



ACCOUNTING STANDARDS UPDATE

No. 2025-06

September 2025

Intangibles—Goodwill and Other— Internal-Use Software (Subtopic 350-40)

Targeted Improvements to the Accounting for
Internal-Use Software

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

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Financial Accounting Standards Board
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CONTENTS

	Page Numbers
Summary.....	1–4
Amendments to the <i>FASB Accounting Standards Codification</i> ®	5–40
Background Information and basis for conclusions	41–75
Amendments to the GAAP Taxonomy	76

Summary

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The Board is issuing this Update to modernize the accounting for software costs that are accounted for under Subtopic 350-40, Intangibles—Goodwill and Other—Internal-Use Software (referred to as “internal-use software”).

Feedback from preparer and practitioner stakeholders on the 2021 FASB Invitation to Comment, *Agenda Consultation*, indicated that the accounting for software costs should be a top priority for the Board. Those stakeholders encouraged the Board to better align the accounting with how software is developed because the current guidance is outdated and lacks relevance given the evolution of software development. Specifically, many entities have shifted from using a prescriptive and sequential development method (for example, waterfall) to using an incremental and iterative development method (for example, agile). Stakeholders stated that the current internal-use software accounting requirements do not specifically address software developed using an incremental and iterative method. As a result, stakeholders stated that there are challenges in determining when to begin capitalizing internal-use software costs.

Considering this feedback, the Board decided to make targeted improvements to Subtopic 350-40 to increase the operability of the recognition guidance considering different methods of software development.

Who Is Affected by the Amendments in This Update?

The amendments in this Update apply to all entities subject to the internal-use software guidance in Subtopic 350-40. The amendments also apply to all entities that account for website development costs in accordance with Subtopic 350-50, Intangibles—Goodwill and Other—Website Development Costs.

The amendments in this Update do not affect software costs subject to Subtopic 985-20, Software—Costs of Software to Be Sold, Leased, or Marketed (referred to as “external-use software”).

What Are the Main Provisions?

The amendments in this Update remove all references to prescriptive and sequential software development stages (referred to as “project stages”) throughout Subtopic 350-40. Therefore, an entity is required to start capitalizing software costs when both of the following occur:

1. Management has authorized and committed to funding the software project.
2. It is probable that the project will be completed and the software will be used to perform the function intended (referred to as the “probable-to-complete recognition threshold”).

In evaluating the probable-to-complete recognition threshold, an entity is required to consider whether there is significant uncertainty associated with the development activities of the software (referred to as “significant development uncertainty”). The two factors to consider in determining whether there is significant development uncertainty are whether:

1. The software being developed has technological innovations or novel, unique, or unproven functions or features, and the uncertainty related to those technological innovations, functions, or features, if identified, has not been resolved through coding and testing.
2. The entity has determined what it needs the software to do (for example, functions or features), including whether the entity has identified or continues to substantially revise the software’s significant performance requirements.

The amendments in this Update specify that the disclosures in Subtopic 360-10, Property, Plant, and Equipment—Overall, are required for all capitalized internal-use software costs, regardless of how those costs are presented in the financial statements. Additionally, the amendments clarify that the intangibles disclosures in paragraphs 350-30-50-1 through 50-3 are not required for capitalized internal-use software costs.

Furthermore, the amendments in this Update supersede the website development costs guidance and incorporate the recognition requirements for website-specific development costs from Subtopic 350-50 into Subtopic 350-40.

How Do the Main Provisions Differ from Current Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

Under current GAAP, entities are required to capitalize development costs incurred for internal-use software depending on the nature of the costs and the project stage during which they occur. Stakeholders said that applying this guidance can be challenging because entities have trouble differentiating between the project stages, particularly in an iterative development environment. The amendments in this Update improve the operability of the guidance by removing all references to software development project stages so that the guidance is neutral to different software development methods, including methods that entities may use to develop software in the future.

Considering stakeholder feedback, the Board expects that capitalization of internal-use software costs generally will not change significantly for most types of software under the amendments in this Update. For the development of software to be provided via a cloud computing arrangement (CCA), the Board expects that the amendments could result in a decrease in software capitalization. This decrease in capitalization will better align with the accounting outcomes for the development of software sold via an on-premises license (under Subtopic 985-20), which could help to establish greater consistency in financial reporting outcomes in most cases and, in turn, benefit investors that analyze entities that primarily develop software.

When Will the Amendments Be Effective and What Are the Transition Requirements?

The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2027, and interim reporting periods

within those annual reporting periods. Early adoption is permitted as of the beginning of an annual reporting period.

The amendments in this Update permit an entity to apply the new guidance using any of the following transition approaches:

1. A prospective transition approach
2. A modified transition approach that is based on the status of the project and whether software costs were capitalized before the date of adoption
3. A retrospective transition approach.

Under a prospective transition approach, an entity should apply the amendments in this Update to new software costs incurred as of the beginning of the period of adoption for all projects, including in-process projects.

Under a modified transition approach, an entity should apply the amendments in this Update on a prospective basis to new software costs incurred (for all projects, including costs incurred for in-process projects), except for in-process projects that, as of the date of adoption, the entity determines do not meet the capitalization requirements under the amendments but meet the capitalization requirements under current guidance. For those in-process projects, an entity should derecognize any capitalized costs through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the date of adoption.

Under a retrospective transition approach, an entity should recast comparative periods and recognize a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the first period presented.

Amendments to the *FASB Accounting Standards Codification*[®]

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–15. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is struck-out.

Amendments to Master Glossary

2. Supersede the Master Glossary term *Preliminary Project Stage*, with a link to transition paragraph 350-40-65-4, as follows:

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.~~

3. Add the new Master Glossary term *Performance Requirements*, with a link to transition paragraph 350-40-65-4, as follows:

Performance Requirements

Performance requirements are what an entity needs the software to do (for example, functions or features).

4. Add the Master Glossary term *Probable* to Subtopic 350-40 as follows:

Probable

The future event or events are likely to occur.

Amendments to Subtopic 350-40

5. Amend paragraphs 350-40-05-1D, 350-40-15-2, 350-40-25-1 and its related heading, 350-40-25-4 through 25-5, 350-40-25-12 through 25-13 and their related heading, 350-40-30-1 and its related heading, 350-40-35-3, 350-40-50-1, and 350-40-55-4, supersede paragraphs 350-40-05-7, 350-40-25-2 through 25-3 and their related heading, 350-40-25-6 through 25-11 and their related headings, and 350-40-55-3, and add paragraphs 350-40-25-12A, 350-40-25-17A through 25-17J and their related headings, and 350-40-55-5 through 55-21 and their related headings, with a link to transition paragraph 350-40-65-4, as follows:

Intangibles—Goodwill and Other—Internal-Use Software

Overview and Background

350-40-05-1C The Internal-Use Software Subtopic presents guidance in the following Subsections:

- a. General
- b. Implementation Costs of a Hosting Arrangement That Is a Service Contract.

350-40-05-1D 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.

350-40-05-7 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Paragraph 350-40-55-3 illustrates the various stages and related processes of computer software development.~~

Scope and Scope Exceptions

> Transactions

350-40-15-2 The guidance in the General Subsections of 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.
- e. Costs incurred to develop a website. **[Content moved from paragraph 350-50-15-2(a)]**

Recognition

General

> Costs to Be Expensed as Incurred ~~Preliminary Project Stage~~

350-40-25-1 Internal and external costs incurred prior to meeting the capitalization requirements in paragraphs 350-40-25-12 through 25-12A ~~during the preliminary project stage~~ shall be expensed as they are incurred.

> ~~Application Development Stage~~

350-40-25-2 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Internal and external costs incurred to develop internal-use computer software during the application development stage shall be capitalized.~~

350-40-25-3 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs to develop or obtain software that allows for access to or conversion of old data by new systems shall also be capitalized.~~ **[Content amended and moved to paragraph 350-40-30-1(d)]**

350-40-25-4 Internal and external training ~~Training costs are not internal-use software development costs and, if incurred during this stage, shall be expensed as incurred.~~

350-40-25-5 Data conversion costs, except as noted in paragraph 350-40-30-1(d) ~~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.

> ~~Postimplementation-Operation Stage~~

350-40-25-6 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Internal and external training costs and maintenance costs during the postimplementation-operation stage shall be expensed as incurred.~~

> ~~Upgrades and Enhancements~~

350-40-25-7 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~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. [Content amended and moved to paragraph 350-40-25-17A]~~

350-40-25-8 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Internal costs incurred for upgrades and enhancements shall be expensed or capitalized in accordance with paragraphs 350-40-25-1 through 25-6. [Content amended and moved to paragraph 350-40-25-17B]~~

350-40-25-9 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Internal costs incurred for maintenance shall be expensed as incurred. [Content amended and moved to paragraph 350-40-25-17C]~~

350-40-25-10 Paragraph superseded by Accounting Standards Update No. 2025-06.~~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. [Content moved to paragraph 350-40-25-17D]~~

350-40-25-11 Paragraph superseded by Accounting Standards Update No. 2025-06.~~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. [Content amended and moved to paragraph 350-40-25-17E]~~

> Capitalization of CostsCost

350-40-25-12 Capitalization of costs shall begin when both of the following occur:

- a. Subparagraph superseded by Accounting Standards Update No. 2025-06. Preliminary project stage is completed.
- b. Management, with the relevant authority, implicitly or explicitly authorizes and commits to funding a computer software project.~~project~~ and it is probable that the project will be completed and the software will be used to perform the function intended. **[Content amended and moved to paragraph 350-40-25-12(c)]** Examples of authorization and commitment to funding a computer software project 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. **[Content amended as shown and moved from paragraph 350-40-25-12]**
- c. ~~It and it is~~ **{add glossary link}**probable**{add glossary link}** that the project will be completed and the software will be used to perform the function intended (referred to as the probable-to-complete recognition threshold). **[Content amended as shown and moved from paragraph 350-40-25-12(b)]** In evaluating whether the probable-to-complete recognition threshold has been met, an entity shall assess whether there is significant uncertainty associated with the development activities of the software (referred to as significant development uncertainty) in accordance with paragraph 350-40-25-12A.

~~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.~~
[Content amended and moved to paragraph 350-40-25-12(b)]

350-40-25-12A If significant development uncertainty exists, the probable-to-complete recognition threshold in paragraph 350-40-25-12(c) is not met until that significant development uncertainty has been resolved. Significant development uncertainty exists if either of the following factors is present:

- a. The software being developed has technological innovations or novel, unique, or unproven functions or features, and the uncertainty related to those technological innovations, functions, or features, if identified, has not been resolved through coding and testing.
- b. The significant **performance requirements** of the software have not been identified, or the identified significant performance requirements continue to be substantially revised.

For some types of software projects, the assessment of whether significant development uncertainty exists will be straightforward, such as illustrated in Example 1 (see paragraphs 350-40-55-5 through 55-8). For other types of software projects, the assessment will be more complex, such as illustrated in Example 3 (see paragraphs 350-40-55-13 through 55-17). If significant development uncertainty does not exist or if there was significant development uncertainty that has been resolved, an entity shall evaluate the requirements in paragraph 350-40-25-12 to determine when to begin capitalizing costs.

350-40-25-13 If the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are no longer met for software being developed~~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.

350-40-25-14 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.

350-40-25-15 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.

350-40-25-17 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.

> Upgrades and Enhancements

350-40-25-17A 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 evaluated for capitalization~~capitalized~~ in accordance with paragraphs ~~350-40-25-17B~~~~350-40-25-8 through 25-17E~~~~25-10~~, it must be probable that those expenditures will result in additional functionality. **[Content amended as shown and moved from paragraph 350-40-25-7]**

350-40-25-17B Internal and external costs incurred for upgrades and enhancements shall be expensed or capitalized in accordance with paragraphs ~~350-40-25-1 through 25-6~~, ~~350-40-25-4 through 25-5~~, ~~350-40-25-12 through 25-14~~, and ~~350-40-25-17~~. **[Content amended as shown and moved from paragraph 350-40-25-8]**

350-40-25-17C Internal and external costs incurred for maintenance shall be expensed as incurred. **[Content amended as shown and moved from paragraph 350-40-25-9]**

350-40-25-17D 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. **[Content moved from paragraph 350-40-25-10]**

350-40-25-17E 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~~, ~~350-40-25-4 through 25-5~~, ~~350-40-25-12 through 25-14~~, and ~~350-40-25-17~~. 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. **[Content amended as shown and moved from paragraph 350-40-25-11]**

> Additional Considerations for Website Development Costs

350-40-25-17F Fees incurred for website hosting, which involve the payment of a specified, periodic fee to an internet service provider in return for hosting the website on its server(s) connected to the internet, generally are expensed over the period of benefit. **[Content moved from paragraph 350-50-25-5]**

350-40-25-17G Accounting for website content involves issues that also apply to other forms of content or information that are not unique to websites. **[Content moved from paragraph 350-50-25-10]** Costs to input content into a website shall be expensed as incurred. **[Content moved from paragraph 350-50-25-11]** Content refers to information included on the website, which may be textual or graphical in nature (although the specific graphics described in paragraph 350-40-25-17H~~350-50-55-4~~ are excluded from content). For example, articles, product photos, maps, and stock quotes and charts are all forms of content. Content may reside in separate databases that are integrated into (or accessed from) the web page with software, or it may be coded directly into the web pages. **[Content amended as shown and moved from paragraph 350-50-55-6]**

350-40-25-17H Graphics are a component of software. The costs of developing initial graphics shall be evaluated for capitalization under this Subtopic~~accounted for under Subtopic 350-40~~ for internal-use software, and Subtopic 985-20 for software marketed externally. **[Content amended as shown and moved from paragraph 350-50-25-8]** For purposes of this Subtopic, graphics involve the overall design of the web page (use of borders, background and text colors, fonts, frames, buttons, and so forth) that affect the look and feel of the web page and generally remain consistent regardless of changes made to the content. **[Content moved from paragraph 350-50-55-4]**

350-40-25-17I Costs to register the website with internet search engines represent advertising costs and shall be expensed as incurred under paragraph 720-35-25-1. **[Content moved from paragraph 350-50-25-17]**

350-40-25-17J Costs to obtain and register an internet domain shall be evaluated for capitalization~~capitalized~~ under Section 350-30-25. **[Content amended as shown and moved from paragraph 350-50-25-7]**

Implementation Costs of a Hosting Arrangement That Is a Service Contract

350-40-25-18 An entity shall apply the General Subsection of this Section as though the **hosting arrangement** that is a service contract were an internal-use computer software project to determine when implementation costs of a hosting arrangement that is a service contract are and are not capitalized.

Initial Measurement

> Capitalizable Costs~~Cost~~

350-40-30-1 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. Design~~design of chosen path, including software configuration and software ~~interfaces~~interfaces, ~~Coding~~coding, ~~Installation to hardware~~installation to hardware, and ~~Testing~~testing, including parallel processing phase. **[Content amended as shown and moved from paragraph 350-40-55-3(b)(1) through (b)(4)]**
- c. Interest costs incurred while developing internal-use computer software. Interest shall be capitalized in accordance with the provisions of Subtopic 835-20.
- d. Costs to develop or obtain software that allows for access to or conversion of old data by new systems ~~shall also be capitalized.~~ **[Content amended as shown and moved from paragraph 350-40-25-3]**

350-40-30-2 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.

350-40-30-3 General and administrative costs and overhead costs shall not be capitalized as costs of internal-use software.

Subsequent Measurement

> Impairment

350-40-35-3 If the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are~~When it is no longer met~~~~probable that computer software being developed will be completed and placed in service for software being developed~~, 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 capitalization requirements in paragraphs 350-40-25-12 through 25-12A are~~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.

Disclosure

350-40-50-1 The disclosure requirements in Subtopic 360-10 on property, plant, and equipment apply to capitalized costs accounted for under this Subtopic, regardless of how those costs are presented in the financial

statements. For purposes of applying those disclosure requirements, any disclosures in Subtopic 360-10 related to property, plant, and equipment shall be applied to internal-use software costs and related amortization.~~The General Subsection of this Subtopic does not require any incremental disclosures.~~ Additionally, disclosure~~Disclosure~~ shall be made in accordance with existing authoritative literature including the following:

- a. Topic 275
- b. Subtopic 730-10
- c. Topic 235
- d. Subparagraph superseded by Accounting Standards Update No. 2025-06.~~Subtopic 360-10.~~

Implementation Guidance and Illustrations

> Implementation Guidance

350-40-55-3 Paragraph superseded by Accounting Standards Update No. 2025-06.~~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~~ **[Content amended and moved to paragraph 350-40-30-1(b)]**
 - 2. ~~Coding~~ **[Content amended and moved to paragraph 350-40-30-1(b)]**
 - 3. ~~Installation to hardware~~ **[Content amended and moved to paragraph 350-40-30-1(b)]**
 - 4. ~~Testing, including parallel processing phase.~~ **[Content amended and moved to paragraph 350-40-30-1(b)]**
- c. ~~Postimplementation operation stage:~~
 - 1. ~~Training~~
 - 2. ~~Application maintenance.~~

350-40-55-4 This Subtopic recognizes that certain development activities such as 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 meeting the capitalization requirements in paragraphs 350-40-25-12 through 25-12A 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 subsequent to meeting the capitalization requirements in paragraphs 350-40-25-12 through 25-12A and before the software project is substantially complete and ready for its intended use in the application development stage, it should be expensed as incurred as required in paragraph 350-40-25-4 paragraphs 350-40-25-2 through 25-6.

> Illustrations

• > Example 1: Implementation and Customization of an Enterprise Resource Planning System

350-40-55-5 On February 1, 20X3, a professional services company starts internal discussions to transform its information technology by implementing an enterprise resource planning system to support finance, human resources, accounting, and client relationships.

350-40-55-6 After researching different solutions and performing its due diligence procedures, management executes a contract with a third party on August 1, 20X3, to implement and customize a hybrid solution that offers on-premises software and cloud computing services for the enterprise resource planning system. Within this solution, the third party offers different functionality and features, and the company will have to make customization decisions throughout the development process to select which functionality and features it wants included.

350-40-55-7 The company assesses whether the internal and external costs to implement and customize the enterprise resource planning system meet the capitalization requirements in paragraphs 350-40-25-12 through 25-12A, as follows:

- a. As part of its assessment under paragraph 350-40-25-12(c), the company evaluates whether there is significant development uncertainty

in accordance with paragraph 350-40-25-12A. As of August 1, 20X3, the company determines that:

1. It has identified the significant **performance requirements** and does not expect to continue to substantially revise those requirements because the only expected customization is selecting from existing functionality and features.
2. The software being developed does not have technological innovations or novel, unique, or unproven functions or features because the company has selected a developed solution.

Therefore, as of August 1, 20X3, the company determines that significant development uncertainty does not exist.

- b. The company evaluates the requirements in paragraph 350-40-25-12 to determine when to begin capitalizing software costs:

1. The company determines that management authorized and committed to funding the software project on August 1, 20X3, when it executed the contract with the third party.
2. Considering all other relevant facts and circumstances (for example, the company has engaged an established and experienced third party to implement and customize the software), as of August 1, 20X3, the company determines that it is **probable** that the software project will be completed and the software will be used to perform the function intended.

350-40-55-8 As a result, on August 1, 20X3, the company determines that the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are met, and it begins capitalizing eligible software costs, including those related to implementation and customization of the on-premises software license and those related to implementation of the cloud computing service features of the hybrid solution.

• > Example 2: Development of a Mobile Application

350-40-55-9 A company is in the process of internally developing X-Crowd, which is a mobile application that will allow users to see how crowded a restaurant or store is on the basis of a user's real-time input. An internet connection is required to be able to access the application.

350-40-55-10 On February 1, 20X1, management approved funding for internal development of the application. However, the company has not yet identified what functions and features would be included in the application. Through November 30, 20X1, the company continues to develop the functions and features of the application, including getting feedback on preliminary product versions from user groups and modifying the development of those functions and features to incorporate the feedback. On December 1, 20X1, management determines that it has identified the significant performance requirements (the significant functions and features it needs the application to have), and it does not anticipate substantial changes to those requirements. Throughout the development of X-Crowd, management determines that the application does not have technological innovations or novel, unique, or unproven functions or features.

350-40-55-11 The company assesses whether the internal and external costs to develop the application meet the capitalization requirements in paragraphs 350-40-25-12 through 25-12A, as follows:

- a. As part of its assessment under paragraph 350-40-25-12(c), the company evaluates whether there is significant development uncertainty in accordance with paragraph 350-40-25-12A. As of February 1, 20X1, the company determines that:
 1. It has not yet identified the significant performance requirements.
 2. The software being developed does not have technological innovations or novel, unique, or unproven functions or features.

Therefore, as of February 1, 20X1, the company determines that significant development uncertainty exists and, in accordance with paragraph 350-40-25-12A, the software project does not meet the requirements to begin capitalizing software costs in paragraph 350-40-25-12(c).
- b. As of December 1, 20X1, the company determines that:
 1. It has identified the significant performance requirements and does not expect to continue to substantially revise those requirements.
 2. The software being developed does not have technological innovations or novel, unique, or unproven functions or features.

Therefore, as of December 1, 20X1, the company determines that significant development uncertainty has been resolved.

- c. As of December 1, 20X1, the company evaluates the requirements in paragraph 350-40-25-12 to determine when to begin capitalizing software costs:
1. The company determines that management authorized and committed to funding the software project on February 1, 20X1, when it approved funding for internal development of the application.
 2. Considering all other relevant facts and circumstances, as of December 1, 20X1, the company determines that it is probable that the software project will be completed and the software will be used to perform the function intended.

350-40-55-12 As a result, on December 1, 20X1, the company determines that the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are met, and it begins capitalizing eligible software costs.

• > Example 3: Development of a Novel Technology

350-40-55-13 On January 1, 20X1, a software development company starts discussions to develop software with novel functionality.

350-40-55-14 On February 1, 20X1, management completes its due diligence procedures, approves a budget to internally develop the software, and allocates an internal development team to start developing the novel software. At the time that the company started discussions and management approved a budget, the software still had novel functionality.

350-40-55-15 On March 1, 20X3, the company resolves the uncertainty related to the novel functionality through coding and testing. Additionally, on March 1, 20X3, the company determines that it does not expect substantial changes to the identified significant performance requirements (the significant functions and features) included in the software. On April 1, 20X3, the company determines that all substantial testing is completed.

350-40-55-16 The company assesses whether the internal and external costs to develop the software meet the capitalization requirements in paragraphs 350-40-25-12 through 25-12A, as follows:

- a. As part of its assessment under paragraph 350-40-25-12(c), the company evaluates whether there is significant development uncertainty

in accordance with paragraph 350-40-25-12A. As of February 1, 20X1, the company determines that:

1. It has not yet identified the significant performance requirements.
2. The software being developed has novel functionality and that functionality has not been resolved through coding and testing.

Therefore, as of February 1, 20X1, the company determines that significant development uncertainty exists and, in accordance with paragraph 350-40-25-12A, the software project does not meet the requirements to begin capitalizing software costs in paragraph 350-40-25-12(c).

b. As of March 1, 20X3, the company determines that:

1. It has identified the significant performance requirements and does not expect to continue to substantially revise those requirements.
2. The uncertainty related to the novel functionality has been resolved through coding and testing.

Therefore, as of March 1, 20X3, the company determines that significant development uncertainty has been resolved.

c. As of March 1, 20X3, the company evaluates the requirements in paragraph 350-40-25-12 to determine when to begin capitalizing software costs:

1. The company determines that management authorized and committed to funding the software project on February 1, 20X1, when it approved a budget and allocated an internal development team.
2. Considering all other relevant facts and circumstances, as of March 1, 20X3, the company determines that it is probable that the software project will be completed and the software will be used to perform the function intended.

350-40-55-17 As a result, on March 1, 20X3, the company determines that the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are met, and it begins capitalizing eligible software costs. On April 1, 20X3, the company determines that the software project is substantially complete and ready for its intended use because all substantial testing has been completed. Therefore, the company ceases capitalizing eligible software costs on April 1, 20X3, in accordance with paragraph 350-40-25-14.

• > Example 4: Development of a Website

350-40-55-18 An animal rescue organization starts discussions on June 15, 20X5, to develop a website that will be used to share information with users of

the organization, including hours of operation, contact details, animals available for adoption, and standard adoption procedures.

350-40-55-19 After researching different website developers and performing its due diligence procedures, management executes a contract with a third party on August 1, 20X5, to develop a website for the organization. The third party is an established website developer and offers different templates that the organization can use to create its website. In addition to website development fees paid to the third party, the organization incurs costs:

- a. To obtain and register an internet domain
- b. To input content into the website
- c. To develop initial graphics for the website
- d. To register the website with internet search engines
- e. For ongoing website hosting fees.

350-40-55-20 The organization assesses whether the internal and external costs to develop the website meet the capitalization requirements in paragraphs 350-40-25-12 through 25-12A, as follows:

- a. As part of its assessment under paragraph 350-40-25-12(c), the organization evaluates whether there is significant development uncertainty in accordance with paragraph 350-40-25-12A. As of August 1, 20X5, the organization determines that:
 - 1. It has identified the significant performance requirements and does not expect to continue to substantially revise those requirements because the website will be created from existing templates that the organization can use to share the information described in paragraph 350-40-55-18.
 - 2. The website being developed does not have technological innovations or novel, unique, or unproven functions or features because it will be developed from existing templates.Therefore, as of August 1, 20X5, the organization determines that significant development uncertainty does not exist.
- b. The organization evaluates the requirements in paragraph 350-40-25-12 to determine when to begin capitalizing costs:
 - 1. The organization determines that management authorized and committed to funding the development of the website on August 1, 20X5, when it executed the contract with the third party.

2. Considering all other relevant facts and circumstances (for example, the organization has engaged an established and experienced third party to develop the website), as of August 1, 20X5, the organization determines that it is probable that the project will be completed and the website will be used to perform the function intended.

350-40-55-21 As a result, on August 1, 20X5, the organization determines that the capitalization requirements in paragraphs 350-40-25-12 through 25-12A are met, and it begins capitalizing eligible costs. In evaluating which costs are eligible for capitalization, the organization determines the following:

- a. Fees paid to the third party for services to develop the website are evaluated for capitalization in accordance with paragraph 350-40-30-1.
- b. Costs incurred to obtain and register the internet domain are evaluated for capitalization in accordance with paragraph 350-40-25-17J.
- c. Costs incurred to input content into the website are expensed as incurred in accordance with paragraph 350-40-25-17G.
- d. Costs incurred to develop initial graphics for the website are evaluated for capitalization in accordance with paragraph 350-40-25-17H.
- e. Costs incurred to register the website with internet search engines are expensed as incurred in accordance with paragraph 350-40-25-17I.
- f. Ongoing website hosting fees are expensed over the period of benefit in accordance with paragraph 350-40-25-17F.

6. Add paragraph 350-40-65-4 and its related heading as follows:

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2025-06, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Targeted Improvements to the Accounting for Internal-Use Software*

350-40-65-4 The following represents the transition and effective date information related to Accounting Standards Update No. 2025-06, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Targeted Improvements to the Accounting for Internal-Use Software*:

Effective date and early adoption

- a. All entities shall apply the pending content that links to this paragraph for annual reporting periods beginning after December 15, 2027, and interim reporting periods within those annual reporting periods.
- b. Early adoption of the pending content that links to this paragraph is permitted in an interim or annual reporting period in which financial statements have not yet been issued or made available for issuance. If an entity adopts the pending content that links to this paragraph in an interim reporting period, it shall adopt the pending content as of the beginning of the annual reporting period that includes that interim reporting period.

Transition methods

- c. An entity shall apply the pending content that links to this paragraph using one of the following transition methods:
 - 1. Prospectively to new software costs incurred for all projects, including costs incurred for in-process projects, during annual reporting periods (and interim reporting periods within those annual reporting periods) beginning after the date that the pending content that links to this paragraph is adopted.
 - 2. On a modified transition approach, as follows:
 - i. Prospectively to new software costs incurred (for all projects, including costs incurred for in-process projects), excluding those described in (c)(2)(ii), during annual reporting periods (and interim reporting periods within those annual reporting periods) beginning after the date that the pending content that links to this paragraph is adopted.
 - ii. For an in-process project that, as of the date that the pending content that links to this paragraph is adopted, the entity determines does not meet the capitalization requirements in paragraphs 350-40-25-12 through 25-12A but had met the capitalization requirements before that date, the entity shall derecognize capitalized costs for that in-process project through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the annual reporting period in which the pending content that links to this paragraph is adopted.
 - 3. Retrospectively through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate

components of equity or net assets in the statement of financial position) as of the beginning of the first period presented.

Transition disclosures

- d. An entity that applies the pending content that links to this paragraph prospectively in accordance with (c)(1) shall provide the transition disclosures required by paragraph 250-10-50-1(a) in both the interim reporting period (if applicable) and the annual reporting period of the change.
- e. An entity that applies the pending content that links to this paragraph using a modified transition approach in accordance with (c)(2) shall provide the transition disclosures required by paragraph 250-10-50-1(a) and 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 annual reporting period in which the pending content that links to this paragraph is adopted in both the interim reporting period (if applicable) and the annual reporting period of the change.
- f. An entity that applies the pending content that links to this paragraph retrospectively in accordance with (c)(3) shall provide the transition disclosures required by paragraph 250-10-50-1(a) through (b)(1), (b)(2) for any prior periods retrospectively adjusted, and (b)(3) and (c)(2) in both the interim reporting period (if applicable) and the annual reporting period of the change.

Amendments to Subtopic 350-30

7. Amend paragraphs 350-30-15-3 through 15-4, with a link to transition paragraph 350-40-65-4, as follows:

Intangibles—Goodwill and Other—General Intangibles Other Than Goodwill

Scope and Scope Exceptions

> Transactions

350-30-15-3 The guidance in this Subtopic applies to the following:

- a. Intangible assets acquired individually or with a group of other assets (but not the recognition and initial measurement of those acquired in a business combination, acquired in an **acquisition by a not-for-profit entity**, or recognized by a **joint venture** upon formation)
- b. Intangible assets (other than goodwill) that an entity recognizes in accordance with Subtopic 805-20, 805-60, or 958-805 after they have been initially recognized and measured, except for those identified in paragraph 350-30-15-4
- c. Subparagraph not used.
- d. Costs of internally developing identifiable intangible assets that an entity recognizes as assets.

The disclosure requirements of paragraphs 350-30-50-1 through 50-3 also apply to capitalized software costs related to software to be sold, leased, or marketed that an entity recognizes in accordance with Subtopic 985-20.

350-30-15-4 The guidance in this Subtopic does not apply to the following:

- a. Subparagraph not used.
- b. Subparagraph superseded by Accounting Standards Update No. 2010-07.
- c. Except for certain disclosure requirements as noted in paragraph 350-30-15-3, capitalized software costs that an entity recognizes in accordance with Subtopic 985-20.
- d. Except for disclosures required by paragraph 944-805-50-1 (however, an insurance entity need not duplicate disclosures that also are required by paragraphs 944-30-50-2A through 50-2B), intangible assets recognized for acquired insurance contracts under the requirements of Subtopic ~~944-805~~944-805.
- e. Crypto assets accounted for in accordance with Subtopic 350-60, except for recognition and initial measurement of crypto assets.
- f. Capitalized software costs that an entity recognizes in accordance with Subtopic 350-40 on internal-use software.

Amendments to Subtopic 350-50

8. Supersede Subtopic 350-50, Intangibles—Goodwill and Other—Website Development Costs, with a link to transition paragraph 350-40-65-4, as follows:

Intangibles—Goodwill and Other—Website Development Costs

Overview and Background

General

350-50-05-1 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~This Subtopic provides guidance on accounting for costs incurred to develop a website, including whether to capitalize or expense the following types of costs:~~

- ~~a. Costs incurred in the planning stage~~
- ~~b. Costs incurred in the website application and infrastructure development stage~~
- ~~c. Costs incurred to develop graphics~~
- ~~d. Costs incurred to develop content~~
- ~~e. Costs incurred in the operating stage.~~

Scope and Scope Exceptions

General

> ~~Overall Guidance~~

350-50-15-1 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~This Subtopic follows the same Scope and Scope Exceptions as outlined in the Overall Subtopic, see Section 350-10-15, with specific transaction qualifications noted below.~~

> ~~Transactions~~

350-50-15-2 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The guidance in this Subtopic applies to the following transactions and activities:~~

- ~~a. Costs incurred to develop a website. [Content moved to paragraph 350-40-15-2(e)]~~

350-50-15-3 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The guidance in this Subtopic does not apply to the following transactions and activities:~~

- ~~a. The cost of hardware~~
- ~~b. Acquisitions of servers and related hardware infrastructure.~~

Recognition

General

350-50-25-1 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The guidance in this Section refers to various website development stages. See Section 350-50-55 for details regarding the types of costs and activities incurred during those stages.~~

> Costs Incurred in the Planning Stage

350-50-25-2 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Regardless of whether the website planning activities specifically relate to software, all costs incurred in the planning stage shall be expensed as incurred.~~

> Costs Incurred in the Website Application and Infrastructure Development Stage

350-50-25-3 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The discussion of website application and infrastructure development assumes that any software is developed for the entity's internal needs and no plan exists or is being developed to market the software externally.~~

350-50-25-4 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~All costs relating to software used to operate a website shall be accounted for under Subtopic 350-40 unless a plan exists or is being developed to market the software externally. Software for which a plan exists or is being developed to market the software externally is subject to Subtopic 985-20, and costs associated with the development of that software shall be expensed until technological feasibility is established. See paragraph 985-20-25-2.~~

350-50-25-5 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Fees incurred for website hosting, which involve the payment of a~~

~~specified, periodic fee to an internet service provider in return for hosting the website on its server(s) connected to the internet, generally are expensed over the period of benefit. [Content moved to paragraph 350-40-25-17F]~~

350-50-25-6 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Costs incurred to purchase software tools, or costs incurred during the application development stage for internally developed tools, shall be capitalized unless they are used in research and development and meet either of the following conditions:~~

- ~~a. They do not have any alternative future uses.~~
- ~~b. They are internally developed and represent a pilot project or are being used in a specific research and development project (see paragraph 350-40-15-7).~~

350-50-25-7 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Costs to obtain and register an internet domain shall be capitalized under Section 350-30-25. [Content amended and moved to paragraph 350-40-25-17J]~~

> ~~Costs Incurred in the Graphics Development Stage~~

350-50-25-8 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Graphics are a component of software. The costs of developing initial graphics shall be accounted for under Subtopic 350-40 for internal-use software, and Subtopic 985-20 for software marketed externally. [Content amended and moved to paragraph 350-40-25-17H]~~

350-50-25-9 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Modifications to graphics after a website is launched shall be evaluated to determine whether the modifications represent maintenance or enhancements of the website.~~

> ~~Costs Incurred in the Content Development Stage~~

350-50-25-10 Paragraph superseded by Accounting Standards Update No. 2025-06.~~Accounting for website content involves issues that also apply to other forms of content or information that are not unique to websites. [Content moved to paragraph 350-40-25-17G]~~

350-50-25-11 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs to input content into a website shall be expensed as incurred.~~
[Content moved to paragraph 350-40-25-17G]

350-50-25-12 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Software used to integrate a database with a website shall be capitalized under paragraphs 350-40-25-2 through 25-4.~~

350-50-25-13 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Data conversion costs shall be expensed as incurred (see paragraph 350-40-25-5).~~

> Costs Incurred in the Operating Stage

350-50-25-14 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs of operating a website shall not be accounted for differently from the costs of other operations; that is, those costs shall be expensed as incurred.~~

350-50-25-15 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs incurred in the operation stage that involve providing additional functions or features to the website shall be accounted for as, in effect, new software. That is, costs of upgrades and enhancements that add functionality shall be expensed or capitalized based on the general model of paragraph 350-40-25-7 (which requires certain costs relating to upgrades and enhancements to be capitalized if it is probable that they will result in added functionality) or, for software that is marketed, paragraphs 985-20-25-3 through 25-4 (which apply a software capitalization model to product enhancements, which include improvements that extend the life or significantly improve the marketability of a product).~~

350-50-25-16 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The determination of whether a change to website software results in an upgrade or enhancement (if internal-use software), or a product enhancement (if externally marketed software), is a matter of judgment based on the specific facts and circumstances. Paragraph 350-40-25-10 states that 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.~~

350-50-25-17 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs to register the website with internet search engines represent advertising costs and shall be expensed as incurred under paragraph 720-35-25-1. [Content moved to paragraph 350-40-25-17]~~

Implementation Guidance and Illustrations

General

> ~~Implementation Guidance~~

350-50-55-1 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The following guidance describes or provides examples of various activities that take place at different stages of website development. See Section 350-50-25 for the relevant accounting guidance.~~

• > ~~Planning Stage~~

350-50-55-2 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Planning stage activities include the following:~~

- ~~a. Develop a business, project plan, or both. This may include identification of specific goals for the website (for example, to provide information, supplant manual processes, conduct e-commerce, and so forth), a competitive analysis, identification of the target audience, creation of time and cost budgets, and estimates of the risks and benefits.~~
- ~~b. Determine the functionalities (for example, order placement, order and shipment tracking, search engine, email, chat rooms, and so forth) of the website.~~
- ~~c. Identify necessary hardware (for example, the server) and web applications. Web applications are the software needed for the website's functionalities. Examples of web applications are search engines, interfaces with inventory or other back-end systems, as well as systems for registration and authentication of users, commerce, content management, usage analysis, and so forth.~~
- ~~d. Determine that the technology necessary to achieve the desired functionalities exists. Factors might include, for example, target audience numbers, user traffic patterns, response time expectations, and security requirements.~~

- e. ~~Explore alternatives for achieving functionalities (for example, internal versus external resources, custom-developed versus licensed software, company-owned versus third-party-hosted applications and servers).~~
- f. ~~Conceptually formulate and/or identify graphics and content (see paragraphs 350-50-25-8 through 25-13).~~
- g. ~~Invite vendors to demonstrate how their web applications, hardware, or service will help achieve the website's functionalities.~~
- h. ~~Select external vendors or consultants.~~
- i. ~~Identify internal resources for work on the website design and development.~~
- j. ~~Identify software tools and packages required for development purposes.~~
- k. ~~Address legal considerations such as privacy, copyright, trademark, and compliance.~~

~~➤ Application and Infrastructure Development Stage~~

350-50-55-3 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~The website application and infrastructure development stage involves acquiring or developing hardware and software to operate the website. The activities in this stage include the following:~~

- a. ~~Acquire or develop the software tools required for the development work (for example, HTML editor, software to convert existing data to HTML form, graphics software, multimedia software, and so forth).~~
- b. ~~Obtain and register an Internet domain name.~~
- c. ~~Acquire or develop software necessary for general website operations, including server operating system software, Internet server software, web browser software, and Internet protocol software.~~
- d. ~~Develop or acquire and customize code for web applications (for example, catalog software, search engines, order processing systems, sales tax calculation software, payment systems, shipment tracking applications or interfaces, email software, and related security features).~~
- e. ~~Develop or acquire and customize database software and software to integrate distributed applications (for example, corporate databases and accounting systems) into web applications.~~
- f. ~~Develop HTML web pages or develop templates and write code to automatically create HTML pages.~~
- g. ~~Purchase the web and application server(s), Internet connection (bandwidth), routers, staging servers (where preliminary changes to the~~

- ~~website are made in a test environment), and production servers (accessible to customers using the website). Alternatively, these services may be provided by a third party via a hosting arrangement.~~
- ~~h. Install developed applications on the web server(s).~~
 - ~~i. Create initial hypertext links to other websites or to destinations within the website. Depending on the site, links may be extensive or minimal.~~
 - ~~j. Test the website applications (for example, stress testing).~~

➤ ~~Graphics Development Stage~~

350-50-55-4 ~~Paragraph superseded by Accounting Standards Update No. 2025-06.~~ For purposes of this Subtopic, graphics involve the overall design of the web page (use of borders, background and text colors, fonts, frames, buttons, and so forth) that affect the look and feel of the web page and generally remain consistent regardless of changes made to the content. **[Content moved to paragraph 350-40-25-17H]**

350-50-55-5 ~~Paragraph superseded by Accounting Standards Update No. 2025-06.~~ Graphics include the design or layout of each page (that is, the graphical user interface), color, images, and the overall look and feel and usability of the website. Creation of graphics may involve coding of software, either directly or through the use of graphic software tools. The amount of coding depends on the complexity of the graphics.

➤ ~~Content Development Stage~~

350-50-55-6 ~~Paragraph superseded by Accounting Standards Update No. 2025-06.~~ Content refers to information included on the website, which may be textual or graphical in nature (although the specific graphics described in paragraph 350-50-55-4 are excluded from content). For example, articles, product photos, maps, and stock quotes and charts are all forms of content. Content may reside in separate databases that are integrated into (or accessed from) the web page with software, or it may be coded directly into the web pages. **[Content amended and moved to paragraph 350-40-25-17G]**

350-50-55-7 ~~Paragraph superseded by Accounting Standards Update No. 2025-06.~~ Content may be created or acquired to populate databases or web pages. Content may be acquired from unrelated parties or may be internally developed.

350-50-55-8 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Content is text or graphical information (exclusive of graphics described in paragraphs 350-50-55-4 through 55-5) on the website which may include information on the entity, products offered, information sources that the user subscribes to, and so forth. Content may originate from databases that must be converted to HTML pages or databases that are linked to HTML pages through integration software. Content also may be coded directly into web pages.~~

➔ Operating Stage

350-50-55-9 Paragraph superseded by Accounting Standards Update No. 2025-06. ~~Costs incurred during the operating stage include training, administration, maintenance, and other costs to operate an existing website. Activities in the operating stage include the following:~~

- ~~a. Train employees involved in support of the website.~~
- ~~b. Register the website with Internet search engines.~~
- ~~c. Perform user administration activities.~~
- ~~d. Update site graphics (for updates of graphics related to major enhancements, see [h]).~~
- ~~e. Perform regular backups.~~
- ~~f. Create new links.~~
- ~~g. Verify that links are functioning properly and update existing links (that is, link management or maintenance).~~
- ~~h. Add additional functionalities or features.~~
- ~~i. Perform routine security reviews of the website and, if applicable, of the third-party host.~~
- ~~j. Perform usage analysis.~~

Amendments to Subtopic 720-45

9. Amend paragraph 720-45-55-1, with a link to transition paragraph 350-40-65-4, as follows:

Other Expenses—Business and Technology Reengineering

Implementation Guidance and Illustrations

> Implementation Guidance

• > Business Process Reengineering and Information Technology Transformation Project

720-45-55-1 The following table sets forth the accounting for typical components of a business process reengineering/information technology transformation project based on whether the item should be:

- a. Expensed as incurred in accordance with the guidance contained in this Subtopic
- b. Subparagraph superseded by Accounting Standards Update No. 2025-06. Expensed as incurred in accordance with internal-use software guidance contained in Subtopic 350-40
- c. Subparagraph superseded by Accounting Standards Update No. 2025-06. Capitalized in accordance with internal-use software guidance contained in Subtopic 350-40
- d. Capitalized as part of the cost of acquiring a fixed asset in accordance with a company's existing ~~policy~~ policy
- e. Capitalized or expensed in accordance with the internal-use software guidance contained in Subtopic 350-40.

(Note that letters in the grid refer to the corresponding guidance listed above.).

Steps	Third Party		Internal	
	Expense	Capitalize	Expense	Capitalize
Business process reengineering and information technology transformation:				
Preparation of request for proposal	a		a	
Current state assessment	a		a	
Process reengineering	a		a	
Restructuring work force	a		a	
<u>Acquire, develop, or implement internal-use software</u>	<u>e</u>	<u>e</u>	<u>e</u>	<u>e</u>
Preliminary software project stage activities:				
Conceptual formulation of alternatives	b		b	
Evaluation of alternatives	b		b	
Determination of existence of needed technology	b		b	
Final selection of alternatives	b		b	
Application development stage activities:				
Design of chosen path, including software configuration and software interface		e		e
Coding		e		e
Installation to hardware		e		e
Testing, including parallel processing phase		e		e
Data conversion costs:				
a. Costs to develop or obtain software that allows for access of old data by new system		e		e
b. All other data conversion processes	b		b	
Training	b		b	
Post-implementation/operation stage activities:				
Training	b		b	
Application maintenance	b		b	
Ongoing support	b		b	
Acquisition of fixed assets:				
Purchase of new computer equipment, office furniture, or work stations		d	N/A	N/A
Reconfiguration of work area—architect fees and hard construction costs		d		d

Amendments to Subtopic 730-10

10. Amend paragraphs 730-10-25-2 and 730-10-25-4 and supersede paragraph 730-10-60-2A, with a link to transition paragraph 350-40-65-4, as follows:

Research and Development—Overall

Recognition

> Elements of Costs to Be Identified with Research and Development Activities

730-10-25-2 Elements of costs shall be identified with research and development activities as follows ~~(see Subtopic 350-50 for guidance related to website development)~~:

[The remainder of this paragraph is not shown here because it is unchanged.]

> Computer Software

730-10-25-4 Development of software to be used in research and development activities, ~~including~~ includes costs incurred by an entity in developing computer software internally for use in its research and development activities, are research and development costs and, therefore, shall be charged to expense when incurred. The alternative future use test does not apply to the internal development of computer software; paragraph 730-10-25-2(c) applies only to intangibles purchased from others. ~~This includes costs incurred during all phases of software development because all of those costs are incurred in a research and development activity.~~

Relationships

> Intangibles—Goodwill and Other

730-10-60-2A Paragraph superseded by Accounting Standards Update No. 2025-06. ~~For guidance related to website development costs, see Subtopic 350-50.~~

Amendments to Status Sections

11. Amend paragraph 350-30-00-1, by adding the following items to the table, as follows:

350-30-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
350-30-15-3	Amended	2025-06	09/18/2025
350-30-15-4	Amended	2025-06	09/18/2025

12. Amend paragraph 350-40-00-1, by adding the following items to the table, as follows:

350-40-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
Performance Requirements	Added	2025-06	09/18/2025
Preliminary Project Stage	Superseded	2025-06	09/18/2025
Probable	Added	2025-06	09/18/2025
350-40-05-1D	Amended	2025-06	09/18/2025
350-40-05-7	Superseded	2025-06	09/18/2025
350-40-15-2	Amended	2025-06	09/18/2025
350-40-25-1	Amended	2025-06	09/18/2025
350-40-25-2	Superseded	2025-06	09/18/2025
350-40-25-3	Superseded	2025-06	09/18/2025
350-40-25-4	Amended	2025-06	09/18/2025
350-40-25-5	Amended	2025-06	09/18/2025
350-40-25-6 through 25-11	Superseded	2025-06	09/18/2025
350-40-25-12	Amended	2025-06	09/18/2025
350-40-25-12A	Added	2025-06	09/18/2025
350-40-25-13	Amended	2025-06	09/18/2025

Paragraph	Action	Accounting Standards Update	Date
350-40-25-17A through 25-17J	Added	2025-06	09/18/2025
350-40-30-1	Amended	2025-06	09/18/2025
350-40-35-3	Amended	2025-06	09/18/2025
350-40-50-1	Amended	2025-06	09/18/2025
350-40-55-3	Superseded	2025-06	09/18/2025
350-40-55-4	Amended	2025-06	09/18/2025
350-40-55-5 through 55-21	Added	2025-06	09/18/2025
350-40-65-4	Added	2025-06	09/18/2025

13. Add paragraph 350-50-00-1 as follows:

350-50-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
350-50-05-1	Superseded	2025-06	09/18/2025
350-50-15-1 through 15-3	Superseded	2025-06	09/18/2025
350-50-25-1 through 25-17	Superseded	2025-06	09/18/2025
350-50-55-1 through 55-9	Superseded	2025-06	09/18/2025

14. Add paragraph 720-45-00-1 as follows:

720-45-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
720-45-55-1	Amended	2025-06	09/18/2025

15. Amend paragraph 730-10-00-1, by adding the following items to the table, as follows:

730-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
730-10-25-2	Amended	2025-06	09/18/2025
730-10-25-4	Amended	2025-06	09/18/2025
730-10-60-2A	Superseded	2025-06	09/18/2025

The amendments in this Update were adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Richard R. Jones, *Chair*
Hillary H. Salo, *Vice Chair*
Christine A. Botosan
Frederick L. Cannon
Susan M. Cospers
Marsha L. Hunt
Dr. Joyce T. Joseph

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. The objective of the amendments in this Update is to modernize the accounting for software costs that are accounted for under Subtopic 350-40, *Intangibles—Goodwill and Other—Internal-Use Software* (referred to as "internal-use software").

BC3. The amendments in this Update make targeted improvements to Subtopic 350-40 by increasing the operability of the internal-use software recognition guidance considering different methods of software development. The amendments do not affect software costs subject to Subtopic 985-20, *Software—Costs of Software to Be Sold, Leased, or Marketed* (referred to as "external-use software").

BC4. Considering stakeholder feedback, the Board expects that capitalization of internal-use software costs generally will not change significantly for most types of software under the amendments in this Update. For the development of software to be provided via a cloud computing arrangement (CCA), the Board expects that the amendments could result in a decrease in software capitalization.

BC5. On October 29, 2024, the Board issued the proposed Accounting Standards Update, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Targeted Improvements to the Accounting for Internal-Use Software*, for public comment with the comment period ending on January 27, 2025. The Board received 40 comment letters. Overall, a majority of comment letter respondents supported the proposed amendments, noting that those amendments would (a) clarify and improve the application of Subtopic 350-40 and (b) generally be operable and auditable. However, many respondents expressed operability concerns over certain aspects of the proposed amendments, particularly related to the evaluation of whether there is

significant uncertainty associated with the development activities of the software (referred to as “significant development uncertainty”) and the proposed statement of cash flows presentation requirement.

BC6. The Board redeliberated the issues and the comment letter feedback and considered stakeholder feedback on potential revisions and improvements in reaching the conclusions in this Update, as discussed below.

Background Information

BC7. Software, such as application software, is a set of codes or programs that tells hardware what to do. Generally, software is developed independent of the hardware that it can be installed into, such as computer servers, laptops, mobile phones, and other devices. Common examples of application software include word processors, spreadsheets, web browsers, mobile phone applications (apps), databases, and enterprise resource planning (ERP) systems. There are many end users of software, including customers, employees, clients, and vendors (collectively, “end users”).

BC8. Entities utilize software in a wide variety of ways, including to support an entity’s operations, to facilitate services that an entity provides to its end users (such as online banking, online shopping, and online games), and to allow end users of the software to access information. Another way that entities use software is by selling software to their end users through (a) on-premises licenses where the software can be used offline by the end user or (b) arrangements where an end user can only access and use the software through the internet (referred to interchangeably in this Update as CCAs, software-as-a-service [SaaS] arrangements, and hosting arrangements), which have continued to become more prevalent than on-premises licenses as the software industry has evolved. Additionally, software is embedded into tangible items, such as network equipment, cars, household appliances, and industrial robots. Therefore, virtually every entity is affected by the accounting for software costs.

BC9. Historically, software was developed using the waterfall method, which often is described as a prescriptive and sequential method. While the waterfall method may be suitable in the development of certain software, it is not considered to be adaptive to changes in software requirements. Because each phase under the waterfall method should be completed in sequential order before moving to the next phase, it may be challenging and costly to go back

to a previous phase. Additionally, entities may find it difficult to outline all the performance requirements at the beginning of the software project, and significant changes in later phases can be challenging and costly to incorporate.

BC10. To overcome challenges with the waterfall method, other software development methods have emerged, including the agile method. The agile method allows software developers to make incremental and iterative adaptations in response to changes in performance requirements. Within the agile method, a software project is broken down into smaller efforts (or sprints) to develop a specific function or feature within the software project. This iterative environment makes the software project more manageable and allows for entities to quickly incorporate and develop changes.

BC11. The internal-use software guidance was issued when software was primarily developed using the waterfall method; therefore, the current guidance does not contemplate other methods of software development (for example, agile).

Current Requirements

BC12. Software costs are costs that an entity incurs to acquire, internally develop, or modify software (collectively, “software development” or “development”). Subtopics 350-40 and 985-20 are the principal areas in the Codification applicable to software costs. Determining what guidance applies is important because there are different requirements for when an entity is required to start capitalizing software costs, and those differences can result in significantly different financial reporting outcomes.

BC13. Determining whether Subtopic 350-40 or Subtopic 985-20 applies to software development costs largely depends on how an entity plans to use the software. When an entity has a substantive plan to sell, lease, or otherwise market the software externally (including software licensed on premises or software embedded in a tangible item), the entity is required to account for the software costs under Subtopic 985-20. Conversely, Subtopic 350-40 applies when an entity acquires or develops software that will be used internally in its own operations (such as an internal payroll system). Subtopic 350-40 also applies when an entity develops software that will be used to provide services (rather than to license the software) to external parties—these arrangements can vary significantly in nature and are often referred to as CCAs. As a result, Subtopic 350-40 applies to both (a) an entity that is incurring costs to develop

the software that will be provided to an end user in a CCA (referred to as “software that will be provided via a CCA”) and (b) an end user that incurs costs to implement a CCA. However, the external-use software guidance applies to software developed for customers to access in CCAs in which (1) the customer has a contractual right to take possession of the software at any time during the hosting period without significant penalty and (2) 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. The determination of whether software is accounted for under Subtopic 350-40 or Subtopic 985-20 is not affected by the amendments in this Update.

Internal-Use Software (Subtopic 350-40)

BC14. The guidance for internal-use software largely originated from AICPA Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, which was issued in 1998. In developing SOP 98-1, which is included in the current internal-use software guidance, the Accounting Standards Executive Committee (AcSEC) considered the definition of an asset in now superseded FASB Concepts Statement No. 6, *Elements of Financial Statements*, and the recognition criteria in now superseded FASB Concepts Statement No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises*. Paragraph 25 of Concepts Statement 6 defined assets as “probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events” (footnote reference omitted).

BC15. Entities are currently required to capitalize costs incurred for software developed for internal use and CCA implementation costs depending on the nature of the costs and the project stage during which they occur. The guidance describes three sequential stages of software development and implementation activities (referred to as “project stages”) as follows:

- a. **Preliminary project stage.** This stage generally occurs when an entity considers and defines its software needs and possible solutions, regardless of whether it ultimately pursues a project to develop internal-use software or enter into a CCA.
- b. **Application development stage.** This stage begins after (1) the preliminary project stage is complete, (2) management, with the relevant authority, implicitly or explicitly authorizes and commits to funding a computer software project, and (3) it is probable that the project will be

completed and the software will be used to perform the function intended.

- c. **Post-implementation operation stage.** This stage begins when the software project is substantially complete and ready for its intended use, which is analogous to the period after all substantial testing is complete.

BC16. Generally, entities are required to expense costs incurred during the preliminary project stage and to capitalize eligible costs incurred during the application development stage. During the post-implementation operation stage, entities are required to capitalize eligible costs that add functionality as enhancements in the same manner as described in paragraph BC15 and to expense maintenance costs as incurred.

BC17. Entities must make various judgments in applying the current guidance for internal-use software, some of which the Board considered in developing the amendments in this Update, including judgments related to determining:

- a. The area of GAAP that applies to costs incurred to develop software that will be provided via a CCA, particularly for a hybrid software arrangement in which on-premises software interacts with a cloud-based solution
- b. The unit of account in applying Subtopic 350-40 (that is, what constitutes a software project)
- c. Whether software costs are for enhancements that add functionality or are maintenance costs
- d. The area of GAAP that applies to an asset that incorporates both internal-use software and tangible assets and whether the software component should be accounted for under Subtopic 350-40 or as part of a tangible asset under other GAAP, such as Subtopic 360-10, Property, Plant, and Equipment—Overall.

External-Use Software (Subtopic 985-20)

BC18. The guidance for external-use software originated from FASB Statement No. 86, *Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed*, which was issued in 1985.

BC19. Generally, entities are required to expense all costs incurred to establish technological feasibility of the software as research and development (R&D) costs in accordance with Subtopic 730-10, Research and Development—Overall. Entities are required to capitalize eligible costs incurred after

establishing technological feasibility until the product is available for general release. Following general release, entities are required to capitalize eligible costs of enhancements that extend the life or significantly improve the marketability of the software product in the same manner as described in the previous sentence and to expense maintenance costs as incurred.

Key Challenges of Current Requirements

BC20. Stakeholders provided the following feedback on the key challenges that exist in the accounting for and disclosure of software costs, including in response to the 2021 FASB Invitation to Comment, *Agenda Consultation*:

- a. **The methods used to develop software have evolved.** As described in paragraph BC10, many entities shifted from using a prescriptive and sequential method to using an incremental and iterative method. As a result, entities find it challenging to apply the project stages in Subtopic 350-40 to software costs incurred in an iterative environment.
- b. **Financial reporting outcomes sometimes are unintuitive.** While the internal-use software guidance is applied to software that is used solely for internal purposes (such as an internal payroll system), it also applies to software that is sold as a service (such as software that will be provided via a CCA). Under the external-use software guidance, entities often expense a significant amount of software costs as incurred. Conversely, under the internal-use software guidance, some entities capitalize significant costs, including the costs to develop software that will be provided via a CCA. Overall, stakeholders have trouble understanding why similar projects yield different amounts of capitalized costs depending on how the software is delivered to end users.
- c. **Information about an entity's software costs could be enhanced.** Overall, many investors noted that transparency about an entity's software costs could be enhanced, and, in certain circumstances, additional information could be decision useful. Many investors indicated that they were not aware that the costs to develop software that will be provided via a CCA are accounted for differently from the costs to develop software that will be sold via a license. Furthermore, investors observed that companies often have inconsistent financial reporting outcomes (for example, some companies capitalize software costs, while others expense all software costs).

Basis for Conclusions

Benefits and Costs

BC21. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC22. Over the course of this project, the Board and the FASB staff conducted extensive outreach with investors, preparers, practitioners, and others to obtain information about potential improvements to the accounting for and disclosure of software costs.

BC23. On the basis of that outreach and comment letter feedback received on the proposed Update, the Board concluded that the expected benefits of the amendments in this Update are as follows:

- a. Removing the project stages will clarify and increase the operability of applying the internal-use software guidance to software costs incurred in an iterative development environment. Additionally, because the amendments are neutral to different software development methods, there is less chance that the guidance could become outdated over time.
- b. Aligning the recognition requirements for internal-use software costs more closely with the requirements for external-use software costs, as well as articulating certain judgments needed to recognize internal-use software costs, could help to establish greater consistency in the financial reporting outcomes across entities and within an entity, especially for entities that develop software that will be sold. This increased consistency in financial reporting will, in turn, benefit investors that analyze entities that primarily develop software. As described in paragraph BC20, stakeholders expressed concern about the different

recognition requirements for the costs to develop software that will be provided via a CCA under the internal-use software guidance and the costs to develop software that will be sold via an on-premises license under the external-use software guidance, which can result in different capitalization outcomes. These stakeholders said that the costs that are capitalized for software that is developed for sale should not differ depending on how the software is delivered to end users. As noted in paragraph BC4, the Board expects that the amendments could result in more of the costs to develop software that will be provided via a CCA being expensed, which will better align with the financial reporting outcomes for the costs of software sold via an on-premises license in most cases. However, the Board acknowledges that the amendments will not entirely eliminate the differences in accounting between software that will be provided via a CCA and software that will be sold via an on-premises license. Additionally, the Board acknowledges that because application of the amendments requires judgment to determine whether and when an entity capitalizes software costs (see paragraph BC32), some entities may have different financial reporting outcomes for similar facts and circumstances.

BC24. The Board also acknowledges that the amendments in this Update will introduce additional costs for preparers, including (a) one-time costs to update systems, processes, and/or accounting policies and (b) ongoing costs to comply with the amendments. However, on the basis of comment letter feedback, the Board does not expect that the extent of one-time and ongoing costs will be significant. Additionally, the Board expects that the amendments could reduce ongoing costs (as compared with current guidance) because entities that capitalize less software costs under the amendments will not need to track costs at the same level of detail that they do currently.

BC25. Therefore, the Board concluded that the expected benefits of the amendments in this Update justify the expected costs. The Board's specific considerations about the benefits and costs of these amendments are further discussed in subsequent sections.

Targeted Improvements to Subtopic 350-40—Overall

BC26. The amendments in this Update make targeted improvements by (a) removing all references to project stages throughout Subtopic 350-40 and (b) clarifying the starting capitalization threshold.

BC27. The Board considered other recognition models that would have resulted in more extensive changes to GAAP and the extent of capitalization, including the single model, the dual model, and the expense all model (see paragraphs BC76–BC89 for alternatives considered). The Board’s analysis considered the definition of an asset in Chapter 4, *Elements of Financial Statements*, of FASB Concepts Statement No. 8, *Conceptual Framework for Financial Reporting*. Paragraph E16 of Chapter 4 defines an asset as “a present right of an entity to an economic benefit.” Although Chapter 4 does not include the term *probable* in the definition of an asset, paragraph E36 implies that because the facts and circumstances that generate intangible assets are so varied, whether an asset has been created often must be resolved at the standards level.

BC28. Feedback from investors generally indicated that they are not interested in significant increases in the level of software costs capitalized, especially for software to be provided to external parties. Investors strive to compare earnings across entities, and different levels of capitalization can make that comparison challenging. For example, if one entity capitalizes some software costs and another entity expenses all software costs, the amount of expenses on those entities’ income statements will not be comparable. Some investors also are concerned about the level of management judgment that is needed to evaluate whether software development costs should be capitalized. Additionally, some investors view expenditures to develop revenue-producing software as representing recurring operating expenses and do not support greater capitalization and amortization of those expenditures. Furthermore, feedback from preparers indicated that more extensive changes to the recognition of software costs that would have increased capitalization could be costly to implement, initially and on an ongoing basis.

BC29. The Board considered an analysis of the definition of an asset and the recognition criteria in the Board’s Conceptual Framework in the broader context of the objective of general-purpose financial reporting, which is to provide decision-useful information to investors, and the feedback received from stakeholders, including the strong investor feedback described in paragraph BC28. In light of this consideration and weighing the expected benefits relative to the expected costs, the Board ultimately decided to pursue targeted improvements to Subtopic 350-40 rather than more extensive changes to the recognition of software costs.

BC30. For those reasons, the amendments in this Update focus on the key challenge that entities face in applying Subtopic 350-40—applying that

guidance to software that is developed using an incremental and iterative method. The Board acknowledges that there are other challenges that the amendments do not address, including those described in paragraphs BC58–BC70.

BC31. Throughout this project, the Board also considered feedback from various stakeholders on the judgment required to apply (a) current software cost guidance, (b) certain recognition requirements considered but dismissed by the Board, and (c) the amendments in the proposed Update. Some comment letter respondents expressed concerns about the level of judgment required to evaluate significant development uncertainty. Those respondents expressed concern that the level of judgment could result in diversity in practice and may require the use of information technology (IT) experts. Other comment letter respondents said that the proposed amendments would appropriately describe the judgments that entities currently perform and that it is important that the guidance be flexible to enable entities to apply judgment when evaluating their specific facts and circumstances. Additionally, some comment letter respondents suggested that the Board explicitly acknowledge the use of judgment within the internal-use software guidance.

BC32. The Board acknowledges that application of the amendments in this Update requires judgment to determine whether and when an entity capitalizes software costs on the basis of the entity's evaluation of its specific facts and circumstances. The Board noted that the application of judgment is inherent in GAAP and concluded that the use of judgment is appropriate in the internal-use software guidance because management is best positioned to evaluate its facts and circumstances, considering the diverse and continuously evolving nature of software development. Additionally, as noted by various stakeholders, including comment letter respondents, the amendments are consistent with certain judgments that entities currently make in practice. Therefore, the Board does not expect that application of the amendments will require entities to use IT experts.

BC33. In response to comment letter feedback, the Board considered but dismissed amending the internal-use software guidance to explicitly state that an entity needs to apply judgment when evaluating significant development uncertainty. While all Board members agreed that entities should use judgment, some Board members would have preferred to explicitly acknowledge the use of judgment in the guidance to (a) address comment letter feedback and (b) ensure that the guidance is applied in practice consistent with the Board's intent. However, other Board members noted that

the application of judgment is inherent in GAAP and that including an acknowledgement in the amendments in this Update could create a precedent for future standard setting.

Removal of Project Stages

BC34. The amendments in this Update remove all references to project stages throughout Subtopic 350-40. As a result, all entities should determine when to begin capitalization by evaluating whether (a) management has authorized and committed to funding the software project and (b) it is probable that the project will be completed and the software will be used to perform the function intended.

BC35. The Board considered whether to provide different recognition guidance for different software development methods—that is, whether to retain the project stages guidance for software developed using a linear method (for example, waterfall) and add requirements for entities that develop software using a nonlinear method (for example, agile). Stakeholders indicated that (a) it is uncommon to develop software using an entirely linear development method and (b) requiring entities to distinguish between linear and nonlinear software development methods could add costs and unnecessary complexity. Generally, stakeholders indicated that operability would be enhanced and consistency would be increased by removing the project stages and requiring the same recognition threshold for all internal-use software, regardless of the development method. Comment letter respondents also generally supported the removal of references to project stages throughout Subtopic 350-40 because it would (1) simplify the guidance and (2) better align with modern software development methodologies (for example, agile). Therefore, the Board decided to remove all references to project stages and not to require entities to distinguish between linear and nonlinear development methods.

Definition of Probable

BC36. The term *probable* in Subtopic 350-40 is not linked to a Master Glossary term. The amendments in this Update link the term *probable* in Subtopic 350-40 to the Master Glossary definition. Probable is defined as “the future event or events are likely to occur.” This definition originated from FASB Statement No. 5, *Accounting for Contingencies*, and is used in numerous Topics.

BC37. Stakeholders have said that the Master Glossary definition of probable is well understood and is widely used in GAAP. Comment letter respondents

did not raise concerns about linking the definition of probable in Subtopic 350-40 to the Master Glossary definition. Therefore, to increase consistency in application and provide clarity, the Board decided to link the term *probable* in Subtopic 350-40 to the Master Glossary definition.

Significant Development Uncertainty

BC38. The amendments in this Update clarify that if there is significant uncertainty associated with the development activities of the software (referred to as “significant development uncertainty”), the probable-to-complete recognition threshold is not met.

BC39. The amendments in the proposed Update stated that an entity *may* be able to determine that a software project meets the probable-to-complete recognition threshold without having to evaluate significant development uncertainty. For example, in the implementation and customization of an ERP system using a developed solution, an entity might have been able to conclude that the probable-to-complete recognition threshold had been met without having to evaluate significant development uncertainty. The Board proposed this amendment so that entities would be able to avoid incurring incremental implementation costs when assessing the capitalization of costs for software projects that clearly meet the probable-to-complete recognition threshold under current guidance.

BC40. Some comment letter respondents suggested that the evaluation of significant development uncertainty be required for *all* software projects. Those respondents stated that an entity would evaluate the same or similar facts and circumstances to demonstrate that significant development uncertainty does not exist as it would to demonstrate that significant development uncertainty does not need to be evaluated. Therefore, those respondents observed that a requirement to apply the significant development uncertainty evaluation for all software projects would likely result in the same, or similar, levels of costs for the types of internal-use software that clearly meet the capitalization threshold under current guidance.

BC41. In response to the feedback received, the Board decided to require that entities evaluate significant development uncertainty for *all* software projects. This revision clarifies and streamlines the amendments in this Update without significantly changing the expected costs to apply the amendments. The Board also expects that the evaluation of significant development uncertainty will be straightforward for some software projects (for example, in the implementation

and customization of an ERP system using a developed solution) and will be more complex for others.

BC42. Some comment letter respondents suggested that the Board replace the proposed evaluation of significant development uncertainty with the evaluation of technological feasibility from Subtopic 985-20. Additionally, other respondents suggested leveraging the guidance about technological feasibility to help establish when significant development uncertainty is resolved. In contrast, other comment letter respondents strongly discouraged incorporating technological feasibility into Subtopic 350-40 because assessing technological feasibility would be a significant change to that guidance and could result in less capitalization of internal-use software costs. The Board noted that assessing technological feasibility for some types of software would represent a significant change from Subtopic 350-40. For these reasons, the Board did not incorporate an evaluation of technological feasibility into the amendments in this Update.

Factors That Indicate Significant Development Uncertainty Exists

BC43. The amendments in this Update provide the following two factors that indicate that significant development uncertainty exists. If either factor is present, then the probable-to-complete recognition threshold is not met.

- a. **Novel or unproven software.** The software being developed has technological innovations or novel, unique, or unproven functions or features, and the uncertainty related to those technological innovations, functions, or features, if identified, has not been resolved through coding and testing.
- b. **Significant performance requirements.** The significant performance requirements of the computer software have not been identified or the identified significant performance requirements continue to be substantially revised.

BC44. The amendments in the proposed Update would have included novel or unproven software and significant performance requirements as factors that *may* indicate that there is significant development uncertainty. Several comment letter respondents observed that the proposed amendments were unclear about whether an entity (a) could conclude that significant development uncertainty does not exist even if one or both of those factors are present and (b) should consider other factors.

BC45. Considering that feedback, the Board decided to make novel or unproven software and significant performance requirements the only two factors to indicate that significant development uncertainty exists. While some Board members were concerned that creating a list of factors could become outdated, the Board ultimately decided that this revision improves the operability and consistency of applying the amendments in this Update. Additionally, consistent with current guidance, entities are required to evaluate whether it is probable that a software project will be completed and that the software will be used to perform the function intended before beginning to capitalize software costs. Therefore, if there are other facts and circumstances an entity currently considers in that evaluation, the entity should continue to consider those facts and circumstances in applying the probable-to-complete recognition threshold.

Novel or unproven software

BC46. The first factor that indicates that significant development uncertainty exists is whether the software being developed has technological innovations or novel, unique, or unproven functions or features. This language is similar to current guidance for the development of external-use software. Specifically, paragraph 985-20-25-2(a)(3) requires an entity to evaluate whether a “detail program design has been reviewed for high-risk development issues” and uses “novel, unique, unproven functions and features or technological innovations” as examples of high-risk development issues. The Board considered whether the novel or unproven software factor should be described as *high-risk development issues*, consistent with the language used in Subtopic 985-20. However, stakeholders suggested that if *high-risk development issues* means that the software being developed has technological innovations or novel, unique, or unproven functions or features, that should be stated directly, rather than introducing a new term to Subtopic 350-40. Therefore, the Board decided to avoid using the term *high-risk development issues* in the amendments in this Update.

BC47. The Board also considered whether entities should specifically be required to account for and disclose novel or unproven software expenses as R&D (under Subtopic 730-10). However, many stakeholders said that it would be more logical to require entities to consider whether software is novel or unproven in determining when to capitalize software costs (that is, as part of the recognition guidance) because that is relevant in evaluating whether a

project is probable of being completed. For example, some stakeholders, particularly SaaS entities, observed that their evaluation of whether software being developed is novel and the identification of significant performance requirements are often performed concurrently. Additionally, some stakeholders expressed concern that some novel or unproven software expenses could be related to operational or administrative software and that requiring entities to account for all internal-use software costs that are novel or unproven as R&D would be a change in practice and is inconsistent with stakeholders' views about the nature of those costs. Moreover, some stakeholders that are currently expensing costs to develop revenue-producing software under Subtopic 350-40 said that they typically disclose those expenses in R&D because they are directly related to future revenues.

BC48. Therefore, the Board decided to include consideration of whether the software is novel or unproven as part of the recognition guidance. Entities should continue to apply the scope guidance in Subtopics 350-40 and 730-10 to determine relevant disclosures for software costs that are not capitalized. For example, Subtopic 730-10 applies to software to be used in R&D and activities aimed at developing or significantly improving a product or service or a process or technique whether the product or process is intended for sale or use.

Significant performance requirements

BC49. The second factor that indicates that significant development uncertainty exists is whether the software's significant performance requirements have not been identified or continue to be substantially revised. The amendments in this Update define performance requirements as what an entity needs the software to do (for example, functions or features). That definition is consistent with how performance requirements are currently described in the Master Glossary definition of the term *preliminary project stage*.

BC50. The Board included the significant performance requirements factor to improve the operability of the amendments in this Update by acknowledging that an entity may develop software using a nonlinear method and may revise the performance requirements throughout the project. However, the amendments do not require an entity to identify and cease revising *all* of the software's performance requirements before it begins to capitalize its software

development costs. Rather, an entity should identify only those performance requirements that are significant and/or are significant and expected to continue to be substantially revised.

BC51. Stakeholders, including comment letter respondents, broadly supported the significant performance requirements factor in considering whether there is significant development uncertainty. Those stakeholders acknowledged that this factor is similar to current requirements, especially for entities that develop software using a nonlinear method. Additionally, comment letter respondents agreed that if an entity has not identified or continues to substantially revise the significant needs of the software, then it is likely that significant development uncertainty exists and that the entity should not begin capitalizing costs.

BC52. Most comment letter respondents indicated that the proposed definition of performance requirements is clear and operable. Those respondents provided several reasons, including that the definition is generally consistent with current practice and that it strikes an appropriate balance between providing specific guidance and requiring management judgment. Other comment letter respondents provided suggestions for improvements, including removing functions or features from the definition (that is, not citing examples) and changing functions or features from being examples to being the explicit definition of what an entity needs the software to do. The Board decided not to revise the proposed definition of performance requirements on the basis of those suggestions because the Board concluded that those suggestions would reduce the operability of the guidance or inhibit management's ability to apply appropriate judgment.

BC53. A few comment letter respondents noted that evaluating significance in the terms *significant performance requirements* and *significant development uncertainty* would be highly judgmental and might lead to inconsistent application. Those respondents requested that the Board replace *significant* with another term, such as *more than insignificant*, or provide additional guidance on how an entity should evaluate significance. The Board decided to maintain the term *significant* and decided not to provide additional guidance on how to evaluate significance. The Board noted that the term *significant* is widely used in GAAP and well understood in practice.

Resolution of Significant Development Uncertainty

BC54. The amendments in the proposed Update would have required an entity to determine when to begin capitalizing costs once significant development

uncertainty had been resolved but did not specifically address how an entity would resolve significant development uncertainty or demonstrate that it had been resolved. Several comment letter respondents noted that it was unclear how an entity would identify the point at which significant development uncertainty had been resolved. Furthermore, some comment letter respondents said that the proposed amendments were unclear on how an entity should determine when software is no longer novel or unproven.

BC55. On the basis of this feedback, the Board decided to specify that the uncertainty related to novel or unproven software should be resolved through coding and testing, similar to how uncertainties related to *high-risk development issues* are resolved in Subtopic 985-20. The amendments in this Update require an entity to first identify whether the software being developed is novel or unproven. If the software is novel or unproven, then the amendments require that the uncertainty related to the novel or unproven nature of that software be resolved through coding and testing. For example, if an entity identifies that there are unproven features in the software, it is then required to establish that those features are no longer unproven through coding and testing before it begins capitalizing eligible software costs.

BC56. The Board made these revisions to the amendments in the proposed Update to improve the operability and the consistency of applying the amendments in this Update. Additionally, the Board expects that the combination of specifying when the novel or unproven factor is resolved and its decision to require that there are only two factors that indicate significant development uncertainty exists (see paragraph BC45) will alleviate comment letter respondents' concerns about how to evaluate when significant development uncertainty is resolved.

BC57. Additionally, the Board discussed how the amendments in this Update could affect the financial reporting of SaaS entities that are developing novel or unproven software. The Board observed that there could be a limited amount of time between when capitalization of costs begins and when it ends for these entities in applying the amendments because (a) uncertainty related to the development of novel or unproven software needs to be resolved through coding and testing and (b) capitalization of internal-use software costs ends after all substantial testing is completed. This may result in most software costs to develop novel or unproven software being expensed. The Board concluded that this is a reasonable accounting outcome for the costs to develop novel or unproven software.

Other Considerations

Unit of Account for Software Components and Tangible Assets (Embedded Software)

BC58. The amendments in the proposed Update would have required an entity to use a reasonable and consistent method to determine the unit of account for an asset that incorporates both software components and tangible assets and whether the software component should be (a) accounted for separately under Subtopic 350-40 or (b) combined with the tangible asset in accordance with other GAAP, such as Subtopic 360-10.

BC59. Because software often is embedded in hardware, in developing the amendments in the proposed Update, some Board members questioned whether an entity should account for the internal-use software under Subtopic 350-40 or as part of the tangible asset (under other GAAP). The Board understands that, in practice, when software is critical to or enhances the functionality of related property, plant, and equipment (PP&E), entities often account for those software costs as one unit of account with the related PP&E. However, some Board members expressed concerns that practice could, in the future, interpret the lack of clear guidance to indicate that an entity should separate the software component for accounting and disclosure purposes. Therefore, the Board proposed a requirement to clarify that entities should apply a reasonable and consistent method in making that determination. The Board did not expect that the proposed amendments would have changed how an entity determines whether embedded software should be accounted for as software or as part of another asset.

BC60. Some comment letter respondents expressed concerns about the operability and auditability of these amendments in the proposed Update. Specifically, those respondents observed that the proposed amendments could (a) be viewed as an accounting policy election; (b) imply that there is a change from current practice because the guidance has been revised, which would be inconsistent with the Board's intent; (c) create complexity for preparers and practitioners; and (d) increase diversity in practice that could affect investors. As a result of this feedback, to avoid changing current practice, the Board decided not to include the proposed amendments related to embedded software in the amendments in this Update.

The Unit of Account in Applying Subtopic 350-40

BC61. The unit of account when applying the capitalization requirements in Subtopic 350-40 is a software project. However, a software project is not defined in Subtopic 350-40, and the amendments in this Update do not specifically define what constitutes a software project.

BC62. Several comment letter respondents questioned what the unit of account should be when applying the proposed recognition requirements (specifically, what constitutes a software project). Those respondents indicated that this determination is unclear, particularly in an agile environment. For example, while some entities might view the unit of account to be an entire project, others might view the unit of account to be one phase of a project or even a single sprint. Therefore, those respondents suggested that the Board define the unit of account. In contrast, other respondents commented that the Board should not define the unit of account and should allow an entity to apply judgment in determining the unit of account on the basis of its facts and circumstances.

BC63. The Board decided not to address the unit of account in applying Subtopic 350-40 because providing guidance could change practice or limit the judgment that is currently allowed. In the Board's view, entities should continue to apply judgment in determining what constitutes a software project on the basis of its specific facts and circumstances under the amendments in this Update.

Upgrades and Enhancements

BC64. The amendments in this Update do not change the accounting in Subtopic 350-40 for software upgrades and enhancements; however, several comment letter respondents provided feedback on that accounting. Specifically, some respondents recommended that enhancements be expensed as incurred, while others questioned how an entity would evaluate the capitalization threshold for enhancements of existing software (as compared with a new software project).

BC65. The Board decided not to amend the accounting for upgrades and enhancements in this Update because it is beyond the scope of what the Board sought to address in the targeted improvements to Subtopic 350-40 (see paragraph BC30). Therefore, an entity should continue to apply judgment to account for upgrades and enhancements under the amendments in this

Update, including in its evaluation of the capitalization threshold for enhancements of existing software.

Artificial Intelligence (AI) Training and Data Conversion Costs

BC66. Subtopic 350-40 does not provide specific guidance for AI development costs, and the amendments in this Update do not specifically address how to apply the current guidance to those costs. Some comment letter respondents suggested that the Board clarify whether certain areas of Subtopic 350-40 apply to training an AI model and data conversion costs.

BC67. The Board decided not to provide specific guidance for training an AI model and data conversion costs. The Board viewed changes to clarify which costs are eligible for capitalization under Subtopic 350-40 as beyond the scope of what the Board sought to address in the targeted improvements to Subtopic 350-40 (see paragraph BC30).

Costs Incurred to Develop Software That Will Be Provided via a CCA

BC68. The amendments in this Update do not change the area of GAAP that applies to costs incurred to develop software that will be provided via a CCA. Several comment letter respondents suggested that the Board change the scope of the software cost guidance so that software costs incurred to develop software that will be provided via a CCA are accounted for in the same way as software that will be sold via an on-premises license. Consistent with stakeholder feedback on key challenges of the current requirements (see paragraph BC20), some respondents observed that software that will be provided via a CCA and software that will be sold via an on-premises license have similar economics and development processes and, therefore, should be subject to the same guidance.

BC69. While the Board acknowledges these challenges, it ultimately decided to retain the scope of the software cost guidance as part of the amendments in this Update because changing the scope of current software cost guidance is beyond the scope of what the Board sought to address in the targeted improvements to Subtopic 350-40 (see paragraph BC30). Several Board members also noted that it would be challenging to define what internal-use software to separate from the scope of Subtopic 350-40 because software

often facilitates services that an entity provides to its end users. One Board member would have preferred to expand the scope of Subtopic 985-20 by extending the phrase *otherwise marketed* in the scope of that Subtopic to include software provided via a CCA.

BC70. Notwithstanding its decision to retain the scope of the current software cost guidance, the Board observed that the amendments in this Update more closely align the recognition requirements for software costs that will be provided via a CCA with the requirements for software costs that will be sold via an on-premises license (see paragraph BC23).

Alternatives Considered but Dismissed

Modernize the External-Use Software Guidance

BC71. The Board considered whether it would be helpful to make targeted improvements to modernize the external-use software guidance (in Subtopic 985-20), specifically to address how to evaluate technological feasibility.

BC72. Technological feasibility is established when an entity has (a) completed all the planning, designing, coding, and testing activities that establish that the product will meet its design specifications and (b) evidenced that technological feasibility has been established through the development of either a detail program design or a working model. Additionally, Subtopic 985-20 requires that if an entity's process excludes the development of a detail program design, a working model of that software must have been completed before the entity can begin capitalizing software costs.

BC73. Stakeholders that apply Subtopic 985-20 indicated that entities generally do not complete a detail program design in a nonlinear development method. Therefore, entities typically rely on the completion of a working model to establish technological feasibility when applying the guidance.

BC74. The Board considered two targeted improvements to Subtopic 985-20. First, the Board considered adding an acknowledgement that an entity often will not create a detail program design when developing software in a nonlinear development method and, therefore, should rely on completion of a working model to determine when technological feasibility has been established. Second, the Board considered adding an acknowledgement that completion of a working model may occur late in the development cycle in a nonlinear

development method and, therefore, may limit which costs are eligible for capitalization.

BC75. Ultimately, the Board decided that targeted improvements to Subtopic 985-20 were unnecessary because the current guidance (paragraph 985-20-25-2(b)) explicitly requires an entity to use a working model when it does not create a detail program design. Furthermore, stakeholders have not expressed a significant need to change the guidance in Subtopic 985-20. Comment letter respondents generally did not raise concerns about the Board's decision not to pursue amendments to Subtopic 985-20.

The Single Model

BC76. The Board considered requiring an entity to capitalize all direct software costs from the point at which it is probable that the software project will be completed and the software will be used to perform the function intended (referred to as the "single model"). This model would have replaced the recognition requirements for all software costs in Subtopics 350-40 and 985-20.

BC77. Stakeholders that supported the single model stated that it would eliminate the challenge of determining whether the software costs should be accounted for under the internal- or external-use software guidance. Additionally, some stakeholders noted that because they view the development of software to be provided via a CCA and software to be sold via an on-premises license as having similar—if not identical—economics, the accounting requirements should be the same. The single model would have established the same requirements for all software costs, regardless of how an entity plans to use the software or deliver the software to end users.

BC78. When discussing the single model, stakeholders broadly expected that it would increase the amount of software costs that would be capitalized. Investors generally expressed concern about this potential outcome. In particular, investors were concerned that entities would capitalize more costs to develop software that they sell to end users, which are generally expensed under current GAAP. These investors said that they strive to compare earnings across entities and that different levels of capitalization make that comparison more challenging. Additionally, investors were concerned about the potential increase in the level of management judgment that would be applied in evaluating when to capitalize software costs under the single model. Furthermore, some investors said that capitalizing and amortizing expenditures

incurred in the development of revenue-producing software would not faithfully represent the economic activity of developing software for sale to customers and would make key performance metrics such as earnings before interest, taxes, depreciation, and amortization (EBITDA) less decision useful.

BC79. Preparers, particularly those that develop external-use software, that did not support the single model raised concerns about (a) extensive one-time implementation costs to apply the single model because new or updated systems and/or processes would be required to track software costs and (b) a significant increase in ongoing costs to track the capitalized software costs. Additionally, some preparers were concerned that entities would have a high risk of recognizing software asset impairments before and/or after a software project is substantially complete because, in their view, costs would be capitalized too early under the single model.

BC80. Given the input from investors on their preference for expensing rather than capitalizing certain software costs and concerns from preparers about the increased costs to track capitalized software costs, the Board ultimately decided not to pursue the single model. Additionally, some Board members and investors were concerned that the single model would not have portrayed the differences in economic activity between software that is sold to end users and software that is used to run an entity's business. Those Board members said that those differences should be reflected in the accounting for software costs to provide investors with decision-useful information.

BC81. Comment letter respondents generally agreed with the Board's decision not to pursue the single model. Their reasons for supporting targeted improvements over the single model aligned with those considered by the Board. Some respondents said that they would have preferred the single model but acknowledged the Board's reasons for pursuing targeted improvements.

The Dual Model

BC82. The Board acknowledges that current GAAP is a dual model and will continue to be a dual model under the amendments in this Update. However, the Board considered various alternatives to improve the current distinction between external-use software costs and internal-use software costs, which stakeholders noted can be challenging to understand. Specifically, the Board considered requiring entities to recognize costs to develop external-use software (in Subtopic 985-20) as incurred expenses and to capitalize costs to develop internal-use software (in Subtopic 350-40) (referred to as the "dual

model”). The main objective of that dual model would have been to align the accounting for the development of software that will be provided via a CCA and software that will be sold via an on-premises license, which has been identified as a challenge when applying the current guidance. Some of the ways that the Board considered distinguishing between different types of software development were based on whether the software would (a) be commercialized or noncommercialized, (b) be external facing or internal facing, (c) be monetized or nonmonetized, or (d) meet the definition of R&D.

BC83. Stakeholders’ support for the dual model was generally contingent upon whether they agreed with the financial reporting outcome in a specific situation, and there was no clear consensus from stakeholders that preferred the dual model on how to improve the distinction between different types of software development. In particular, stakeholders were concerned that any requirement that would include the development of software that will be provided via a CCA in the expense as incurred model also would include the development of software that an entity uses to perform the services it sells (for example, a banking app). Stakeholders generally did not support requiring software development costs for software that an entity uses to perform the services it sells to be expensed as incurred. Therefore, a majority of the Board expressed concern that there may not be a feasible way to improve the distinction between external- and internal-use software costs.

BC84. Additionally, stakeholders and several Board members were concerned that the dual model would introduce additional unnecessary complexity by requiring entities to evaluate which model they should apply. Furthermore, given the evolving nature of software development (and related methods of use and delivery), several Board members were not convinced that an operable distinction between commercialized software and noncommercialized software could be identified. Feedback from stakeholders indicated that significant implementation guidance and examples would be needed to illustrate which recognition model applies. Board members were concerned that as software development continues to evolve, the distinction between different types of software development and any implementation guidance and illustrative examples would have a risk of becoming outdated.

BC85. The Board ultimately decided not to pursue the dual model for the reasons described above. Although comment letter respondents suggested that the Board revisit the scope of current guidance (see paragraphs BC68–BC70), respondents generally did not raise concerns about the Board’s decision not to pursue the dual model.

The Expense All Model

BC86. The Board considered requiring entities to expense all costs to develop software as incurred (referred to as the “expense all model”).

BC87. Stakeholders that initially supported the expense all model said that it would be simple and operable and would result in consistent financial reporting outcomes across entities. Additionally, those stakeholders said that information for investors about an entity’s investment in software could be provided through supplemental disclosures.

BC88. However, when the expense all model was fully introduced with its limitations and outcomes, stakeholders broadly agreed that the model would not improve GAAP. Those stakeholders cited the following reasons:

- a. At some point in the software development process, the software costs represent an asset that should be recognized as such.
- b. Entities would be required to expense acquired software, including term and perpetual licenses, up front rather than over the life of the software or license term.
- c. The expense all model would require reconsideration of software acquired as part of a business combination or further exacerbate differences between the accounting for software acquired in a business combination and software acquired in an asset acquisition or developed internally.
- d. Entities could potentially be required to separate the acquisition of a software component from a tangible component and expense the allocated cost of the software component upon acquisition. If not, software acquired as a component of a tangible asset may receive different accounting treatment than software that is not part of a tangible asset, which would place significant pressure on that determination.
- e. The potential costs of providing sufficient disclosures for investors about an entity’s investment in software would likely outweigh the benefits of the expense all model because preparers would still need to track software costs to provide those disclosures.

BC89. The Board ultimately decided not to pursue the expense all model for the reasons described above. Comment letter respondents generally did not raise concerns about the Board’s decision not to pursue the expense all model.

Presentation and Disclosure

BC90. The amendments in this Update clarify that (a) the PP&E disclosures in Subtopic 360-10 are required for all capitalized software costs accounted for under Subtopic 350-40, regardless of how those costs are presented in the financial statements, and (b) the intangibles disclosures in paragraphs 350-30-50-1 through 50-3 are not required for software costs capitalized under Subtopic 350-40. Additionally, the Board decided not to require any other incremental presentation or disclosure requirements for software costs accounted for under Subtopics 350-40 and 985-20. In arriving at these conclusions, the Board considered current presentation and disclosure requirements (including those described in paragraph BC95), several alternatives to enhance transparency about an entity's internal- and external-use software costs, and stakeholder feedback on the expected benefits and costs of providing that information. Even though the Board decided not to pursue amendments to the recognition guidance in Subtopic 985-20, it considered incremental disclosure requirements for software costs accounted for under Subtopic 985-20 to enhance transparency about an entity's external use software costs.

Intangible Asset and PP&E Disclosures

BC91. Subtopic 350-30, Intangibles—Goodwill and Other—General Intangibles Other Than Goodwill, addresses the financial accounting and reporting for (a) intangible assets (other than goodwill) acquired individually or with a group of other assets and (b) the cost of developing, maintaining, or restoring internally generated intangible assets. Paragraph 350-30-15-4 specifically excludes *capitalized software costs* from the scope of Subtopic 350-30, except for the disclosure requirements in paragraphs 350-30-50-1 through 50-3. The guidance in paragraph 350-30-15-4 originated from the FASB Staff Q&A, *Computer Software: Guidance on Applying Statement 86*, which addressed stakeholder questions on the accounting for external-use software. However, paragraph 350-30-15-4 does not specify whether the term *capitalized software costs* refers to internal- or external-use software costs or both. Additionally, while the external-use software guidance references the intangible asset disclosures in Subtopic 350-30, the internal-use software guidance does not.

BC92. The Board considered whether to require the disclosures in paragraphs 350-30-50-1 through 50-3 for capitalized internal-use software costs. Some

Board members said that the information required by those paragraphs would be relevant for all capitalized software costs, regardless of whether they are for internal- or external-use software. Other Board members viewed those requirements as duplicative of many of the disclosures required for PP&E (in Subtopic 360-10), which entities are required to consider for capitalized internal-use software. The Board decided that the intangibles disclosures in paragraphs 350-30-50-1 through 50-3 should not be required for software costs capitalized under Subtopic 350-40.

BC93. Comment letter respondents generally did not raise concerns about the amendments to Subtopic 350-30 in the proposed Update. However, one comment letter respondent observed that those proposed amendments could lead to some entities not providing any disclosures for licensed internal-use software, which is required to be classified as an intangible asset according to paragraph 350-40-25-17. Specifically, an entity would not provide the intangibles disclosures in Subtopic 350-30 if internal-use software was explicitly excluded from the scope of that Subtopic and may not provide the PP&E disclosures in Subtopic 360-10 for that software because the license is required to be classified as an intangible asset.

BC94. After considering this feedback, the Board decided that the amendments in this Update should specify that the PP&E disclosures in Subtopic 360-10 are required for all capitalized software costs accounted for under Subtopic 350-40, regardless of how those costs are presented in an entity's financial statements. Some Board members noted that requiring the application of the PP&E disclosures to software costs accounted for under Subtopic 350-40 would give investors more consistent information about an entity's internal-use software costs. Additionally, as noted in paragraph BC100 of Accounting Standards Update No. 2024-03, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses*, the Board is aware of diversity in practice about the classification of the amortization of internal-use software within the scope of Subtopic 350-40. The Board does not expect that the amendments in paragraph 350-40-50-1 will change an entity's conclusion on whether the amortization of internal-use software should be reflected in the disclosures required by Subtopic 220-40, *Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures*, as either depreciation or amortization.

Other Presentation and Disclosure Considerations

BC95. Other than limited presentation and disclosure requirements for implementation costs of a hosting arrangement that is a service contract, Subtopic 350-40 does not require specific presentation or disclosures for internal-use software costs. However, Subtopic 350-40 references disclosure requirements in other GAAP that should be considered, including PP&E (Subtopic 360-10), R&D (Subtopic 730-10), notes to financial statements (Topic 235), and risks and uncertainties (Topic 275). Subtopic 985-20 requires entities to provide disclosures about unamortized software costs, amortization, and impairments, and it references additional disclosure requirements in other GAAP (the intangibles and R&D disclosures).

BC96. The amendments in the proposed Update would have required entities to present separately cash paid for capitalized internal-use software costs, other than cash outflows incurred to implement a hosting arrangement that is a service contract, as investing cash outflows in the statement of cash flows. In developing that proposed presentation requirement in Subtopic 350-40, Board members observed that investors frequently provide feedback that the statement of cash flows is a key part of their analyses. Several Board members noted that requiring specific presentation in the statement of cash flows could be responsive to this feedback.

BC97. In addition to the proposed presentation requirement for Subtopic 350-40, the Board considered whether the current disclosure requirements in Subtopics 350-40 and 985-20 should be expanded to include one or more of the following disclosures (referred to as the “incremental disclosures”):

- a. The total internal-use and external-use software costs capitalized during the period (with or without the related amortization)
- b. A rollforward of the beginning to ending balance of net capitalized internal-use and external-use software costs (including additions, amortization, impairments, and disposals)
- c. The total internal-use software costs expensed before the probable-to-complete recognition threshold is met as R&D
- d. The total internal- and external-use software costs expensed during the period.

BC98. Investors indicated that the information that would be provided by the proposed presentation requirement, the incremental disclosures, or both could be useful in their analyses. Specifically, investors said that they (a) consider

software and technology spending to be a current-period cost of doing business and (b) are concerned about the level of management judgment that is applied to capitalize software costs. Therefore, many investors stated that they would use the information about capitalized costs and amortization to recognize capitalized software costs in current-period earnings, EBITDA, or both. Additionally, while many investors supported a disclosure about total internal- and external-use software costs expensed during the period, those investors also indicated that they would like information about an entity's total technology spend beyond software costs, including spending related to an entity's data servers.

BC99. In contrast, many stakeholders, including comment letter respondents, expressed concerns about the operability of providing additional information about software costs and/or questioned the incremental value of providing that information. Stakeholders provided the following reasons:

- a. **Expected incremental costs.** Some stakeholders indicated that incremental costs would be incurred to comply with the proposed presentation requirement, the incremental disclosures, or both. However, other preparers indicated that providing additional information on capitalized software costs generally would be operable because the information should be readily available. Several preparers stated that they would incur significant costs (both initially and on an ongoing basis) to provide incremental disclosures of software costs that were expensed because entities would need to establish new systems and processes, including detailed time tracking, to obtain that information.
- b. **Separation of cash components from total capitalized software costs.** Several comment letter respondents noted that total software costs capitalized during the period can be significantly different from the cash paid for capitalized software costs in that same period. For example, the cash outflows would not include noncash components, such as share-based payments. Those respondents stated that disaggregating between cash and noncash components of capitalized software costs would pose significant operational challenges and would be a costly undertaking for some preparers. Additionally, some stakeholders, including some investors, observed that the proposed presentation requirement would not represent a full picture of capitalized software costs.
- c. **Incremental information from current presentation and disclosure requirements.** Some practitioner and preparer comment letter

respondents questioned whether the proposed presentation requirement, the incremental disclosures related to capitalized software costs, or both would provide incremental information to investors that would be more decision useful than what they currently receive. Those respondents stated that current disclosures for capitalized software costs are sufficient.

BC100. In considering the feedback, the Board decided not to require any incremental presentation or disclosure requirements for internal- or external-use software costs (other than clarifying that the PP&E disclosures in Subtopic 360-10 are required for all software costs accounted for under Subtopic 350-40, regardless of how those costs are presented in the financial statements).

BC101. Some Board members would have preferred to require a disclosure of the total amount of internal-use software costs capitalized and amortized in the period because investors said that this disclosure would provide decision-useful information for their analyses. Specifically, those Board members referenced investors' requests for the information to adjust the effects of capitalization in their analyses. Additionally, those Board members noted that many preparers indicated that providing additional information about capitalized software costs would be operable because the information should be readily available.

BC102. However, some Board members questioned the relative benefits and costs of incremental disclosures about capitalized software costs, especially if the amendments in this Update result in decreased capitalization of software costs. While the Board recognizes that investors have indicated that they would like more information about software and technology costs, several Board members said that additional disclosures about software costs should be considered more holistically with other disclosures on intangibles and could potentially include revisiting the definition of R&D costs. Additionally, the Board notes that a public entity will be required to disclose incremental information about its expenses as a result of applying the amendments in Update 2024-03.

Private Company Considerations

BC103. The *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*, provides guidelines that assist the Board and the Private Company Council (PCC) in determining whether and in what circumstances to provide alternative recognition, measurement, disclosure, display, effective date, and transition

guidance for private companies reporting under GAAP. The assessment of significant differential factors between private companies and public companies is an important source of input when considering whether to provide accounting alternatives.

BC104. The amendments in this Update make targeted improvements to the internal-use software guidance for all entities, including private companies. According to research and outreach, including feedback from PCC members, private companies have many of the same challenges in applying the internal-use software guidance as public business entities. Comment letter respondents broadly supported the application of the amendments to all entities, including private companies, because the development of software using the agile method is no less prevalent in private companies. Additionally, comment letter respondents generally did not indicate that private company alternatives or practical expedients were warranted. Therefore, the Board decided not to require or permit any accounting alternatives or practical expedients for private companies.

Website Development Costs

BC105. Subtopic 350-50, Intangibles—Goodwill and Other—Website Development Costs, addresses whether an entity is required to expense or capitalize website development costs. That guidance includes development stages—similar to Subtopic 350-40—and heavily leverages Sections of Subtopic 350-40 that have been changed by the amendments in this Update. Certain areas of Subtopic 350-50 directly reference guidance in Subtopic 350-40; other areas of Subtopic 350-50 provide incremental guidance on a standalone basis.

BC106. When the website development costs guidance was issued, websites were typically used as a means to promote products, replace manual processes or services, and sell products. Since then, technology has rapidly evolved, and, currently, websites are most often used as an interface to access underlying software, the development of which is generally accounted for under Subtopic 350-40. For those reasons, some stakeholders, including comment letter respondents, stated that the website development costs guidance is infrequently applied or that the costs to develop a website separately from the underlying software are often immaterial. Therefore, the Board decided to supersede Subtopic 350-50 and to incorporate relevant and incremental guidance that is unique to website-specific development costs into Subtopic 350-40. The Board did not incorporate guidance from Subtopic 350-50 that

would be redundant to Subtopic 350-40. Comment letter respondents broadly supported the amendments in the proposed Update, noting that they would align the accounting for costs to develop websites with the costs to develop internal-use software, which they do not view to be different in nature.

BC107. The Board also considered an alternative that would have replaced the references to *stages* in Subtopic 350-50 with the term *activities* (for example, replace *costs incurred in the planning stage* with *costs incurred during planning activities*). However, the Board did not pursue this alternative because the guidance in Subtopic 350-50 is outdated and infrequently used. Some Board members noted that they view the development of websites and software similarly and, therefore, entities should account for the costs to develop websites and software under the same guidance. Comment letter respondents generally preferred the amendments in the proposed Update as compared with this alternative, noting that it is more operable to have the guidance for website development costs and internal-use software development costs in the same Subtopic of the Codification.

Effective Date, Transition, and Early Adoption

Effective Date

BC108. The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2027, and interim reporting periods within those annual reporting periods. Comment letter respondents generally indicated that the amendments in the proposed Update would not require significant time or costs to implement. However, some respondents noted that additional implementation time may be needed because of the concurrent implementation of other guidance.

BC109. The Board concluded that an effective date for annual reporting periods beginning after December 15, 2027, and interim reporting periods within those annual reporting periods, should provide sufficient time for public business entities to implement the amendments in this Update on the basis of the timing of the issuance of this Update. Additionally, because the Board decided to permit early adoption (see paragraph BC119), the Board noted that a later effective date would not affect public business entities that want to adopt the amendments earlier.

BC110. Comment letter respondents generally supported providing entities other than public business entities with additional time for implementation. The

Board noted that because many private companies do not issue GAAP financial statements for interim reporting periods, those private companies would have approximately three years before they are required to adopt the amendments in this Update. Considering that timing, the Board decided to require the same effective date for all entities.

Transition

BC111. The Board decided that the amendments in this Update may be applied by using a prospective transition approach, a retrospective transition approach, or a modified transition approach based on the status of the project and whether software costs were capitalized before the date of adoption.

BC112. The amendments in the proposed Update would have required entities to apply the new guidance on either a prospective basis or a retrospective basis. Overall, comment letter respondents indicated that the proposed transition requirements would be operable and auditable and that the ability to elect either a retrospective transition method or a prospective transition method would be helpful and provide reasonable alternatives for preparers. However, some respondents described challenges that entities may face during transition (see paragraphs BC114 and BC115). After considering these challenges, the Board decided to include a third transition approach.

BC113. While the Board acknowledges that providing three transition methods could reduce comparability across entities, the Board concluded that the unique characteristics of internal-use software development and the varying availability of information among preparers warrant these options. Also, the amendments in this Update generally are not expected to change significantly the amounts of software costs capitalized for most types of internal-use software, which could reduce comparability issues among entities that apply different transition methods.

BC114. Under the prospective transition approach, an entity should apply the amendments in this Update to new software costs incurred as of the beginning of the period of adoption, for all projects, including in-process projects. Stakeholders, including comment letter respondents, indicated that a prospective basis would be operable and would align with the primary transition method in the most recent Accounting Standards Update on software costs, Accounting Standards Update No. 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a*

Service Contract, which most entities found operable to apply. However, some comment letter respondents raised concerns that a prospective approach could result in (a) multiple capitalization models being applied to a single software asset and (b) impairment challenges upon transition (particularly for an in-process project for which software costs were capitalized before the date of adoption and that project does not meet the requirements for capitalization under the amendments).

BC115. In developing the amendments in the proposed Update, the Board decided not to require a retrospective transition approach because an entity might not have enough detail about historical software costs to adjust prior periods. However, the Board proposed a retrospective transition option because it would allow entities to determine whether the expected benefits of providing comparable information about software costs to investors would justify the expected costs of providing that information. Stakeholders, including comment letter respondents, generally supported an option to retrospectively apply the guidance to allow for financial statement comparability. However, some comment letter respondents noted that it could be challenging for entities to assess and conclude on significant development uncertainty in retrospective periods without applying hindsight.

BC116. On the basis of comment letter feedback, the Board decided to permit a modified transition approach. Under this approach, an entity should apply the amendments in this Update on a prospective basis to new software costs incurred (for all projects, including costs incurred for in-process projects), except for any in-process projects that, as of the date of adoption, the entity determines do not meet the capitalization requirements under the amendments but met the capitalization requirements under current guidance. For those in-process projects, an entity should derecognize any capitalized costs through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the date of adoption. The Board decided on this approach to provide a transition method that would (a) allow entities to align the accounting for ongoing projects without requiring an entity to identify detailed information about historical software projects that have been completed and (b) address the impairment challenges raised by comment letter respondents for an in-process project for which capitalization has begun. The Board acknowledges that the amendments do not address the impairment challenges raised by respondents for entities that apply the prospective transition approach (see paragraph BC114).

BC117. The Board decided to require entities that apply the amendments in this Update to disclose the nature of and reason for the change in accounting principle in accordance with paragraph 250-10-50-1(a). The Board also decided that if an entity elects the retrospective transition approach, it should provide transition disclosures (consistent with paragraphs 250-10-50-1 through 50-2, except for the requirements in paragraph 250-10-50-1(b)(2) and (c)(1) for the current period and in (b)(4)). The Board decided not to require the disclosures in paragraphs 250-10-50-1(b)(2) and (c)(1) and 250-10-50-3 related to the current periods because those disclosures can be viewed as overly burdensome, since they would require that an entity account for software costs under both the current guidance and the new guidance in the current period. Comment letter respondents did not raise concerns about the transition disclosures.

BC118. Additionally, the Board decided that if an entity elects the modified transition approach, it is required to disclose 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 date of adoption.

Early Adoption

BC119. The amendments in this Update permit early adoption for both interim and annual financial statements that have not yet been issued or made available for issuance. If an entity adopts the amendments in an interim period, the entity is required to adopt them as of the beginning of the annual reporting period that includes that interim period. Comment letter respondents broadly supported permitting early adoption.

Amendments to the GAAP Taxonomy

The amendments to the *FASB Accounting Standards Codification*® in this Accounting Standards Update require improvements to the GAAP Financial Reporting Taxonomy and SEC Reporting Taxonomy (collectively referred to as the “GAAP Taxonomy”). Those improvements, which will be incorporated into the proposed 2026 GAAP Taxonomy, are available through [GAAP Taxonomy Improvements](#) provided at www.fasb.org, and finalized as part of the annual release process.