

Memorandum

Software Technology

February 6, 2025

To: Members of the Board
From: Josh R. Williams, Senior Analyst
Thru: Monica R. Valentine, Executive Director
Subject: **Software Technology - (Development Paper)** - (Topic A)

INTRODUCTION

At the December 2024 meeting, the Board deliberated scope and recognition guidance for software licenses. The objective for this meeting is for the Board to review and consider the following staff recommendations for shared software assets in the federal government:

1. Scope and recognition frameworks for shared services
2. Recognition framework for shared software code

Staff is requesting the Board's feedback on the proposals.

REQUEST FOR FEEDBACK

Prior to the Board's February meeting, please review the attached staff analysis and respond to the questions by February 21, 2025.

Please submit responses to Josh Williams at WilliamsJR@fasab.gov with a cc to Monica Valentine at ValentineM@fasab.gov.

NEXT STEPS

Pending Board feedback, staff will coordinate with stakeholders to further research and propose updates, as needed, to existing accounting guidance in SFFAS 10, *Internal Use Software*.

ATTACHMENTS

1. Staff Analysis
2. Prior Board Meeting Discussion Timeline

Analysis

Software Technology

February 6, 2025

INTRODUCTION

Purpose

This material pertains to the Board's project to update accounting guidance for software technology.

Background

This project began with the Board considering adopting a right-to-use asset framework for cloud-service arrangements. The Board initially considered adopting guidance that the Governmental Accounting Standards Board (GASB) issued in Statement No. 96, *Subscription-Based Information Technology Arrangements*.

During the October 2022 meeting, some members viewed cloud-service arrangements as service contracts while some members thought it reasonable to conceptualize cloud-service arrangements as right-to-use assets. However, most members were concerned that the preparer burden and lack of reporting benefits may not justify the need for asset recognition. The members suggested that disclosures could adequately provide information about how federal entities use cloud-services for operational needs versus purchasing or developing the information technology (IT) resource internally.

During the April 2023 meeting, the Board considered potential preparer burdens and user benefits of four reporting options that staff proposed in a cost-benefit analysis. The Board overwhelmingly supported developing guidance to require reporting entities to disclose cloud-service expenses.

During the October 2023 meeting, the majority of members supported proposed guidance that would establish that reporting entities should apply existing liability and prepaid asset guidance to cloud-service arrangements and expense payments for cloud services as incurred. However, the Board had mixed opinions about whether guidance should require reporting entities to disclose any information on cloud-service arrangements. Staff noted they would defer disclosure guidance proposals and focus on recognition guidance for the software-technology project topics.

At the April 2024 meeting, the majority of members agreed that reporting entities should not capitalize implementation costs for cloud-service arrangements unless the implementation activities result in a distinct internal use software asset, in accordance with SFFAS 10, *Accounting for Internal Use Software*, independent of the associated cloud-service arrangement.

At the December 2024 meeting, the Board agreed on a scope to distinguish software license assets from cloud services for financial statement recognition purposes. The Board also agreed on a recognition guidance framework for perpetual and term-based software licenses.¹

Recommendations and Analyses

This paper recommends accounting guidance frameworks for shared software assets in the federal government. Specifically, this paper recommends:

1. Scope and recognition frameworks for shared services
2. Recognition framework for shared software code

Staff requests the Board's feedback on the recommendations.

Research

For this session, staff coordinated with the working group and other stakeholders to research characteristics and recognition guidance possibilities for shared services and shared software code in the federal government. Additionally, staff researched prior working group correspondence, prior Board meeting deliberations, shared service and open-source software government websites, and applicable federal laws and policies.

Staff specifically researched the following documents for this issues paper:

- GAO Report 19-94, *Streamlining Government: OMB and GSA Could Strengthen Their Approach to Implementing a New Shared Services Plan*, March 7, 2019
- OMB Memorandum M-16-21, *Federal Source Code Policy: Achieving Efficiency, Transparency, and Innovation through Reusable and Open Source Software*, August 8, 2016
- OMB Memorandum M-19-16, *Centralized Mission Support Capabilities for the Federal Government*, April 26, 2019
- SFFAC 1, *Objectives of Federal Financial Reporting*, September 2, 1993
- SFFAC 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, December 26, 2007
- SFFAS 10, *Accounting for Internal Use Software*, October 9, 1998

¹ See Attachment 2 for a more detailed summary of previous Board meeting deliberations on the software technology project.

- Technical Release 16, *Implementation Guidance for Internal Use Software*, January 19, 2016
- Technical Release 23, *Omnibus Technical Release Amendments 2024: Conforming Amendments to Technical Releases 10, 16, 20, and 21*
- U.S. Statute 118-213, *SHARE IT Act*, September 9, 2024

To obtain feedback on the types of shared service information that could be useful in federal financial reports, staff spoke with personnel from two advocacy groups that support the benefits of shared services in the federal government.

RECOMMENDATION NO. 1

Staff recommends the Board apply the software license accounting framework, that the Board approved during the December 2024 meeting, to shared services.

ANALYSIS

The following analysis will discuss the Board's prior decision with software license guidance, characteristics and examples of shared services, current FASAB guidance on shared services, and staff's recommendation.

Applicable Prior Board Decisions

During the December 2024 meeting, the Board agreed on the following accounting guidance framework for software licenses:

- *Software license Guidance Scope* - *This guidance applies to internal use software that a reporting entity has the right and ability to either run the software on its own hardware or contract with another party, unrelated to the vendor, to host the software.*
- *Software License Recognition and Measurement* – *If the software license has a perpetual or initial term of two years or more the reporting entity should recognize an asset for the cost of the license and a liability for any software licensing fees not paid upon acquisition of the license. The useful life of the asset should not exceed the binding arrangements of the contractual or legal terms of the software license. If the binding arrangements are for a limited term that can be renewed, the useful life of the asset should include the renewal period(s) only if the cost to renew is nominal.*

The Board deliberated this framework in the context of software that federal entities acquire from private vendors.

Shared Service Characteristics

In coordination with the working group, staff developed the following working definition for shared services in the federal government:

- *Shared Service - a mission, operation, or administrative support function provided by a federal entity to other federal entities (interagency) or to separate components within the same federal entity (intra-agency).*

In 2019, OMB issued memorandum M-19-16, *Centralized Mission Support Capabilities for the Federal Government*. This memorandum encouraged adoption of shared services to consolidate mission-support functions to promote cost savings by leveraging resources and reducing duplicative functions (e.g., human resources, payroll, technology, etc.) across the federal government.²

The U.S. Department of the Treasury Bureau of Fiscal Service currently operates the Financial Management Quality Service Management Office (FM QSMO).³ This office acts as a broker between federal agencies and service providers in marketplace. Several of the shared services discussed below exist in this marketplace.⁴

Many federal entities have provided and received shared services in the federal government for decades. Examples include:

- The National Finance Center is a shared service provider for financial management and human resource management services (<https://nfc.usda.gov/>).
- Interior Business Center is a federal shared services provider that operates under a fee-for-service, full cost recovery business model, offering acquisition, financial management and human resources systems and services to federal organizations (<https://www.doi.gov/ibc>).
- Administrative Resource Center is a federal shared service provider for multiple administrative functions, such as financial management, human resources, information technology, investment accounting, procurement, and travel (<https://home.treasury.gov/services/government-shared-services/administrative-resource-center>).
- Enterprise Services Center - is a designated shared service provider that provides information technology and financial management services to a wide range of federal agencies. Financial services include transaction processing to

² GAO issued Report 19-94, *Streamlining Government: OMB and GSA Could Strengthen Their Approach to Implementing a New Shared Services Plan* in 2019 that stated, "The federal government can reduce duplicative efforts and free up resources for mission-critical activities by consolidating mission-support services that multiple agencies need—such as payroll or travel—within a smaller number of providers so they can be shared among agencies." (<https://www.gao.gov/products/gao-19-94>)

³ <https://tfx.treasury.gov/fmqsmo/marketplace-catalog>

⁴ The FM QSMO marketplace also offers commercial services through GSA governmentwide contract vehicles.

financial statements, to reporting and analysis. Information technology services include applications services, customer support services (Service Desk), managed digital services, cybersecurity services, media solutions, office automation support, project management office, national wireless program, and network/telecommunication services (<https://www.esc.gov/>).

- Pegasys Financial Services is federal shared service provider of core financial system and financial transactional processing services, such as administrative payment, general accounting, reporting and analysis, travel and relocation, and audit services (<https://www.gsa.gov/buy-through-us/purchasing-programs/shared-services/pegasys-financial-services>).
- USA Performance is a software solution to assist Federal agencies in implementing their personnel performance management programs and systems (<https://www.opm.gov/services-for-agencies/technology-systems/usa-performance/>).
- GovTA is a web-based system that is used to submit work time and leave information to the Department's payroll/personnel service provider (<https://www.commerce.gov/hr/practitioners/compensation-policies/GovTA>).
- GrantSolutions supports Federal agencies throughout the full grants lifecycle – from pre-award planning through application, award, and closeout (<https://home.grantsolutions.gov/home/about/>).

From the customer perspective, research and working group feedback indicates that federal entities acquire shared services from other federal entities through interagency agreements (IAA). Working group members stated that the IAAs typically require fixed payments for the overall service (e.g., payroll, HR, cybersecurity services) that includes the cost for labor, software application, and other costs for providing the service.

Research and working group feedback indicated that the federal customer of the shared service is sometimes able to possess and operate the software component of the service on their own hardware. However, the examples of such scenarios from the working group were minimal.

Additionally, research and working group feedback indicates that federal shared service providers acquire software licenses or internally develop and operate software on their own systems and/or acquire cloud services to provide shared services in the same way they would for other internal use purposes. The shared service provider typically charges the federal customer through the IAA to reimburse the cost of providing the service, which includes labor, software, and other costs.

Current FASAB Guidance

It does not appear that any standard setters other than FASAB provide accounting guidance specifically for shared services. FASAB currently addresses shared services in implementation guidance in TR 16, paragraphs 30-32:

30. Shared Service means a mission or support function provided by one business unit to other business units within or between organizations. The funding and resourcing of the service is shared and the providing entity effectively becomes an internal/external service provider. There are three types of shared service structures in the federal government: intra-agency, interagency and commercial. Intra-agency shared services include those provided within the boundaries of a specific organization such as a federal department or agency, to that organization's internal units. Interagency shared services are those provided by one federal provider's organizational boundaries. Commercial shared services are those provided by private vendors.

31. For intra-agency shared services, a cost allocation methodology could be developed in accordance with SFFAS 4, paragraphs 120-125. For interagency shared services and commercial shared services, the service provider entity that owns (receives funding/responsible for maintaining) the software should account for the software in accordance with SFFAS 10. In the event that the entity receiving the service (the customer) has 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, then the customer should account for the software in accordance with SFFAS 10.

32. If the shared service arrangement includes a perpetual software license, the customer should account for the software license element of the arrangement consistent with the acquisition of their other software licenses, as discussed in paragraph 26A of this TR. SFFAS 10 is not applicable to a shared service arrangement that does not convey a contractual right to the IUS or to ones that do not include an IUS license.

From a customer perspective, TR 16 requires reporting entities to recognize an intragovernmental software asset acquired as part of a shared service. From a shared service provider perspective, TR 16 requires that the reporting entity account for the software as IUS within the scope of SFFAS 10.⁵

Staff notes that paragraph 32 provides the same guidance that TR 16 currently provides for cloud computing. Similar to cloud computing, staff believes the current TR 16 guidance is too vague for distinguishing software licenses from shared services. For example, preparers and auditors could interpret the meaning of “a contractual right to the IUS” differently and TR 16 does not define “IUS license”. The IT community uses

⁵ See SFFAS 10, par. 2

“license” informally to describe both on-premise software and rights to access software as a service.

Additionally, the last sentence in TR 16, par. 31 states, “In the event that the entity receiving the service (the customer) has 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, then the customer should account for the software in accordance with SFFAS 10.” This language is similar to the software license scope that the Board agreed on during the December 2024 meeting and, as currently written, seems to overlap with and duplicate the perpetual software license guidance in paragraph 32. Furthermore, TR 16 did not apply this guidance to software licenses or cloud computing.

Staff Analysis

It appears that reporting entities currently account for software as an IUS asset in accordance with SFFAS 10 if the entity uses the software to provide shared services to another federal entity. The working group did not note any difficulties with interpreting the current scope of SFFAS 10, par. 2 to apply to this scenario.⁶ Therefore, the following analysis and recommendation will focus on accounting guidance recommendations for federal shared services from the customer perspective.

Staff recommends the Board apply the accounting guidance framework for software licenses, that the Board agreed to in the December 2024 meeting, to software acquired through shared services that a federal entity receives from another federal entity:

- [Shared Software Guidance Scope](#) - This guidance applies to internal use software that a reporting entity has the right and ability to either run the software on its own hardware or contract with another party, unrelated to the vendor, to host the software.
- [Shared Software Recognition and Measurement](#) – If the shared software has a perpetual or initial term of two years or more the reporting entity should recognize an asset for the cost of the license and a liability for any fees not paid upon acquisition of the software. The useful life of the asset should not exceed the binding arrangements of the contractual or legal terms of the arrangement. If the binding arrangements are for a limited term that can be renewed, the useful life of the asset should include the renewal period(s) only if the cost to renew is nominal.

Similar to the accounting framework for software licenses acquired from private vendors, this recommended framework would provide principle-based guidance for reporting entities to recognize an intragovernmental software asset acquired through

⁶ SFFAS 10, par. 2 includes, “software that is developed or obtained for internal use and subsequently provided to other federal entities with or without reimbursement.”

shared services from another federal entity if the receiving entity has control over the software.

From a practical standpoint, staff believes this framework would result in the same recognition requirements that TR 16 currently provides. However, in accordance with the GAAP hierarchy, staff believes it is appropriate for the Board to provide guidance for shared services in level A GAAP since SFFAS 10 does not address intragovernmental IUS recognition.⁷

Furthermore, staff believes the recommended framework would align with the software license guidance framework and streamline the accounting guidance that requires federal entities to apply judgment when determining whether a software resource meets the criteria for an asset, whether acquired from a private vendor or another federal entity. Staff continues to believe a flexible and principle-based approach to software asset recognition is optimal in a complex and fast changing software environment.⁸

As previously noted, it appears that federal entities do not often recognize a shared service software asset, as a customer, and staff does not believe that would change with the recommended framework. However, staff believes there are reporting benefits to recognizing a software asset acquired from other federal entities, when it does occur.

The OMB memorandum, GAO report, and SHARE IT Act indicate there is congressional and executive branch interest in reducing duplicative costs associated with software acquisitions in the federal government.⁹ Staff believes that recognizing intragovernmental software assets when they do occur would provide transparency over duplicative acquisitions of software among federal entities.

Stakeholder feedback

The working group did not identify many issues with applying the existing guidance in TR 16. One working group member stated that it is difficult to assess what the terms “contractual rights to IUS” and “software license” means in paragraph 32. Another working group member stated that “commercial shared services” as described in paragraph 30 seems to describe a typical service contract or cloud-service arrangement with a private vendor and did not seem to apply to federal shared services.

Furthermore, the working group identified only minimal instances where they recognized a software asset in accordance with TR 16 when receiving shared services. The working group noted that in a shared service arrangement, the receiving entity typically receives an administrative or operational service and rarely acquires the software in a

⁷ Software is not physically transferred between entities like tangible PP&E.

⁸ Following the issuance of the updates to level A accounting guidance for software, the ASIC (pending Board approval) could then update TR 16 to conform with the new standards and provide implementation guidance as needed.

⁹ The SHARE IT Act is a 2024 law that requires federal agencies to share custom-developed code amongst each other in an effort to prevent duplicative software development contracts (<https://fedscoop.com/agencies-must-share-custom-source-code-under-new-share-it-act/>)

manner that allows them to run the software on its own hardware or contract with another party to host the software.

Staff spoke with a few interest groups that advocate for the federal government to implement shared services in its operations. One stakeholder did not suggest any specific accounting or reporting needs but emphasized that it was important to promote accountability over the costs that federal entities incur in their administrative functions and identify savings from implementing shared services. Another stakeholder did not have an opinion on accounting for shared services but suggested it would be beneficial for federal entities to discuss efforts to use shared service in the management discussion and analysis sections (MD&A) of their annual reports.

Staff Recommendation

In summary, staff believes the recommended framework would appropriately account for intragovernmental software assets that a federal entity acquires from another federal entity through shared services in a manner consistent with the previous software asset framework the Board agreed on for cloud-service arrangements and software licenses. This would appropriately match the cost of acquiring an asset to the economic benefits and services that the reporting entity receives from the asset in future reporting periods.

As noted, the recommended guidance is similar to what is in TR 16 and staff therefore does not expect the recommended framework to result in accounting changes among reporting entities. However, staff believes the Board should address accounting for shared services in level A GAAP in conformance with the principle-based framework for software asset recognition.

Question for the Board:

1. Does the Board agree with staff's proposed accounting framework for shared services? Please provide your feedback on staff's analysis and recommendation.

RECOMMENDATION NO. 2

Staff recommends the Board apply existing recognition guidance in SFFAS 10 to costs associated with shared software code.

ANALYSIS

The following analysis will discuss characteristics and examples of shared software code, applicable FASAB guidance, and staff's recommendation.

Characteristics of Shared Software Code

In coordination with the working group, staff developed the following working definition for shared software code in the federal government:

- *Shared software code - software applications or code developed by one federal entity made available for use by other federal entities, allowing them to access and utilize the same functionality without needing to develop or purchase their own software.*

Existing federal policy and law aims to promote the use of shared software code across the federal government to streamline development and reduce costs. In 2016, OMB issued memorandum M-16-21, *Federal Source Code Policy: Achieving Efficiency, Transparency, and Innovation through Reusable and Open Source Software* that promoted ensuring that new custom-developed federal source code be made broadly available for reuse across the Federal Government.

A recent 2024 law, the SHARE IT Act, requires agencies to publicly list custom code and share that code with other agencies. The law aims to address the inefficiency that can happen when federal entities unknowingly hire contractors to develop code that another agency has already developed.¹⁰

Research and working group feedback indicate that some federal entities utilize shared software code. Examples include:

- U.S. Web Design System provides principles, guidance, and code to help you design and build accessible, mobile-friendly government websites and digital services (<https://designsystem.digital.gov/how-to-use-uswds/>).
- Code.gov is the federal government's platform for sharing America's open-source software and helps agency partners and developers save money and increase quality by promoting code reuse and educating and connecting the open source community (<https://code.gov/>).
- Open Source @ NSA provides open-source software, developed by NSA, to the public for free (<https://code.nsa.gov/>).

One federal entity stated that they utilized infrastructure as code from one entity to use as a platform to develop a software factory.¹¹ Of the federal entities that reported using shared software code, they stated they can use the code for free but can incur costs to

¹⁰ <https://fedscoop.com/agencies-must-share-custom-source-code-under-new-share-it-act/>

¹¹ Infrastructure as code – is the use of code to deliver and support computing infrastructure instead of a manual process.

Software factory - is a structured collection of related software assets that aids in producing computer software applications or software components according to specific, externally defined end-user requirements through an assembly process.

further develop the code to customize, modify, enhance, and add application capabilities to meet the entity's needs.¹²

Staff Analysis

Staff recommends the following recognition framework for shared software code:

- Reporting entities should not recognize software acquired from other federal entities at no cost. However, reporting entities should recognize costs incurred to further develop or enhance the software if such costs result in a distinct IUS component with significant additional capabilities.

Staff believes the Board can address accounting for software code shared between federal entities within the current guidance in SFFAS 10. If a federal entity uses shared software previously developed by another federal entity for free, then there is no additional cost to recognize as an intragovernmental IUS asset. However, if the federal entity incurs costs in using the shared software to further develop or enhance the software that results in an IUS component with significant additional capabilities, staff believes the federal entity should capitalize those costs in accordance with existing guidance in SFFAS 10, par. 3, 15-18, and 25-27.¹³

Furthermore, staff believes this would align with the asset concepts in SFFAC 5. If the federal entity used the shared software as a foundation to further develop a new IUS component or enhance the software with significant additional capabilities, the federal entity would have control over a unique software module, with measurable value, that would provide future economic benefits and services to the entity.

Finally, staff believes this framework aligns with prior Board decisions around an asset recognition framework for software licenses and implementation costs for cloud-service arrangements.¹⁴

Working Group Input

Working group members that reported that their federal entity has used shared software generally agreed that costs incurred to further develop and enhance the software code could be capitalized as assets if the costs resulted in an IUS component with additional capabilities from the original shared code. One working group member emphasized it was important that the guidance make it clear the federal entity could use the software

¹² Some federal entities also reported using free open-source software code in general when developing software applications for internal use. However, staff has focused this meeting topic on software assets shared among federal entities.

¹³ As part of this project, staff plans to research and recommend updates to development and enhancement guidance in SFFAS 10 as needed.

¹⁴ During the April 2024 meeting, the Board agreed that reporting entities should not capitalize implementation costs for cloud-service arrangements unless the implementation activities result in a distinct internal use software asset, in accordance with SFFAS 10, independent of the associated cloud-service arrangement.

as a building block to either develop new applications or additional capabilities (enhancement).

However, one working group member stated it could be difficult for federal entities to separate those development/enhancement costs from other service aspects of the contract.

Staff Recommendation

Staff believes the recommended guidance for accounting for shared software code would be practical to apply and fits with the existing guidance in SFFAS 10. Furthermore, staff believes the recommended accounting requirements would appropriately match costs incurred to develop a software asset with the future economic benefits and services of the asset and would improve transparency and accountability of costs that federal entities incur regarding shared software assets.

Question for the Board:

2. Does the Board agree with staff's recommended recognition framework for shared software code? Please provide your feedback on staff's analysis and recommendation.

Final Thoughts

In this paper, staff recommended accounting guidance frameworks around shared software assets in the federal government. Like the previous intangible asset and software license guidance deliberations, staff believes the recommended accounting frameworks for shared software assets would apply to the operating performance objectives in SFFAC 1, *Objectives of Federal Financial Reporting*. For example, staff believes the recommended frameworks would improve accountability over federal resources and would match expenses to the services provided by the asset.

Like cloud computing and software licenses, staff also believes there are potential reporting benefits with note disclosures for shared services/software. Staff plans to provide the Board note disclosure recommendations after the Board deliberates recognition guidance updates.

Next Steps

Pending Board feedback, staff will coordinate with stakeholders to further research and propose updates, as needed, to existing accounting guidance in SFFAS 10. Staff next plans to consider SFFAS 10 updates pertaining to the scope guidance paragraphs 2-3 and recognition guidance for internally developed software in paragraphs 10-18.

Prior Board Meeting Discussion Timeline

February 2022

At the February 2022 meeting, staff presented an issues paper that provided a framework for developing reporting guidance updates for software technology assets. Specifically, the issues paper recommended a scope and project plan for developing updates for software guidance based on specific needs identified during research. The scope consists of four major categories of software resources that staff plans to address individually in the following order:

1. Cloud-service arrangements
2. Shared services
3. Internal use software updates
4. Other software technology

The Board overwhelmingly supported staff's recommended scope and planned approach. Additionally, members supported staff's approach of addressing each scope category separately but noted that the categories would ultimately overlap and relate to one another.

The Board decided to first focus on reporting-guidance needs for cloud-service arrangements. Research indicated that federal entities are using cloud services at an increasing rate for operational purposes similar to internally developed software, generally due to the need for less investment risk and more flexibility to alter the amount and type of services received based on current needs. Therefore, it is critical to address reporting guidance for this commonly used software-technology resource to ensure reporting consistency throughout the federal government.

April 2022

At the April 2022 meeting, staff presented characteristics of cloud-service arrangements along with an asset-guidance framework for which to apply the characteristics. The framework analyzes previous asset-guidance decisions that will assist the Board when deliberating whether cloud-service arrangements can represent assets in the federal government. There were three primary takeaways from the discussion:

- The National Institute of Standards and Technology's (NIST) cloud-computing characteristics are widely accepted and used in the federal government.
- Based on the asset-guidance framework, it is appropriate to approach cloud-service arrangements as lease-type transactions that provide a federal entity

access to a provider's software technology resources for the federal entity to use as internal use software for a specified period.

- More research and outreach is needed to develop an informed decision on whether cloud-service arrangements can meet all of the essential characteristics of an asset established in SFFAC 5, Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements.

The Board generally supported using the NIST's cloud-computing characteristics for developing financial reporting guidance for cloud-service arrangements. Several members agreed with staff's observation that federal entities widely use the NIST cloud-computing characteristics and that it is practical to defer to the information technology (IT) professionals when describing cloud-service arrangements.

The Board generally agreed with staff's proposed asset-guidance framework and observation that it is particularly important to continue to research and deliberate whether cloud-service arrangements can meet the essential characteristics of an asset from SFFAC 5. Some members noted that for an asset to exist, the cloud-service arrangement must represent economic benefits and services that the federal government can use in the future. Other members stated that it is critical to determine whether a consumer of a cloud service could control access to the economic benefits and service of the underlying resource and, particularly, if the user could deny or regulate access to others in accordance with the arrangement.

June 2022

At the June 2022 meeting, two panelists from the General Services Administration (GSA) provided the Board an educational session on cloud-service arrangements. The panelists provided members an overview of the characteristics, service models, and deployment models of cloud computing and discussed ways that federal entities procure and pay for cloud services. Additionally, Board members, staff, and panelists discussed potential financial reporting needs and challenges associated with cloud-service arrangements.

August 2022

During the August 2022 meeting, the Board continued deliberations on reporting guidance for cloud-service arrangements. Staff presented an issues paper that proposed:

- A framework of cloud-service arrangements that could meet the essential characteristics of an asset for financial reporting purposes
- Potential benefits and challenges of reporting cloud service arrangements as assets in federal financial reports

The Board generally supported staff's analysis on whether certain cloud-service arrangement categories could meet the SFFAC 5 essential characteristics of an asset. Some members recommended more research to better understand how federal entities typically incur costs for long-term cloud-service arrangements. One member recommended more research and deliberation on whether cloud-service arrangements are typical service contracts or if they are more akin to leases or right-to-use assets. Another member recommended consideration of how other standard-setters made their determinations on asset reporting for cloud-service arrangements.

The Board also generally agreed with staff's analysis on the user benefits and preparer challenges with reporting cloud-service arrangements as assets in federal financial reports. One member stated that the identified reporting challenges were valid but thought that they could be overcome with proper guidance. A few members suggested further research and deliberation on the financial reporting benefits with note disclosure options versus asset recognition in financial statements. One member added that it was important to continue to seek out a wide range of federal financial report users that have an interest in cloud-service arrangement reporting.

October 2022

During the October 2022 meeting, the Board continued deliberations on reporting guidance for cloud-service arrangements. Staff presented an issues paper that:

- Analyzes how other standard-setting bodies have deliberated the differences between a service contract and a right-to-use asset, along with how those positions have influenced their cloud-service reporting guidance; and
- Examines FASAB's previous discussions of tangible right-to-use assets and service contracts and analyzes whether cloud-service arrangements in the federal environment resemble right-to-use assets or service contracts.

The Board had different opinions on whether multi-year cloud-service arrangements were right-to-use assets or service contracts. One member favored referring to cloud-service arrangements as service contracts because it was difficult to conceive how an entity could exclude others from using an intangible right-to-use asset. Another member stated that cloud services and other types of service contracts possessed a spectrum of right-to-use asset and service components and was concerned that deciding cloud-service arrangements are right-to-use assets could open the door to considering whether other types of service contracts include right-to-use assets.

Several members agreed it was reasonable to conceptualize cloud-service arrangements as right-to-use assets but were concerned that the associated preparer burden and lack of reporting benefits may not justify the need for asset recognition on the balance sheet. The members suggested that disclosures could adequately provide

information about the extent that federal entities use cloud-services for mission and operational needs versus purchasing or developing the IT resource internally.

April 2023

At the April 2023 meeting, staff presented a cost-benefit analysis that considered potential preparer burdens and user benefits for the following financial reporting options for cloud-service arrangements:

1. Balance sheet recognition
2. Commitment disclosure
3. Expense disclosure
4. Expense recognition only

The Board overwhelmingly agreed with the cost-benefit analysis and supported staff's recommendation that reporting guidance should require federal entities to disclose cloud-service expenses. Most members agreed that expense disclosure was optimal after considering the potential preparer burdens and user benefits of each reporting option. Additionally, the majority of members initially favored disclosing cloud-service expenses in required supplementary information rather than financial statement notes.

June 2023

At the June 2023 meeting, staff recommended definition and scope language for the Board's consideration in developing cloud-service arrangement standards. The purpose of the definition is only to inform readers about cloud-computing resources in the federal environment that the standards will address. However, the purpose of the scope is to provide authoritative guidance by explaining the economic transactions associated with cloud-service arrangements that would and would not apply to the standards.

The Board generally agreed to include the cloud-computing definition developed by the National Institute of Standards and Technology (NIST) Special Publication 800-145, The NIST Definition of Cloud Computing, in the draft reporting guidance proposal. The Board generally agreed that the NIST definition along with a reference to the special publication thoroughly explains cloud-computing resources and including the definition in the standards would help readers understand the reporting guidance. Two members voiced concern that the NIST definition was detailed and technical and, therefore, may not be the most effective definition for financial reporting guidance. One member generally preferred to use a more generic and broad definition to provide flexibility in the reporting guidance.

The Board also generally agreed to include staff's recommended scope language in the draft reporting guidance proposal. The scope includes the following guidance:

- A cloud-service arrangement is defined as a contract or agreement that provides a federal entity access to IT resources over a network, provided by a vendor in exchange for consideration, without the federal entity taking possession of the IT resource.
- The Statement applies to cloud services that federal entities acquire from nongovernmental vendors for internal use purposes in accordance with paragraph 2 of SFFAS 10, Accounting for Internal Use Software, as amended.
- The Statement does not apply to
 - cloud-based IT services acquired from other federal entities (such as, but not limited to shared services);
 - internally developed or purchased commercial off-the-shelf software that is reported in accordance with SFFAS 10 and TR 16, Implementation Guidance For Internal Use Software;
 - licensed software that allows the federal entity to possess and control the underlying software resource on its own hardware or systems that is reported in accordance with SFFAS 10 and TR 16; or
 - arrangements that provide the federal entity the right to control the use of property, plant, and equipment that is reported in accordance with SFFAS 54, Leases, as amended.

The Board generally agreed that the Board should revisit the definition and scope if a need arises while deliberating reporting requirements. Staff recommended that the Board eventually consider if the scope should also include shared services.

October 2023

At the October 2023 meeting, the Board deliberated financial statement recognition and note disclosure requirements for cloud-service arrangements.

The proposed recognition guidance would establish that reporting entities should apply existing liability and prepaid asset guidance to cloud-service arrangements and expense payments for cloud services as incurred. Additionally, the proposed guidance would require reporting entities to disclose total annual cloud-service expenses along with a general description, terms and conditions, and risks and benefits of significant cloud-service arrangements in financial statement notes.

The Board generally supported the proposed recognition guidance but preferred the guidance to directly reference existing liability and prepaid asset recognition

requirements in SFFAS 1, *Accounting for Selected Assets and Liabilities*. The Board had mixed opinions about whether the guidance should require reporting entities to disclose information on cloud-service arrangements.

Some members supported the requirements to disclose annual cloud-service expenses along with some of the proposed qualitative information on significant cloud-service arrangements. The members viewed cloud services as significant to federal IT spending and supported a forward-looking approach with issuing reporting guidance to address a fundamental change with how federal agencies use software technology resources.

However, some members did not support any of the proposed note disclosure requirements because they viewed the requirements as too burdensome relative to the benefits. The members questioned why the Board would require the note disclosures for cloud-service arrangements when the Board does not require reporting that level of information for other service contracts.

Some members did not believe that annual cloud-service costs would ever be material relative to what the federal government spends each year. Other members acknowledged that may be true for government-wide and some component entity financial reports. However, the members believed that the information would be useful to some stakeholders and thought it beneficial for reporting entities to have the reporting guidance to apply if cloud-service arrangements are determined by a reporting entity to be qualitatively or quantitatively material now or in the future.

For now, staff will defer disclosure guidance proposals and focus on recognition guidance needs for the software-technology project topics.

April 2024

At the April 2024 meeting, the Board deliberated accounting options for implementation costs associated with cloud-service arrangements. The majority of members agreed that reporting entities should not capitalize implementation costs for cloud-service arrangements unless the implementation activities result in a distinct internal use software asset, in accordance with SFFAS 10, *Accounting for Internal Use Software*, independent of the associated cloud-service arrangement.

August 2024

At the August 2024 meeting, the Board discussed an accounting guidance framework for software licenses. The framework includes the following working definitions:

- A software license is a legal instrument that provides a federal entity the right to use a software resource under specific terms and conditions. Software licenses allow the federal entity to install and control the underlying software on its own IT

hardware. This term does not apply to software that federal entities access over a network on a hosted platform as part of a cloud-based SaaS arrangement.

- A perpetual software license is a non-expiring license that provides a federal entity the right to use a software resource indefinitely.
- A term-based software license is a temporary license that provides a federal entity the right to use a software resource for a specified period.

The Board also discussed key distinctions between a software license and cloud-service arrangement.

December 2024

At the December 2024 meeting, the Board agreed to move forward with the following accounting guidance framework for software licenses:

Software license Guidance Scope - This guidance applies to internal use software that a reporting entity has the right and ability to either run the software on its own hardware or contract with another party, unrelated to the vendor, to host the software.

Perpetual Software License Recognition and Measurement - Reporting entities should account for perpetual software licenses as a purchase of software and capitalize and amortize the cost over its estimated useful life. Reporting entities should recognize a liability for any software licensing fees not paid upon acquisition of the license.

Term-based Software License Recognition and Measurement - If a term-based software license has a useful life of two years or more, the reporting entity should recognize an asset for the cost of the license and a liability for any software licensing fees not paid upon acquisition of the license. The useful life of the asset should not exceed the binding arrangements of the contractual or legal terms of the software license. If the binding arrangements are for a limited term that can be renewed, the useful life of the asset should include the renewal period(s) only if the cost to renew is nominal.

Some members suggested that the Board also consider disclosure guidance to address reporting needs for software licenses with option periods, such as disclosing probable future costs associated with renewal periods. Additionally, some members emphasized that the Board should also consider accounting guidance for software license transactions that do not meet the useful life threshold for asset recognition to ensure accounting consistency across federal entities.