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# Summary of the October Meeting of the Emerging Issues Task Force

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This *EITF Snapshot* summarizes the October 12, 2017, meeting of the Emerging Issues Task Force (EITF or “Task Force”). Initial Task Force consensus (“consensus-for-exposure”) are exposed for public comment upon ratification by the Financial Accounting Standards Board (FASB). After the comment period, the Task Force considers comments received and redeliberates the issues at a scheduled meeting to reach a final consensus. Those final consensus are then provided to the FASB for final ratification and, ultimately, issuance as an Accounting Standards Update (ASU).

After each meeting, the official EITF minutes, including the results of the FASB’s ratification process, will be posted to the [Deloitte Accounting Research Tool \(DART\)](#) and to the [FASB’s Web site](#) (note that the official EITF minutes may contain details that differ from those in this publication). EITF Issue Summaries (released before the meeting and used to frame the discussion) are also available on those sites.

## **Issue 17-A, “Customer’s Accounting for Implementation, Setup, and Other Upfront Costs (Implementation Costs) Incurred in a Cloud Computing Arrangement That Is Considered a Service Contract”**

**Status:** Initial deliberations (although the Task Force has reached tentative agreement on various matters).

**Affects:** Entities that incur costs for implementation activities (implementation costs) as customers in cloud computing arrangements (CCAs) that are considered service contracts.

**Background:** In April 2015, the FASB issued [ASU 2015-05](#),<sup>1</sup> which clarifies the circumstances under which a customer in a CCA would account for the arrangement as a license of internal-use software under ASC 350-40.<sup>2</sup> The ASU provides guidance on whether a CCA contains a software license or whether it is considered a service contract and thus is not within the scope of ASC 350-40. ASC 350-40 only addresses the accounting for costs for implementation activities related to software licenses used internally. As noted in the Background Information and Basis for Conclusions of ASU 2015-05, at that time the Board decided not to address the accounting for costs for implementation activities related to CCAs that are considered service contracts.

As the prevalence of these arrangements has grown, stakeholders have raised concerns that the guidance in GAAP is unclear about the accounting for implementation costs associated with CCAs that are considered service contracts. Stakeholders have indicated that there is currently diversity in practice as entities look to various Codification topics for guidance on accounting for such costs.

At its May 10, 2017, meeting, the FASB acknowledged that the accounting for a customer's implementation costs in a CCA is an emerging and prevalent issue and added a narrow-scope project on this issue to the EITF's agenda.

At the July 20, 2017, EITF meeting, the Task Force discussed the accounting for a customer's implementation costs incurred in a CCA that is considered a service contract, primarily focusing on the following alternatives:

- Account for the costs on the basis of existing GAAP, including ASC 340, ASC 350-40, ASC 360, and ASC 720-45 (Alternative B was proposed in the [July Issue Summary](#)).
- Account for the costs in a manner consistent with how an entity accounts for a customer's implementation costs associated with a software license (i.e., under ASC 350-40) (Alternative C was proposed in the July Issue Summary).

No formal votes on the proposed alternatives were taken and no decisions were made at the July meeting. The Task Force requested that the FASB staff continue to research Alternative B and Alternative C.

**Summary:** At this meeting, the Task Force continued discussing the accounting for a customer's implementation costs incurred in a CCA that is considered a service contract. On the basis of the FASB staff's research after the July meeting, the staff presented two revised alternatives for the Task Force to consider. The discussion also included Alternative C from the July Issue Summary. The following alternatives were discussed:

- *Revised Alternative B* — Account for the costs on the basis of existing GAAP, including ASC 340, ASC 350-40, ASC 360, and ASC 720-45. Costs for implementation activities that are not within the scope of existing GAAP should be evaluated to determine whether they are distinct from the hosting element of the agreement. These costs will be either expensed as incurred if the implementation activity is distinct from the hosting service element or capitalized as a prepaid asset of the hosting service if they are not distinct from the hosting element. To determine whether an implementation activity is distinct from the hosting element, the customer should look to guidance in ASC 606 or other separation models could be considered (Alternative B was proposed in the [October Issue Summary](#)).
- *Revised Alternative C* — Account for the software element of the CCA not as a service but as an asset (i.e., a right to access specified software). Customers are required to record an asset for the software element and a liability to the extent that fees related

<sup>1</sup> FASB Accounting Standards Update No. 2015-05, *Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*.

<sup>2</sup> For titles of FASB Accounting Standards Codification (ASC) references, see Deloitte's "[Titles of Topics and Subtopics in the FASB Accounting Standards Codification](#)."

to the software element are paid over time in a manner similar to those related to a finance lease under ASC 842. However, the asset would be accounted for in a manner consistent with the framework in ASC 350-40 for internal-use software, including capitalization of certain implementation costs. Under this approach, the software element and hosting service element must be separately identified and the transaction price must be allocated between the two elements. This accounting is similar to a transaction in which the entity purchases a license for internal-use software and will pay for the license over time (Alternative C was proposed in the October Issue Summary).

- *Original Alternative C* — Account for the costs in a manner consistent with how an entity accounts for a customer’s implementation costs associated with a software license (i.e., under ASC 350-40) (original Alternative C was described in the October Issue Summary).

The Task Force reached a tentative decision that a customer should apply the revised Alternative C approach to account for implementation costs incurred in a CCA that is considered a service contract.

In addition, the Task Force discussed other issues related to a customer’s implementation costs incurred in a CCA that is considered a service contract and reached tentative agreement on the following points:

- At the July meeting, some Task Force members indicated that the guidance under ASC 350-40 was viewed as outdated and presented operational challenges for entities that must apply the guidance. On the basis of this feedback, the FASB staff performed additional research and found that there would not be significant challenges in applying ASC 350-40 to implementation costs of a CCA that is a service contract. At the October meeting, the Task Force decided not to add guidance on how to apply ASC 350-40 to CCAs.
- At the July meeting, the Task Force discussed how a customer would separate elements of a contract when accounting for CCAs. The FASB staff performed additional research and determined that the question of how to separate elements in a cloud computing arrangement is beyond the scope of the issue. At the October meeting, the Task Force decided not to provide additional guidance on separation of elements.
- The Task Force considered whether to add a definition of the term “implementation costs” to the ASC master glossary or, if not, whether a description of such costs should be provided. The Task Force tentatively reached agreement on the revised Alternative C, which results in accounting that is consistent with the framework in ASC 350-40 on capitalization of implementation costs. Therefore, the Task Force tentatively agreed not to add a definition or further description of implementation costs.

**Next Steps:** The Task Force requested that the FASB staff further examine practical questions related to capitalization of the software element of a CCA under the revised Alternative C (such as how to determine discount rates in the present value calculations and how to consider variable payments, renewal options, and termination options), as well as issues associated with analogizing to existing guidance in ASC 842. This research, as well as other issues that the Task Force has not yet discussed (e.g., scope, disclosures, transition), will be addressed at a future meeting.

## Administrative Matters

The next EITF meeting, which is tentatively scheduled for November 16, 2017, is likely to be canceled both because there are no other issues on the agenda and so that the staff has adequate time to research the items discussed above. The next meeting after that is scheduled for January 18, 2018.

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