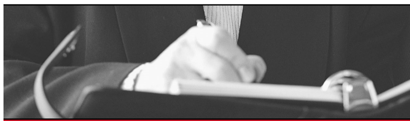

Accounting Policies

Accounting Policy Group

Update May 2024

A.5 Contract Costs: Transition Costs

<table>
<tr>
<td>CGI Policy - Summary</td>
<td>
Transition costs consist of directly attributable expenses associated with the installation of systems and processes incurred <u>after</u> the signature of managed IT contracts, including relocation of transitioned employees and exit from client facilities. Under business process services contracts, the costs consist primarily of expenses related to activities such as the conversion of the client’s applications to CGI’s platforms. These transition costs are comprised essentially of labour costs, including compensation and related fringe benefits, as well as subcontractor costs.

Transition costs must be deferred and capitalized as contract costs provided the following criteria are satisfied:

Costs generate or enhanced <u>ressources that will be used in delivering the services</u>;
Costs are <u>directly attributable</u> to the implementation of a new or amended contract;
Costs are <u>recoverable</u> based on the revenue stream over the period of the contract;

Transition is paid upfront
The client cannot terminate the contract for convenience
Transition costs are covered entirely during the term of the contract by a termination fee for convenience

If that is not the case, business unit must assess if it is probable that CGI will recover the costs by performing under the contract by considering the following factors:

Past history with the client;
CGI’s knowledge of the client;
Past history with the type of services rendered or goods delivered, and/or CGI’s knowledge of the industry;
CGI’s has experience with successfully rendering the service or delivering the goods.

All transition costs budgeted to <u>exceed $200K Canadian</u> must be documented and approved by the Business units (BU) controllers in appendix J of the revenue recognition checklist before it is sent to the Accounting Policy Group (APG) for review.
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<td>Scope and scope exceptions</td>
<td>
In scope
This policy applies to qualifying costs relating to transition activities (including set-up costs) of a managed IT and business process service contract that doesn’t qualify as a separately identifiable components. Refer to policy R.1.2 Contracts with Multiple Components).

Out of scope

Hardware and software costs incurred during the transition period are capitalized and amortized according to their asset category.
Costs associated with an internal decision to transfer the management of a contract to another BU cannot be capitalized.
Pre-contract costs are outlined in policy A.5.1 Pre-contract Costs.
Impairment considerations for contract costs are discussed in policy R.1.10 Provision for Loss on Contracts.
Contract costs consisting of incentives are discussed in policy R.1.8 Consideration Given to a Client (Incentives, Discounts, Rebates and Free Services).

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Authoritative Pronouncements	IFRS 15 *Revenue from contract with customers*

Initial recognition	Transition costs must be capitalized when the following criteria are satisfied:
	• Costs generate or enhanced ressources that will be used in delivering the services;
	• Costs are directly attributable to the implementation of a new or amended contract;
	• Costs are recoverable based on the revenue stream over the period of the contract;
	  ○ Transition is paid upfront
	  ○ The client cannot terminate the contract for convenience
	  ○ Transition costs are covered entirely during the term of the contract by a termination fee for convenience
	    ▪ If that is not the case, business unit must assess if it is probable that CGI will recover the costs by performing under the contract by considering the following factors:
	      • Past history with the client;
	      • CGI's knowledge of the client;
	      • Past history with the type of services rendered or goods delivered, and/or CGI's knowledge of the industry;
	      • CGI's has experience with successfully rendering the service or delivering the goods.
	
	Transition costs **must** be capitalized as incurred. No provision can be set up at the beginning of the contract.

Measurement	Total transition costs must be able to be measured reliably in order to be recorded.
	  ○ Costs must be directly attributable, where "directly attributable" includes those costs incurred to implement a contract in the manner as documented in the contract that can be directly linked to the contract. For example:
	  ○ Labour costs including compensation and related fringe benefits (see below)
	  ○ Subcontractor costs/third-party costs;
	  ○ Expense accounts (meals, travel, hotels, meetings) on the transition activities mentioned below;
	  ○ Relocation costs;
	  ○ Overlap costs (costs incurred in parallel during the transition period):
	    ▪ Hardware maintenance costs/lease costs/depreciation
	    ▪ Software maintenance costs/lease costs/depreciation
	    ▪ Circuit costs;
	  ○ Borrowing costs for transition over 12 months that is not paid upfront by the client. Refer to Policy A.7 – *Borrowing Costs*
	
	The following section outlines the types of directly attributable labour costs that can be capitalized once they meet the criteria stated in "Initial Recognition".
	
	Labour Costs
	Labour costs consist of the following:
	  ○ Labour costs, for employees including overhead costs that are directly related to the transition. For example :
	    ○ Payroll and payroll related costs (salary, fringes and profit sharing);
	    ○ Normal inefficiencies (bench factor);

	○ Labor-related tax credits; ○ PC rental/amortization; ○ Application software; and ○ Rent office Additional considerations: ○ In order to simplify the process, the BU can use 100% of the standard costs rate (SCR) for capitalization of labour efforts. Any tax credit not reflected in the SCR should be considered. ○ Any inconsistency with the aforementioned eligible capitalized costs will be monitored annually to ensure the net impact on the consolidated and statutory financial statements is not significant. ○ BU controllers must review the SCR annually, subject to SBU controllers approval and ensure any changes are reflected accordingly in the system (i.e. PCB). Consultants that have been hired specifically for the transition projects; ○ Termination costs for client employees upon the signature of a managed IT and business process service contract; ○ Termination costs for CGI employees upon renewal or amendment of a contract where the termination is due to the client's decision; ○ Note: Managerial staff activities can be capitalized if they are directly related to the transition. Salaries of management are not expected to be eligible if they have not been replaced in their current duties (in which case, the lower of the two costs can be capitalized). Nevertheless, capitalization is based on activities rather than a title; ○ Retention costs (i.e. stay put bonuses). <u>Activities</u> Below is a list of examples of capitalizable activities that may be performed in a transition: ○ Data center preparation and set up; ○ Relocation: moving data center equipment or workload (i.e. database, software) from the client site to CGI (movement from a CGI data center to another (both CGI's) could not be capitalized); ○ Knowledge transfer and documentation (i.e. shadowing: learning what the client is doing, documenting, applying what was documented, etc.); ○ Operational Framework; ○ Off shoring plans from a client decision (internal decision of offshoring could not be capitalized); ○ Contract transfer – Hardware and Software (includes member costs and transfer fees); ○ Physical inventory (if performed during the transition phase); ○ Overlap activities (done in parallel during the transition period): ▪ Hardware maintenance/lease/depreciation ▪ Software maintenance /lease/depreciation ▪ Circuit activities; ○ Infrastructure set-up (including CGINET). The following costs <u>cannot</u> be capitalized: ○ Training activities to operate the assets; ○ Selling, administrative and other general overhead expenditures unless

	they can be directly attributed to implementing the contract; ○ Abnormal inefficiencies and initial operating losses incurred during the transition period; ○ Interco margin included in pricing mainly from India, Philippines and Morocco but also applicable for all interco transactions.
Subsequent measurement	***Amortization considerations*** Transition costs are amortized over their useful life which correspond to the period of services it relates to, i.e. using a straight-line method over the term of the contract. The term of the contract corresponds to the base period (i.e. the stated term of the contract) and renewals are usually not taken into account when determining the amortization period, unless the option to extend a contract provides a significant discount. When the client is making a non-refundable payment up-front to cover for the transition when entering in a contract, it is because the client expects to use the service over the full term of the contract. When the client request a TFC, the TFC period reflects the period of service that are expected to be used by the client. Thus, the TFC period is the best estimate of the useful life. At the end of each financial year-end, the estimate of the amortization period should be reviewed. If expectations differ from previous estimates, the change is accounted for a change in accounting estimate. Therefore, the undepreciated cost of the asset is recognized in the income statement over the revised remaining period of service. The transition period is the period of time between the date of the contract is signed and the transition activities specified in the contract are completed, which is generally 6-18 months. • Amortization must be determined on an <u>activity</u> basis. When an activity is completed, the amortization should start even if all activities specified in the transition plan included in the contract are not completed. ***Exceeding budget*** Transition costs and the transition period should not exceed the budgeted amounts presented to top management. • Note: In rare circumstances, transition costs that are forecasted to exceed the budgeted figures can be capitalized if they can be justified and if they are approved in accordance with the operational management framework. ***Contract modifications or renewal*** • <u>Additional scope</u>: capitalization of additional transition costs and amortization over the extended length of the contract may be justified when the termination for convenience fee is adjusted accordingly to cover the additional costs. • <u>Same scope</u>: capitalization of additional transition costs and amortization over the extended length of the contract may be justified when the transition is due to the client's decision, the termination fee schedule is modified accordingly to cover additional costs and the original transition costs are written off. • If there are no additional transition costs (i.e. contract extension only) the amortization of the original transition costs over the extended length of contract may be justified when the termination fee schedule is modified accordingly and there is no restriction clause in the contract that would restrict CGI from amortizing over the new period.

	• <u>Reduction of scope:</u> The original transition costs related to the reduction of scope should be written off. If the additional transition costs generate additional revenue, the appropriate level of approval required in accordance with the operational management framework will be based on the amount of additional revenue.
Derecognition	Transition costs are assessed for impairment according to revenue recognition rules as per policy *R.1.10 Provision for Loss on Contracts.* For contract amendments, if transition costs were capitalized under the original contract and the costs incurred no longer have value to the amended contract, they cannot remain capitalized.
Documentation Required	***Checklist*** For all transition costs budgeted over **CAN $200K**, appendix J of the revenue recognition checklist (see policy R.1 Revenue Recognition – Basic Concepts) must be completed and approved by the BU Controller. After it is approved, it must be sent to the APG for review. BU controller could approve and capitalize up to CAN $200k even if the total budgeted transition is expected to exceed CAN $200k, but the BU would need APG final approval once the incurred cost reaches this threshold. BU will inform Fixed Asset Group via Myworkspace of the maximum amount approved by APG and the length of the transition period. The Fixed Asset Group will not allow capitalization greater than the budget without the APG's review.
Presentation	Transition costs are classified as contract costs within their own line in long-term assets on the balance sheet in the account 151001. The accumulated amortization is recorded in the account 151501. <u>No other accounts can be used to capitalize transition costs</u>. BU must ask the Fixed Asset Group to set up the asset. The cost accumulated amortization and net book value of contract costs are presented in a note disclosure in the financial statements. Additions to contract costs are presented in the cash flow statement as part of CGI's investing activities. ***Accounting for Transition Costs in the System*** Transition costs are recorded in the system via the asset management subledger. Once they are approved by the BU controller and reviewed by APG, the BU is responsible for ensuring the costs are recorded properly in the system and informing the Fixed Asset Group of when amortization begins. • BU using the PSA system should complete the asset form and journal entry template for reclasses for the initial entry of the transition costs as an asset. If the asset management subledger is closed, then the BU must account for their entries in Other Accounting Systems accounts (OAS accounts).