



STAFF PAPER

March 2021

IFRS® Interpretations Committee meeting

Project	Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)		
Paper topic	Comment letters		
CONTACT	Wei Shun Tan	wtan@ifrs.org	+81 (0) 3 5205 7282
	Jawaid Dossani	jdossani@ifrs.org	+44 (0) 20 7332 2742

This paper has been prepared for discussion at a public meeting of the IFRS Interpretations Committee (Committee) and does not represent the views of the International Accounting Standards Board (Board), the Committee or any individual member of the Board or the Committee. Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Decisions by the Board are made in public and reported in IASB® *Update*. Decisions by the Committee are made in public and reported in IFRIC® *Update*.

Introduction

1. This paper reproduces comment letters on the IFRS Interpretations Committee’s tentative agenda decision ‘Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)’ published in December 2020.



Sue Lloyd
Chair of the IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH

United Kingdom

IFRS Technical Committee

Phone: +49 (0)30 206412-12

E-Mail: info@drsc.de

Berlin, 22 January 2021

Dear Sue,

IFRS IC's tentative agenda decision in its December 2020 video conference

On behalf of the Accounting Standards Committee of Germany (ASCG), I am writing to comment on the tentative agenda decisions taken by the IFRS Interpretations Committee (IFRS IC) as published in the December 2020 *IFRIC Update*.

We agree with all tentative agenda decisions and deem an appropriate application of the literature. Notwithstanding our agreement, we provide additional comments on two of these.

We consider the tentative agenda decision on IAS 1 (Classification of liabilities with covenants as current or non-current) constituting an appropriate description of how to apply the requirements of IAS 1 that had been amended recently. In this context, we deliberated again the underlying principles. Our finding is that under certain facts and circumstances – e.g. Case 3 that the IFRS IC had discussed – the resulting classification of liabilities may appear counter-intuitive. According to paragraph 72A of IAS 1, an entity must comply with the conditions at the end of the reporting date even if the lender does not test compliance until a later date. Given that contractually agreed covenant hurdles may vary depending on the (interim) reporting period they relate to (e.g. reflecting the seasonality of an entity's business), paragraph 72A of IAS 1 may lead to a breach of a condition at the reporting date, although, from an economic perspective, the entity does not need to comply with that condition until a later testing date. As classification depends on the (non-)compliance with the condition at the reporting date, management's expectations (regarding future compliance with covenants) would not be reflected. However, we believe that, in practice, entities will likely adapt their contractual agreements in a way that ensures a classification that appropriately reflects the economic substance of their lending agreement (e.g. obtain a waiver for at least 12 months after the reporting date).

As regards the tentative agenda decision on IAS 38 (Accounting for configuration or customizing costs with SaaS arrangements), the IFRS Technical Committee considers that the reference to IFRS 15 – to be applied by analogy – may imply that the timing of cost to be recognised by the entity would have to mirror the revenue recognition pattern of the arrange-

Contact:

Joachimsthaler Str. 34
D-10719 Berlin
Phone: +49 (0)30 206412-0
Fax: +49 (0)30 206412-15
E-Mail: info@drsc.de

Bank Details:

Deutsche Bank Berlin
IBAN-Nr.
DE26 1007 0000 0070 0781 00
BIC (Swift-Code)
DEUTDE33XXX

Register of Associations:

District Court Berlin-Charlottenburg, VR 18526 Nz
President:
Prof Dr Andreas Barckow
Executive Director:
Prof Dr Sven Morich



ment's counterparty. We wonder whether this conclusion would be appropriate for all fact patterns or would only apply in certain circumstances. In case of the latter, we suggest clarifying and amending the agenda decision. Further, it appears unclear whether and how the findings by the IFRS IC would apply were the customizing service performed by a third party. Again, we suggest a clarification in this regard.

If you would like to discuss our views further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Sven Morich

Executive Director

Rio de Janeiro, January 29, 2021

CONTRIB 0009/2021

Ms. Lloyd, Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD, United Kingdom

Subject: Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)

Reference: Tentative Agenda Decision (TAD)

Dear Ms. Lloyd,

Petrobras welcomes the opportunity to comment on the IFRS Interpretations Committee's Tentative Agenda Decision - Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38). We believe this is an important opportunity for all parties interested in the future of IFRS and we hope to contribute to the progress of the Committee's activities.

We noted in the answer provided by the TAD to question II that the Committee observed that IAS 38 does not include requirements that deal with the identification of the services the customer receives and when the supplier performs those services in accordance with the contract to deliver them. Regarding this observation, we have identified the paragraphs BC 46E and BC 46 F in IAS 38 that provides more detailed about paragraph 69A, as reproduced below (emphasis added):

BC 46E The Board noted that when the entity has received the related goods or services, it ceases to have the right to receive them. Because the entity no longer has an asset that it can recognise, it recognises an expense. However, the Board was concerned that the timing of delivery of goods should not be the determinant of when an expense should be recognised. The date on which physical delivery is obtained could be altered without affecting the commercial substance of the arrangement with the supplier. **Therefore, the Board decided that an entity should recognise an expense for goods when they have been completed by the supplier in accordance with a contract to supply them and the entity could ask for delivery in return for payment—in other words, when the entity had gained a right to access the related goods.**

BC 46F A number of commentators on the exposure draft of proposed Improvements to International Financial Reporting Standards published in 2007 thought that it was unclear when the Board intended an expense to be recognised. In response to those comments, the Board added paragraph 69A to clarify when entities would gain a right to access goods or receive services.

In this sense, IAS 38 provides a principle to recognize expenses, i.e. when an entity gain a right to access goods or receive services. Paragraph 69A clarify that services are received when they are performed by a supplier **in accordance with a contract** to deliver them to the entity (emphasis added). It suggests that the terms of the contract that determines whether or not the service has been performed and the timing of recognition of expenses.

The guidance sets forth by IAS 38 to determine when the service is performed seems to be different from the principle set out in paragraph 31 of IFRS 15 that deals with the transference of control, as reproduced below (emphasis added):

31. An entity shall recognise revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (ie an asset) to a customer. An asset is transferred when (or as) **the customer obtains control of that asset.**

Considering the different approaches and principles between IAS 38 and IFRS 15, it appears that the conclusion reached by the Committee regarding question II may not comply with the requirements of IAS 38.

Furthermore, it is worth mentioning that IAS 38 was issued prior to the IFRS 15 and the TAD may have some unintended consequences regarding accounting policies related to paragraph 69A of IAS 38 that have been developed since its initial application.

Another concern is related to the proposal to issue an agenda decision to address the matter. As provided in paragraph 8.4 of the Due Process Handbook, **an explanatory material explains how the applicable principles and requirements in IFRS Standards apply to the transaction or fact pattern described in the agenda decision.** We note that IAS 38 does not contain requirements that refer to the application of IFRS 15 - Revenue from Contracts with Customers and neither the requirements contained in the scope of IFRS 15 support the application of this standard. Additionally, the need to develop an accounting policy to deal with the matter seems to indicate that the existing requirements are not clear or sufficient. Thus, we believe the issue cannot be formally addressed with a TAD. The only alternatives would be updating existing requirements of IAS 38 or issuing of an IFRIC Interpretation.

Lastly, we would also ask the Committee to clarify in the fact pattern described whether the upfront cost of configuring or customizing were incurred with the supplier of the software or a third-party provider.

If you have any questions in relation to the content of this letter, please do not hesitate to contact us (cc-contrib@petrobras.com.br).

Respectfully,

/s/Rodrigo Araujo Alves
Rodrigo Araujo Alves
Chief Accountant and Tax Officer

February 2, 2021

IFRS Foundation
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

SOCPA Comments on Tentative Agenda Decision: Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)

Dear Colleagues,

The Saudi Organization for Certified Public Accountants (SOCPA) appreciates the efforts of the IFRS Interpretations Committee (Committee) and welcomes the opportunity to comment on the *Tentative Agenda Decision: Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)*.

First of all, we would like to bring to your attention that the Committee issued in March 2019 an agenda decision dealing with '*Customer's Right to Receive Access to the Supplier's Software Hosted on the Cloud*'. In that agenda decision the Committee has covered all the aspects about whether such an access is an asset, lease, or a service contract. Therefore, the Committee may find it appropriate to cross reference that agenda decision instead of discussing the issue of whether the transaction in the tentative agenda decision results in an asset or not.

Secondly, we notice from the fact patterns listed in the tentative agenda decision that the customisation service, by nature, is a necessary step to allow the customer to access the supplier's software. Therefore, we believe that the judgment involved in deciding about the configuration service is inseparable from the judgment involved in deciding about the right to access the supplier's software. Therefore, and according to the fact pattern that the '*right to receive access does not provide the customer with a software asset at the contract commencement date*' and, therefore, '*the access to the software is a service that the customer receives over the contract term*', the committee may directly guide the inquirer to amortize the upfront cost over the contract term in a systematic basis as the customer receives the access service according to paragraph 69 of IAS 38 which states that "... *In the case of the supply of services, the entity recognises the expenditure as an expense when it receives the services*". That is because the cost of configuration is, by nature, a part of the cost of the right to access the service as such right, which is received over the contract term, cannot be exercised without that configuration. Consequently, reference to the requirements in IFRS 15 is not necessary to guide the inquirer to the proper accounting for the transaction in question.

Please feel free to contact Dr. Abdulrahman Alrazeen at (razeena@socpa.org.sa) for any clarification or further information.

Sincerely,



Dr. Ahmad Almeghames

Secretary General

International Financial Reporting
Standards Interpretations Committee
IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

3 February 2021

Dear IFRS Interpretations Committee members,

Invitation to Comment - Tentative Agenda Decision (TAD): Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38 *Intangible Assets*)

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above TAD of the IFRS Interpretations Committee (the Committee) published in the December 2020 *IFRIC Update*.

The Committee discussed the questions “whether, applying IAS 38, the customer recognises an intangible asset in relation to configuration or customisation of the application software” and, if not, “how the customer accounts for the configuration or customisation costs.”

We agree with the Committee’s conclusion on the application of IAS 38 to the configuration and customisation of the application software, which is consistent with our published view. We also broadly agree with the Committee’s conclusion on how the customer should account for the configuration or customisation costs. However, we do not agree with the conclusion in the TAD that IFRS 15 *Revenue from Contracts with Customers* must be applied to this arrangement under IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

IAS 8 requires management to use its judgement in developing and applying an accounting policy that results in information that is both relevant and reliable. IAS 8 requires management to refer to, and consider the applicability of, the requirements in IFRS standards that deal with similar and related issues in making that judgement. We believe that management of an entity, in its judgement, may determine that IFRS 15 deals with similar and related issues to those included in the TAD. But equally, management, in its judgement, could also conclude that IFRS 15 is not applicable, because it provides accounting guidance for the supplier/vendor in a revenue arrangement, not the customer.

Furthermore, we believe that the TAD could be interpreted to imply that all customers should apply IFRS 15 to determine whether elements in a multiple-element arrangement should be accounted for separately because IFRS standards do not include general guidance for customers in service arrangements or other multiple-element arrangements. We understand that many customers do not apply IFRS 15, in practice, to determine separate elements of a multiple-element arrangement with a vendor/supplier. That is because IFRS 15 provides

accounting guidance for the supplier/vendor in a revenue arrangement, and the customer does not have access to the same information as the supplier/vendor (and the information they do have may not be sufficient) to apply the requirements in IFRS 15.

We recommend that the Committee clarifies in the agenda decision that management should develop an accounting policy under IAS 8, which may be based on the requirements in IFRS 15, but that this is not the only policy that an entity could consider.

We also recommend that the Committee clarifies that, if the customer analogises to IFRS 15 and the configuration or customisation services are provided by an unrelated third party (and neither party is acting as an agent), the third-party service contract cannot be combined with the cloud computing arrangement. That is, the configuration services would always be considered distinct from the cloud computing service if the configuration services are provided by an unrelated third party. Without this clarification, stakeholders may misapply the agenda decision to a different fact pattern than the one that has been included in it and incorrectly conclude that the two services are not distinct.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas at the above address or on +31 88 407 5035.

Yours faithfully

Ernst + Young Global Limited



February 3, 2021

IFRS Interpretations Committee

Re: Configuration or Customization Costs in a Cloud Computing Arrangement (IAS 38)

Submitted via [//www.ifrs.org/projects/work-plan/](http://www.ifrs.org/projects/work-plan/)

Dear Sir/Madam:

Alberta-Pacific Forest Industries Inc. ("Al-Pac") appreciates the opportunity to comment on the IFRS Interpretations Committee's ("IC") project paper *Configuration or Customization Costs in a Cloud Computing arrangement (IAS 38)*.

In the current environment, technology providers (software, platform, infrastructure) are shifting their business model from selling licenses to provide a wide range of services under cloud computing arrangements, as this model has many benefits to both the software providers and the customers. Despite the change in the business model, significant implementation costs are still needed in these cloud computing arrangements in order to be ready for use by customers. From a customer perspective the new vendor business model does not change the main drivers and ultimate main strategic benefits expected from operating with a new technology.

However, under the observed IFRS IC interpretation the accounting recognition of implementation costs should be different, based on whether or not there is an associated license. More specifically the implementation costs related to a cloud computing agreement would result in an immediate expense; however, if a substantial license was conveyed the same costs would have been capitalized and amortized into earnings over the term of such license.

Our company and a large number of entities are currently undergoing a complex Enterprise Resource Planning (ERP) systems implementation under a software as a service (SaaS) arrangement. A SaaS arrangement is a type of a cloud computing arrangement in which the supplier (cloud service provider) provides the customer access to the application software residing in the supplier's infrastructure. SaaS arrangements are prevalent in the strategy of the leading enterprise software companies and are expected to continue to grow.

It is common for the customer to incur implementation costs before and at the inception of a SaaS arrangement which, depending on a number of factors, could be quite complex and significant. In particular, the nature, type and structure of cloud ERP systems implementation costs under a SaaS are similar to those needed in "internal-use software" projects (i.e. an internally developed software system owned by the user or in an arrangement that contain a substantive license to use software transferred to a company). Certain entities use a third-party implementer which is different than the cloud ERP SaaS provider.

Alberta-Pacific Forest Industries Inc.

Millsite
684009 Range Road 195
P.O. Box 8000
Boyle, AB T0A 0M0
(780) 525-8000

Edmonton
1 Tache Street, Suite 600
St. Albert, AB T8N 1B4
(780) 495-1220

We acknowledge the IC staff conclusion reached in your paper published December 2020 where it states in para 52 *“A customer typically would not recognize an intangible asset for configuration or customization of the supplier’s application software because it would not have the power to obtain the future economic benefits flowing from the underlying resources. (i.e. the software being configured or customized) and to restrict the access of others (including the supplier) to those benefits.”*

However, we disagree with the fundamentals for that conclusion:

- *“Not have the power to obtain future economic benefits flowing from the underlying resource”*: We believe our company truly will obtain future economic benefits from the implementation costs since those costs will allow us to use the ERP in a SaaS agreement and get the envisioned future economic benefits through the term of the SaaS agreement. Without the implementation costs the SaaS is not feasible. The benefits are probable, identifiable and quantifiable: process improvement, increased productivity and efficiencies; improvement on managing IT costs, better decisions on multiple matters all with positive economic impact derived from better utilization of resources. Negation of the “power to obtain” those future economic benefits contradicts our business case, and probably the business cases of other companies supporting the decision to enter into a SaaS agreement to use an ERP.
- *“Restrict the access of other (including the supplier) to those benefits”*: The configuration and customization are exclusive in benefit of our company and cannot be used by other company (i.e. a competitor in the same industry). Also, our company cannot use configuration or customization of the application in SaaS that was done for a competitor using the same business application in the SaaS. Therefore, there is a real restriction to obtain the benefits of the configuration and customization. The benefits mentioned above are undoubtedly exclusive to the company incurring the implementation cost. The access of the configured or customized software to the supplier is basic to the provision of SaaS but does not mean the supplier can replicate exactly the configuration and customization to other customers, which are unique.

In general, a cloud ERP implementation project structure includes the following phases:

- Preliminary project activities
- Application development activities
- Post implementation and operations activities

The complexity of all these activities, time and costs of the implementation of a cloud ERP system are not different than those present in “internal-use software” implementation. Therefore, we believe the capitalization of implementation costs under SaaS arrangement would be consistent to the recognition of similar costs in implementation of “internal-use software”.

The preliminary project phase is used to make strategic decisions (i.e. develop or buy decisions, vendor selection, etc.) in a similar manner when the arrangement entered into is ultimately a hosting arrangement (SaaS). Further, we believe the activities in the application development and implementation stage (i.e. costs to develop, configure or customize, changes to other systems, data conversion, testing) and the post-implementation-operation phase would be similar regardless of whether the arrangement is a hosting arrangement or a license to “internal-use software”.

We believe that it would be appropriate to capitalize certain implementation costs incurred during the application development phase (i.e. system integration costs, coding, configuration or customization etc.), as those costs incurred do not provide just one-time benefit at implementation or at the time of readiness to use. Rather, we believe these implementation costs will benefit the company throughout the term of the arrangement when they will materialize, thereby, providing better matching of expenses with the period of benefits justifying the recognition in profit or loss over the term of the arrangement.

A hosting arrangement is a service contract, which may indicate a future benefit to the entity beyond the period over which the implementation services are performed. In a service contract, while the right to receive the service and the obligation to pay for the service as the service is provided are not recognized on the balance sheet, we think that certain costs to implement the hosting arrangement enhance the unrecognized right to receive the related service. Accordingly, in our view implementation cost of a hosting arrangement that is a service contract could be attached to the service contract and, therefore, should be capitalized as

an asset and recognized over a period longer than the period over which the implementation services are provided.

As we all know, FASB Emerging Issues Task Force pronouncement ASU 2018 -15 "*Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*" allow companies entering into a cloud computing agreement that is a service contract to apply the same guidance toward the implementation costs that are used for "internal-use software".

The convergence of accounting standards is since several decades a goal, driven by multiple factors, one increasing or facilitating the comparability of financial reporting. Current IFRS IC interpretation if confirmed may lead to a lack of comparability between financial reporting in different jurisdictions on one matter of certainly increased materiality.

Based on all the above we respectfully request the IFRS Interpretation Committee to revisit the discussion and add the recognition of this topic Configuration or Customization Costs in a Cloud Computing Arrangement (IAS 38) to the standard setting agenda.

Thank you for your kind consideration.

Alalani

Amin Lalani, CPA, CA

Business Unit Leader, Financial Reporting



Carlos Guichon, CIA, CISA, CPA(URY)

Director of Finance

12 February 2021

Phone: +44 (0)20 7936 3000
Fax: +44 (0)20 7583 0112
www.deloitte.com/about

Direct phone: 020 7007 0884
vepoole@deloitte.co.uk

Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
United Kingdom
E14 4HD

Dear Ms Lloyd

Tentative agenda decision – Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38 *Intangible Assets*)

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the December 2020 IFRIC Update of the tentative decision not to take onto the Committee's agenda the request for clarification on accounting for costs of configuring or customising the supplier's application software in a Software as a Service (SaaS) arrangement.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision. However, we believe that the wording of the decision could be clarified as indicated below.

The agenda decision states that in some circumstances an arrangement may result in the customer having to assess whether additional code meets the recognition criteria in IAS 38. We believe these circumstances are limited and, in order to avoid misinterpretation, we would suggest adding a reference to the Committee's Agenda Decision of March 2019. We suggest that this could be achieved by adding the following sentence to the end of this paragraph: "The analysis considered in the Committee's Agenda Decision of March 2019 *Customer's Right to Receive Access to the Supplier's Software Hosted on the Cloud (IAS 38 Intangible Assets)* provides additional guidance on how to make this assessment."

To confirm that the customer does not receive a software asset at any point during the contract we would also suggest that the fact pattern could be clarified by adding the underlined words in the following sentence: "that right to receive access does not provide the customer with a software asset at the contract commencement date or during the contract period".

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'V. Poole', with a long horizontal flourish extending to the right.

Veronica Poole
Global IFRS Leader

15 February 2021

Ms. Sue Lloyd
Chair of the IFRS Interpretations Committee
International Accounting Standards Board
Columbus Building, 7 Westferry Circus
Canary Wharf, London, E14 4HD
United Kingdom

**Comments on the Tentative Agenda Decision Relating to
Configuration or Customisation Costs in a Cloud Computing Arrangement
(IAS 38 *Intangible Assets*)**

1. The Accounting Standards Board of Japan (“the ASBJ” or “we”) welcome the opportunity to comment on the IFRS Interpretation Committee (“the Committee”)’s tentative agenda decision relating to “Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38 *Intangible Assets*)” in the December 2020 IFRIC Update.

Reference to IFRS 15 *Revenue from Contracts with Customers* for the configuration or customisation costs

2. We agree that IAS 38 does not include requirements that deal with the identification of the services the customer receives and when the supplier performs those services to deliver them in relation to configuration or customisation costs described in the request if the customer does not recognise an intangible asset. We also agree that, accordingly, the customer shall refer to the requirements in IFRS Standards dealing with similar and related issues, applying paragraphs 10-11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
3. However, the tentative agenda decision states that “the Committee observed” that IFRS 15 includes requirements that suppliers apply in identifying the promised goods or services in a contract with a customer and when those promised goods or services

are transferred to the customer. In addition, the Committee notes that, in the fact pattern described in the request, those requirements in IFRS 15 deal with issues similar and related to those faced by the customer in determining when the supplier performs the configuration or customisation services in accordance with the contract to deliver those services.

4. In this context, we think the agenda decision may be read in various ways, and we are concerned that one of such ways could be that the agenda decision would require entities to always refer to IFRS 15. We also note that, even though paragraph 42 of Agenda Paper 5 prepared by IASB staff for discussion at the December 2020 IFRIC meeting stated that “we are not saying that a customer would always look to IFRS 15 in the absence of specific requirements regarding a particular transaction,” the tentative agenda decision does not include such description nor does it state that the fact pattern is merely an example.
5. Furthermore, as the IASB staff acknowledges in the aforementioned Agenda Paper, IFRS 15 applies to contracts with customers from the perspective of the seller. Although both the fact pattern in the request and IFRS 15 focus on the supplier, we believe it is inappropriate to include in the tentative agenda decision a conclusion that would imply that symmetrical accounting is required, when IFRS Standards do not necessarily require symmetrical accounting between the buyer and the seller. Even if the tentative agenda decision clearly states that the treatment is limited to "the fact pattern described in the request," we are concerned that the tentative agenda decision would lead to effectively requiring symmetrical accounting between the buyer and the seller by analogy.
6. For the reasons stated above, we do not support the issuance of this tentative agenda decision unless it is clarified that entities are not always required to refer to IFRS 15 and that symmetrical accounting between the buyer and the seller would not always be required.
7. We hope that our comments are helpful for the Committee’s and the IASB’s consideration in the future. If you have any questions, please feel free to contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to read "A. Kogasaka". The signature is fluid and cursive, with the first letter of each name being capitalized and prominent.

Atsushi Kogasaka

Chair

Accounting Standards Board of Japan



IFRS Interpretations Committee
IFRS Foundation
Columbus Building
7 Westferry Circus
London
E14 4HD

15 February 2021

Subject: Tentative Agenda Decision— Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)

Dear IFRS Interpretations Committee:

On behalf of the International Air Transport Association's ("IATA") Industry Accounting Working Group ("IAWG"), we are writing to comment on the Tentative Agenda Decision— Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38) issued on December 15, 2020.

IAWG is made up of senior finance professionals of major airlines and represents over 290 IATA member airlines.

IAWG does not agree that the configuration or customization services in the fact pattern provided would not qualify as an intangible asset in all scenarios. We believe that in some contracts the economic benefits and access to these services are controlled by the customer as we would not see any other party capable of benefitting from their use. We also believe that if an intangible asset was not recorded it would follow that performance of the configuration and customization services could only be transferred as the software modified by the service is accessed eliminating the need to analogize to IFRS 15.. Even if IFRS 15 is applied, the services must be distinct to be treated separately from the underlying software. This is because the resource necessary to benefit from the configuration or customization is not available until it is accessed in the future. Therefore the configuration and customization services would be non-distinct assets and if the payment is made prior to assessing this bundle of services it would be treated as a prepaid expense and not a cost in all circumstances covered by the fact pattern in the tentative agenda decision. We further explain our position below.

IAWG does not agree with the Committee's conclusion that the principles and requirements in IFRS Standards provide an adequate basis for a customer to determine its accounting for configuration or customization costs incurred in relation to the SaaS arrangement described in the request and that the Committee should add a standard-setting project to the work plan as part of a full review of IAS 38.



If you would like to discuss our comments further, please do not hesitate to contact Thomas Egan, IAWG Accounting Technical Expert at egant@iata.org.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Thomas Stellpflug".

Thomas Stellpflug
Chairman
IATA IAWG

A handwritten signature in blue ink, appearing to read "Donal Cahalan".

Donal Cahalan
Vice-Chairman
IATA IAWG



Background

The Committee received a request about the customer's accounting for costs of configuring or customizing the supplier's application software in a Software as a Service (SaaS) arrangement. In the fact pattern described in the request:

- a. a customer enters into a SaaS arrangement with a supplier. The contract conveys to the customer the right to receive access to the supplier's application software over the contract term—that right to receive access does not provide the customer with a software asset at the contract commencement date. Therefore, the access to the software is a service that the customer receives over the contract term.
- b. the customer incurs upfront costs of configuring or customizing the supplier's application software to which the customer receives access. The request describes configuration and customization as follows:
 - i. configuration involves the setting of various 'flags' or 'switches' within the application software, or defining values or parameters, to set up the software's existing code to function in a specified way.
 - ii. customization involves modifying the software code in the application or writing additional code. Customization generally changes, or creates additional, functionalities within the software.

In analyzing the request, the Committee considered two question.

Question 1: Does the customer recognize an intangible asset in relation to configuration or customization of the application software?

Applying paragraph 18 of IAS 38, an entity recognizes an item as an intangible asset when the entity demonstrates that the item meets both the definition of an intangible asset and the recognition criteria in paragraphs 21–23 of IAS 38. IAS 38 defines an intangible asset as 'an identifiable non-monetary asset without physical substance'. IAS 38 notes that an asset is a resource controlled by an entity and paragraph 13 specifies that an entity controls an asset if it has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits.

In the fact pattern described in the request, the supplier controls the application software to which the customer has access. The assessment of whether configuration or customization of that software results in an intangible asset for the customer depends on the nature and output of the configuration or customization performed. The Committee observed that, in the SaaS arrangement described in the request, the customer often would not recognize an intangible asset because it does not control the software being configured or customized and those activities do not create an asset that is separate from the software. In some circumstances however, the arrangement may result in, for example, additional code from which the customer has the power to obtain the future economic benefits and to restrict others' access to those benefits. In that case, the customer assesses whether the additional code is identifiable and meets the recognition criteria in IAS 38 in determining whether to recognize the additional code as an intangible asset.



IAWG generally agrees with the thought process applied, but questions how the Committee determined that the customization or configuration of software controlled by others but used by them to provide a service to the customer would not in some cases result in the benefits from the configuration or customization of the software flowing to the customer and the customer being able to restrict others from benefitting. We would expect that in many cases only the customer and supplier would have access to the configuration and customization. We do not see in those scenarios that the supplier would benefit from using the configuration or customization as they are services provided by the supplier. If a third party provided these services, we still do not see how the supplier could benefit from using these services.

IAWG would expect in these scenarios that contracts for SaaS services where configuration or customization were to take place on software controlled by the supplier that the agreement to confer rights over these assets to the customer.

We call your attention to agenda decision Customer's Right to Receive Access to the Supplier's Software Hosted on the Cloud (IAS 38) issued in March 2019. In that decision the Committee stated that:

The Committee observed that, if a contract conveys to the customer only the right to receive access to the supplier's application software over the contract term, the customer does not receive a software intangible asset at the contract commencement date. A right to receive future access to the supplier's software does not, at the contract commencement date, give the customer the power to obtain the future economic benefits flowing from the software itself and to restrict others' access to those benefits.

The Committee provided no basis for this observation. It appears that this tentative agenda decision uses that decision as a basis for the same observation, but the Committee does not consider how configuration or customization of the software is more than just future access. It is actual control over that software as the customer is able to modify the software. While we believe that the customer would not obtain the future benefits flowing from the software or be able to restrict access to that underlying software, the issue is whether that is true of the configuration or customization. We do not believe that anyone other than the customer could benefit or access those assets to obtain benefits in many scenarios. This would be true in cases where they are customized assets and very likely to be controlled by the customer under the contract.

We also noted that the Committee observed that, in the SaaS arrangement described in the request, the customer often would not recognize an intangible asset because it does not control the software being configured or customized and those activities do not create an asset that is separate from the software. IAS 38, paragraph 12(b) does not require that an asset be created separate from the software to establish an identifiable asset.

For those reasons, we believe that unless the agreement with the supplier confers the economic benefits of the configuration or customization of the software to the supplier the customer should recognize an intangible asset if all other recognition criteria are met. The



AD should reflect that this requires a determination of fact and not a default finding that no recognizable intangible asset exists.

IAWG further observed that this TAD provided for an accounting treatment for the configuration and customization costs that would differ from the treatment of the software if it were licensed to the customer rather than the supplier, despite the customer receiving identical economic benefits from the configuration and customization services. This is inconsistent with the Board's philosophy that the accounting treatment should reflect the economic substance and not the legal form of the transaction.

Question 2: If an intangible asset is not recognized, how does the customer account for the configuration or customization costs?

If the customer does not recognize an intangible asset in relation to configuration or customization of the application software, it applies paragraphs 68–70 of IAS 38 to account for those costs. The Committee observed that:

the customer recognizes the costs as an expense when it receives the configuration or customization services (paragraph 69). Paragraph 69A specifies that 'services are received when they are performed by a supplier in accordance with a contract to deliver them to the entity and not when the entity uses them to deliver another service...'. In assessing when to recognize the costs as an expense, IAS 38 therefore requires the customer to determine when the supplier performs the configuration or customization services in accordance with the contract to deliver those services.

IAWG believes that it is clear when the configuration or customization services is performed by the supplier. The question to be addressed is whether the configuration and customization services are provided in the form of access to those services at the same time as the underlying software. If so, they should be treated as a service performed over time. If the asset is controlled by the supplier as determined by the Committee above, it would follow that the access to these services are performed over time.

The Committee further observed that IAS 38 does not include requirements that deal with the identification of the services the customer receives and when the supplier performs those services in accordance with the contract to deliver them. Paragraphs 10–11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* require the customer to refer to, and consider the applicability of, the requirements in IFRS Standards that deal with similar and related issues. The Committee observed that IFRS 15 *Revenue from Contracts with Customers* includes requirements that suppliers apply in identifying the promised goods or services in a contract with a customer and when those promised goods or services are transferred to the customer. In the fact pattern described in the request, those requirements in IFRS 15 deal with issues similar and related to those faced by the customer in determining when the supplier performs the configuration or customization services in accordance with the contract to deliver those services.

IAWG does not disagree with considering the principles in IFRS 15 but is concerned about linking revenue recognition and expense when the two issues are not symmetrical. IFRS 15 is based on when the asset is transferred to the customer and not when the service is performed.



The Committee further observed in referring to the requirements in IFRS 15 to determine when the supplier performs the configuration or customization services in accordance with the contract to deliver them:

- i. if the services the customer receives are distinct, then the customer recognizes the costs as an expense when the supplier configures or customizes the application software.
- ii. if the services the customer receives are not distinct (because those services are not separately identifiable from the customer's right to receive access to the supplier's application software), then the customer recognizes the costs as an expense when the supplier provides access to the application software over the contract term.

IAWG agrees and suggests that the Committee expand on this analysis to address the principle in IFRS 15 paragraph 27 regarding the concept of distinct:

A good or service that is promised to a customer is distinct if both of the following criteria are met:

- a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and*
- b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).*

As the access to the software, which has been modified by the configuration or customization is provided in the future, it is clear that the resource needed to benefit from these services is not readily available and therefore the services are not distinct and if the customer pays the supplier before receiving the services, it recognizes the prepayment as an asset in accordance with paragraph 70 of IAS 38.

IAWG does not agree with the Committee's conclusion that the principles and requirements in IFRS Standards provide an adequate basis for a customer to determine its accounting for configuration or customization costs incurred in relation to the SaaS arrangement described in the request and that the Committee should add a standard-setting project to the work plan. The FASB undertook standard-setting in relation to this issue. We believe the IASB should the same. We would ask that this effort be part of a full review of IAS 38 as the significance and types of intangible assets have substantially changed from the time when IAS 38 was issued.



Ms Sue Lloyd
Chair
IFRS interpretations committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

15th February 2021

Dear Sue,

Tentative Agenda Decision (TAD): Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38 Intangible Assets)

We are responding to your invitation to comment on the tentative agenda decision - Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38) - published in December 2020, on behalf of PricewaterhouseCoopers.

Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on the tentative agenda decision. "PricewaterhouseCoopers" refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We agree with the conclusion of the committee to Question 1 that the customer would often not recognise an intangible asset because it does not control the software being configured or customised. However, in situations where the customer obtains control of an identifiable intangible asset, it should be recognised.

We recommend that the Committee clarify that the use of IFRS 15's principles might not always be appropriate when considering paragraph 69 and 69A of IAS 38. We agree that in situations in which an intangible asset is not recognised, the customer could consider some of the principles in IFRS 15 to determine when a service is received and whether a prepayment asset is recognised. However, we are concerned that IFRS 15 will not be helpful or appropriate in all circumstances. In particular, the guidance on multiple element arrangements in IFRS 15 was designed to identify and separate performance obligations of a (single) supplier. It was not developed to determine whether a multiple element arrangement exists for the customer nor how to account for such an arrangement when multiple interrelated services are provided to a customer by more than one supplier.

PricewaterhouseCoopers International Limited
1 Embankment Place
London WC2N 6RH
T: +44 (0) 20 7583 5000, F: +44 (0) 20 7822 4652



We note that the tentative agenda decision does not address the assessment of a potential prepayment when the setup services are provided by a third party rather than the supplier. We think that the Committee should clarify that in this fact pattern, the assessment would be the same regardless of whether the setup services are provided by the supplier of the SaaS services or a third party. We see no reason why the accounting from the customer's perspective should depend on the counterparty that supplies the related services. Rather, we think that the accounting should depend on the nature of the services received and whether they are distinct from the SaaS services from the customer's perspective. We think this is consistent with the IFRS 15 principle relating to identifying distinct goods or services in this fact pattern. In many cases, the customisation or setup risk and SaaS service risk are inseparable and the customisation significantly modifies or customises the service that will be provided (IFRS 15 paragraph 29(b), BC105). We believe that it would be appropriate for the customer to conclude that no distinct service has been delivered if the requirement of IFRS 15 paragraph 27(b) is not met. This assessment would be the same regardless of the party that supplied the customisation *from the customer's perspective*.

If you have any questions in relation to this letter please do not hesitate to contact Henry Daubeney PwC Head of Reporting and Chief Accountant (+44784159635) or Gary Berchowitz +447535100574).

Yours faithfully

A handwritten signature in blue ink that reads "PricewaterhouseCoopers". The signature is written in a cursive style and is positioned above the typed name and title.

Henry Daubeney
Partner, Global Chief Accountant and Head of Reporting
Mobile: 07841569635
Email: henry.daubeney@pwc.com
PricewaterhouseCoopers LLP

PO Box 1411
Beenleigh QLD 4207
15 February 2021

Ms Sue Lloyd
Chair IFRS Interpretations Committee
International Accounting Standards Board
Columbus Building, 7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Online submission: [IFRS - Configuration or Customisation Costs in a Cloud Computing Arrangement \(IAS 38\)](#)

Dear Sue

Tentative agenda decision - Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)

I am pleased to make this submission on the above Tentative Agenda Decision (TAD) relating to Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38).

I have extensive experience in accounting advice on International Financial Reporting Standards across a wide range of clients, industries and issues in the for-profit, not-for-profit, private and public sectors.

My clients have included listed companies, unlisted and private companies, charitable and not-for-profit organisations, federal, state and local government departments and agencies in the public sector, and government owned corporations (government business enterprises). I also have some commercial, standard setting and academic experience.

Overall

I do not agree with the TAD as it fails to analyse the consequences of the cloud computing services contract being an intangible asset, even if the intangible asset is not the computer code.

I also find that applying the IFRS 15 performance obligation methodology from the perspective of the customer results in nonsensical outcomes.

I also consider the effect of applying the IFRS 15 reasoning from the perspective of the customer to the capitalisation of listing fees.

Cloud Computing Services Contract is an intangible asset

A cloud computing services **contract** is an intangible asset under IAS 38:

- 12 An asset is identifiable if it either:**
- (a) ... or**
 - (b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.**

I agree the intangible asset is not the computer code. However, the services contract is an intangible asset because of its contractual and other legal rights.

Under a cloud computing services contract, I have very similar rights to future benefits from the computer system as if I had acquired the rights through an upfront licence fee. I have a contract with the cloud computing services company for them to provide me with services such as ERP (Enterprise Resource Planning), general ledger, accounts receivable, accounts payable, etc. over the contract term.

From a functional point of view, there is very little difference between paying an upfront licence fee, and annual updates, with an ongoing monthly or annual fee. Consequently, any set-up costs (configuration and customisation costs) should be capitalised similarly for upfront licences, and regular payment licences.

Costs of getting the Cloud Computing Services Contract intangible asset ready for use should be capitalised

The costs of getting the intangible asset (the cloud computing services contract) ready for use should be capitalised under IAS 38 as part of the cost of the intangible asset:

- 27** The cost of a separately acquired intangible asset comprises:
- (a)** its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
 - (b)** any directly attributable cost of preparing the asset for its intended use.
- 28** Examples of directly attributable costs are:
- (a)** costs of employee benefits (as defined in AASB 119) arising directly from bringing the asset to its working condition;
 - (b)** professional fees arising directly from bringing the asset to its working condition; and
 - (c)** costs of testing whether the asset is functioning properly.

While I would normally expect 27(a) to be nil for service contracts based on as a pay as you go basis (and the service cost expensed when the services are provided), 27(b) requires that the costs for getting the contract ready for use are capitalised.

Flawed outcome of applying IFRS 15 from customer perspective

When applying IFRS 15 from the perspective of the customer, in some circumstances when the cloud computing company provides the configuration and customisation services, those services will be regarded as being not distinct, with the outcome under the TAD being that the customer is regarded as receiving the services over time. However, if a third-party company provides those same services, those services will always be distinct, as there is no other output to combine the services with. The outcome under the TAD will then be that the customer is regarded as receiving the services upfront.

To me this is a nonsensical outcome. It is the same configuration and customisation activities being provided by either party. Therefore, the services should be recognised as having been received by the customer on the same basis, irrespective of whether they are provided by the cloud computing company or the third-party company.

I regard the application of the IFRS 15 methodology from the customer perspective to be spurious reasoning. Spurious being defined as “not being what it purports to be; false or fake” and “apparently but not actually valid”/

<https://www.lexico.com/definition/spurious>

Viewed 13 February 2021

Whatever the appeal of the IFRS 15 methodology, with its separation and combination requirements, it provides nonsensical outcomes. Therefore, it is not appropriate to be mandated from a customer perspective in determining when services are received.

Application to listing fees

The IFRS Interpretations Committee recently concluded that the initial fees are not a separate obligation of the supplier¹.

Applying the IFRS 15 reasoning in the TAD to the customer would mean that the listing services would be regarded as having been received by the customer over time. Consequently, following the IFRS 15 reasoning in the TAD, the listing fees would be capitalised and expensed over time. This contrasts with current practice of expensing those fees. This outcome provides further support to me that despite the appeal of the IFRS 15 methodology, it is spurious reasoning and is a flawed approach.

Then there would be the question over what period the listing fees would be amortised, that may depend on which stock exchange you are listed on. For example, Bursa Malaysia Berhad (Malaysian Stock Exchange) might be over 18 years², Australia (Australian Securities Exchange - ASX) 5 years for initial listing³, and Australia (National Stock Exchange – NSX) 3 years⁴.

Yours sincerely,

David Hardidge

<https://www.linkedin.com/in/davidhardidge/>

1 Assessment of Promised Goods or Services (IFRS 15) (January 2019)

<https://cdn.ifrs.org/-/media/project/assessment-of-promised-goods-or-services/agenda-decision/ifrs-15-assessment-of-promised-goods-or-services-jan-19.pdf>

² Submission by the Malaysian Accounting Standards Board on the Tentative Agenda Decision and refers to an 18 year period

http://eifrs.ifrs.org/eifrs/comment_letters//509/509_25064_TanBeeLengMalaysianAccountingStandardsBoardMASB_0_CL_IFRICTAD_ifrs15.pdf

³ ASX Ltd (Australian Securities Exchange) Annual Report 2020, Note B2

<https://www2.asx.com.au/content/dam/asx/annual-reports/asx-annual-report-2020.pdf>

⁴ NSX Ltd (National Stock Exchange of Australia) Annual Report 2020, Note 2

<https://www.nsx.com.au/documents/financials/NSXLimitedAnnualFinancialReport2020.pdf>

15 February 2021

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd,

IFRS Interpretations Committee Tentative Agenda Decisions

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the following Tentative Agenda Decisions published in December 2020:

- (a) Attributing Benefit to Periods of Service (IAS 19 *Employee Benefits*)
- (b) Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38 *Intangible Assets*)

We agree with the Interpretations Committee's reasons set out in the Tentative Agenda Decision for not adding these items onto its agenda.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,



TAN BEE LENG
Executive Director

February 15, 2021

Ms. Sue Lloyd,
Chair, IFRS Interpretations Committee,
Columbus Building
7 Westferry Circus
Canary Wharf, London E14 4HD
United Kingdom

Dear Ms. Sue,

Subject: Comments of the Institute of Chartered Accountants of India (the ICAI) on Tentative Agenda Decision (TAD) issued by IFRS Interpretations Committee on ‘Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)’

The Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) welcomes the opportunity to comment on above referred Tentative Agenda Decision of IFRS Interpretations Committee.

The aforesaid Tentative Agenda Decision dealt with the accounting of configuration or customisation costs incurred on supplier’s application software in a Software as a Service (SAAS) arrangement, in the books of customer.

At the outset, we agree with the conclusions laid down in the TAD. However, we have concerns on making reference to IFRS 15, *Revenue from Contracts with Customers*. To determine when the supplier performs the configuration or customisation services in accordance with the contract, the TAD refers IFRS 15 and concluded that:

- a) if the services the customer receives are distinct, then the customer recognises the costs as an expense when the supplier configures or customises the application software.
- b) if the services the customer receives are not distinct (because those services are not separately identifiable from the customer’s right to receive access to the supplier’s application software), then the customer recognises the costs as an expense when the supplier provides access to the application software over the contract term.

IFRS 15 provides guidance from the perspective of supplier and requires recognition of revenue when the supplier satisfies a performance obligation. For this purpose various elements of multiple elements arrangement need to be

identified by the supplier. The analysis contained in the TAD leads to the conclusion that the customer has to always mirror the supplier's accounting. Requiring application of principles of IFRS 15 to the customer, in all the cases, may not be appropriate as customer may not have access to the information available to the supplier.

Therefore, we request the IFRS Interpretation Committee to specify that the reference to IFRS 15 does not imply mirror accounting by the supplier and customer in all the cases. Alternatively, the analysis may drop direct reference to IFRS 15, while retaining the conclusion.

With kind regards,

Chairman
Accounting Standards Board
Institute of Chartered Accountants of India



International Accounting Standards Board/IFRS IC
Columbus Building
7 Westferry Circus, Canary Wharf
London E14 4HD
UK

Stockholm February 15, 2021

Implementation of IFRS IC Agenda Decisions

The current tentative IFRS IC Agenda Decision Configuration or Customisation Costs in a Cloud Computing Arrangement brings to date the issue of implementation time for changes in accounting policy that result from agenda decisions. For several reporting entities, this agenda decision may give rise to significant changes in accounting policies that require an extended time for preparation. As the agenda decisions are expected to be adopted by the IFRS IC at a point in time when a majority of the reporting entities are in the midst of preparing their financial statements, implementation for the financial year 2020 is hardly possible.

The Board has previously expressed the view that companies should be entitled to “sufficient” time for implementation of changes due to IFRS IC agenda decisions. However, for reporting entities and their auditors the period that can be considered “sufficient” in this context is not obvious. According to a statement by Board Member Sue Lloyd published on the Board’s website “sufficient” is a matter of months rather than years.

We believe that the current confusion around when an agenda decision needs to be implemented is both unfortunate and unnecessary. An evident way to clarify the situation and avoid needless deliberations would be to add time for implementation of agenda decisions to the Due Process Handbook. Until such an addition to the handbook can be made, we believe that IFRS IC should state time for implementation within its agenda decisions.

Kind regards,

CONFEDERATION OF SWEDISH ENTERPRISE

Sofia Bildstein-Hagberg

The Swedish Enterprise Accounting Group (SEAG) represents more than 40 international industrial and commercial groups, most of them listed. The largest SEAG companies are active through sales or production in more than 100 countries.



ASSOCIATION OF NATIONAL ACCOUNTANTS OF NIGERIA

Comments on the Tentative Agenda Decision and comment letters on Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38)

The Association of National Accountants of Nigeria (ANAN) has critically and painstakingly reviewed the basis of IFRS Interpretations Committee's decision and welcomes the opportunity to comment on the Tentative Agenda Decision and comment letters: Configuration or Customisation Costs in Cloud Computing Arrangement (IAS 38). Our responses to the two issues/questions contained therein are as follows:

QUESTION 1:

Does the customer recognize an intangible asset in relation to configuration of the application software?

Comment 1

The Association of National Accountants of Nigeria (ANAN) agrees with the conclusion of IFRS Interpretations Committee that the SaaS arrangement in the fact pattern described in the request will not qualify as intangible asset for lack of control. We are however of the opinion that configuration or customization costs under the SaaS arrangement should be generally recognized as part of the intangible asset subject to materiality level so as to determine whether or not to capitalize based on management's approval.

Our position is informed by the fact that IAS 38-INTANGIBLE ASSETS has adequately provided answers to the question.

QUESTION 2:

If an intangible asset is not recognized, how does the customer account for configuration or customization costs?

Comment 2

Intangible asset is a very critical area of concern to all stakeholders. However, the standard has simplified it by providing the models for the classifications and accounting treatment. If an intangible asset is not recognized, the customer will account for configuration or customization costs by expensing the costs, provided the supplier performs the configuration services. This view is in tandem with IFRS Interpretations Committee's conclusion.

For any further information or clarification, please contact the undersigned.

Dr. Nuruddeen Abba Abdullahi, mni, FCNA
Chief Executive Officer
Association of National Accountants of Nigeria
abdullahi@anan.org.ng

February 12, 2021

(By e-mail to ifric@ifrs.org)

IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Sirs,

Re: Tentative agenda decision on IAS 38 *Intangible Assets* – Configuration or Customization Costs in a Cloud Computing Arrangement

This letter is the response of the staff of the [Canadian Accounting Standards Board](http://www.frascanada.ca) (AcSB) to the IFRS Interpretations Committee's (Committee) tentative agenda decision on configuration or customization costs in a cloud computing arrangement. This tentative agenda decision was published in the December 2020 IFRIC® Update.

The views expressed in this letter take into account discussions with individual members of the AcSB staff.

While we agree with the Committee's analysis under existing guidance in IFRS Standards, we think there are additional aspects to consider in addressing Question II on how the customer accounts for the configuration or customization costs. Additional aspects that affect the accounting include how the contract term is determined if the services the customer receives are not distinct (e.g., should renewal options be considered) and whether the prepayment asset should be subject to impairment. Given entities need to look to requirements in other IFRS Standards to apply paragraph 69A of IAS 38 *Intangible Assets*, we think that the Committee should add a project to its standard-setting agenda to address Question II more holistically. Furthermore, we think that adding a project also enables the Committee to consider whether the accounting outcome reached under existing guidance properly

reflects the economic substance of the transaction. We are aware that some stakeholders view implementation costs of a cloud computing arrangement to be economically similar to the implementation costs of on-premise software, which raises the question whether the accounting outcome should be same.

We also think it would be important for the Committee to clarify how the analysis applies to configuration or customization services performed by a third-party service provider. In practice, it is common for an entity to contract with a third-party to implement the cloud-based solution in addition to working with a cloud supplier. However, we think it would be difficult to support that third-party services are not distinct from the customer's right to receive access to the cloud supplier's application software because the third-party services would be delivered in accordance with a contract that is separate from the cloud provider's contract. Therefore, we suggest the Committee be clear in its conclusion to avoid misapplication.

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me at +1 416-204-3453 (e-mail kkhalilieh@acsbcanada.ca), or, alternatively, Davina Tam, Principal, Accounting Standards at +1 416 204-3514 (e-mail dtam@acsbcanada.ca).

Yours truly,



Kelly Khalilieh, CPA, CA
Director, Canadian Accounting Standards Board
kkhalilieh@acsbcanada.ca
+1 416-204-3453

13 February 2021

IFRS Interpretations Committee
IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

Dear Committee,

Request for Comment on Tentative Agenda Decision: Configuration or Customisation Costs in a Cloud Computing Arrangement (IAS 38) (“TAD”)

Seven Group Holdings Limited (“SGH”) is a leading Australian diversified operating and investment Group with market leading businesses and investments in industrial services, media and energy.

SGH welcomes the opportunity to comment on the TAD from a preparer of financial statements perspective who deals with capital markets and investors.

Cloud computing or Software as a Service (SaaS), typically involves software applications licensed on subscription, centrally hosted in a cloud and accessed via the internet. This cloud may be public or private depending on the nature of the organisation and software being provided. This contrasts to software applications licensed and self-hosted and accessed over an internal network. Currently SGH utilises both cloud and self-hosted applications, such as SAP, across our various operations.

As a SaaS customer we usually cannot take possession of the software. Instead, our businesses access and uses the software on an as-needed basis over the internet or via a dedicated line. Our SaaS arrangements typically have an initial non-cancellable period with extension options. The associated fees, which are generally paid periodically throughout the contract term and can have tiered pricing based on volume. We have adopted SaaS to gain access to enhanced IT security environments and ensure upgrade paths and patches are always maintained across elements of our ERPs.

We understand the proposed approach outlined in the TAD is to amend the existing accounting practice of capitalising the costs associated with configuration of these major ERPs, to expensing the implementation and configuration costs as incurred. In this regard we observe that the position outlined:

- Is inconsistent with current practice under IAS 38 where costs of configuration and customisation of self-hosted computer software is capitalised and amortised over the period of usage by the customer over its period of intended use, usually multiple years;
- provides a disincentive to update systems and potentially migrate core applications to cloud based environments due to proposed expense upfront, as opposed to the cost being matched against the benefits received, from the use of the system configuration and implementation;
- would likely result in restructuring commercial SaaS arrangements and delivery models by developers/vendors/providers to build in configuration and customisation costs into subscription or annual licencing fees charged to enable the costs to be spread, resulting in reduced use of third-party resellers/partners/consultants who are currently involved in implementation of SaaS and in turn reducing competition and increasing costs in system implementation; and
- The position also appears to result in an accounting outcome that is incongruent with the commercial substance of the arrangement. When a company commercially agrees to incur such significant upfront costs, this is because there is an expectation of future benefit flowing to the entity (in the form of the contractual expectation to be able to access the cloud-based system for the foreseeable future).

We believe that while SaaS is a different method by which software developers/vendors deliver customers their computer software, centrally versus self-hosted, this should not, in our opinion, change the treatment of associated configuration and customisation costs of the customer, from current treatment of self-hosted costs as an asset that is amortised over time to match the benefits received from the software.

As outlined in the TAD, IAS 38 defines an intangible asset as 'an identifiable non-monetary asset without physical substance'. IAS 38 notes that an asset is a resource controlled by an entity and paragraph 13 specifies that an entity controls an asset if it has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits.

IAS 38.10 notes the definition of an intangible asset as identifiability, control over a resource and existence of future economic benefits. We believe configuration and customisation of SaaS, as with configuration and customisation of self-hosted software, meets the definition of an intangible asset under IAS 38 as follows:

Identifiability

IAS 38.12 states:

An asset is identifiable if it either:

- a. is separable, ie is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or*
- b. arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.*

We believe the configuration and customisation is identifiable arising from the legal rights of the subscription and contract with the software vendor and/or consultant performing the configuration and customisation. In our experience large organisations do not look to update major ERP applications regularly but when they do the costs can be significant and provide enduring economic benefit.

Control over a resource

IAS 38.13 states:

"An entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way."

We believe the customer does control the software being configured or customised for the period of the subscription and the customer has from the legal rights of the subscription the power to obtain the future economic benefits from the software and restrict other entities from the use of its own configuration and customisation.

Existence of future economic benefits

IAS 38.17 states:

The future economic benefits flowing from an intangible asset may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity. For example, the use of intellectual property in a production process may reduce future production costs rather than increase future revenues.

We believe configuration and customisation of SaaS increases the benefits resulting from the use of the software. Unconfigured software is unable to be used. Customisation by its nature is designed to increase the functionality and usefulness to the customer.

Costs

We believe costs of configuration and customisation should be included in the cost of a separately acquired intangible asset for SaaS subscription.

IAS 38.27 states:

The cost of a separately acquired intangible asset comprises:

- a. *its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and*
- b. *any directly attributable cost of preparing the asset for its intended use.*

IAS 38.28 states:

Examples of directly attributable costs are:

- a. *costs of employee benefits (as defined in AASB 119) arising directly from bringing the asset to its working condition;*
- b. *professional fees arising directly from bringing the asset to its working condition; and*
- c. *costs of testing whether the asset is functioning properly*

We believe configuration and customisation costs paid by the customer to software vendor and/or consultant are directly attributable cost of preparing the SaaS for its intended use and would fit the example of professional fees arising directly from bringing the asset to its working condition for the customer.

We believe there should be consistency in accounting for implementation configuration and customisation costs between SaaS and self-hosted software.

We also understand this is the approach taken on this topic under US GAAP. FASB issued US GAAP guidance with no IFRS equivalent that requires capitalizing certain implementation costs and specifies their presentation.

As outlined in ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement, FASB has explicit criteria for determining whether or not to recognise an asset for SaaS arrangements.

The customer recognises an intangible asset, assuming criteria for capitalisation of internal-use software are met, if the customer has both:

- The contractual right to take possession of the software at any time during the hosting period without significant penalty; and
- It is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software.

If either criterion is not met, the arrangement is accounted for as a service contract.

However, the customer needs to ensure that the implementation costs are not capitalised under other guidance – e.g. as property, plant and equipment or because they create an intangible asset in their own right.

US GAAP was recently amended to require implementation costs incurred by customers in a service arrangement to be deferred and recognised over the term of the arrangement if those costs would be capitalised under the internal-use software guidance in ASC 350-40.7

The change is expected to reduce diversity in practice and lead to more implementation costs being deferred. In essence, the timing of expensing implementation costs should now align, whether the arrangement is accounted for as a service contract or as the transfer of a software license. Only the presentation may be different – i.e. deferred implementation costs presented as other assets if a service contract or as an intangible asset if a software license. A company also presents amortisation of the implementation costs in the same line item in the income statement as the expense for fees for the associated arrangement.

As a result of the above we request the Committee reconsider the proposed treatment and suggest it specifically adopts the additional guidance provided by FASB guidance in ASC 350-40.7 which we believe more reflects the economic substance of implementation and configuration costs associated with SaaS.

Please do not hesitate to contact us should you wish to discuss this matter further.

Kind regards,

Richard Richards
Group Chief Financial Officer
ACA

Phil Clewett
Deputy Chief Financial Officer
ACA

February 15, 2021

Submitted electronically via ifric@ifrs.org

IFRS Interpretations Committee
IFRS Foundation
Columbus Building
7 Westferry Circus
London, E14 4H4
United Kingdom

Subject: Tentative Agenda Decision – Configuration or Customization Costs in a Cloud Computing Arrangement (IAS 38 *Intangible Assets*)

Dear members of the IFRS Interpretations Committee (“Committee”),

This letter is submitted in response to the Committee’s consideration of the accounting for configuration or customization costs in a cloud computing arrangement. Nutrien Ltd. is the world’s largest provider of crop inputs and services, with a market capitalization of approximately US \$23 billion and its shares publicly traded on the New York Stock Exchange and the Toronto Stock Exchange. Nutrien has been applying IFRS since 2011, and reports in quarterly intervals.

We appreciate the Committee’s consideration on this topic, as we have observed diverse views and practices emerging of whether up-front costs should be capitalized or not. Our budget on software implementation costs can be upwards of US\$100 million per year. This spending is only increasing, given the exponential shift in technologies and focus on digitization which requires adaptation of cloud computing arrangements – including software as a service, platform as a service, infrastructure as a service and other similar hosting arrangements. Appendix A provides some research on global trends observed in cloud computing.

From a customer/user’s perspective, implementation costs of cloud computing arrangements are significant, and considerably more costly than the underlying license. The arrangements are quite complex and often take months or years to implement from start to finish. Similar to on-premise software implementations, these projects are completed in phases: research, development, deployment, and maintenance. Most of the work and costs incurred relate to the development stage through customization, configuration and testing.

For example, Nutrien is in the middle of implementing a cloud-based Enterprise Resource Planning (ERP) system and a cloud-based consolidation system. In our experience, the amount of cost and effort to implement these cloud-based arrangements are no different than development of on-premise systems. We also note it is common to use third-party implementers, different from the cloud service provider.

We believe that accounting guidance for capitalization should be aligned regardless of whether we elect to maintain the software on our servers in an on-premise arrangement, or whether we have contracted to have it maintained on a third-party server’s cloud environment. Implementation costs (i.e. integration, coding,

configuring, customization, testing etc.) should be capitalizable in the development phase consistent with IAS 38 para 52 through 67.

If the tentative agenda decision is finalized as drafted, this will not be the case. Accounting for implementation costs as an upfront expense does not reflect the economics of many of our arrangements, where the implementation time can extend beyond one year, and the expected benefits of the cloud arrangement will yield benefits throughout the life of the contractual term, which can be upwards of 10+ years. These significant implementation costs are entered into with the expectation that they will result in enhanced future benefits over the term of the cloud computing arrangement.

Nutrien is an early adopter of cloud-computing arrangements, and it's anticipated that we will continue to use these hosting arrangements. However, if we are limited on our ability to capitalize implementation costs, this may influence our future purchasing decisions to on-premise software arrangements. All projects are evaluated internally for overall impacts on our key performance indicators, and a significant one-time charge to expense for implementation projects that are expected to provide benefits for three to 10 years are not looked upon favorably. The unintended consequence is that technology will be stifled as not being able to capitalize costs will dissuade companies, such as ours, from entering into cloud computing arrangements. There may also be an environmental sustainability impact, as reports indicate cloud computing output uses less energy than non-cloud alternatives. One report noted that on average, using the public cloud for office productivity applications emits about 6-7 kg of CO₂ per employee per year, while a nonvirtualized on-premise solution would be responsible for nearly 30 kg of CO₂ per employee per year (reported by Deloitte, referenced in Appendix A).

Notably these concerns were expressed directly to the Financial Accounting Standards Board in response to ASU No. 2015-05 *Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement ("Update 2015-05")*¹ by cloud hosting service providers, which prompted standard setting by the FASB, discussed further below.

It is our view that IFRS is not explicit in this area resulting in diversity in practice that was noted in the original submission to the Committee. While we agree that the analysis performed by IASB staff as to the application of IFRS to the particular fact patterns submitted is sound, we are significantly concerned with the unintended consequences of this tentative agenda decision.

Instead, we strongly recommend that this matter be directed to the IASB for standard setting.

This is not the only matter that has been raised indicating that IAS 38 does not produce information that may not be useful. We respectively point out a number of public responses received against IAS 38 in accounting for Holdings of Cryptocurrencies, and that several Committee members and IASB Board members expressed significant concern in public meetings about whether IAS 38 provides the most useful information, if applied to holdings of cryptocurrencies. We share these overall concerns that IAS 38 is not being adaptive to emerging technologies.

In considering the Committee's tentative agenda decision, we draw the Committee's attention to recent standard setting activities by the FASB in Update 2018-15 *Intangibles – Goodwill and Other – Internal-Use*

¹ Refer to Google Inc.'s response to the FASB on Update 2015-05 dated November 25, 2014, and salesforce.com, Inc.'s response to the FASB on Update 2015-05 dated November 17, 2014.

Software (Subtopic 350-40): Customer's Accounting for Implementation Costs incurred in a Cloud Computing Arrangement That is a Service Contract ("Update 2018-15"). Now available for adoption, Update 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and the hosting arrangements that include an internal-use software license). Costs for implementation activities in the application development stage are capitalized depending on the nature of the costs and are expensed over the term of the hosting arrangement.

This standard setting initiative was in direct response to Update 2015-05, which clarified when a software license arrangement is an intangible asset or a service contract. Similar conclusions were reached in the Committee's March 2019 published agenda decision for IFRS. The FASB undertook standard setting in Update 2018-15 based on several stakeholders' request for additional guidance on accounting for implementation activities performed in a cloud computing arrangement that is a service contract. The FASB concluded that the *FASB Accounting Standards Codification* is not explicit and undertook standard-setting activities to address the resulting diversity in practice.

The direction taken by the FASB is notably different than the Committee's discussion in the tentative agenda decision. The tentative agenda decision which will require that in most circumstances, configuration or customization costs will be expensed as the supplier configures/customizes the application software. It is only if the services the customer receives are not distinct, then can these costs be expensed over the contract term. As noted in the discussion by Committee members, and consistent with our own experience to date, the ability to capitalize as a prepaid asset and expense over the contract term is thought to be rare. It is more likely that the services the customer receives are distinct as they are either performed or can be performed by third parties other than the supplier of the cloud computing arrangement or in house.

The FASB specifically amended U.S. GAAP to allow for capitalization of these expenditures as a prepaid asset, expensed over the contractual term of the arrangement. This amendment results in consistent capitalization of implementation costs regardless of whether it is a service contract or on-premise software. We would note that the FASB received 53 comment letters on the proposed Update 2018-15 with "almost all respondents support[ing] the proposed amendments that would require an entity to capitalize implementation costs of a hosting arrangement that is a service contract."².

Weighing into the FASB's consensus on this matter was the following consideration extracted from the Update 2018-15 Basis of Conclusions by the FASB Emerging Issues Task Force ("Task Force"):

BC8 In reaching this consensus, the Task Force noted that an entity may incur significant costs when implementing a hosting arrangement that is a service contract, which may indicate a future benefit to the entity beyond the period over which the implementation services are performed. In a service contract, while the right to receive the service and the obligation to pay for the service as the service is provided are not recognized on the balance sheet, the Task Force observed that certain costs to implement the hosting arrangement enhance the unrecognized right to receive the related service. Accordingly, the Task Force decided that the implementation costs of a hosting arrangement that is a service contract could be attached to the service contract and, therefore, should be capitalized as an asset and recognized over a period longer than the period over which the implementation services are

² https://www.fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1176171138858&acceptedDisclaimer=true

provided. That is, those capitalized costs, while not representative of an asset on a standalone basis, result in an increase in future benefits to be received under the hosting arrangement, thus resulting in an asset related to the service contract.

The Task Force recognized that this decision might not be the most technically sound based on current U.S. GAAP, but it represented a practical solution that addressed the original concern that was raised to the Task Force, and the Task Force was responsive to the unique characteristics of hosting arrangements that are service contracts. By allowing for capitalization of a prepaid asset, the Task Force wasn't disrupting current guidance on capitalization of costs, but merely recognizing that there is some resource generation for an entity.

We agree with the standard setting process and rationale presented by the Task Force in issuing Update 2018-15.

We are concerned that IFRS issuers will be at a competitive disadvantage relative to U.S. GAAP counterparts. Many of our peer competitors apply U.S. GAAP, and we are continually monitoring for divergent standard setting activities. In Canada, domestic Canadian public companies listed on the Toronto Stock Exchange that have a dual listing with the New York Stock Exchange may apply either IFRS or U.S. GAAP. As such, we continue to monitor whether IFRS is the most appropriate generally accepted accounting principles for our stakeholders.

We appreciate your thoughtful consideration of the views and recommendations provided in this letter. If you have any questions or need additional information, please do not hesitate to contact me (+14032257026).

Yours sincerely,

Janice Anderson

Janice Anderson CPA, CA
Director, Technical Accounting and Research Advisory Services

T 403-225-7026 c 403-835-8935
janice.anderson@nutrien.com
www.nutrien.com

Appendix A: Research Trends on Cloud Computing

We note that this is a trend observed globally through two research organizations:

Gartner, Inc.

Research and advisory company Gartner, Inc. has forecasted that worldwide end-user spending on public cloud services is forecasted to grow 18.4% in 2021 to total \$304.9 billion, up from \$257.5 billion in 2020, as the pandemic validated the cloud's value proposition. Gartner expects that the proportion of IT spending that is shifting to the cloud will accelerate, with cloud projected to make up 14.2% of the total global enterprise IT spending in 2024, up from 9.1% in 2020. This increased consumption is being driven by the need for remote workers to have access to high-performing, content-rich and scalable infrastructure to perform their duties, which largely comes in the form of modernized and cloud-native applications. Gartner survey data indicates that almost 70% of organizations using cloud services today plan to increase their cloud spending in the wake of the disruption caused by COVID-19.³

Deloitte's Technology, Media, and Telecommunications group

Deloitte recently published its Technology, Media, and Telecommunications Predictions for 2021, and one of their top prediction is "The Cloud Migration Forecast" where they comment that "growth in cloud computing has been a megatrend over the last decade, with the market experiencing triple-digit annual growth...we predict that revenue growth will remain at or above 2019 levels (that is greater than 30%) for 2021 through 2025 as companies move to save money, become more agile, and drive innovation". Deloitte references an April 2020 survey of 50 CIOs which found that "respondents expected to see the proportion of total workload done on-premise drop from 59% in 2019 to 35% in 2021...[and] they expected public cloud's proportion of total workload to grow from 23% to 38%". The benefits of cloud computing are clear to Deloitte: "cloud can support benefits including collaboration, automation, scale, innovation and agility", and Deloitte makes an argument that cloud computing is more sustainable and uses less energy than non-cloud alternatives.⁴

³ *Gartner Forecasts Worldwide Public Cloud End-User Spending to Grow 18% in 2021* (November 17, 2020 article) <https://www.gartner.com/en/newsroom/press-releases/2020-11-17-gartner-forecasts-worldwide-public-cloud-end-user-spending-to-grow-18-percent-in-2021> Accessed December 21, 2020 from www.gartner.com.

⁴ *Deloitte Insights: Technology, Media, and Telecommunications Predictions 2021* <https://www2.deloitte.com/global/en/insights/industry/technology/technology-media-and-telecom-predictions.html> Accessed February 4, 2021 from www.deloitte.com.



THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA

(Established by Act of Parliament No. 15 of 1965)

PLOT 16, IDOWU TAYLOR STREET,
VICTORIA ISLAND,
P.O BOX1580, MARINA, LAGOS, NIGERIA

Tel: 09053847510-1

Email: info.ican@ican.org.ng, rce@ican.org.ng

Website: www.icanig.org

Registrar/Chief Executive

AHMED M. KUMSHE (PROF.), FCA

February 8th, 2021.

ICAN/CP/R&T/FEB8/2020

IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD.

Dear Sir,

Re: Configuration or Customization Costs in a Cloud Computing Arrangement (IAS 38)

Please find below our comments on the above-named Tentative Agenda Decision.

Conclusion:

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for a customer to determine its accounting for configuration or customisation costs incurred in relation to the SaaS arrangement described in the request. Consequently, the Committee [decided] not to add a standard-setting project to the work plan.

Response:

We agree with the Committee's conclusion that the principle and requirements in IFRS Standards provide an adequate basis for a customer to determine its accounting for configuration or customisation costs incurred about the SaaS arrangement described in the request. We welcome the clarification provided by the committee on the accounting treatment of SaaS arrangements. SaaS arrangements are now common and the need for entities to correctly analyse the recognition and measure of such arrangements cannot be overemphasized.

We thank you for giving us the opportunity to contribute to the Agenda Decision and we are available should there be need for further clarification.

Yours faithfully,

For: Ahmed M. Kumshe (Prof.), FCA
Registrar/Chief Executive

Asset Realization in Procuring Software Services

By

Syamantak Saha

Canberra, Australia

8th February 2021

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I. Background

The digital economy has provided opportunities for businesses to conduct transactions electronically, and without the essential needs of pen and paper for critical business activities such as book-keeping of accounting transactions. With a client-server architecture, the opportunities to have a centralized database for all occurring transactions of a business, at different branches and geographic locations, on a real-time basis, has indeed cut the processing time and costs for such activities with immense business benefits.

Such benefits, that are provided to the business by digitalization, provides a source of further business improvements, in terms of efficiency, new products and services and employing better resources for the business itself. Hence, whilst a business may look forward to savings in time and costs by implementing a digital system for its business, such savings can then be better directed to upgrading existing assets, including training its existing human resources and investing in research and development that would enable the business to align better and further with the digital economy.

Hence, investment into a digital business system, is a two-way benefit, firstly, in gaining efficiency with current practices, and secondly, to incur financial benefits, that would complete the circular economy by providing an improved and aligned digital product and service for the business and its economic markets. So, as a business implements a digital business system, and incurs costs for its implementation, it can simultaneously become more innovative and invest in such digital products and services that the business may not have provided prior to such digital abilities. Otherwise, if implementing a digital solution would only entail an expense over existing status quo of business practices and the respective products and services, then the business would have no real incentive to implement such digital solutions, as it would only be an added cost without any further advantages or return on such investments.

So, a business by undertaking activities such as installing an accounting software, that maybe to a certain extent based on the internet, undertakes a step towards digitalization of its business activities, and implicitly avails further opportunities in the digital economy - whilst sourcing funds from efficiency gains in addressing previous manual methods replaced by such digital processes. Hence, a fair expectation of businesses is that the step towards digitalization is enabled by having core business accounting systems in a digital format, including being on the internet, that would then bring further financial and economic developments, including and limited to investing from such savings into new product and services development, and further activities alignment to the digital economy. Certainly, a business would hope that such efficiency gains are realized as assets at all

stages of such a transformation. Indeed, such ‘Digital Assets’ at their creation, have to be appropriately identified and accounted for, in an efficient business.

II. Business Software Services

A Business Software service is mainly employed as a core effort to digitalize existing business practices. Whilst initially, such business softwares were mainly developed in-house, where business analysts and computer programmers were employed to develop technical requirements documents and then to produce the working technology, gradually, the concept of such in-house developed software was starting to be replaced by third-party provided services.

Enterprise Resource Planning softwares were gradually developed and given the market to provide such third party services for business transactions. When a business uses any ERP solution, it indeed has to undertake certain amount of 'configuration' that may range from setting a few flags in the software through to more complex developments as in customizing the off-the-shelf software for its particular requirements, that may not be currently provided in the procured software. Customization may require developing further end-user screens and background processes that is essential for the business. As specific jurisdictions have particular requirements for certain financial accounting transactions, and that such requirements are constantly evolving due to regulations and market conditions, seldom a business who procures such an off-the-shelf ERP system, would find that the product is already compliant with its specific regulatory and business practice requirements, and needs no further modifications at all, whether be for regulatory implications or specific business practices.

When a business procures such a software, there is also a requirement for the business to understand and apply the setup and flag mechanism of the software for its particular practices. Indeed, the business has to now interact with the business software in a way that is effective and efficient with the provided software features and offerings. Also, a business may well need to change and adapt certain business practices to fit-in with the software service, as otherwise, such a business system may not be workable at all.

Hence, over time, the procured off-the-shelf business system, with its added modifications and business requirement upgrades, would often become indistinguishable from an in-house software system, that may have been developed with the business employing its own sets of analysts and computer programmers. As the software starts to 'know' the individual business practice and the business reciprocates by adopting the available features and offerings, whether the business had originally procured an off-the-shelf software or developed its own in-house asset, certainly becomes dissolved over time. Further, it is not expected that any two businesses that had implemented a business software service at the same time, would have exactly the same state of the software, after an extended use of the software for its business, due to differentiated products and services, financial elements, regulative interpretations, competition and other economic factors that would

affect the respective businesses individually, requiring such an individual customization of its core business systems.

III. Categories of SaaS

Whilst ERP Systems was a latest trend for business systems till a few years ago, today, with the advent of Internet-of-Things, the concept of a stand alone ERP System, is replaced by a connected business system with such future oriented Internet-of-Things stature.

In the concept of Internet-of-Things, all things of individuals and businesses are conceptualized to be connected to the Internet. ERP and business systems are no exceptions, and indeed, with some of the latest versions of ERP Systems, the procured system may not actually function as expected, unless it is connected to the Internet at all times. Whilst this introduces several cybersecurity risks, but that the software itself is always on the Internet and undertaking vital transactions for the business, is a choice that the business takes by adequate consideration of its operational risks.

However, the range of Software as a Service (SaaS) business software that are available to businesses are spread from buying specific ERP softwares that have limited connection to the Internet, possibly only to download critical upgrades, through to softwares that are completely resident on the Internet and requiring the business to transact all activities through the Internet. Indeed, the growing trend has been for previous ERP vendors to up-sell their software as an Internet-of-Things solution, such that it may better connect with the future customer, and require that the business have its critical business operations exposed to such opportuned risks.

So, a SaaS Service maybe correlated with its exposure requirements to the Internet and ranked on a scale of 1 to 100, where 1 may mean that it seldom requires an Internet connection to work, through to 100 where it is critical for the business system to be connected to the Internet, failing which the software would not function as required.

Internet Exposure Requirement Index

1.....100

1 : Limited or No Internet Connection Required

100 : Internet Connection Critical

Whilst a common mis-conception about SaaS is that it only categorizes softwares that are resident on the Internet and have to be accessed through a proprietary web address or Universal Resource

Locator (URL), however, that most ERP Systems are currently developed to be accessed through the Internet and have specific URLs and address locators for its services, cross-qualifies such previously developed ERP systems, as SaaS services as well.

Hence, a generic and contemporary definition of SaaS would include even such ERP systems, who have any dependency on the Internet to provide any of its functionalities. As seldom, any such ERP systems would be scarce where any connection to the Internet is not required, ERP systems would be intrinsically qualified as a SaaS software, however with a varying degree of Internet connection requirements. As implementing and keep running ERP business systems is a major expense for a company, to appropriately and adequately account for its implementation and running expenses, becomes a critical question for IFRS accounting standards, including inheriting Internet requirements by virtue of upgrading to a SaaS software for any business activity that previously did not have any such dependency for its undertaking.

IV. The Expensing Issue Raised

The particular issue raised for this project is whether and how to allocate an expense as a business transaction, when the business incurs costs to implement a SaaS solution.

Here, the condition assumption is that the business is procuring an off-the-shelf product, that is already ready and catered for its particular business, and only needs to set a few flags to get the software setup and working for its business requirements. The condition explained raises the concern of how a business should allocate the expense as any asset acquired, if the associated functionality is only to configure the already available and working software for its own business purposes.

Indeed, for this issue, the particular expense-asset ratio would depend on the degree to which the procured software requires Internet Connection for its to function and continue to provide its core functionalities for business. Also, a reliable asset can be established if the asset meets the particular and specific market requirements for the business, without any further customization requirements at all.

So, the expense could be credited as an Asset, depending on the ratio of combination of the two factors :

- a. Intensity of Internet Connection Requirement
- b. Amount of Further Customization Required

Indeed, if a SaaS is completely on the Internet and a business easily implements its business on this software with some minor setting of flags etc., then the business system asset is more a creation of the SaaS provider, however, if the software requires very limited Internet connection for updates and fixes, and the business requires heavy and significant customization for the software to work with its existing requirements, the procured software would thereby, be a better creation of the business than otherwise. By benefit of more significant creation for the software to work for a particular business, the asset in question, would get the appropriate ownership, dependent on such conditions, that produced its incurrence, namely the two conditions a and b as stated above.

So, it can be defined that:

Asset Ownership Ratio = fn (Intensity of Internet Requirement, Customization Requirement)

where fn represents a function of the two variable. When fn is 1, the summed average of the two variables,

$$\text{Asset Ownership by Business} = (\text{Intensity} + \text{Customization})/2$$

For example,

With $fn = 1$

If Intensity = 80%

and Customization = 50%

Asset Ownership by Business = 65%

Asset Ownership by SaaS Vendor = 35%

Where,

$$\text{Intensity} = (100 - \text{Internet Connection Requirements of Software})$$

Certainly, a more appropriate value of fn can be allocated by regulation, or by individual businesses as may be required by its current accounting practices of procuring similar assets for business operations.

Indeed, fn maybe determined by certain regulations, that mandate the ability of the Internet connection to be a realistic value, as maybe in certain developing economies with under-developed telecommunication infrastructure, or other economic conditioning, such as Cybersecurity risks inherited by business that has such an Internet dependency for its core business functionalities, or even to the extent that some Reserve Bank policies of economic management requires such a check and balance of Asset erosion by any act of well-intended digitalization by businesses. Such regulated value of fn could then be used by all businesses within an economy, having a uniform

derivation for assets that are created in the act of developing the digital economy, and where such asset misplacements or erosions, are adequately addressed by regulative policy.

fn could also be determined by a particular business, set to a certain value, that best suits its business, depending on the particular business characteristics. Such business determination would also have reciprocal implications for regulative reporting, including asset depreciation value, asset churn ratios and associated taxation implications for such specific business. So, when a business determines its own value of ***fn***, it would certainly best represent its business condition in the digital economy, considering all aspects of regulations, customers and markets.

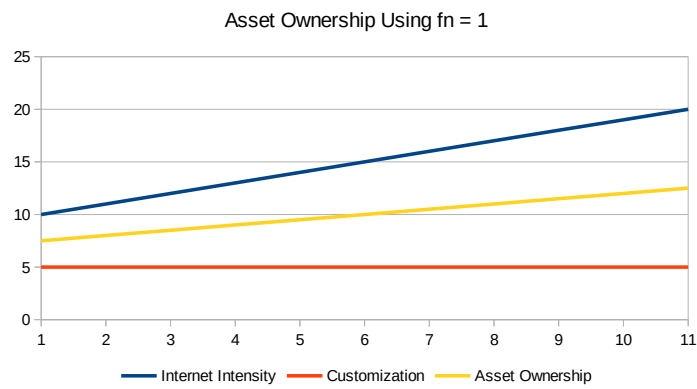


Figure 1 : Business Asset Ownership Dependent on Internet Requirements

V. Operational Risks

The operational risk for such procured Assets increases in the developing landscape of procured business systems services from third party vendors, as under such conditions, most, if not all ERP and similar software vendors would require constant and critical connection to the Internet for its system to work as required. Indeed, some latest data solutions require constant connections such that it updates certain internal databases etc., that is projected to benefit the customer, however, at the cost of reducing ability for the business to realize this expense as its own created asset, due to such constant Internet dependencies. Whilst the connection to the Internet maybe required by the SaaS/ERP software as a method to update its own technology, that the technology being pushed via the Internet is being executed to all businesses who are using this software, concurrently reduces the point-of-creation for the business and moves it towards the software vendor, as by virtue of such unanimous market operations, that may well be quite insignificant to the business user, the vendor establishes a certain 'Common Control' over the business, reducing it ability to realize such an Asset on such implicitly agreed conditions of dependencies.

The SaaS/ERP vendor may well into the future, put such mechanisms in place that prevents any further ability to customize the software for particular business. In this case, any regulative changes that impacts the business and may require customization would remain un-fulfilled, or awaiting vendor interpretations and associated implementation, creating a further liability condition for the business, as the business develops an limited ability to interpret regulation and becomes dependent on the SaaS service provider to provide such business abilities. This becomes an issue when the provider is based in a different country, as the economic risk for each business and the collective set of businesses in the economy, becomes subjected to such foreign interpretation of developing regulations, that may not be in the best interest of the business or the economy as a whole.

Indeed, if a foreign owned SaaS software provider benefits the interpretation of subjected regulations, the provider brings enormous and exponential advantages for its own financial markets as opposed to that of the particular business, as the regulative implications of such a target business economy, becomes of reduced risk for the economy of the software provider, having an impact on insurance and other cross-market costs for the foreign operator in the particular regulated economy.

In the Internet-of-Things environment, there is a constant competition between the vendor and the business user to have asset ownership, not only for the financial benefit of owning the asset, but with further implications for regular business operations, that may well be intended to be directed by the vendor for such reasons, as opposed to the management preferences of the company in a particular economy.

VI. Recommendations

Connected business systems is indeed a way for the future, but that it could be inappropriately used by third party vendors for financial benefits, remains a business risk for companies who want to adopt such SaaS/ERP systems. The condition, that once-bought-always-liable is not sustainable as a standard accounting practice, including initially on how to expense and create a fair asset for such costs that are undertaken by the company for such technology upgrades. Fair Asset Creation is currently not defined by any such Accounting Practices for expensing the incurred costs of digitalization of business practices using such SaaS services, creating an opportunity for such financial market mis-functioning and inefficiency.

VI-a. Fair Asset Creation Standard

It is recommended that IFRS provide a standard for Fair Asset Creation, owing to the miscalculations and misunderstandings that maybe generated from readers of financial information, who may perceive a difference in the reading of such expenses between different entities in the same or global market. A reader would indeed benefit, if there is a standard method introduced for such accounting expenses, as a realizable asset, as currently, and without any such standards, different entities would report differently on such expenses, creating a mis-match for such a developing digital economy.

The method could use the value of ***fn*** in conjunction with Intensity and Customization, as described earlier. The fair value of ***fn*** could be an undertaking of the particular market regulator, who may further delegate certain such values to particular businesses, depending on their circumstances.

Expense Incurred = \$100

fn = 1

Intensity = 80%

Customization = 50%

Fair Asset Created = 65% of \$100

= \$65

Accordingly, in the Balance Sheet Statement :

Without Fair Asset Creation

	<u>31/12/2021</u>	<u>31/12/2020</u>
Non-current Assets		
<i>Property, Plant and Equip</i>	1200	1500
Current Assets		
<i>Inventories</i>	1500	1800

With Fair Asset Creation*

	<u>31/12/2021</u>	<u>31/12/2020</u>
Non-current Assets		
<i>Property, Plant and Equip</i>	1265	1500
Current Assets		
<i>Inventories</i>	1500	1800

* Applying modified IFRS Standard xxx in Procuring SaaS Services

VII. Summary

It is important for the digital economy to have a clear and concise method to account for services that are procured or used online through the Internet. Without such a standardisation, there is considerable financial risk for developing digital economies, as well as for the readers of financial statements to obtain the most useful information about the company from such statements, especially in an environment where there is an increasing adoption of digital technologies. However, often, there may be a required clarity on issues such as Intellectual Property that may be used for using such digital technologies.

Whilst SaaS/ERP vendors would capitalize their balance sheet on selling softwares based in their proprietary IP, businesses who adopt such vendors software would also claim on such expensed resources as procuring a certain asset for the company, leading to a combined practice of inflationary accounting. This exchange of IP and associated technology, certainly requires further clarity as to the acceptable measures and market standards that maybe expected and applied both by the business as well as the vendor, in the best interest of a reliable digital economy with associated accounting standards at all required stages.

By having a set standard for asset creation during procurement of a SaaS service, both business as well as the vendor would have a fair opportunity to realize the Asset in fair value use respectively, creating a better defined and level playing field for both parties, who indeed should work in conjunction for a successful developing digital economy, and without added risks of IP theft, inflationary accounting, and risks of financial fraud due to asset misplacements. Irrespective of the vendor, the underlying digital technologies should not be deprived of the best available solutions for business due to such introduced risks to the digital economy, that would be better addressed through a standardised accounting method.