

Financial Reporting Update

Accounting for cloud computing
arrangements

June 2025



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Agenda

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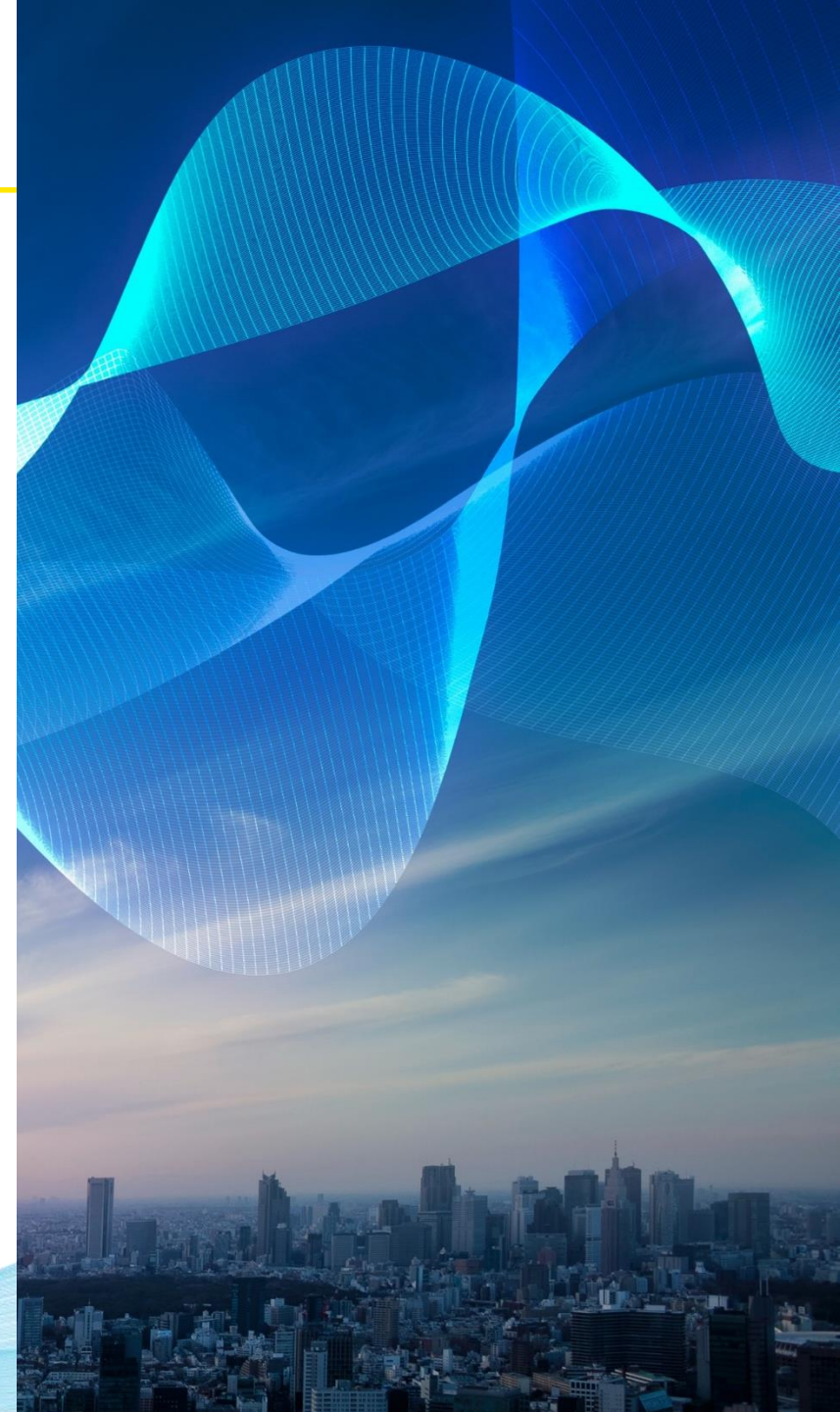
- ▶ Overview of cloud computing arrangements

2

- ▶ Evaluating whether an arrangement includes a lease
- ▶ Evaluating and accounting for an arrangement that includes an intangible asset

3

- ▶ Accounting for an arrangement that does not include an intangible asset



Overview of cloud computing arrangements



Overview of cloud computing arrangements

What is a cloud computing arrangement?

Customer does not currently have possession of the underlying software used in the arrangement, but rather, the customer accesses and uses the software on an as-needed basis



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What are some examples of cloud computing arrangements



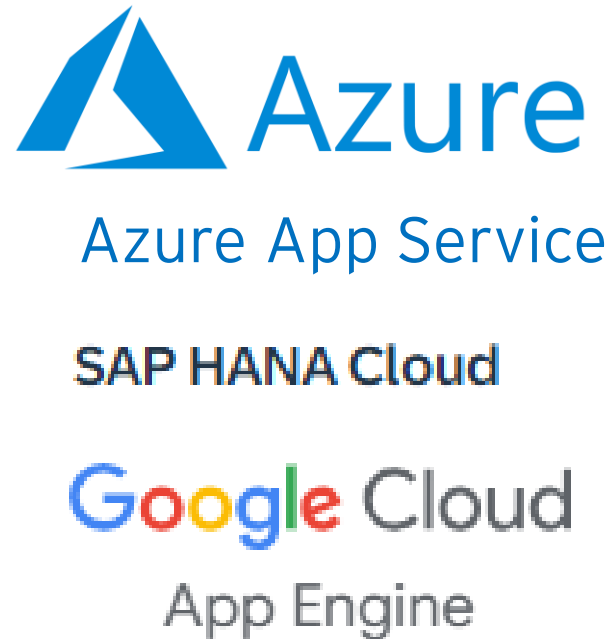
Examples of cloud computing services

Types of cloud computing services

Software as a service



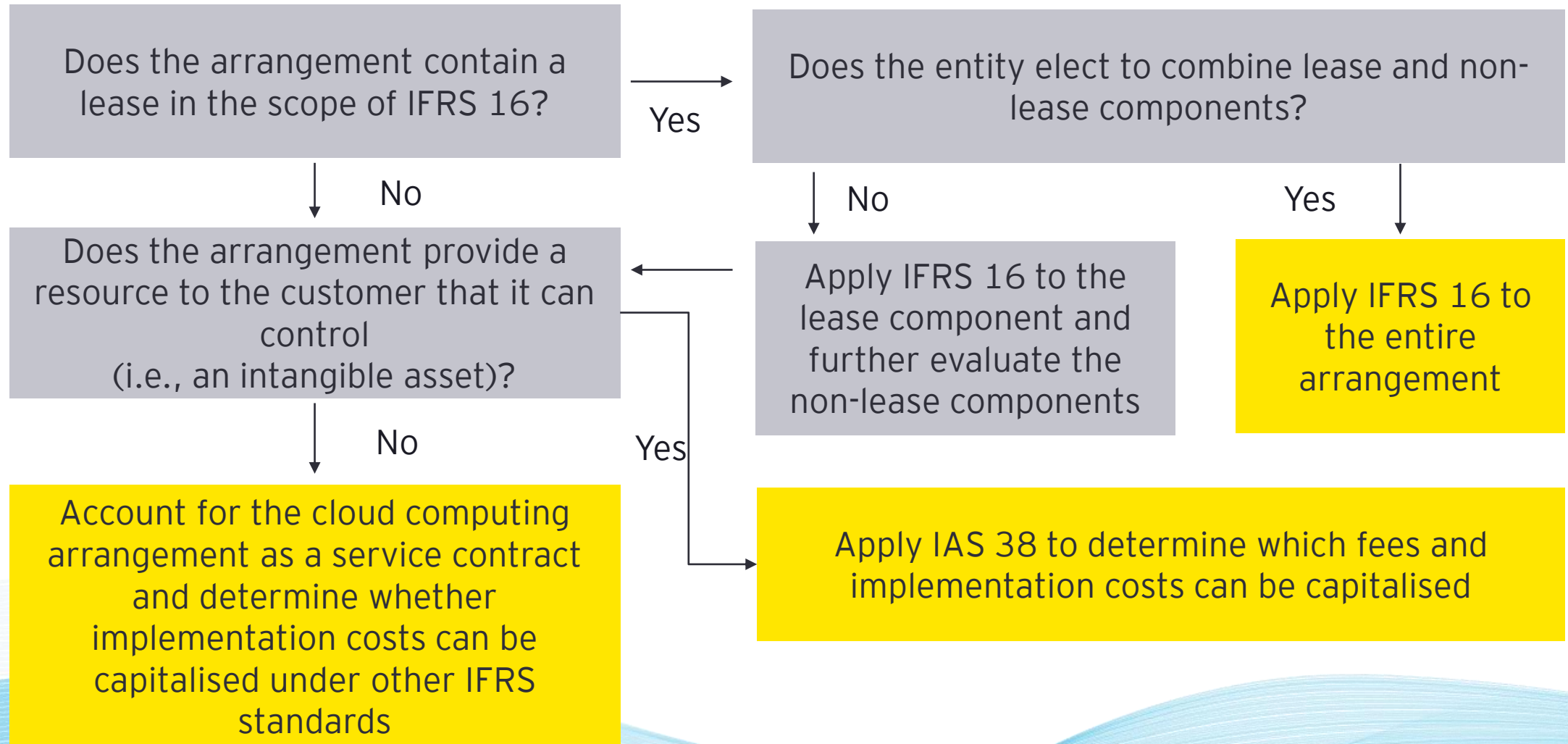
Platform as a service



Infrastructure as a service



Overview of cloud computing arrangements



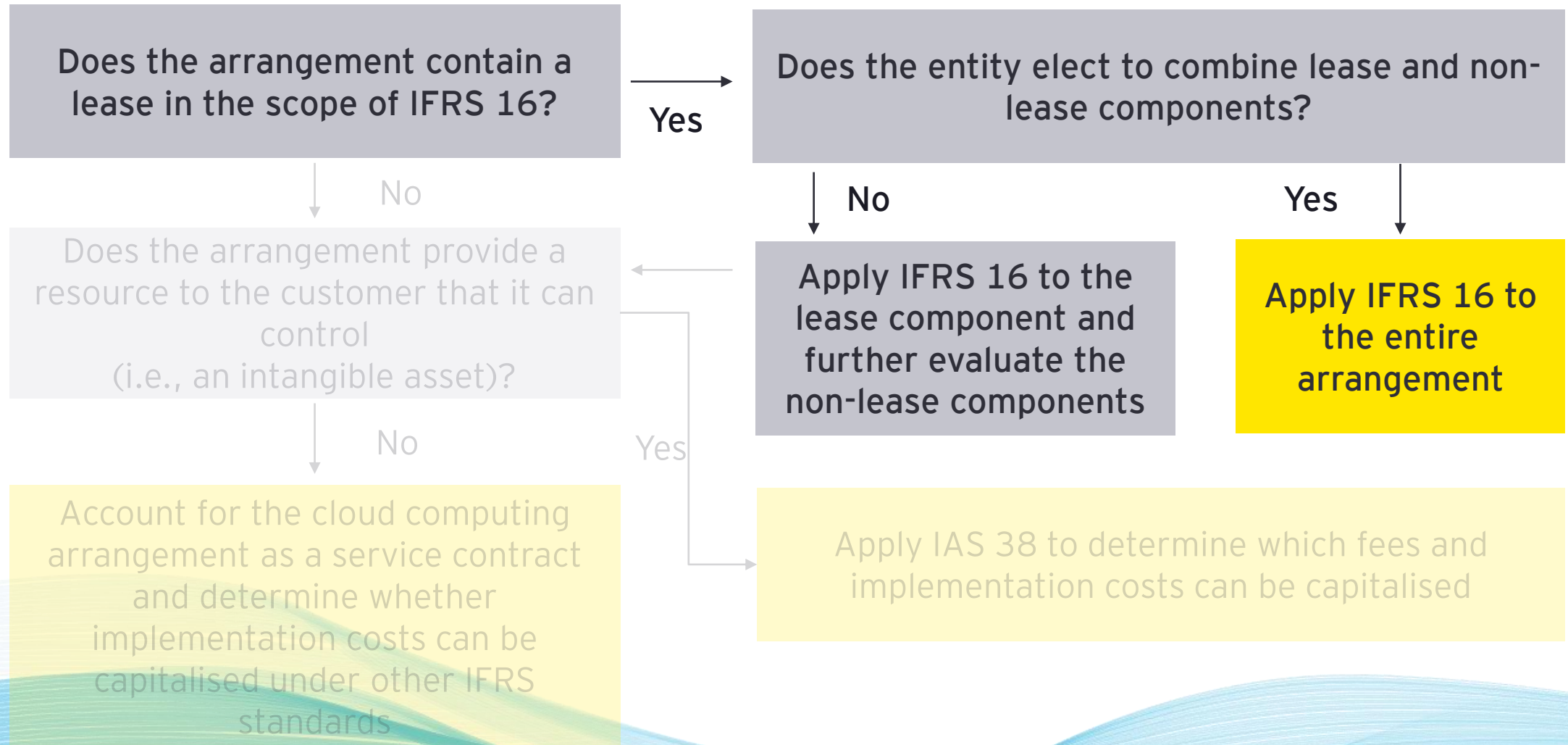
Source: Applying IFRS Accounting for cloud computing costs Updated July 2021 - www.ey.com

Possible outcomes



Evaluating whether an arrangement includes a lease

Overview of cloud computing arrangements



Source: Applying IFRS Accounting for cloud computing costs Updated July 2021 - www.ey.com

Evaluating whether an arrangement includes a lease

Definition of a lease

'a contract, or part of a contract, that conveys the **right to use an asset** (the underlying asset) for a period of time in exchange for consideration'

Right to use an asset means:

1 Right to obtain substantially all economic benefits

&

2 Right to direct the use

Do I have the right to use my

- Underlying servers
- Private cloud
- Software licence



Right to use an asset

Right to use an asset means:

1 Right to obtain substantially all economic benefits

- Directly or indirectly
- Primary outputs and by-products
- Use the asset in a commercial transaction (e.g. subleasing)
- Limited to defined scope of use in the contract



&

2 Right to direct the use

- Directs how and for what purpose
- If the purpose is pre-determined:
 - Right to operate the asset without supplier changing this, or
 - Designed the asset in a way that predetermines purpose



Evaluating whether an arrangement includes a software lease

Fact pattern

- ▶ Entity A enters into a Software as a Service (SaaS) arrangement.
- ▶ The entity has a **right to receive access** to the software over the contract term.
- ▶ Entity A incurs upfront costs for the following:
 - **Configuration:** Defining parameters within the existing software
 - **Customisation:** Modifying software code for additional functionalities



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Does Entity A have the right to use the asset?

Evaluating whether an arrangement includes a software lease

A

The right to receive future access does not in itself give the customer the right to use



No decision-making rights about how and for what purpose the software is used



Supplier decides how and when to update or reconfigure software

How would the answer change if this related to software licenses?



Software licenses

Software licenses

IFRS 16.3 &
16.4 [extract]

3. An entity shall apply this Standard to all leases ... except for ...
(e) rights held by a lessee under licensing agreements **within the scope of IAS 38 *Intangible Assets*** for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights.
4. A lessee may, but is not required to, **apply this Standard** to leases of intangible assets **other than those described in paragraph 3(e).**



Entity to conclude if the
lease is in scope of IFRS
16



Excluded:

- ▶ Assess if there's an intangible asset

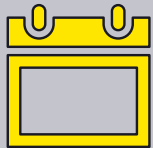
Not excluded:

- ▶ Lease and non-lease components
 - ▶ Allocate consideration

IFRS 16 Reminders

Reminders when accounting for a lease:

Initially measure right-of-use asset and lease liability at present value of lease payments



Reassess the lease term upon a significant event or significant change in circumstances



Discount rate is the rate implicit in the lease

Subsequently lease liability accrues interest and is reduced by payments

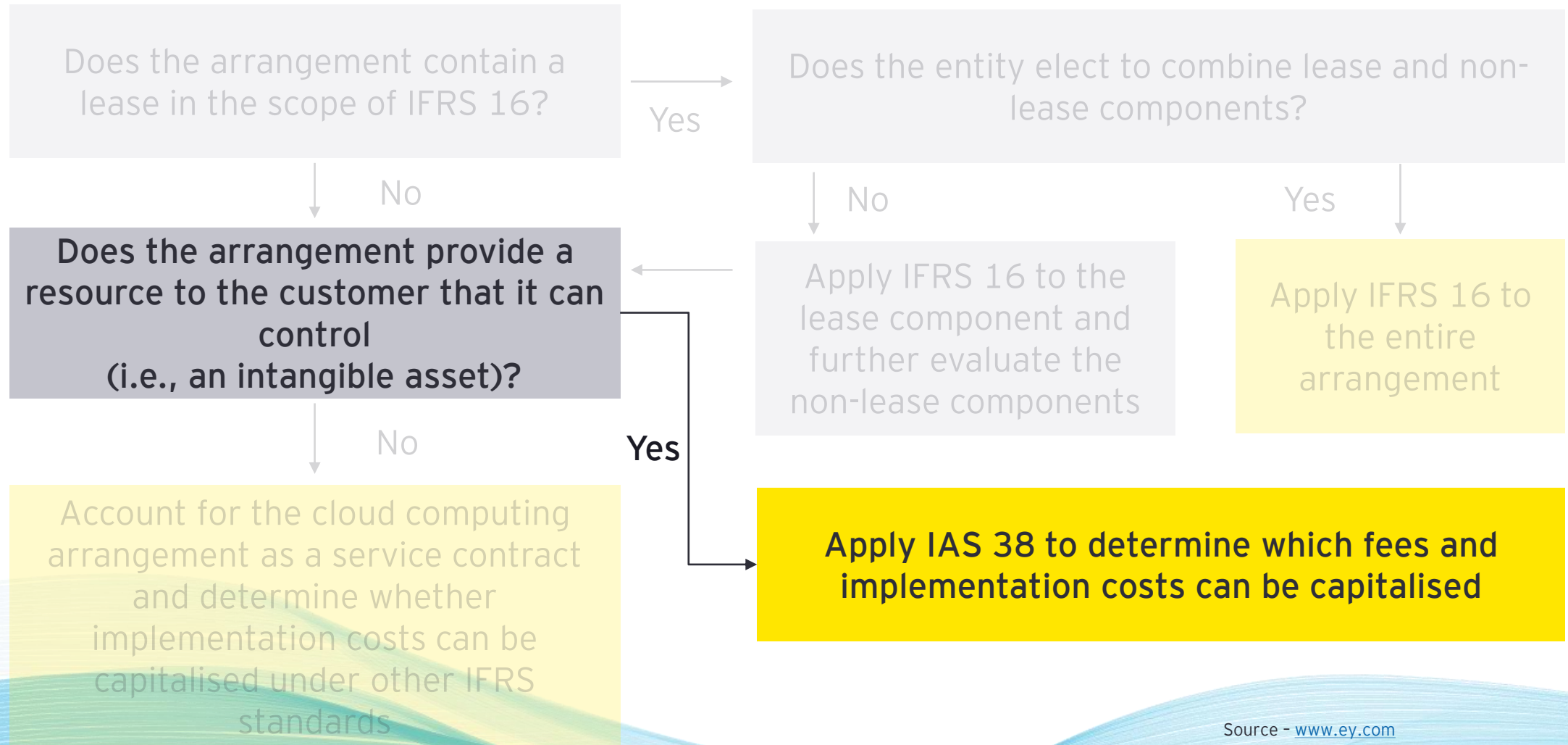
ROU asset is depreciated as set out in IAS 16



Evaluating whether an arrangement includes an intangible asset



Overview of cloud computing arrangements



Source - www.ey.com

Overview: Requirements for recognition

Definition of an intangible asset

Identifiable non-monetary asset

Without physical substance

Control

Elements of control



- ▶ Obtain future economic benefits
- ▶ Restrict the access of others to those benefits

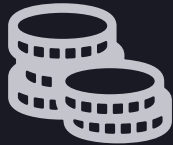
Requires careful consideration

If the entity receives resources it can control - IAS 38 is applied
(Assuming the intangible asset is not accounted for as a lease)

Software license: Requirements for recognition

One situation where a software licence is recognised as an intangible asset in a cloud computing arrangement:

Contractual right to take possession of software without significant penalty



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Feasible to run the software on entity's own or third party hardware



At inception

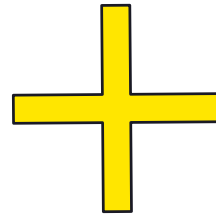


A license of software hosted by the supplier, in itself, is insufficient to conclude that an arrangement contains an intangible asset.

Software license: Significant penalty

Does the customer have the right to take possession of the software without significant penalty?

Ability to take delivery of the software without incurring significant costs



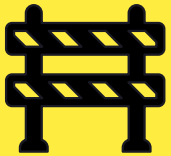
Ability to use the software separately without significant diminution in utility or value



Software license: Significant penalty

Does the customer have the ability to take delivery of the software without incurring significant costs?

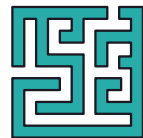
Financial penalties and operational barriers



Penalty is significant that the entity would not incur it

Explicit, reasonable mechanism for entity to take possession

Absence of adequate replacement service providers

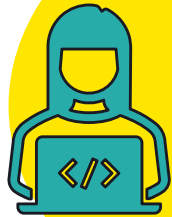


Economic barriers and other costs

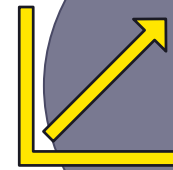


Software license: Significant penalty

Does the customer have the ability to use the software separately without significant diminution in utility or value?



Utilise all of the functionality if software is not hosted by the supplier



Software upgrades only available to those for whom the supplier hosts the software

Example: Recognition of software license

Fact pattern

- ▶ Entity A enters into a contract to receive a license of software which is hosted by the supplier.
- ▶ Software is configured to meet the needs of Entity A with custom templates designed for Entity A's use (ie. customised invoices and statements).
- ▶ Entity A may take possession of the software, but new hardware and specialised technicians would be required to run the software at a significant cost.
- ▶ Software updates required to run the software will only be available if hosted by the supplier.
- ▶ There are no significant penalties on cancellation.



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Can Entity A recognise the software as an intangible asset?

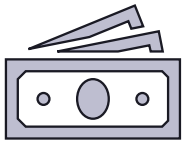
Example: Recognition of software license

A

Entity A cannot recognise the software as an intangible asset



Entity cannot use the software separately without significant diminution in value



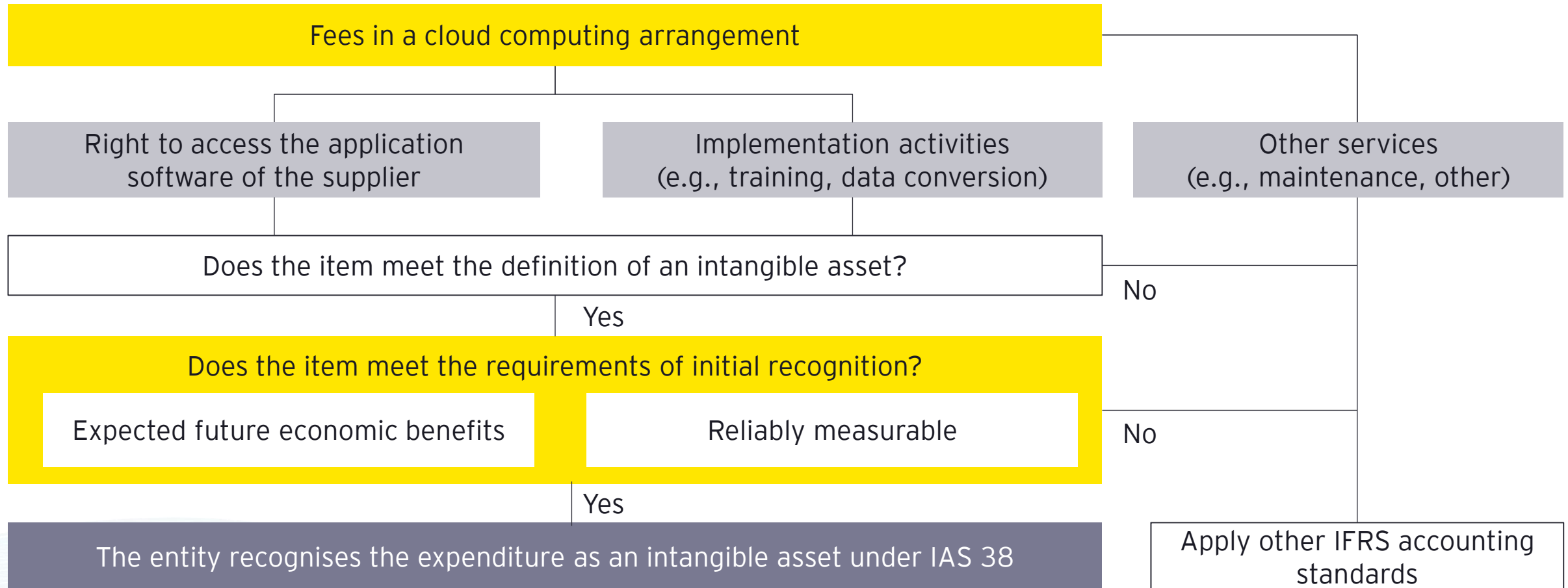
Not feasible to run the software on its own or with an unrelated supplier

Decision requires significant judgement and involvement of specialists may be necessary

Accounting for an arrangement that includes an intangible asset:



Overview: Accounting for an arrangement that includes an intangible asset



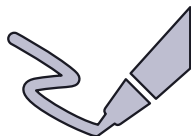
Reminder to perform this test each time potentially eligible costs are incurred

Fees relating to separately acquired intangible assets

Allocation of fees to the different services



IAS 38 does not include guidance on allocation

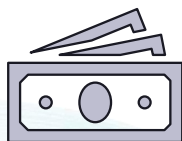


Entity should determine an accounting policy, such as allocation based on the relative stand-alone selling prices of each component



Apply judgement to determine components as this affects capitalisation

The entity recognises the expenditure as an intangible asset under IAS 38

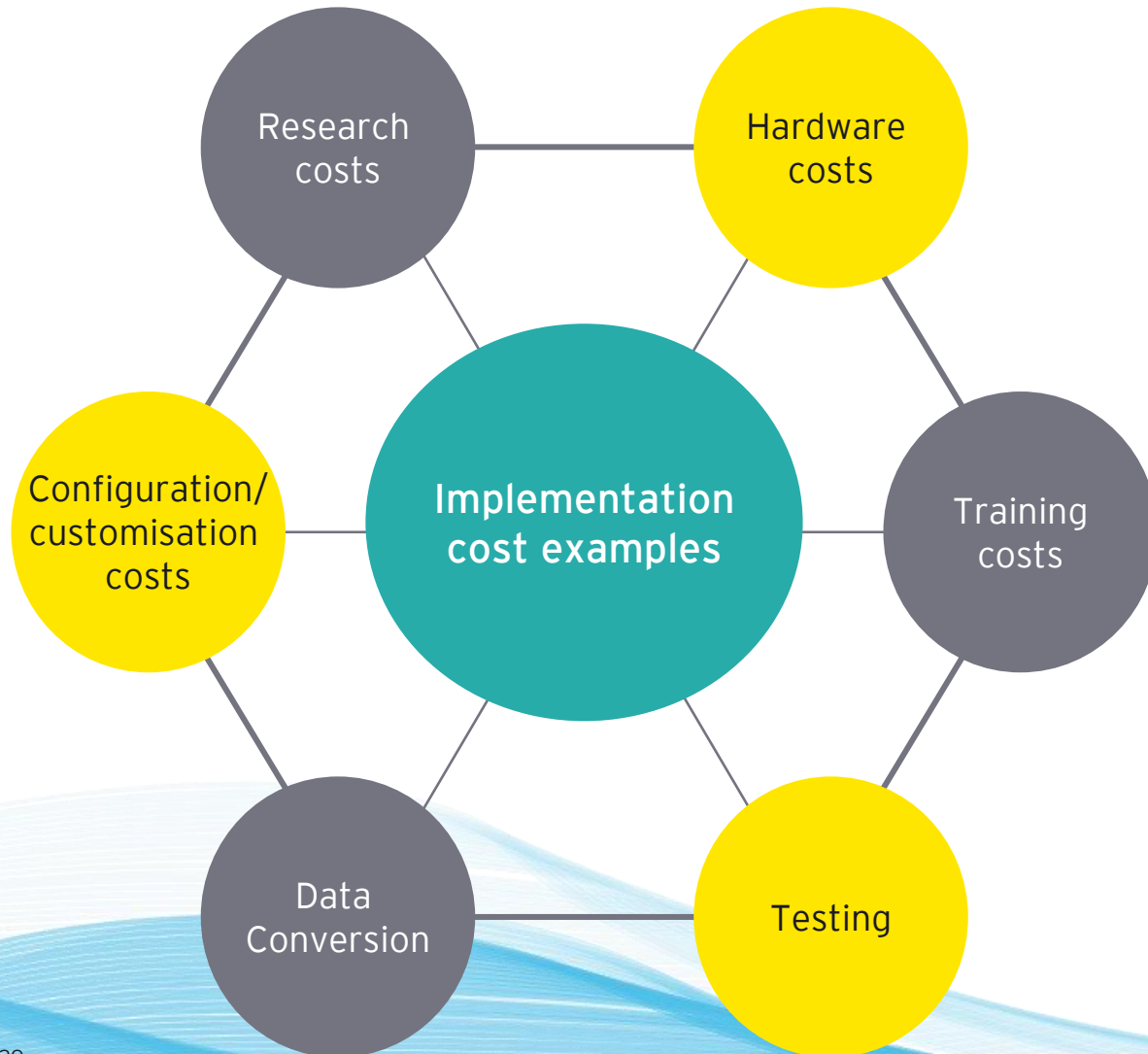


Assumes purchase price usually reflects expectations on future economic benefits



Cost is the present value of the obligation if paid for over time

Implementation costs



Costs incurred to implement a cloud computing arrangement that includes a software licence:

- ▶ Accounted for based on the nature of the cost
- ▶ Follow IAS 38 guidance on capitalisation and expensing
- ▶ Costs may be a part of separately acquired or internally generated intangible assets

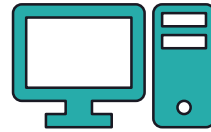
Accounting for implementation costs

Guidance on various implementation costs



Research costs

- Performance and technology requirements
- Exploring alternatives
- Developing project plan
- Selecting vendors
- Expensed as incurred



Hardware costs

- Includes servers, storage and other network equipment
- Generally capitalised under IAS 16 *Property, plant and equipment*




Data conversion

- Transferring data from the existing system to the new system
- Capitalise costs to obtain or develop software which allows data conversion
- All other costs expensed

Accounting for implementation costs

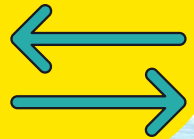
Guidance on various implementation costs

Configuration costs

- Costs to code, configure or customise the software 
- Generally, directly attributable and **capitalised**
- Minor or **cosmetic changes** to the interface while capable of operating in intended manner are **expensed**
- Requires **judgement**

System change costs

- Costs to enhance existing software
- **Capitalise** costs which provide additional functionality
- **Expense other costs**
- If unable to distinguish between maintenance and relatively minor upgrades - expense otherwise capitalise based on nature



Indirect costs and general overheads

These costs cannot be capitalised

Even if they can be allocated on a reasonable and consistent basis

Even if costs are incurred directly by the entity or services by third parties

Examples:

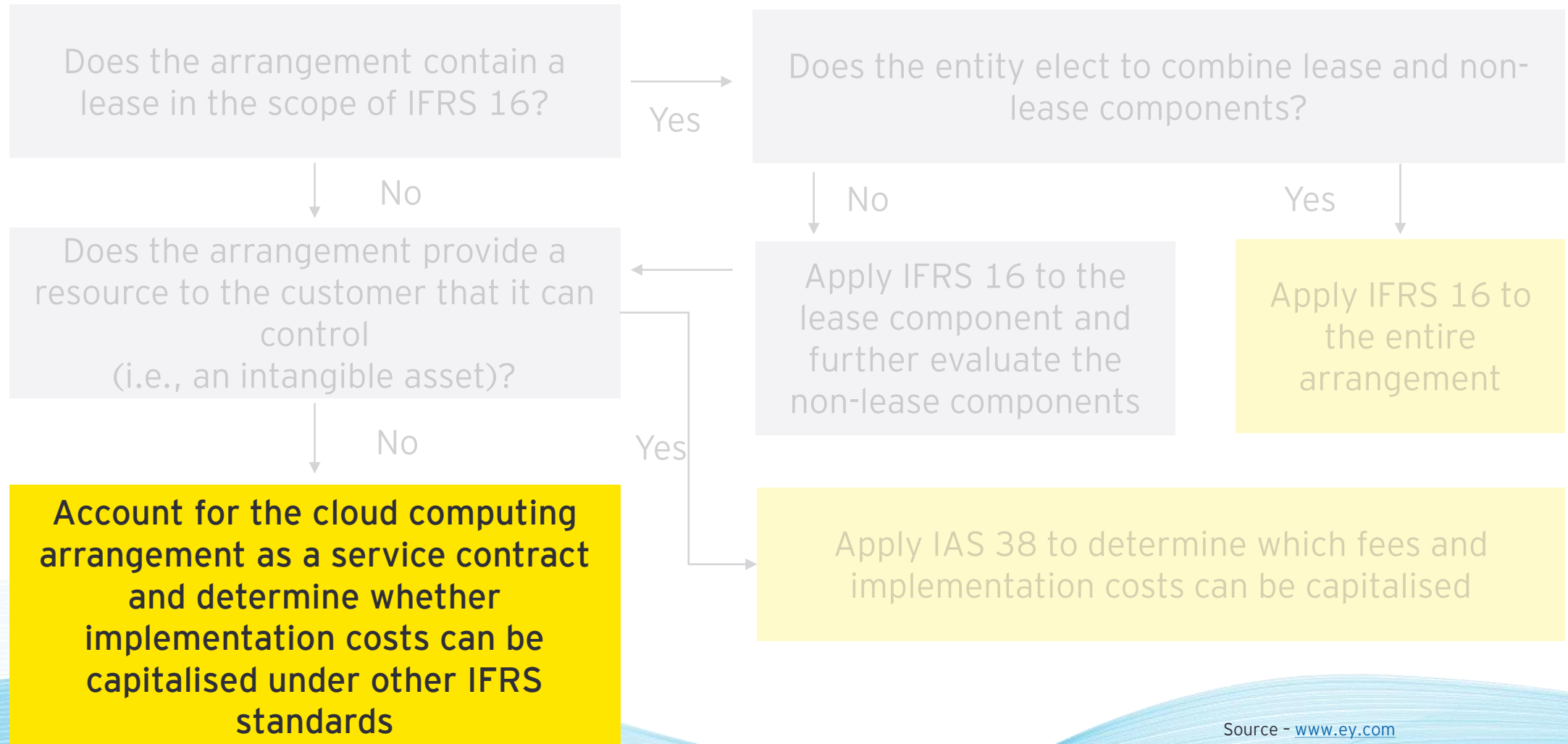
- Selling, administrative and other general overheads
 - Identified inefficiencies
- Initial operating losses before asset achieves planned performance
 - Training staff





Accounting for an
arrangement that does not
include an intangible asset

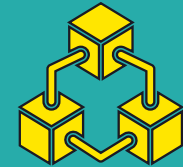
Overview of cloud computing arrangements



Source - www.ey.com

Accounting for implementation and other costs

Implementation and other upfront costs



Expense

Prepaid asset

Capitalised under other
IFRS Accounting
Standards

Customers must determine which goods or services must be accounted for separately



Accounting for implementation and other costs

Implementation and other upfront costs

IAS 38 does not include guidance on identification of goods and services received

Develop an accounting policy under IAS 8.10-11

IFRS 15 is applied by analogy in identifying goods and services

Reminder:

Significant judgement is required to identify the promised implementation goods and services received



Example: Separately identifiable

Fact pattern

- ▶ Entity A promises to provide a customer with software.
- ▶ The entity also promises to significantly customise the software.
- ▶ The customisation will allow the software to function with the customer's existing software.

Q

Is the software and customisation separately identifiable?



Determining whether goods or services are distinct

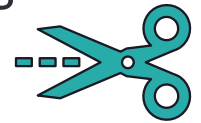
Promised goods and services are distinct when:



Benefit on their own or with readily available resources



Goods and services are separately identifiable



Three factors indicating promises are not separately identifiable:

The goods or services are highly interdependent or interrelated

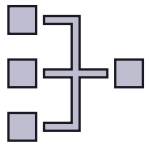
Significant service of integrating goods in the contract

One or more goods/services significantly modifies other goods

Example: Separately identifiable

A

The software and customisation are not separately identifiable



The entity is providing the customer with a fully integrated system



The customisation will significantly modify the software such that the risks of providing it and the customisation are inseparable

Careful consideration required under long-term arrangements to determine appropriate accounting for the costs

Example: Other costs

What if Entity A had incurred other costs?



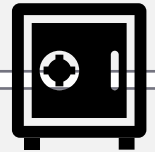
Expensed at a point in time/as incurred

- Data cleaning
- Staff training
- Data migration
- Disaster recovery



Expensed over time

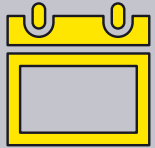
- Data storage costs
- Security/compliance fees
- Access to tech support fee
- Parallel running of legacy system



Judgement and careful review of contract terms and conditions required

Accounting for a service contract

Reminders on accounting for a service contract



Assess whether each service is distinct at a contract level, therefore unrelated third-party services are distinct from the initial arrangement

Allocate the fee to distinct promises to determine when allocated amounts will be recognised as an expense



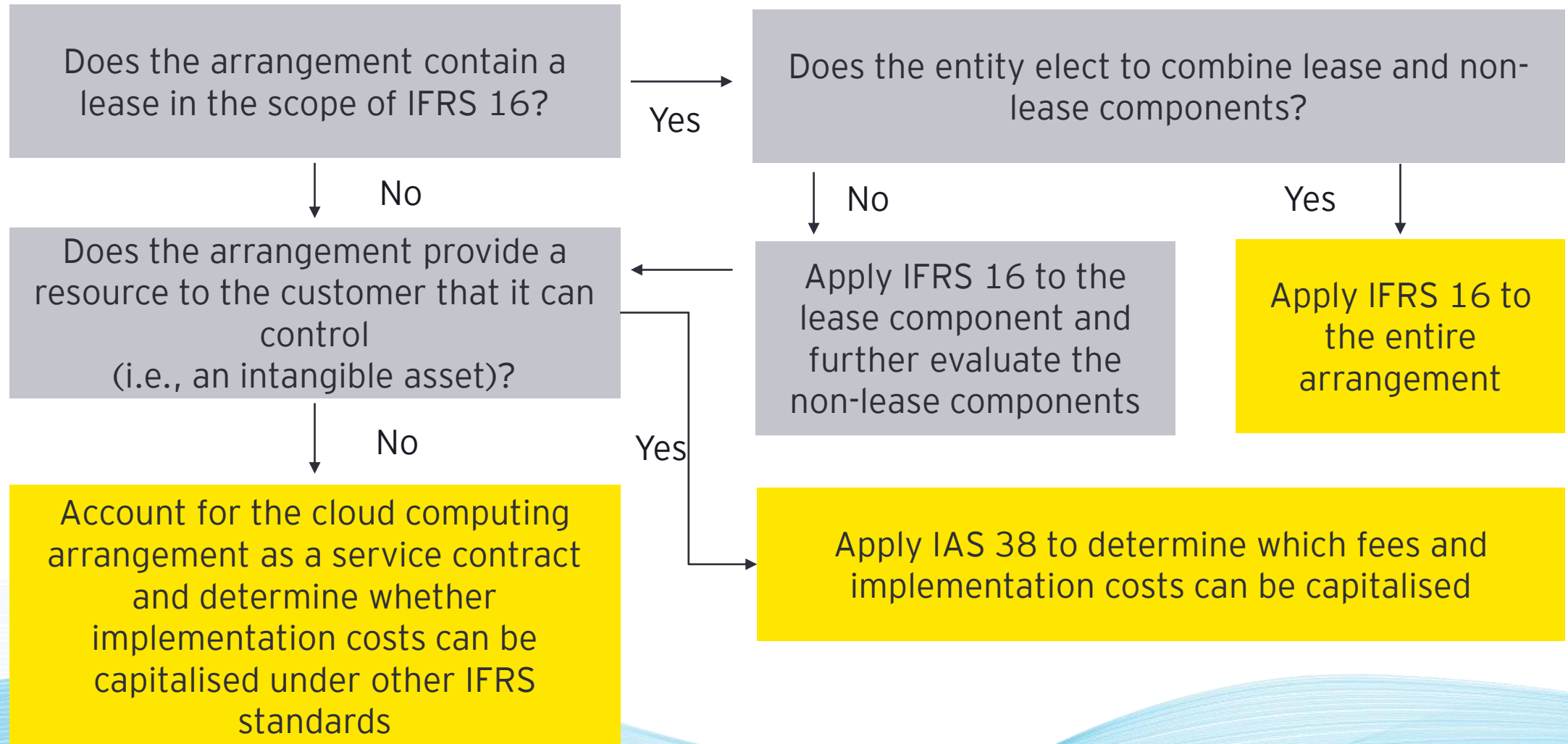
Develop an accounting policy

When promises are not distinct, recognise fees over term of contract

When fees are paid in advance, may recognise a prepaid asset



Summary of cloud computing arrangements



Source: Applying IFRS Accounting for cloud computing costs Updated July 2021 - www.ey.com



One minute recap

Resources



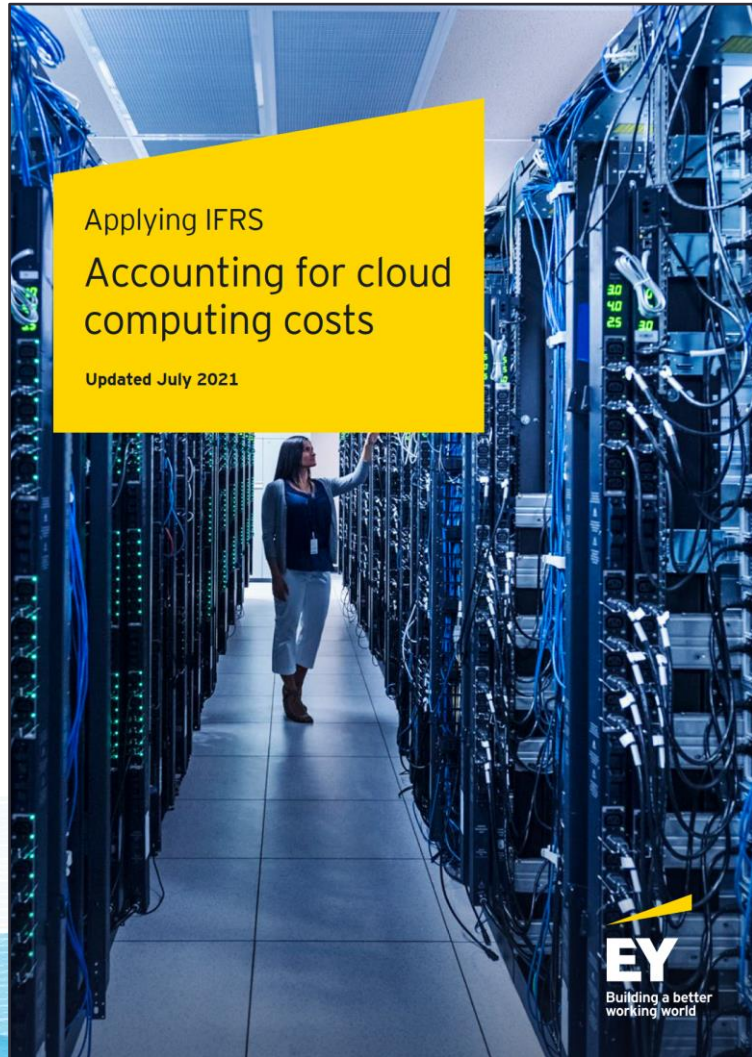
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Resources



Applying IFRS: Accounting for cloud computing costs





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