA) and net income, and the understanding of cash flow impact in both current and future periods.

6 The AcSB also considered the work of other standard setters. For example:

(a) U.S. Financial Accounting Standards Board (FASB) issued amendments in 2015 and 2018 to address the customer's accounting for fees paid in a cloud computing arrangement and implementation costs when the arrangement is a service contract. 1

(b) The IFRS Interpretations Committee of the International Accounting Standards Board (Interpretations Committee) issued agenda decisions in 2019 and 2021, clarifying how a customer accounts for a Software as a Service (SaaS) cloud computing arrangement and the costs of configuring or customizing the software in the arrangement. 2

7 Based on the information gathered, the AcSB decided that the project's objectives are to:

(a) address stakeholders' financial reporting concern of reflecting the economic benefits from implementing the software in a cloud computing arrangement that is a service contract;

(b) clarify which Section applies to account for cloud computing arrangements, including the disclosure requirements to improve information reported to users; and

(c) simplify the existing requirements to address some of the difficulties and challenges with accounting for cloud computing arrangements.

8 In March 2022, the AcSB issued its Exposure Draft, "Customer's Accounting for Cloud Computing Arrangements." In developing the proposals, the Board sought the advice of its Advisory Committees. These Advisory Committees include financial statement users, auditors and preparers, with a range of backgrounds and experience from across Canada. Advisory Committee members include representatives from organizations of differing sizes and in a variety of industries.

9 The AcSB received 10 comment letters and heard from 53 stakeholders from across Canada at various virtual outreach sessions. Respondents, including participants from the outreach sessions, generally supported the overall proposed solution in accounting for cloud computing arrangements. However, respondents provided additional comments suggesting changes to some of the proposals. The specific issues addressed in this project, including the comments received on the Exposure Draft and any changes made in response to those comments, are highlighted in the subsequent sections.

APPLICABILITY TO NFPOS

10 NFPOs apply the standards for private enterprises in Part II of the Handbook to the extent that Part II standards address topics not addressed in Part III of the Handbook. Except as otherwise noted:

(a) INTANGIBLE ASSETS HELD BY NOT-FOR-PROFIT ORGANIZATIONS, Section 4434, directs NFPOs to apply Section 3064 in Part II of the Handbook; and

(b) TANGIBLE CAPITAL ASSETS HELD BY NOT-FOR-PROFIT ORGANIZATIONS, Section 4433, directs NFPOs to apply PROPERTY, PLANT AND EQUIPMENT, Section 3061 in Part II of the Handbook.

11 AcG-20 addresses the specific topic of cloud computing arrangements in the context of Section 3064. Therefore, NFPOs are required to apply the Guideline. Accordingly, while developing the Guideline, the AcSB consulted its Not-for-Profit Advisory Committee on any unique considerations for NFPOs applying this Guideline (see Unique considerations for NFPOs below).

EFFECTS ANALYSIS

12 AcG-20 aims to:

(a) enhance the relevance of financial information provided by:

- (i) improving disclosures; and
- (ii) allowing for an exception to capitalize expenditures to implement a software in a cloud computing arrangement that is a service contract to reflect multi-year economic benefits; and

(b) reduce the cost of preparing financial statements by:

- (i) providing clear guidance on stakeholders' areas of concern and on Sections to apply; and
- (ii) permitting enterprises to expense as incurred the expenditures related to the elements in a cloud computing arrangement within the scope of Section 3064.

13 In developing AcG-20, the AcSB considered the consequences of applying this Guideline relative to the objective of financial statements and the benefit versus cost constraint. As described in FINANCIAL STATEMENT CONCEPTS, paragraph 1000.12, the objective of financial statements is to "communicate information that is useful to investors, creditors and other users in making their resource allocation decisions and / or assessing management stewardship." Also, as described in paragraph 1000.13, the Board considered the benefit versus cost constraint, which states: "In developing accounting standards, the Board weighs the anticipated costs and benefits of its proposals in general terms to assess whether they are justified on cost / benefit grounds."

Exception to capitalize expenditures on implementation activities that do not meet the definition of an asset

14 Based on research and input from the AcSB's Advisory Committees, some users find it helpful to understand if an enterprise has made investments to support cloud-based solutions as doing so may increase the value in merger and acquisition situations.

15 The AcSB's view is that if the enterprise does not control the software in the cloud computing arrangement, expenditures to implement the software do not form part of an intangible asset and the enterprise should expense those expenditures as incurred. However, the Board acknowledges there may be benefit for users to understand the multi-year economic benefit resulting from making significant investments to implement a cloud-based solution. The Board also understands preparers' concern for having to expense such costs in one period, particularly if such expenditures are significant. Therefore, the Board thinks developing an exception to the definition of an asset can be justified as the intent is to enable preparers to communicate information that is useful to their investors, members, contributors, creditors and other financial statement users.

Optional simplification approach to expense as incurred the expenditures related to the elements in a cloud computing arrangement

16 The AcSB considered whether it was necessary to require an enterprise to analyze whether an intangible asset exists in a cloud computing arrangement. Based on research and input from its Advisory Committees, the Board understands that SaaS arrangements are common in practice and the software element is not typically controlled by the enterprise. Furthermore, some users are indifferent on whether an intangible asset in the arrangement is recognized because they may exclude such asset from their decision-making process.

17 The AcSB recognizes that for some small private enterprises and NFPOs, performing this analysis would be difficult and costly. Given users' feedback, the Board decided to develop this optional simplification approach that permits an enterprise to expense as incurred the expenditures related to the elements in a cloud computing arrangement within the scope of Section 3064. If an enterprise applies this simplification approach, it is not required to analyze whether an intangible asset exists in the cloud computing arrangement. The Board recognizes that optional application of the simplification approach affects comparability. However, the Board concluded that the cost / benefit considerations justified developing the simplification approach.

Conclusion on effects analysis

18 Having considered the effects of AcG-20, as discussed above, the AcSB thinks this Guideline will improve the financial reporting of private enterprises and NFPOs.

PURPOSE AND SCOPE

19 The AcSB considered whether to include the guidance through amendments to existing Sections in Part II of the Handbook, or by issuing a Guideline. As described in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, paragraph 1100.14, "Accounting Guidelines set out how existing Sections shall be applied in specific cases or the Board's conclusions on other particular issues of concern with respect to financial reporting."

20 The AcSB decided to issue a new Guideline because it thinks having the guidance in one location would be simpler for stakeholders. Furthermore, the Board was concerned that amending Section 3064 could lead to unintended consequences for the guidance to be applied to arrangements beyond cloud computing arrangements. Considering paragraph 1100.14, the Board thinks the guidance fits the description of an Accounting Guideline because it involves clarifying how existing Sections shall be applied to cloud computing arrangements and the Board's conclusions on specific financial reporting concerns.

21 The AcSB developed AcG-20 to address the issues identified with accounting for a cloud computing arrangement, as noted in paragraphs 4-5. Specifically on which Sections to apply, the Board noted it is common for a cloud computing arrangement to have multiple elements. For example, an enterprise may acquire new hardware to run the software from the cloud computing arrangement. The Board decided to clarify that if any elements in the arrangement are tangible assets, they would be accounted for under Section 3061 or LEASES, Section 3065. Any remaining elements in the cloud computing arrangement that are not tangible in nature are within the scope of this Guideline.

22 A few participants from the outreach sessions were concerned that the exception to capitalize qualifying expenditures for implementing a software service as an asset would be used by analogy to capitalize other types of expenditures that provide future economic benefits. They suggested the AcSB consider a project on financial statement concepts to ensure these items are treated consistently. The Board discussed this feedback. The Board noted that the exception was developed to address stakeholders' concern that expensing the expenditures on implementation activities in the period incurred may not always produce the most relevant information to users in the context of cloud computing arrangements. Given the increased prevalence of cloud computing arrangements, the Board thought providing the exception to these arrangements will address these stakeholders' concerns both timely and effectively. The Board reiterates that the scope of AcG-20 should be limited to what is stated in paragraph 1 of the Guideline. AcG-20 should not be applied by analogy to other expenditures outside the scope of this Guideline.

RECOGNITION AND MEASUREMENT

23 Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Therefore, the AcSB concludes that an enterprise should apply Section 3064 to account for elements in a cloud computing arrangement that are not tangible in nature. In the context of a cloud computing arrangement, if an element within the scope of Section 3064 does not meet the definition of an intangible asset, the expenditure to acquire it or generate it internally is recognized as an expense when incurred.

24 The AcSB observes that paragraphs 3064.52-54 provide guidance on the recognition of an expense under this Section. In the case of the supply of goods, an enterprise recognizes an expenditure as an expense when it has a right to access those goods. In the case of the supply of services, the enterprise recognizes an expenditure as an expense when it receives the services. Paragraph 3064.53A goes into further detail to assist an enterprise in determining when it has received the goods or services from the vendor. Therefore, the Board thinks that additional guidance is not needed in AcG-20 in applying the requirement to expense as incurred the expenditures related to the elements in a cloud computing arrangement given guidance already exists in Section 3064.

25 Based on the research performed, the AcSB noted that cloud computing arrangements typically include a software element and activities to implement the software. Therefore, these are usually multiple element arrangements. The Board observes that while guidance exists in Section 3064 to determine when goods or services are received, Section 3064 does not provide specific guidance that deals with identifying such goods or services in an arrangement from a customer's perspective.

26 The AcSB recognizes that, from a vendor's perspective, REVENUE, Section 3400, has extensive requirements on evaluating all deliverables in an arrangement to determine whether they represent separate units of account. This evaluation is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction.

27 The AcSB had extensive discussions on whether the customer's accounting should be symmetrical to a vendor's accounting for the elements in the arrangement. For example, an enterprise should consider whether the deliverable(s) in the cloud computing arrangement has value to the customer on a stand-alone basis.

28 When developing the proposals, the AcSB also considered whether there are practical factors that would indicate the elements in the arrangement are always separate. For example, if an enterprise engages a third-party consultant to perform implementation activities, the expenditures for such activities would generally be separate from the software service the vendor offers in the cloud computing arrangement. If the vendor in the arrangement performs the implementation activities, an enterprise should consider whether such activities can only be performed by the vendor and not by other vendors or third-party consultants. The expenditures for the implementation activities are unlikely to be a separate element in the arrangement when such activities can only be performed by the vendor that offers the software service.

29 After extensive deliberations, the AcSB proposed not to provide guidance to assist an enterprise in determining the significant separable elements in a cloud computing arrangement based on these two points:

(a) The purchase of multiple goods or services is not unique to cloud computing arrangements. Other situations may exist in which an enterprise engages with a vendor for a bundle of goods or services to achieve its procurement requirements. In those situations, an enterprise has applied its professional judgment in assessing the contract to account for the goods or services purchased from the vendor.

(b) Explicitly requiring an enterprise to apply Section 3400 guidance in order to apply Section 3064 may introduce a level of complexity that results in a cost / benefit trade-off and leads to unintended consequences for other types of arrangements. In addition, the Board thinks the disclosure requirements in AcG-20 will provide sufficient information for users to understand how a cloud computing arrangement is accounted for in an enterprise's financial statements.

Nevertheless, the Board included a question in the Exposure Draft to understand if an enterprise can apply professional judgment to determine the significant separable elements in a cloud computing arrangement with a vendor.

30 Respondents provided mixed views to the AcSB's question. Some respondents noted that they do not find it challenging to separately identify the software element from the other elements in the arrangement such as activities performed by the vendor to implement the software. Other respondents commented that the ability to obtain information to separate these elements varies by vendor and by the arrangement's complexity. Therefore, professional judgment is needed to separate out the significant elements. These respondents suggested the Board consider including in the Guideline the factors discussed in paragraph 28 to assist financial statement preparers. The Board agreed with this feedback and included factors that indicate whether the software element is a significant separable element from other activities in paragraph 8 of AcG-20.

31 The AcSB notes that once an enterprise has determined the significant separable elements in a cloud computing arrangement, it needs to allocate the arrangement consideration to those elements. The Board heard from its Advisory Committees that it may be difficult to obtain pricing information of the various goods and services the vendor provides in a cloud computing arrangement. Some enterprises may have this information, while others may not. As a result, allocating arrangement consideration to the different elements may be difficult and costly, especially for smaller private enterprises and NFPOs that do not have sufficient resources.

32 While the AcSB recognizes that no guidance exists for allocating arrangement consideration from a customer's perspective, the concept of allocation exists in other Sections. For example:

(a) Section 3061 acknowledges that the cost of an item of property, plant and equipment is made up of significant separable component parts. The cost is allocated to the component parts when practicable and when estimates can be made of the lives of the separate components.

(b) Section 3400 requires that arrangement consideration be allocated at inception of the arrangement to all deliverables on a relative stand-alone selling price basis.

33 However, the AcSB decided that since Section 3064 contains no specific requirements, an enterprise can determine a method for allocating arrangement consideration on a rational and consistent basis for purposes of accounting for when it receives the goods or services. The Board thinks that enterprises can adapt the methods in Section 3400 on allocating arrangement consideration to elements within the scope of the Guideline but did not include this as a requirement.

34 To help an enterprise allocate the arrangement consideration, the AcSB included illustrative examples in the Guideline. The Board acknowledges there could be methods other than what is illustrated in the examples and an enterprise will need to use judgment to determine the allocation method based on its own specific circumstances to apply the guidance in the Guideline. For example, when an enterprise needs to assess whether implementation services received from the vendor are directly attributable to preparing the software for its use for capitalization purposes, it may require a more detailed allocation compared to an enterprise that applies the simplification approach and expenses as incurred the expenditures related to the elements in the arrangement.

35 In the Exposure Draft, the AcSB also sought stakeholders' feedback to understand if an enterprise can apply professional judgment to allocate the arrangement consideration to the significant separable elements in a cloud computing arrangement with a vendor. The feedback from respondents was mixed. Some respondents thought the enterprise can obtain pricing information from their vendors to assist with the allocation of arrangement consideration. Other respondents commented that the ability to obtain information to allocate arrangement consideration varies by vendor and by the arrangement's complexity. As a result, it may take significant time and effort for an enterprise to obtain necessary information to allocate arrangement consideration to these elements.

36 That said, most respondents support the AcSB's decision not to prescribe a method to allocate arrangement consideration. They acknowledged that it would be difficult to prescribe a method given the wide range of goods or services an enterprise can receive in a cloud computing arrangement. Not mandating a specific allocation method permits enterprises to use professional judgment and the information they have available.

37 A few respondents to the Exposure Draft provided the following feedback for the AcSB to consider:

(a) Develop a rebuttable presumption whereby the prices the vendor provides for each component is presumed to be a rational allocation unless there is evidence to the contrary (e.g., if software access is only $1 per year).

(b) Require the enterprise to allocate the arrangement consideration to categories of expenditures, such as software license or subscription for access to the software and expenditures on implementation activities that are directly attributable to preparing the software service for its intended use.

(c) Require an enterprise to disclose its accounting policy for determining the significant separable elements in a cloud computing arrangement and allocating the arrangement consideration to those elements.

38 The AcSB discussed these comments and noted the following:

(a) Developing a rebuttable presumption – The Board concluded that allocating arrangement consideration on a rational and consistent basis does not disregard the use of the vendor's contractually stated price as long as the enterprise can support that the vendor's price is reasonable. However, the Board thought that presuming the prices the vendor provides as a rational allocation is not appropriate in all circumstances. For example, when the vendor only charges one single payment for a bundle of activities or provides an implicit discount to certain activities, an enterprise needs to perform additional analysis to allocate the arrangement consideration. The Board is also concerned that significant judgment is still involved in establishing "evidence to the contrary" as the enterprise has to demonstrate why there is no evidence that suggests the vendor's pricing cannot be used. Therefore, the Board thinks this method may not reduce the complexity for financial statement preparers.

(b) Allocating the arrangement consideration to categories of expenditures – The Board noted that the principle of allocating arrangement consideration on a rational and consistent basis also does not require an enterprise to allocate the consideration to individual activities. Allocating the consideration to categories of expenditures is a permissible method as long as it reflects the outcome of the enterprise's accounting policy chosen when applying AcG-20.

(c) Requiring additional disclosure – The Board noted for contracts with multiple goods or services, there is currently no requirement in Part II of the Handbook to disclose the method an enterprise uses to identify elements in the contract and allocate contract consideration to those elements. Therefore, the Board was concerned that proposing a requirement specifically for cloud computing arrangements can be too burdensome for preparers and could create unintended consequences. In addition, financial statement users who participated in our outreach sessions commented that they are more interested in understanding what amounts have been capitalized or expensed, and the ongoing cash flow impact of implementing a cloud computing arrangement. The Board thought disclosing the allocation method itself is less informative for users. As a result, the Board decided not to require this disclosure in AcG-20.

39 Based on the discussion above, the AcSB decided to retain the proposal of not mandating a specific allocation method as it allows enterprises to use professional judgment to develop the most appropriate method based on the specific circumstances of the individual cloud computing arrangements.

40 Some respondents to the Exposure Draft noted that in some cloud computing arrangements, implementation activities can relate to both software and tangible elements. They commented that separating the implementation activities between these elements can be challenging and recommended additional guidance in this area. The AcSB considered this feedback and noted that, similar to paragraph 3064.04, an enterprise applies judgment to assess whether the tangible element is a significant part of the contract. If the tangible element is a significant part of the cloud computing arrangement, then the enterprise may have more visibility into its related implementation costs. The Board thinks existing guidance in Section 3064 is sufficient to address this issue and decided to leave the proposal unchanged.

Simplification approach

41 The AcSB considered the challenge that some stakeholders raised with respect to determining whether an intangible asset exists in a cloud computing arrangement, specifically assessing whether an enterprise controls an asset as required in Section 3064.

42 The Advisory Committees observed that, in practice, some enterprises consider the criteria in U.S. GAAP to determine if they control the software in a cloud computing arrangement. In most cases, enterprises have found it rare for them to control the software, particularly in SaaS arrangements. However, some enterprises, particularly smaller private enterprises and NFPOs, find it difficult and costly to analyze whether an intangible asset exists in the arrangement.

43 The AcSB notes that in Section 3064, an accounting policy choice exists either to capitalize expenditures on internally generated intangible assets during the development phase, or to expense such expenditures as incurred. This accounting policy choice is only available for internally generated intangible assets and was a simplification the Board provided when Part II of the Handbook was created.

44 Therefore, the AcSB decided to develop an optional simplification approach, similar to what exists for internally generated intangible assets, to permit enterprises to expense as incurred the expenditures related to the significant elements in the cloud computing arrangement. The Board recognized this simplification approach would mean an enterprise could expense an intangible asset, whether separately acquired or internally generated, if it exists in a cloud computing arrangement. The Board's intention was that if an enterprise chooses to apply the simplification approach, this accounting policy would apply to expenditures in a cloud computing arrangement irrespective of an enterprise's existing accounting policy under paragraph 3064.40 relating to internally generated intangible assets.

45 The AcSB consulted its user members on its Advisory Committees. They noted that if sufficient disclosures inform them how the cloud computing arrangement is accounted for in the financial statements, it is not imperative to their analysis to recognize an intangible asset when it exists in the arrangement.

46 Respondents, including participants from the outreach sessions, agreed with the AcSB that an enterprise should be able to apply the optional simplification approach. They noted that this approach will reduce the time and effort smaller enterprises spend on accounting for their cloud computing arrangements.

47 Some respondents to the Exposure Draft commented that the AcSB should expand the scope of the simplification approach to include leases of tangible assets. They noted that identifying and classifying leases within a cloud computing arrangement may be burdensome and challenging to enterprises. The Board considered this comment but is concerned that expanding the scope will change the requirement in Section 3065, which is beyond the scope of this project.

Software intangible asset

48 For an enterprise that chooses not to apply the simplification approach, the Guideline requires the enterprise to analyze the cloud computing arrangement to determine if an intangible asset exists. The AcSB thought including guidance to help an enterprise assess whether the software element in the arrangement is a software intangible asset or a software service will reduce the cost of financial statement preparation. The Board decided to include factors relevant to cloud computing arrangements to assist an enterprise with applying the control criterion in Section 3064. The Board developed these factors by considering the FASB's and the Interpretations Committee's discussions on the topic of cloud computing arrangements.

49 The AcSB concluded that if an enterprise has the contractual right to obtain the software without significant penalty and it is feasible for the enterprise to run the software on its own or on a third party's infrastructure, the enterprise has control over the software and an intangible asset exists. The Board thinks that explaining the contractual right as the ability to obtain a copy of the intellectual property (software) rather than taking possession of the software as referred to in U.S. GAAP would help to clarify that the software does not have to reside in an enterprise's on-premises environment but could reside in an off-premises environment as well. If such contractual right does not exist, the Board also thinks that an enterprise may control the software by considering other factors such as exclusive rights to use the software or decision-making rights over the software. The Board acknowledges that these are not the only factors an enterprise considers in determining if the software is an intangible asset. The Board noted that evaluating whether certain rights indicate control requires professional judgment. Each right may not be in and of itself, a sufficient basis to indicate control. A right should be substantive in the cloud computing arrangement to be considered as an indicator of control.

50 Most respondents agreed with the factors the AcSB proposed to assist an enterprise with applying the control criterion in Section 3064. A few respondents to the Exposure Draft noted that requiring an enterprise to have exclusive rights to use the software to demonstrate control contradicts the conclusion that enterprises may come to when applying paragraph 3064.13. They noted that paragraph 3064.13 defines control as an enterprise's ability to obtain future economic benefits

from an intangible asset that stem from legal rights, which could be achieved in a cloud computing arrangement. The Board considered this comment and noted that in a cloud computing arrangement that is a software service, the contractual rights obtained by the enterprise is the right to access to the supplier's software rather than the right to determine when and how the software is used. The Board thinks that control is demonstrated when the enterprise has exclusive rights to use the software because the enterprise has the ability to decide when, where and how to use the software, and to restrict others from using the software. Therefore, the Board concluded that the exclusive right to use the software does not contradict the definition of control described in paragraph 3064.13.

Software service

51 The AcSB concluded that if the software in the cloud computing arrangement is not an intangible asset, then the arrangement is a service contract. AcG-20 refers to the software in this situation as a software service.

Implementation activities

52 When a software element in the cloud computing arrangement is recognized as a software intangible asset, an enterprise can capitalize any directly attributable costs to implement the software as part of the cost of the intangible asset. The enterprise would account for the intangible asset in accordance with Section 3064.

53 Stakeholders expressed concern with the inability to capitalize costs incurred to implement the software in the cloud computing arrangement when the enterprise does not control the software. Many stakeholders observed that the economic benefits received over time from implementing a software provided by a vendor through a cloud-based deployment model are no different from the economic benefits received from implementing an on-premises software. Therefore, stakeholders thought that capitalizing expenditures associated with implementing a cloud computing arrangement and expensing them over the period for which they expect to receive future economic benefits better reflects the substance of the arrangements.

Developing an exception

54 The AcSB sought input from its user members on its Advisory Committees whether to develop an exception to capitalize expenditures on implementation activities incurred in a cloud computing arrangement that is a software service. Although lenders typically do not lend against intangible assets and exclude them from their decision-making process, some users observed that an enterprise's value may be higher if significant investments are made to support cloud-based solutions. The Not-for-Profit Advisory Committee noted that some funding from contributors may be for capital purposes, while other funding is for operating purposes.

55 The key focus for users is having sufficient disclosures in the financial statements to inform them on how an enterprise accounts for a cloud computing arrangement so that they can use the information to make necessary adjustments in their analysis. Improving disclosures to explain what amounts are expensed in the income statement or capitalized onto the balance sheet relating to a cloud computing arrangement is important. The AcSB understands that some NFPOs also provide other information to their contributors for special reporting purposes.

56 Considering this input, the AcSB decided to develop an accounting policy choice that would allow enterprises an exception to capitalize expenditures on implementation activities that are directly attributable to preparing the software for use when the enterprise does not control the software (i.e., a software service). If an enterprise does not choose to capitalize such expenditures, it will continue to expense as incurred according to existing guidance when the arrangement is a software service.

57 The AcSB decided this was an exception to the asset definition but was convinced by the feedback that expensing the expenditures on implementation activities in the period incurred may not always produce the most relevant information to users in the context of cloud computing arrangements. However, the Board decided that this exception should not be used for arrangements beyond cloud computing arrangements.

58 Two AcSB members disagreed with the Board's proposal to develop this exception and voted against publishing the Exposure Draft. Since the software in a cloud computing arrangement is not controlled by the enterprise, it is a service contract. These Board members thought the expenditures incurred to implement a software service should be treated as a period expense because they do not meet the definition of an asset on a stand-alone basis.

59 Respondents, including participants from the outreach sessions, supported the AcSB's decision to provide this exception. They share a similar view, as noted in paragraph 53, that capitalizing expenditures on implementation activities and expensing over multiple periods better reflects the economic benefits an enterprise receives over time. They also agreed with the accounting policy choice described in paragraph 56, which would allow enterprises to choose the method that best achieves their financial reporting objectives.

60 The AcSB also decided that the period over which the capitalized expenditures from applying the exception are expensed should be the enterprise's expected period of access to the software service. The Board recognized that determining this expected period may require significant judgment. Therefore, the Board developed some factors to assist an enterprise in this regard. These factors consider the concepts used in determining an intangible asset's useful life and the term of a lease, while reflecting the common occurrence in practice that many cloud computing arrangements may have a term on a month-to-month basis or may not specify a term.

61 The AcSB's intent is that an enterprise can look beyond the arrangement term in determining the expected period of access to the software service. An enterprise should consider:

(a) its plans for continuing to access the software service with the vendor;

(b) any clauses in the arrangement that would impact the expected period of access; and

(c) whether the effects of obsolescence, technology, competition and other economic factors may limit the enterprise's expected period of access to the software service.

The enterprise should also consider what evidence it has to support its expectations (e.g., business plan showing the importance of the cloud computing arrangement in achieving its overall business objectives and how long the enterprise expects to engage the vendor for the software service).

62 Respondents to the Exposure Draft agreed that the factors the AcSB proposed are helpful to an enterprise in determining the expected period of access to the software service. A few respondents requested the Board clarify further how a customer should treat renewal or termination rights. They noted that if a cloud computing arrangement contains a non-cancellable period and a renewal option, the customer should be "reasonably assured" to exercise such option for the renewal period to be considered as part of the expected period of access. The Board agreed with this feedback and provided this clarification in paragraph 26 of AcG-20.

Other matters

63 For enterprises that do not apply the simplification approach, the AcSB thought it was important to clarify that they need to consider whether any elements in addition to the software element may give rise to other intangibles assets. For example, the Board is aware there could be a situation when a vendor develops additional software code that the enterprise can use in another cloud computing arrangement. In this situation, developing code could give rise to a separate internally generated intangible asset. The enterprise would apply paragraph 3064.40 as it relates to internally generated intangible asset, to determine whether recognition is required.

64 The AcSB also heard from its Advisory Committees that there could be additional modules or upgrades to the software in the cloud computing arrangement. Section 3064 does not provide guidance on accounting for enhancements of an intangible asset. Paragraph 3064.20 indicates that the nature of an intangible asset is such that in many cases subsequent expenditures are likely to maintain the asset as opposed to add or replace part of the asset. Furthermore, it is often difficult to attribute subsequent expenditures directly to a particular intangible asset rather than to the business.

65 The AcSB understands that, in practice, some enterprises capitalize enhancements or upgrades to software if it results in additional functionality. Although paragraph 3064.20 indicates that most subsequent expenditures are likely to maintain the future economic benefits of the intangible asset, the Board thinks the enhancements made to software and hardware should be accounted for similarly. Therefore, the Board decided to incorporate the betterment guidance in paragraph 3061.14 into the Guideline to assist enterprises in determining whether subsequent expenditures incurred in a cloud computing arrangement enhance the software intangible asset or software service.

66 Expenditures capitalized through applying the exception are tested for impairment in accordance with the provisions of IMPAIRMENT OF LONG-LIVED ASSETS, Section 3063, which is the same for a software intangible asset that is subject to amortization in Section 3064. However, if an NFPO is applying this Guideline, it would test for impairment in accordance with the provisions of INTANGIBLE ASSETS HELD BY NOT-FOR-PROFIT ORGANIZATIONS, Section 4434, as the Section contains guidance for recognizing write-downs of intangible assets for NFPOs.

67 Some respondents to the Exposure Draft commented that an enterprise should be allowed to apply the accounting policies provided by the Guideline on an arrangement-by-arrangement basis. They noted that an enterprise may enter into arrangements with varying complexity. The simplification approach may be more suitable to account for simple, off-the-shelf cloud solutions while the accounting policy to capitalize expenditures on implementation activities in a complex cloud computing arrangement provides more useful information to users regarding the multi-period benefits. In addition, the ability to apply the simplification approach to a specific arrangement can address practical challenges when an enterprise prefers a policy to capitalize but cannot obtain reliable pricing information for certain arrangements. The AcSB discussed this feedback and considered its Advisory Committees' advice. The Board noted that AcG-20 already provides flexibility for the enterprise to consider which accounting policy best suits its circumstances and would provide relevant information to its users relating to cloud computing arrangements. The Board is concerned that allowing an enterprise to apply its accounting policy on an arrangement-by-arrangement basis will further reduce the comparability and understandability of the enterprise's financial statements for users. Therefore, the Board decided to retain the requirement that an enterprise applies its chosen accounting policy consistently to all cloud computing arrangements.

PRESENTATION

68 Currently in Section 3064, an enterprise presents software meeting the definition of an intangible asset as an intangible asset, including any directly attributable costs to prepare the software for use. The intangible asset is subject to amortization over its useful life. The amortization expense would not affect EBITDA.

Presentation of capitalized expenditures using the exception

69 The AcSB considered how to present expenditures capitalized using the exception it developed. Prior to the Exposure Draft, the Board consulted its Advisory Committees and considered the following two views:

(a) Intangible asset presentation – Given the nature of the expenditures on implementation activities is the same regardless of whether the enterprise controls the software, the presentation should be consistent with how an enterprise will present expenditures on implementation activities if it controls the software. The enterprise should present expensing of capitalized expenditures using the exception as amortization expense, therefore not affecting EBITDA.

(b) Prepaid expenses presentation – As the enterprise does not control the software in the cloud computing arrangements, it expenses as an operating expense the subscription fees paid to access the software. If an enterprise presents expenditures capitalized using the exception as prepaid expenses, these expenditures would also be presented as an operating expense in the same manner as the subscription fees. This view is also consistent with U.S. GAAP, which requires enterprises to present capitalized implementation costs incurred in a cloud computing arrangement that is a service contract in the same line item as a prepayment of the fees for the associated hosting arrangement.

70 The AcSB acknowledged that both views have merit. However, the Board noted that since the enterprise does not present the software itself as an intangible asset, it would be counterintuitive to present the related expenditures on implementation activities as an intangible asset. The Board also thought that since the nature of the cloud computing arrangement is a software service, presenting the related expenditures on implementation activities as prepaid expenses will result in an income statement that aligns with where the subscription fees will be recognized. Therefore, in the Exposure Draft, the Board proposed that the qualifying expenditures for implementing a software service should be presented as prepaid expenses.

71 The AcSB also proposed that an enterprise classify prepaid expenses that do not meet the definition of a current asset in accordance with CURRENT ASSETS AND CURRENT LIABILITIES, paragraph 1510.03, as long-term assets.

72 Respondents, including participants from the outreach sessions offered different views on the AcSB's proposal. Some respondents were concerned that the proposed prepaid expenses presentation creates confusion and reduces understandability of an enterprise's financial statements because typically prepaid expenses represent cash paid in advance for future expenses, such as rent or insurance. In addition, financial statement users commented that the proposed prepaid expenses presentation can distort an enterprise's working capital ratio. Other respondents supported the Board's proposal, agreeing with the Board's rationale noted in paragraph 70.

73 The AcSB considered respondent feedback and its Advisory Committees' advice on this issue. The Board noted that the diverse feedback is consistent with its discussions during the development of the proposal. The Board reaffirmed its decision that an enterprise should not present the qualifying expenditures for implementing a software service as an intangible asset for the rationale included in paragraph 70. However, the Board shared respondents' concern that a prepaid expenses presentation can create confusion and reduce the understandability of financial statements. The Board considered other presentation options included in BALANCE SHEET, paragraph 1521.04, but thought none of them accurately reflect the nature of capitalized expenditures on implementation activities. As a result, the Board decided to create a new caption to separately present assets for implementation of software services on the balance sheet.

74 Considering the capitalized implementation activities relate to the software service that generally lasts longer than one year, the AcSB decided an enterprise should classify the asset for implementation of software services as long-term assets unless the expected period of access to the software at inception is within one year from the balance sheet date. The Board noted that classifying as long-term assets would also avoid impacting an enterprise's working capital, which was a concern for some financial statement users over the proposed prepaid expenses presentation. The Board's intent is that similar to capital assets, no subsequent reclassification from long-term to current is required when the enterprise's remaining expected period of access to the software service is less than one year.

75 Given the software is a service rather than an asset the enterprise controls, the AcSB thinks the presentation of the related expenditures on implementation activities should convey the operating nature of such costs for the service. Therefore, the Board decided to require an enterprise to present the subsequent expensing of the asset for the implementation of a software service in the same line item in the income statement as the expense for subscription fees for the software service.

76 On the statement of cash flow, the AcSB thinks since the capitalized expenditures on implementation activities are paid to a vendor for goods and services received in a cloud computing arrangement that is a software service, the cash flow should be classified as cash flows from operating activities. This classification is consistent with the cash flow classification for the subscription fees for the software service.

DISCLOSURE

77 The disclosure requirements in AcG-20 are consistent with the disclosure requirements in Section 3064 and CONTRACTUAL OBLIGATIONS, Section 3280.

78 The AcSB decided it was important to include disclosure requirements in the Guideline, even if some requirements highlight what exists in other Sections. Users noted that currently in practice, it is sometimes difficult to understand how an enterprise accounts for a cloud computing arrangement in its financial statements.

79 In addition to highlighting existing disclosure requirements, the AcSB decided to require an enterprise that applies the simplification approach to disclose that fact. If an enterprise does not apply the simplification approach, it should disclose the accounting policy it chose to account for directly attributable expenditures on implementation activities for a software service. An enterprise that chooses to capitalize such directly attributable expenditures on implementation

activities should also disclose the impact on the balance sheet and the income statement. This disclosure would be consistent with expenditures capitalized as part of a software intangible asset in Section 3064.

80 Some respondents to the Exposure Draft were concerned that requiring an enterprise that chooses to apply the simplification approach to disclose amounts expensed for the period is onerous and costly because the enterprise needs to track such expenditures in each period. However, during outreach sessions, financial statement users found this information useful when comparing enterprises that choose different accounting policies to account for expenditures in a cloud computing arrangement. The AcSB considered the feedback and decided that the benefit to users in understanding the amounts capitalized or expensed in the financial statements outweighs the costs of collecting this information. Therefore, the Board decided to retain this disclosure requirement in AcG-20.

UNIQUE CONSIDERATIONS FOR NFPOS

Capital asset recognition exemption

81 A simplified accounting approach for both tangible capital assets and intangible assets is currently available to small organizations in Part III of the Handbook if their average of annual revenues recognized in the statement of operations for the current and preceding period of the organization and any entities it controls is less than $500,000 ("capital asset recognition exemption"). Eligible small organizations can continue to apply this capital asset recognition exemption and will not need to refer to Sections in Part II of the Handbook for topics specific to tangible capital assets and intangible assets.

Contributions received in a cloud computing arrangement

82 A few participants from the outreach sessions noted that NFPOs may receive contributed materials and services in a cloud computing arrangement (e.g., materials such as software or hardware and services to implement the arrangement). NFPOs may also receive cash funding for a cloud computing arrangement. The AcSB discussed the interaction between AcG-20 in Part II of the Handbook with the guidance on contributions in Part III.

83 NFPOs apply CONTRIBUTIONS – REVENUE RECOGNITION, Section 4410, to account for contributions. In applying paragraphs 4410.16-18, an NFPO needs to determine the nature of the contributed items received because there are different accounting requirements for contributions of materials and services and for contributions of capital assets recognized in accordance with Sections 4433 and 4434.

84 Once an NFPO determines the nature of the contributed items received, it would apply the other requirements in Section 4410 to determine the revenue recognition pattern of the contribution. This revenue recognition pattern will be influenced by whether the NFPO determines the contribution to be restricted and its method of accounting for contributions (i.e., deferral method or restricted fund method). The AcSB considered whether to provide additional guidance on whether contributions received in a cloud computing arrangement could be restricted. However, the Board currently has a project that considers improvements needed to the guidance on accounting for contributions and related topics for NFPOs. One of the topics considered in that project is the definition of restricted and unrestricted contributions. Therefore, the Board thought it is beyond the scope of this Cloud Computing Arrangements project to provide any further guidance on the accounting for contributed cloud arrangements. The Board expects that NFPOs will continue to apply professional judgment using the existing requirements in Section 4410 in making the determination whether the contributions received in a cloud computing arrangement are restricted or unrestricted.

85 As noted in paragraph 83, an NFPO needs to determine the nature of the contributed items received. Paragraph 4410.16 provides an NFPO with a policy choice to recognize contributed materials and services and there are other requirements for contributed capital assets. The AcSB concluded that an NFPO would apply AcG-20 to make this determination. The Guideline first directs an NFPO to apply other Sections if there are tangible assets in the arrangement. If there are contributed tangible assets, the NFPO would apply existing guidance in Section 4433 unless the capital asset recognition exemption applies.

86 For all other contributed items, the NFPO considers the accounting policy it has selected in AcG-20 to determine the nature of the contribution.

(a) If an NFPO applies the simplification approach, the Guideline specifies that the expenditures in the arrangement are treated as the supply of services. As a result, the NFPO would apply its accounting policy for contributed materials and services in accordance with paragraph 4410.16 to account for the contribution.

(b) If an NFPO does not apply the simplification approach, the Guideline provides guidance for determining whether there are intangible assets in the cloud computing arrangement or whether the arrangement itself is a software service.

  (i) If there are contributed intangible assets, the NFPO would apply existing guidance in Section 4434 unless the capital asset recognition exemption applies.

  (ii) If there are contributed materials and services in the arrangement, the NFPO would apply its accounting policy in accordance with paragraph 4410.16 to account for the contribution. Therefore, regardless of whether the NFPO has chosen to capitalize or expense expenditures on implementation activities in a software service situation in accordance with AcG-20, it will account for the contribution of materials and services for implementation activities in accordance with paragraph 4410.16.

87 During its deliberations, the AcSB considered whether the accounting policy choice for contributed materials and services in paragraph 4410.16 is appropriate in the context of cloud computing arrangements. The Board recognizes that if an NFPO has historically selected an accounting policy to not recognize contributed materials and services in accordance with paragraph 4410.16, then it would not be able to recognize contributed materials and services in a cloud computing arrangement unless the NFPO retrospectively changes its accounting policy. The Board consulted its Not-for-Profit Advisory Committee on whether this could be an issue in practice. The Committee expressed mixed views. Contributed materials and services in a cloud computing arrangement may be more prevalent in some sectors than others. Furthermore, the significance of contributed materials and services received in a cloud computing arrangement may vary.

88 The AcSB considered whether it should amend the accounting policy in paragraph 4410.16 to address contributed materials and services in a cloud computing arrangement. However, the Board noted there are broader implications because this policy applies to all material and services. The Board considered the pervasiveness of this issue and observed that it would only affect NFPOs that:

(a) have a policy not to recognize contributed materials and services;

(b) receive significant contributed materials and services in a cloud computing arrangement;

(c) determine that recognizing such contributions would provide useful information to their users; and

(d) determine a change in accounting policy would be costly because of the effort to obtain information to recognize other contributed materials and services that satisfy the recognition criteria in paragraph 4410.16.

89 The AcSB also thought that since it has a project on accounting for contributions and related topics for NFPOs, it would be better to consider stakeholders' feedback on whether changes are needed to the policy choice in paragraph 4410.16 more holistically than considering an accommodation for a subset of contributed materials and services received in a cloud computing arrangement. Therefore, the Board decided not to change the policy choice in paragraph 4410.16 because such change would be beyond the scope of this Cloud Computing Arrangements project and the issue is expected to only affect a narrow population of NFPOs.

Presentation of net assets

90 A few participants from the outreach sessions noted that some NFPOs may present net assets invested in capital assets. These participants noted it was important to clarify whether capitalized expenditures on implementation activities when the arrangement is a software service should be presented as part of net assets invested in capital assets. The AcSB concluded that since the NFPO does not control the software when the arrangement is a software service, the capitalized amounts are not capital assets. The Guideline makes clear that such amounts are presented as assets for implementation of software services.

TRANSITION

91 The AcSB proposed retrospective application of AcG-20 to cloud computing arrangements that exist on or after the beginning of the earliest period presented in the financial statements in which the enterprise first applies the Guideline. In developing this proposal, the Board considered its Advisory Committees' feedback that some enterprises may want to apply the Guideline retrospectively to capitalize expenditures previously expensed under existing guidance. However, other enterprises may want to apply the Guideline prospectively as it would be less costly.

92 The AcSB acknowledged that AcG-20 may result in some enterprises changing their accounting for cloud computing arrangements, which would increase the cost of financial reporting. However, the Board thought that applying the Guideline would improve financial reporting and that retrospective application would be useful since it would provide comparable information for the prior period.

93 Some respondents to the Exposure Draft expressed a concern that retrospective application may not be possible when the detailed cost information necessary to allocate costs to the significant separable elements of a contract entered into in the past is unavailable.

94 In response to this concern, the AcSB decided to provide an optional transition relief. This optional relief would allow an enterprise that chooses not to apply the simplification approach to apply AcG-20 retrospectively but limit retrospective application to expenditures on implementation activities incurred on or after the beginning of the earliest period presented. The Board decided to require disclosure of the transition method chosen to ensure readers understand the extent of retrospective restatement applied. The Board thinks that this optional relief will provide greater comparability between the current and comparative figures, while reducing cost and complexity by eliminating the need to obtain and analyze historical information to identify costs to capitalize.

95 The AcSB understands that some enterprises may have recognized an asset for costs incurred related to cloud computing arrangements prior to applying AcG-20. If an enterprise chooses not to apply the simplification approach and applies the optional transition relief described in paragraph 94 above, the Board thinks it is still important these assets are measured consistently in accordance with the Guideline. Doing so improves comparability of an enterprise's period-to-period financial results, particularly since the impact on the balance sheet and the income statement is different between a software intangible asset and software service. In addition, the amounts capitalized as an asset may be different under the Guideline. Therefore, the Board requires retrospective application of the Guideline to assets resulting from capitalization of cloud computing costs incurred prior to the beginning of the earliest period presented. Any adjustment

to those assets would be adjusted to opening retained earnings of the comparative period. Costs capitalized during the comparative period would be restated as expenses and any amortization expense reported in the comparative period would be reclassified to operating expense.

96 If an enterprise chooses the simplification approach and had recognized an asset for costs incurred related to cloud computing arrangements in the prior period, the AcSB acknowledged that it would be inconsistent to report an asset when the enterprise's accounting policy is to expense as incurred expenditures in a cloud computing arrangement. As a result, the Board decided that these assets should be written off as part of retrospective application of AcG-20. This includes costs of intangible assets that form part of the cloud computing arrangement as these costs would be expensed as incurred under the simplification approach.

EFFECTIVE DATE

97 Selecting an effective date for AcG-20 is an important step in the AcSB's due process. The Board proposed an effective date of fiscal years beginning on or after January 1, 2023, with early application permitted. The Board thought this will provide private enterprises and NFPOs sufficient time to implement the proposals.

98 Some respondents, including participants from the outreach sessions, expressed a concern that the proposed effective date would not provide sufficient time for stakeholders to gain an understanding of the Guideline, to obtain information to implement the policy and provide required disclosures, and to determine prior period adjustments to apply the Guideline retrospectively. The AcSB acknowledged this concern and decided to defer the effective date of AcG-20 to fiscal years beginning on or after January 1, 2024, with early application permitted. This would permit:

(a) private enterprises with a December 31 year-end to apply this Guideline to their 2022 financial statements; and

(b) NFPOs with a March 31 year-end to apply this Guideline to their 2022-2023 financial statements.

ILLUSTRATIVE EXAMPLES

99 The AcSB developed illustrative examples to demonstrate the application of the Guideline to a particular situation. The Exposure Draft included two examples. Illustrative Example 1 demonstrated the application of the Guideline when an enterprise chooses to apply the simplification approach. Illustrative Example 2 demonstrated the application of the Guideline when an enterprise chooses not to apply the simplification approach.

100 Respondents, including participants from the outreach sessions, found these illustrative examples useful. Most respondents suggested including additional illustrative examples would be beneficial for more complicated scenarios seen in practice. The most common scenario requested was when new modules are added to the base cloud computing software after the enterprise has obtained access to the provider's software. The AcSB considered this feedback and decided to include an additional example to illustrate this scenario. The new Illustrative Example 2B is based on the fact pattern in Example 1 and adds an additional software module to illustrate the application of the Guideline to account for implementation activities after access to the software is obtained.

101 A few respondents to the Exposure Draft also suggested the AcSB include an example in which the enterprise determines it has control over the software element. While acknowledging such an example will be helpful, the Board noted that the control assessment depends highly on individual facts and circumstances. In addition, some respondents to the Exposure Draft commented that, in practice, it would be rare for an enterprise to control the software element. Consequently, the Board thinks such example would not be widely applicable or useful to stakeholders.

CONSEQUENTIAL AMENDMENTS

102 The changes AcG-20 introduces will affect other Sections. The AcSB decided to clarify that these consequential amendments are applied when the Guideline is applied, and notes that the amendments should be applied using the same transition provisions as the Guideline. The rationale for some of the more significant amendments are described throughout the Basis of Conclusions, as well as below.

FIRST-TIME ADOPTION, Section 1500, and FIRST-TIME ADOPTION BY NOT-FOR-PROFIT ORGANIZATIONS, Section 1501 in Part III

103 The AcSB decided to allow a first-time adopter to apply the transitional provisions in AcG-20. Without such a provision in Section 1500 and 1501, first-time adopters would be required to apply AcG-20 retrospectively without any relief, which may not be possible when the detailed cost information necessary to allocate costs to the significant separable elements of a contract entered into in the past is unavailable.

BALANCE SHEET, Section 1521

104 The AcSB decided to create a new balance sheet caption to present the expenditures on implementation activities capitalized in accordance with paragraph 24(b) of AcG-20. The Board's intent is to clearly communicate the nature of the capitalized expenditures, which are assets for implementation of software services recognized only in accordance with AcG-20. The Board recognized that presenting such expenditures using any existing balance sheet caption, such as prepaid expenses or intangible assets, may cause confusion because many respondents expressed these expenditures do not fit the nature of those assets and could distort an enterprise's key ratio analysis. Furthermore, creating a new balance sheet caption to separately present assets for implementation of software services further reinforces the Board's intention that the exception in the Guideline should not be used for arrangements beyond cloud computing arrangements. Although this new balance sheet caption is required to be presented on the face of the balance sheet, an

enterprise should consider materiality when applying this requirement similar to any other required asset class presentation.

INTANGIBLE ASSETS HELD BY NOT-FOR-PROFIT ORGANIZATIONS, Section 4434 in Part III

105 The AcSB decided to make a consequential amendment to paragraph 4434.01 to clarify that an NFPO not only applies Section 3064 and the disclosure requirements in Section 3063, but also AcG-20 when accounting for intangible assets acquired or developed by a not-for profit organization. This clarification is also important for an NFPO that receives contributed items in a cloud computing arrangement because it would have to apply the Guideline to determine the nature of the contribution received, as discussed in paragraphs 82-89.

EXPOSURE FOR COMMENT

106 After resolving the issues arising during the exposure period, the AcSB considered, as part of its due process, whether the revisions to the proposals should be exposed for comment.

107 The revisions are highlighted in the relevant sections throughout this Basis for Conclusions. These revisions are clarifications based on feedback received from stakeholders. Other than clarifications already highlighted in the Basis for Conclusions, only minor drafting changes were made. Therefore, the AcSB decided that there was no need for re-exposure.

DISSENTING OPINIONS

DO1 Two AcSB members dissent from the issuance of ACCOUNTING GUIDELINE AcG-20, Customer's Accounting for Cloud Computing Arrangements. Their dissenting opinions are set out below.

DO2 The two AcSB members support the simplification approach to expense as incurred all expenditures related to cloud computing arrangements in the application of GOODWILL AND INTANGIBLE ASSETS, Section 3064. Section 3064 already provides certain accommodations that permit the expensing of expenditures that may otherwise qualify for capitalization as intangible assets. Furthermore, feedback received from stakeholders indicates that expenditures for a cloud computing arrangement would rarely result in an intangible asset as typically there is no control of the software in the arrangement.

DO3 However, the two AcSB members disagree with the exception to capitalize directly attributable expenditures on implementation activities incurred in a cloud computing arrangement that is a software service. Expenditures that relate to implementation activities of a software service do not meet the definition of an asset in FINANCIAL STATEMENT CONCEPTS, Section 1000, and FINANCIAL STATEMENT CONCEPTS FOR NOT-FOR-PROFIT ORGANIZATIONS, Section 1001. An asset should not be recognized for expenditures related to implementing a software that the entity does not control. These expenditures should be treated as a period expense. Furthermore, users such as lenders may have to adjust out the expenditures recognized as an asset each year when making lending decisions as opposed to making a one-time adjustment for the year in which such expenditures are recognized as a period expense.

DO4 In addition, this exception to capitalize expenditures that do not meet the definition of an asset further reduces comparability as it is an additional policy choice in the Guideline. Applying this policy choice also introduces additional management judgment into the process of preparing financial statements with respect to allocating arrangement consideration to separate elements and determining the appropriate expected period of access to the software service.

DO5 Based on the feedback, some users are indifferent to the option to expense or capitalize expenditures on implementation activities incurred in a cloud computing arrangement that is a software service. Therefore, the two AcSB members think that improving existing disclosure requirements within Section 3064 can provide information that is beneficial to users in making informed decisions without having to create this exception to the definition of an asset.

Footnotes

1. Accounting Standards Update No. 2015-05, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*; and Accounting Standards Update No. 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract.*

2. IFRIC Agenda Decision (published in April 2021 as an addendum to the March 2021 *IFRIC Update*): Configuration or Customisation Costs in a Cloud Computing Arrangement; and IFRIC Agenda Decision (published in the March 2019 *IFRIC Update*): Customer’s right to receive access to the supplier’s software hosted on the cloud.