

1 **Q. Further to the response to PUB-NP-017, explain why the 2019 and 2020 costs**
2 **associated with the Customer Service System replacement are included as operating**
3 **costs and are not capitalized.**
4

5 A. Costs in 2019 and 2020 associated with replacing the Customer Service System (“CSS”)
6 are classified as operating costs in accordance with Newfoundland Power’s adherence to
7 accounting principles generally accepted in the United States (“US GAAP”).¹
8

9 US GAAP is established by the Financial Accounting Standards Board (“FASB”). The
10 FASB Accounting Standards Codification provides guidance on the recognition of
11 software costs.² Specifically, it states that costs incurred during the “preliminary project
12 stage” shall be expensed as they are incurred, while costs associated with the “application
13 development stage” shall be capitalized. Attachment A to this response provides the
14 relevant section of the FASB Accounting Standards Codification Manual.³
15

16 Forecast costs related to replacing Newfoundland Power’s CSS follow this guidance. In
17 2019 and 2020, the Company is completing the necessary assessment and planning work
18 to facilitate system replacement. This work aligns with the definition of the preliminary
19 project stage according to US GAAP. Costs related to this assessment and planning work
20 will be expensed as they are incurred. Once the project shifts to the application
21 development stage, costs will be capitalized.⁴
22

23 For more information on the stages of the CSS replacement project, see response to
24 Request for Information PUB-NP-008, Attachment A, pages 11-12.

¹ Newfoundland Power’s financial statements are prepared in accordance with US GAAP.

² The FASB Accounting Standards Codification (“ASC”), Section 350 Intangibles – Goodwill and Other > 40 Internal Use Software > 25 Recognition (ASC 350-40-25) establishes the accounting guidelines for the recognition of software project costs.

³ This information was accessed through the Deloitte Accounting Research Tool (“DART”). The definition of the preliminary project stage is provided on page 7 of Attachment A. The recognition of costs, as operating or capital costs, during the preliminary project stage and the application development stage is provided on page 9 of Attachment A. Further descriptions of the preliminary project stage and application development stage are provided on pages 18-19 of Attachment A.

⁴ Guidance on the timing of the capitalization of costs relating to an internal-use software project are described on page 11 of Attachment A. Newfoundland Power anticipates capitalizing costs related to the replacement of its CSS following the Board’s approval of the Company’s *2021 Capital Budget Application*.

FASB Accounting Standards Codification Manual
350-40 Internal Use Software

350-40 Internal-Use Software

350-40 Internal-Use Software

00 Status

General Note

The Status Section identifies changes to this Subtopic resulting from Accounting Standards Updates. The Section provides references to the affected Codification content and links to the related Accounting Standards Updates. Nonsubstantive changes for items such as editorial, link and similar corrections are included separately in Maintenance Updates.

General

00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
<u>Contract</u>	Added	Accounting Standards Update No. 2014-09	05/28/2014
<u>Customer</u>	Added	Accounting Standards Update No. 2014-09	05/28/2014
<u>Hosting Arrangement</u>	Added	Accounting Standards Update No. 2015-05	04/15/2015
<u>Public Business Entity</u>	Amended	Maintenance Update 2017-06	04/07/2017
<u>Public Business Entity</u>	Amended	Maintenance Update 2016-11	06/27/2016
<u>Public Business Entity</u>	Added	Accounting Standards Update No. 2015-05	04/15/2015
<u>Revenue</u>	Added	Accounting Standards Update No. 2014-09	05/28/2014
350-40-05-1	Amended	Accounting Standards Update No. 2017-04	01/26/2017
350-40-05-1A	Added	Accounting Standards Update No. 2017-04	01/26/2017
350-40-05-1B	Added	Accounting Standards Update No. 2017-04	01/26/2017
350-40-05-2 through 05-5	Superseded	Accounting Standards Update No. 2017-04	01/26/2017
350-40-05-8	Superseded	Accounting Standards Update No. 2017-04	01/26/2017
350-40-05-9	Superseded	Accounting Standards Update No. 2017-04	01/26/2017

350-40-15-2A through 15-2C	Added	Accounting Standards Update No. 2017-04	01/26/2017
350-40-15-4	Amended	Accounting Standards Update No. 2015-05	04/15/2015
350-40-15-4A through 15-4C	Added	Accounting Standards Update No. 2015-05	04/15/2015
350-40-15-5	Amended	Accounting Standards Update No. 2017-04	01/26/2017
350-40-25-5	Amended	Accounting Standards Update No. 2017-04	01/26/2017
350-40-25-7	Amended	Accounting Standards Update No. 2017-04	01/26/2017
350-40-25-16	Superseded	Accounting Standards Update No. 2015-05	04/15/2015
350-40-25-17	Added	Accounting Standards Update No. 2016-19	12/14/2016
350-40-35-8	Amended	Accounting Standards Update No. 2014-09	05/28/2014
350-40-65-1	Added	Accounting Standards Update No. 2015-05	04/15/2015
350-40-65-2	Added	Accounting Standards Update No. 2016-19	12/14/2016

05 Background

General Note

The Overview and Background Section provides overview and background material for the guidance contained in the Subtopic. It does not provide the historical background or due process. It may contain certain material that users generally consider useful to understand the typical situations addressed by the standards. The Section does not summarize the accounting and reporting requirements.

General

05-1 This Subtopic provides guidance on accounting for the cost of computer software developed or obtained for internal use and for determining whether the software is for internal use. Certain costs incurred for computer software developed or obtained for internal use should be capitalized depending on the nature of the costs and the project stage during which they were incurred in accordance with the guidance in Section 350-40-25. Computer software to be sold, leased, or otherwise marketed externally is not considered to be for internal use.

05-1A Section 350-40-30 includes guidance on the types of costs that should be capitalized, including costs for the purchase of internal-use software in a multiple element transaction.

05-1B Section 350-40-35 includes guidance on the following:

- a How to test the internal-use software for impairment
- b How to amortize the asset

- c How to account for software that previously was considered for internal use, but subsequently was marketed.
-

05-2 Paragraph superseded by Accounting Standards Update No. 2017-04

05-3 Paragraph superseded by Accounting Standards Update No. 2017-04

05-4 Paragraph superseded by Accounting Standards Update No. 2017-04

05-5 Paragraph superseded by Accounting Standards Update No. 2017-04

05-6 Paragraphs 350-40-55-1 through 55-2 provide examples of when computer software is and is not for internal use.

05-7 Paragraph 350-40-55-3 illustrates the various stages and related processes of computer software development.

05-8 Paragraph superseded by Accounting Standards Update No. 2017-04

05-9 Paragraph superseded by Accounting Standards Update No. 2017-04

15 Scope

General Note

The Scope and Scope Exceptions Section outlines the items (for example, the entities, transactions, instruments, or events) to which the guidance in the Subtopic does or does not apply. In some cases, the Section may contain definitional or other text to frame the scope.

General

Overall Guidance

15-1 This Subtopic follows the same Scope and Scope Exceptions as outlined in the Overall Subtopic, see Section 350-10-15, with specific transaction qualifications and exceptions noted below.

Transactions

15-2 The guidance in this Subtopic applies to the following transactions and activities:

- a Internal-use software
- b The proceeds of computer software developed or obtained for internal use that is marketed
- c New internal-use software developed or obtained that replaces previously existing internal-use software
- d Computer software that consists of more than one component or module. For example, an entity may develop an accounting software system containing three elements: a general ledger, an accounts payable subledger, and an accounts receivable subledger. In this example, each element might be viewed as a component or module of the entire accounting software system. The guidance in this Subtopic shall be applied to individual components or modules.

Deloitte Guidance and Illustrations

Internal-Use Software Consisting of Various Modules — 350-40-15 (Q&A 01)

15-2A Internal-use software has both of the following characteristics:

- a The software is acquired, internally developed, or modified solely to meet the entity's internal needs.
- b During the software's development or modification, no substantive plan exists or is being developed to market the software externally.

Deloitte Guidance and Illustrations

Characteristics of Internal-Use Computer Software — 350-40-15 (Q&A 04)

15-2B A substantive plan to market software externally could include the selection of a marketing channel or channels with identified promotional, delivery, billing, and support activities. To be considered a substantive plan, implementation of the plan should be reasonably possible. Arrangements providing for the joint development of software for mutual internal use (for example, cost-sharing arrangements) and routine market feasibility studies are not substantive plans to market software for purposes of this Subtopic. Both characteristics in paragraph 350-40-15-2A must be met for software to be considered for internal use.

15-2C An entity's past practices related to selling software may help determine whether the software is for internal use or is subject to a plan to be marketed externally. For example, an entity in the business of selling computer software often both uses and sells its own software products. Such a past practice of both using and selling computer software creates a rebuttable presumption that any software developed by that entity is intended for sale, lease, or other marketing.

15-3 This Subtopic provides guidance on when costs incurred for internal-use computer software are and are not capitalized.

- 15-4 The guidance in this Subtopic does not apply to the following transactions and activities:
- a Software to be sold, leased, or otherwise marketed as a separate product or as part of a product or process, subject to Subtopic 985-20
 - b Software to be used in research and development, subject to Subtopic 730-10
 - c Software developed for others under a contractual arrangement, subject to contract accounting standards
 - d Accounting for costs of reengineering activities, which often are associated with new or upgraded software applications.
 - e Software that a customer obtains access to in a hosting arrangement that does not meet the criteria in paragraph 350-40-15-4A.
-

15-4A The guidance in this Subtopic applies only to internal-use software that a customer obtains access to in a hosting arrangement if both of the following criteria are met:

- a The customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty.
 - b 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.
-

15-4B For purposes of the guidance in paragraph 350-40-15-4A(a), the term *without significant penalty* contains two distinct concepts:

- a The ability to take delivery of the software without incurring significant cost
 - b The ability to use the software separately without a significant diminution in utility or value.
-

15-4C Hosting arrangements that do not meet both criteria in paragraph 350-40-15-4A are service contracts and do not constitute a purchase of, or convey a license to, software.

15-5 Costs of computer software that is sold, leased, or otherwise marketed as a separate product or as part of a product or process are within the scope of Subtopic 985-20. For example, software designed for and embedded in a semiconductor chip is included in the scope of that Subtopic because it is an integral part of the product. By contrast, software for internal use, though it may be used in developing a product, is not part of or included in the actual product or service sold. If software is used by the vendor in the production of the product or providing the service but the customer does not acquire the software or the future right to use it, the software is covered by this Subtopic. For example, for a communications entity selling telephone services, software included in a telephone switch is part of the internal equipment used to deliver a service but is not part of the product or service actually being acquired or received by the customer. Paragraph 350-40-55-1 includes examples of computer software considered to be for internal use and thus not part of a product or process. Paragraph 350-40-55-2 includes examples of when computer software is not for internal use.

Other Considerations

15-6 The guidance in this Subtopic does not change any of the provisions in the following Subtopics:

- a Subtopic 985-20
- b Subtopic 720-45.

15-7 The following costs of internal-use computer software are included in research and development and shall be accounted for in accordance with the provisions of Subtopic 730-10:

- a Purchased or leased computer software used in research and development activities where the software does not have alternative future uses
- b All internally developed internal-use computer software (including software developed by third parties, for example, programmer consultants) in either of the following circumstances:
 - 1 The software is a pilot project (that is, software of a nature similar to a pilot plant as noted in paragraph 730-10-55-1(h)).
 - 2 The software is used in a particular research and development project, regardless of whether the software has alternative future uses.

Deloitte Guidance and Illustrations

Research and Development Costs — 350-40-15 (Q&A 02)

Research and Development Costs — 350-40-15 (Q&A 03)

Research and Development Costs of Computer Software — 985-20-25 (Q&A 01)

Research and Development Costs — ASC 730-10

20 Glossary

General Note

The Master Glossary contains all terms identified as glossary terms throughout the Codification. Clicking on any term in the Master Glossary will display where the term is used. The Master Glossary may contain identical terms with different definitions, some of which may not be appropriate for a particular Subtopic. For any particular Subtopic, users should only use the glossary terms included in the particular Subtopic Glossary Section (Section 20).

Contract

Note: The following definition is Pending Content; see Transition Guidance in 606-10-65-1

An agreement between two or more parties that creates enforceable rights and obligations.

Customer

A user or reseller.

Note: The following definition is Pending Content; see Transition Guidance in 606-10-65-1.

A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.

Hosting Arrangement

In connection with the licensing of software products, an arrangement in which an end user of the software does not take possession of the software; rather, the software application resides on the vendor's or a third party's hardware, and the customer accesses and uses the software on an as-needed basis over the Internet or via a dedicated line.

Not-for-Profit Entity

An entity that possesses the following characteristics, in varying degrees, that distinguish it from a business entity:

- a Contributions of significant amounts of resources from resource providers who do not expect commensurate or proportionate pecuniary return
- b Operating purposes other than to provide goods or services at a profit
- c Absence of ownership interests like those of business entities.

Entities that clearly fall outside this definition include the following:

- a All investor-owned entities
- b Entities that provide dividends, lower costs, or other economic benefits directly and proportionately to their owners, members, or participants, such as mutual insurance entities, credit unions, farm and rural electric cooperatives, and employee benefit plans.

Preliminary Project Stage

When a computer software project is in the preliminary project stage, entities will likely do the following:

- a Make strategic decisions to allocate resources between alternative projects at a given point in time. For example, should programmers develop a new payroll system or direct their efforts toward correcting existing problems in an operating payroll system?
- b Determine the performance requirements (that is, what it is that they need the software to do) and systems requirements for the computer software project it has proposed to undertake.
- c Invite vendors to perform demonstrations of how their software will fulfill an entity's needs.
- d Explore alternative means of achieving specified performance requirements. For example, should an entity make or buy the software? Should the software run on a mainframe or a client server system?
- e Determine that the technology needed to achieve performance requirements exists.
- f Select a vendor if an entity chooses to obtain software.
- g Select a consultant to assist in the development or installation of the software.

Public Business Entity

A public business entity is a business entity meeting any one of the criteria below. Neither a not-for-profit entity nor an employee benefit plan is a business entity.

- a It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
- b It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.
- c It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.
- d It has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.
- e It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

Revenue

Revenue earned by an entity from its direct distribution, exploitation, or licensing of a film, before deduction for any of the entity's direct costs of distribution. For markets and territories in which an entity's fully or jointly-owned films are distributed by third parties, revenue is the net amounts payable to the entity by third party distributors. Revenue is reduced by appropriate allowances, estimated returns, price concessions, or similar adjustments, as applicable.

Note: The following definition is Pending Content; see Transition Guidance in 606-10-65-1.

Inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

Useful Life

The period over which an asset is expected to contribute directly or indirectly to future cash flows.

25 Recognition

General Note

The Recognition Section provides guidance on the required criteria, timing, and location (within the financial statements) for recording a particular item in the financial statements. Disclosure is not recognition.

General

Preliminary Project Stage

25-1 Internal and external costs incurred during the preliminary project stage shall be expensed as they are incurred.

Deloitte Guidance and Illustrations
Availability of Technology — 350-40-25 (Q&A 01)
Design of Chosen Path — 350-40-25 (Q&A 02)
Preliminary Project Stage — 350-40-25 (Q&A 03)
Enterprise Resource Planning (ERP) Implementations — 350-40-25 (Q&A 16)
Enterprise Resource Planning (ERP) Implementations — 350-40-25 (Q&A 17)

Application Development Stage

25-2 Internal and external costs incurred to develop internal-use computer software during the application development stage shall be capitalized.

25-3 Costs to develop or obtain software that allows for access to or conversion of old data by new systems shall also be capitalized.

Deloitte Guidance and Illustrations
Conversion Costs — 350-40-25 (Q&A 04)

25-4 Training costs are not internal-use software development costs and, if incurred during this stage, shall be expensed as incurred.

Deloitte Guidance and Illustrations
Training Costs — 350-40-25 (Q&A 08)

25-5 Data conversion costs, except as noted in paragraph 350-40-25-3, shall be expensed as incurred. The process of data conversion from old to new systems may include purging or cleansing of existing data, reconciliation or balancing of the old data and the data in the new system, creation of new or additional data, and conversion of old data to the new system.

Deloitte Guidance and Illustrations

Conversion Costs — 350-40-25 (Q&A 05)

Conversion Costs — 350-40-25 (Q&A 06)

Software Used in a “Help Desk” or Maintenance Support System — 350-40-25 (Q&A 07)

Postimplementation-Operation Stage

25-6 Internal and external training costs and maintenance costs during the postimplementation-operation stage shall be expensed as incurred.

Upgrades and Enhancements

25-7 Upgrades and enhancements are defined as modifications to existing internal-use software that result in additional functionality—that is, modifications to enable the software to perform tasks that it was previously incapable of performing. Upgrades and enhancements normally require new software specifications and may also require a change to all or part of the existing software specifications. In order for costs of specified upgrades and enhancements to internal-use computer software to be capitalized in accordance with paragraphs 350-40-25-8 through 25-10, it must be probable that those expenditures will result in additional functionality.

25-8 Internal costs incurred for upgrades and enhancements shall be expensed or capitalized in accordance with paragraphs 350-40-25-1 through 25-6.

25-9 Internal costs incurred for maintenance shall be expensed as incurred.

25-10 Entities that cannot separate internal costs on a reasonably cost-effective basis between maintenance and relatively minor upgrades and enhancements shall expense such costs as incurred.

25-11 External costs incurred under agreements related to specified upgrades and enhancements shall be expensed or capitalized in accordance with paragraphs 350-40-25-1 through 25-6. If maintenance is combined with specified upgrades and enhancements in a single contract, the cost shall be allocated between the elements as discussed in paragraph 350-40-30-4 and the maintenance costs shall be expensed over the contract period. However, external costs related to maintenance, unspecified upgrades and enhancements, and costs under agreements that combine the costs of maintenance and unspecified upgrades and enhancements shall be recognized in expense over the contract period on a straight-line basis unless another systematic and rational basis is more representative of the services received.

Deloitte Guidance and Illustrations

Maintenance Costs — 350-40-25 (Q&A 09)

Specified Upgrades — 350-40-25 (Q&A 10)

Specified Upgrades — 350-40-25 (Q&A 11)

Unspecified Upgrades — 350-40-25 (Q&A 12)

Capitalization of Cost

25-12 Capitalization of costs shall begin when both of the following occur:

- a Preliminary project stage is completed.
- b Management, with the relevant authority, implicitly or explicitly authorizes and commits to funding a computer software project and it is probable that the project will be completed and the software will be used to perform the function intended.

Examples of authorization include the execution of a contract with a third party to develop the software, approval of expenditures related to internal development, or a commitment to obtain the software from a third party.

Deloitte Guidance and Illustrations

Management With the Relevant Authority — 350-40-25 (Q&A 13)

When It Is No Longer Probable That the Computer Software Project Will Be Completed and Placed in Service — 350-40-25 (Q&A 14)

25-13 When it is no longer probable that the computer software project will be completed and placed in service, no further costs shall be capitalized, and guidance in paragraphs 350-40-35-1 through 35-3 on impairment shall be applied to existing balances.

25-14 Capitalization shall cease no later than the point at which a computer software project is substantially complete and ready for its intended use, that is, after all substantial testing is completed.

25-15 New software development activities shall trigger consideration of remaining useful lives of software that is to be replaced. When an entity replaces existing software with new software, unamortized costs of the old software shall be expensed when the new software is ready for its intended use.

25-16 Paragraph superseded by Accounting Standards Update No. 2015-05

Deloitte Guidance and Illustrations

Licensing Software From Third Parties — 350-40-25 (Q&A 15)

25-17

Pending content

Transition date: (P) December 16, 2016; (N) December 16, 2017 | **Transition Guidance:** 350-40-65-2

Entities often license internal-use software from third parties. A software license within the scope of this Subtopic (see paragraphs 350-40-15-1 through 15-4C) shall be accounted for as the acquisition of an intangible asset and the incurrence of a liability (that is, to the extent that all or a portion of the software licensing fees are not paid on or before the acquisition date of the license) by the licensee. The intangible asset acquired shall be recognized and measured in accordance with paragraphs 350-30-25-1 and 350-30-30-1, respectively.

30 Initial Measurement

General Note

The Initial Measurement Section provides guidance on the criteria and amounts used to measure a particular item at the date of initial recognition.

General

Capitalizable Cost

30-1 Costs of computer software developed or obtained for internal use that shall be capitalized include only the following:

- a External direct costs of materials and services consumed in developing or obtaining internal-use computer software. Examples of those costs include but are not limited to the following:
 - 1 Fees paid to third parties for services provided to develop the software during the application development stage
 - 2 Costs incurred to obtain computer software from third parties
 - 3 Travel expenses incurred by employees in their duties directly associated with developing software.
- b Payroll and payroll-related costs (for example, costs of employee benefits) for employees who are directly associated with and who devote time to the internal-use computer software project, to the extent of the time spent directly on the project. Examples of employee activities include but are not limited to coding and testing during the application development stage.
- c Interest costs incurred while developing internal-use computer software. Interest shall be capitalized in accordance with the provisions of Subtopic 835-20.

Deloitte Guidance and Illustrations

External Direct Costs of Materials and Services Consumed — 350-40-30 (Q&A 01)

Payroll and Payroll-Related Costs — 350-40-30 (Q&A 02)

Payroll and Payroll-Related Costs — 350-40-30 (Q&A 03)
--

Stock-Based Compensation Costs — 350-40-30 (Q&A 04)

Overhead Costs — 350-40-30 (Q&A 05)

30-2 If the entity suspends substantially all activities related to the software developed or obtained for internal use, interest capitalization shall cease until activities are resumed.

30-3 General and administrative costs and overhead costs shall not be capitalized as costs of internal-use software.

Multiple-Element Arrangements Included in Purchase Price

30-4 Entities may purchase internal-use computer software from a third party. In some cases, the purchase price includes multiple elements, such as training for the software, maintenance fees for routine maintenance work to be performed by the third party, data conversion costs, reengineering costs, and rights to future upgrades and enhancements. Entities shall allocate the cost among all individual elements. The allocation shall be based on objective evidence of fair value of the elements in the contract, not necessarily separate prices stated within the contract for each element. Those elements included in the scope of this Subtopic shall be accounted for in accordance with the provisions of this Subtopic.

Deloitte Guidance and Illustrations

Evidence of Fair Value — 350-40-30 (Q&A 06)

Leasing Hardware and Software — 350-40-30 (Q&A 07)
--

Business Process Reengineering (BPR) — 350-40-30 (Q&A 08)

Enterprise Resource Planning (ERP) Implementations — 350-40-25 (Q&A 16)

Enterprise Resource Planning (ERP) Implementations — 350-40-25 (Q&A 17)

35 Subsequent Measurement

General Note

The Subsequent Measurement Section provides guidance on an entity's subsequent measurement and subsequent recognition of an item. Situations that may result in subsequent changes to carrying amount include impairment, credit losses, fair value adjustments, depreciation and amortization, and so forth.

General

Impairment

35-1 Impairment shall be recognized and measured in accordance with the provisions of Section 360-10-35, which requires that assets be grouped at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. The guidance is applicable, for example, when one of the following events or changes in circumstances occurs related to computer software being developed or currently in use indicating that the carrying amount may not be recoverable:

- a Internal-use computer software is not expected to provide substantive service potential.
- b A significant change occurs in the extent or manner in which the software is used or is expected to be used.
- c A significant change is made or will be made to the software program.
- d Costs of developing or modifying internal-use computer software significantly exceed the amount originally expected to develop or modify the software.

35-2 Paragraphs 360-10-35-47 through 35-49 requires that the asset be accounted for as abandoned when it ceases to be used.

Deloitte Guidance and Illustrations

Abandonment of Internal-Use Software — 350-40-35 (Q&A 02)

35-3 When it is no longer probable that computer software being developed will be completed and placed in service, the asset shall be reported at the lower of the carrying amount or fair value, if any, less costs to sell. The rebuttable presumption is that such uncompleted software has a fair value of zero. Indications that the software may no longer be expected to be completed and placed in service include the following:

- a A lack of expenditures budgeted or incurred for the project.
- b Programming difficulties that cannot be resolved on a timely basis.
- c Significant cost overruns.
- d Information has been obtained indicating that the costs of internally developed software will significantly exceed the cost of comparable third-party software or software products, so that management intends to obtain the third-party software or software products instead of completing the internally developed software.
- e Technologies are introduced in the marketplace, so that management intends to obtain the third-party software or software products instead of completing the internally developed software.
- f Business segment or unit to which the software relates is unprofitable or has been or will be discontinued.

Deloitte Guidance and Illustrations

When It Is No Longer Probable That Computer Software Being Developed Will Be Completed and Placed Into Service — 350-40-35 (Q&A 01)

Sale of Uncompleted Software — 350-40-35 (Q&A 03)

Amortization

35-4 The costs of computer software developed or obtained for internal use shall be amortized on a straight-line basis unless another systematic and rational basis is more representative of the software's use.

35-5 In determining and periodically reassessing the estimated useful life over which the costs incurred for internal-use computer software will be amortized, entities shall consider the effects of all of the following:

- a Obsolescence
- b Technology
- c Competition
- d Other economic factors
- e Rapid changes that may be occurring in the development of software products, software operating systems, or computer hardware and whether management intends to replace any technologically inferior software or hardware.

Given the history of rapid changes in technology, software often has had a relatively short useful life.

35-6 For each module or component of a software project, amortization shall begin when the computer software is ready for its intended use, regardless of whether the software will be placed in service in planned stages that may extend beyond a reporting period. For purposes of this Subtopic, computer software is ready for its intended use after all substantial testing is completed. If the functionality of a module is entirely dependent on the completion of other modules, amortization of that module shall begin when both that module and the other modules upon which it is functionally dependent are ready for their intended use.

Internal-Use Computer Software Subsequently Marketed

35-7 If, after the development of internal-use software is completed, an entity decides to market the software, proceeds received from the license of the computer software, net of direct incremental costs of marketing, such as commissions, software reproduction costs, warranty and service obligations, and installation costs, shall be applied against the carrying amount of that software.

Deloitte Guidance and Illustrations

Internal-Use Computer Software Marketed — 350-40-35 (Q&A 04)

Internal-Use Computer Software Marketed — 350-40-35 (Q&A 05)

Reassessment of Policies for Accounting for Software Costs — 985-20-15 (Q&A 09)

35-8 No profit shall be recognized until aggregate net proceeds from licenses and amortization have reduced the carrying amount of the software to zero. Subsequent proceeds shall be recognized in revenue as earned.

Pending content

Transition date: (P) December 16, 2017; (N) December 16, 2018 | **Transition Guidance:** 606-10-65-1

No profit shall be recognized until aggregate net proceeds from licenses and amortization have reduced the carrying amount of the software to zero. Subsequent proceeds shall be recognized as revenue in accordance with Topic 606 on revenue from contracts with customers or recognized as a gain in accordance with Subtopic 610-20 on derecognition of nonfinancial assets if the contract is not with a customer.

35-9 If, during the development of internal-use software, an entity decides to market the software to others, the entity shall follow the guidance in Subtopic 985-20. Amounts previously capitalized under this Subtopic shall be evaluated at each balance sheet date in accordance with paragraph 985-20-35-4. Capitalized software costs shall be amortized in accordance with paragraphs 985-20-35-1 through 35-2.

Deloitte Guidance and Illustrations

Factors to Consider in Assessing Net Realizable Value — 985-20-35 (Q&A 10)

Treatment of Installation Revenue in Assessing Net Realizable Value — 985-20-35 (Q&A 11)

Treatment of Maintenance Revenue in Assessing Net Realizable Value — 985-20-35 (Q&A 12)

Maintenance and Customer Support Required to Satisfy the Enterprise's Responsibility Set Forth at the Time of Sale — 985-20-35 (Q&A 13)

35-10 A pattern of deciding to market internal-use software during its development creates a rebuttable presumption that any software developed by that entity is intended for sale, lease, or other marketing, and thus is subject to the guidance in Subtopic 985-20.

50 Disclosure

General Note

The Disclosure Section provides guidance regarding the disclosure in the notes to financial statements. In some cases, disclosure may relate to disclosure on the face of the financial statements.

General

50-1 This Subtopic does not require any new disclosures. Disclosure shall be made in accordance with existing authoritative literature including the following:

- a Topic 275
- b Subtopic 730-10
- c Topic 235

d Subtopic 360-10.

Deloitte Guidance and Illustrations

Balance Sheet Classification — 350-40-50 (Q&A 01)

55 Implementation

General Note

The Implementation Guidance and Illustrations Section contains implementation guidance and illustrations that are an integral part of the Subtopic. The implementation guidance and illustrations do not address all possible variations. Users must consider carefully the actual facts and circumstances in relation to the requirements of the Subtopic.

General

Implementation Guidance

- 55-1 The following is a list of examples illustrating when computer software is for internal use:
- a A manufacturing entity purchases robots and customizes the software that the robots use to function. The robots are used in a manufacturing process that results in finished goods.
 - b An entity develops software that helps it improve its cash management, which may allow the entity to earn more revenue.
 - c An entity purchases or develops software to process payroll, accounts payable, and accounts receivable.
 - d An entity purchases software related to the installation of an online system used to keep membership data.
 - e A travel agency purchases a software system to price vacation packages and obtain airfares.
 - f A bank develops software that allows a customer to withdraw cash, inquire about balances, make loan payments, and execute wire transfers.
 - g A mortgage loan servicing entity develops or purchases computer software to enhance the speed of services provided to customers.
 - h A telecommunications entity develops software to run its switches that are necessary for various telephone services such as voice mail and call forwarding.
 - i An entity is in the process of developing an accounts receivable system. The software specifications meet the entity's internal needs and the entity did not have a marketing plan before or during the development of the software. In addition, the entity has not sold any of its internal-use software in the past. Two years after completion of the project, the entity decided to market the product to recoup some or all of its costs.
 - j A broker-dealer entity develops a software database and charges for financial information distributed through the database.

- k An entity develops software to be used to create components of music videos (for example, the software used to blend and change the faces of models in music videos). The entity then sells the final music videos, which do not contain the software, to another entity.
 - l An entity purchases software to computerize a manual catalog and then sells the manual catalog to the public.
 - m A law firm develops an intranet research tool that allows firm members to locate and search the firm's databases for information relevant to their cases. The system provides users with the ability to print cases, search for related topics, and annotate their personal copies of the database.
-

55-2 The following list provides examples of computer software that is not for internal use:

- a An entity sells software required to operate its products, such as robots, electronic game systems, video cassette recorders, automobiles, voice-mail systems, satellites, and cash registers.
 - b A pharmaceutical entity buys machines and writes all of the software that allows the machines to function. The pharmaceutical entity then sells the machines, which help control the dispensation of medication to patients and help control inventory, to hospitals.
 - c A semiconductor entity develops software embedded in a microcomputer chip used in automobile electronic systems.
 - d An entity purchases software to computerize a manual catalog and then sells the computer version and the related software to the public.
 - e A software entity develops an operating system for sale and for internal use. Though the specifications of the software meet the entity's internal needs, the entity had a marketing plan before the project was complete. In addition, the entity has a history of selling software that it also uses internally and the plan has a reasonable possibility of being implemented.
 - f An entity is developing software for a point-of-sale system. The system is for internal use; however, a marketing plan is being developed concurrently with the software development. The plan has a reasonable possibility of being implemented.
 - g A telecommunications entity purchases computer software to be used in research and development activities.
 - h An entity incurs costs to develop computer software for another entity under a contract with that other entity.
-

55-3 The following list illustrates the various stages and related processes of computer software development:

- a Preliminary project stage:
 - 1 Conceptual formulation of alternatives
 - 2 Evaluation of alternatives
 - 3 Determination of existence of needed technology
 - 4 Final selection of alternatives.
- b Application development stage:

- 1 Design of chosen path, including software configuration and software interfaces
 - 2 Coding
 - 3 Installation to hardware
 - 4 Testing, including parallel processing phase.
- c Postimplementation-operation stage:
- 1 Training
 - 2 Application maintenance.

Deloitte Guidance and Illustrations

Stages of Computer Software Development — 350-40-55 (Q&A 01)

Availability of Technology — 350-40-55 (Q&A 02)

55-4 This Subtopic recognizes that the development of internal-use computer software may not follow the order shown in the preceding list. For example, coding and testing are often performed simultaneously. Regardless, for costs incurred subsequent to completion of the preliminary project stage, the guidance shall be applied based on the nature of the costs incurred, not the timing of their incurrence. For example, while some training may occur in the application development stage, it should be expensed as incurred as required in paragraphs 350-40-25-2 through 25-6.

65 Transition

General Note

The Transition Section contains a description of the required transition provisions and a list of the related paragraphs that have been modified. This Section will retain the transition content during the transition period. After the transition period, the transition content will be removed yet will be available in archived versions of the Section.

General

65-1 Paragraph superseded on 10/26/2017 after the end of the transition period stated in Accounting Standards Update No. 2015-05, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*.

Transition Related to Accounting Standards Update No. 2016-19, *Technical Corrections and Improvements*

65-2 The following represents the transition and effective date information related to Accounting Standards Update No. 2016-19, *Technical Corrections and Improvements*.

- a For public business entities, the pending content that links to this paragraph shall be effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2016.
- b For all other entities, the pending content that links to this paragraph shall be effective for annual periods beginning after December 15, 2017, and interim periods in annual periods beginning after December 15, 2018.
- c Early application of the pending content that links to this paragraph is permitted by all entities.
- d The pending content that links to this paragraph may be applied either prospectively to all arrangements entered into or materially modified after the effective date or retrospectively.
- e A public business entity that elects prospective transition shall disclose the following in the first interim period and annual period after the effective date:
 - 1 The nature of and reason for the change in accounting principle
 - 2 The transition method
 - 3 A qualitative description of the financial statement line items affected by the change.
- f A public business entity that elects retrospective transition shall disclose the following in the first annual period after the entity's adoption date and in the interim periods within the first annual period:
 - 1 The nature of and reason for the change in accounting principle
 - 2 The transition method
 - 3 A description of the prior-period information that has been retrospectively adjusted
 - 4 The effect of the change on income from continuing operations, net income (or other appropriate captions of changes in the applicable net assets or performance indicator), any other affected financial statement line item(s), and any affected per-share amounts for the current period and any prior periods, retrospectively adjusted
 - 5 The cumulative effect of the change on retained earnings or other components of equity or net assets in the statement of financial position as of the beginning of the earliest period presented.
- g All other entities shall disclose the information in (e) through (f) for prospective transition or retrospective transition, as applicable, in the first annual period after the entity's adoption date, unless the entity elects to early adopt the pending content that links to this paragraph in an interim period, in which case the entity also shall disclose that information in the interim periods within the first annual period after the entity's adoption date.

Confidential and Proprietary — for Use Solely by Authorized Personnel

This publication provides comprehensive guidance; however, it does not address all possible fact patterns, and the guidance is subject to change. Consult a Deloitte & Touche LLP professional regarding your specific issues and questions.

Your feedback will help us improve the FASB Accounting Standards Codification Manual. Please let us know what you think.
Copyright © 2017 Deloitte Development LLC. All rights reserved.

FASB Accounting Standards Codification: Copyright © 2005 - 2017 by Financial Accounting Foundation, Norwalk, Connecticut

Deloitte
Accounting Research Tool

Copyright © 2017 Deloitte Development LLC. All rights reserved.